DSR 2023

TOP 23 DIVIDEND STOCKS

BEST IDEAS FOR EACH SECTOR
BOOK EXCERPT

PROVIDED TO YOU BY

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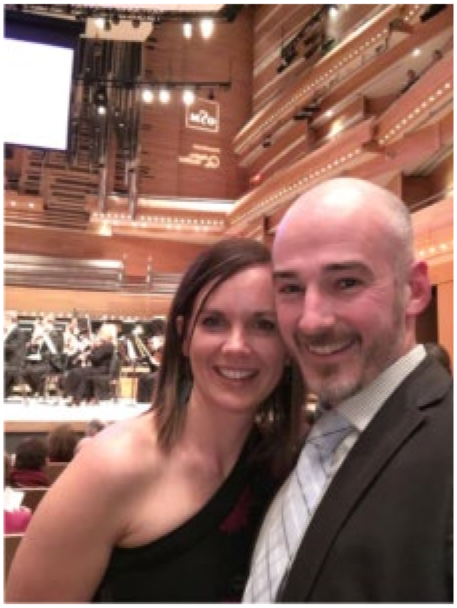
A LITTLE ABOUT ME



First, congratulations on acting and taking care of your investment portfolio! I'm a passionate investor looking forward to connecting with other passionate investors.

My name is Mike Heroux and I'm the author of The Dividend Guy Blog, The Dividend Monk, and Moose Markets (yes, I thrive on staying busy!) along with being the co-owner and portfolio manager at Dividend Stocks Rock (DSR). I have an unusual sense of humor for a "nerdy finance guy". Before you decide if you trust me or not, let's get to the "boring & serious" stuff first.

I earned my bachelor's degree with a double major in finance and marketing, I completed a CFP (Certified Financial Planner) certification along with an MBA in financial services. I worked in the financial industry for over a decade including 5 years as a financial planner and another 5 as a private banker managing accounts for high net worth (read $1M+) clients.

Besides being a passionate investor, I'm also happily married with three amazing children, and I live in the beautiful province of Quebec, Canada. Since I'm French Canadian, and French is my native language, I have most of my writings in English edited to minimize any grammar or spelling errors. I started my online venture to capitalize on my education and professional background by educating people about investing. A most fortunate by product of this professional endeavor is that I can work from home which allows me to be able to spend more time with my family.

In 2016, I decided to leave everything behind and go for a 1-year RV trip across North America and Central America (we made it all the way down to Costa Rica). Upon my return in 2017, I quit my job as a private banker and invested all my energy in my online business. I would rather pursue my dream of helping people invest through my sites. Since then, I have been a full-time online entrepreneur.

You can read more about my investing journey here.

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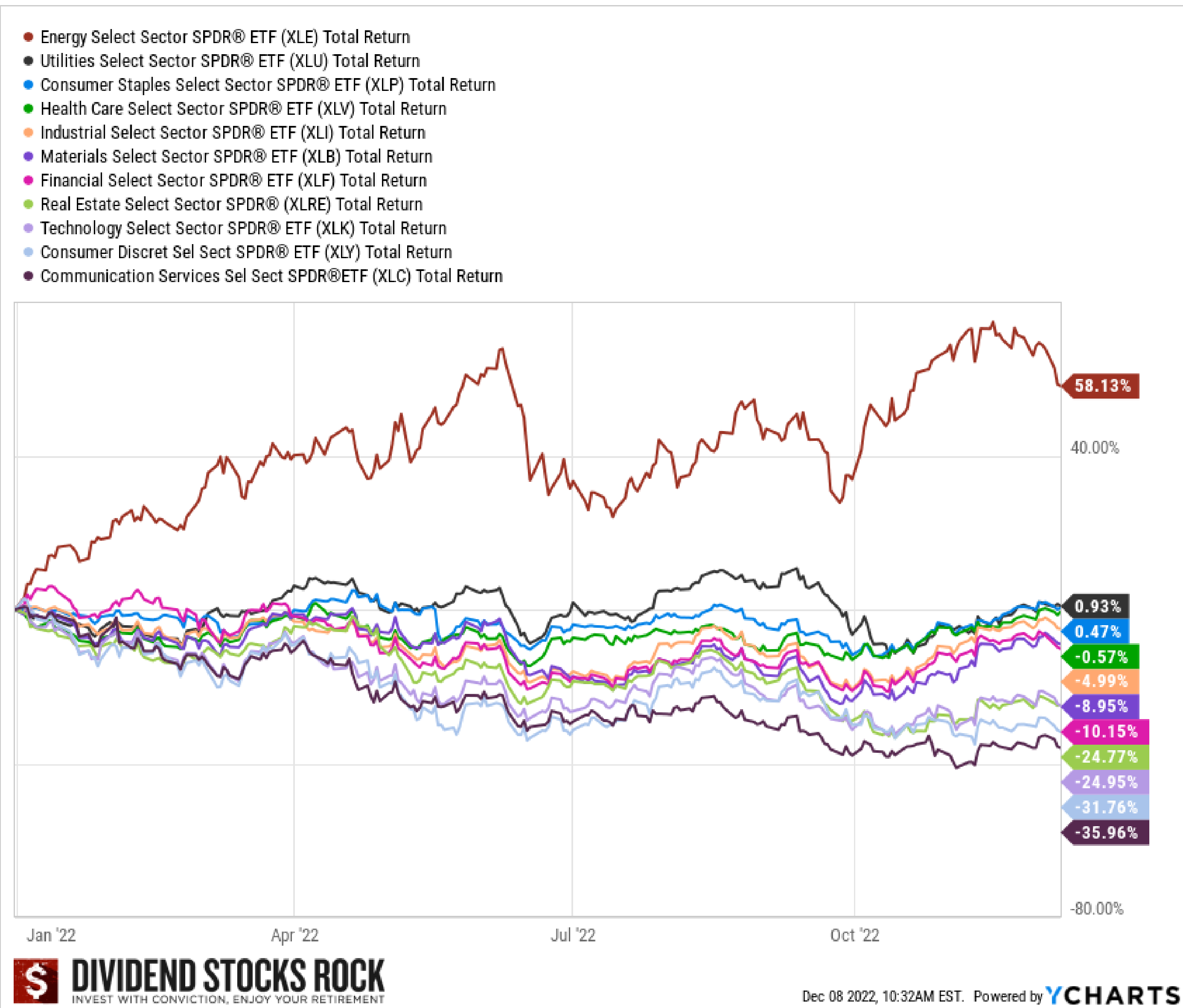
2022, CAN WE GO BACK TO 2021?

Last year, I started this newsletter by asking you who would have thought that 2021 would have been such a great year? Well, we paid the price of karma and here we are, 12 months later, sitting in the middle of a bear market. This is no ordinary bear market, though; it's a bear that is hurting many "investment hedges":

- Bonds suffered as interest rates have increased steadily and it's not over yet
- Bitcoin suffered as it proved to be nothing, but a tulip
- Gold suffered even though it's supposed to be an inflation hedge

Only one thing worked in 2022…Oil & Gas!



Do I regret not investing in oil? Not at all

I've been quite vocal since 2013 that I don't like oil & gas stocks. It has nothing to do with where I live (Quebec), environmental values, and I'm not saying oil stocks are bad investments. When it comes to investing, I would rather focus on the numbers. Numbers tell me energy stocks make bad dividend growers. How many Energy stocks show at least 10 years of dividend growth?

- Enbridge (ENB.TO)
- TC Energy (TRP.TO)
- Canadian Natural Resources (CNQ.TO)
- Imperial Oil (IMO.TO)
- Enterprise Products Partners LP (EPD)
- Magellan Midstream Partners LP (MMP)
- Special mention to Chevron (CVX) and Exxon Mobil (XOM) who didn't increase their dividends in 2020 but kept the "annual total dividend paid" increase streak alive.

Did I miss anyone? That's 6 companies (8 if you want to include CVX and XOM) out of 116 companies in our DSR stock screener. To be fair, there are a few duplicates since some stocks are trading on both markets. Therefore, we can say that 6-8% of all energy stocks qualify as long-term dividend growers.

While I clearly missed this opportunity, I also avoided losing a boat load of money in between 2013 and 2020. But most importantly, I stayed loyal to my investment strategy: dividend growth investing. Investing with conviction means that you will miss opportunities. It will also mean that you will make mistakes. However, that conviction will make sure you don't panic sell, that you make rational decisions, and that you follow a clear plan.

The year is different, the plan is the same

Studies show that most individual investors like you and me lag the market… big time. To illustrate that, we can think of famous investor Peter Lynch who managed the Fidelity Magellan Fund from 1977 to 1990 generating an annualized return of 29%. Fidelity later disclosed that the average Magellan Fund investor lost money during this period. How is that possible? **Investors were simply not investing with conviction, and they would stop following their plan at each market drop**.

We have been spoiled over the past 12 years. In general, an economic cycle will last about 5 to 8 years. That includes a bear market and a bull market and everything in between. The last real bear market we had started in 2008 and stopped in 2009. That was 14 years ago.

I would like to take a pause and reflect on the year that has just passed. For me, 2022 was a year that brought me down to earth. It was a great reminder to stay humble. First, it confirmed that I was dead wrong on the oil & gas rebound. Second, it confirmed that I took a bit too much risk in my stock selections. In a few cases, I focused too much on the narrative and thesis of future growth and I ignored the basics: the dividend triangle.

Fortunately, my investment structure prevented me from making major mistakes as my bad investments were limited by their size in my portfolio. Again, it highlights the importance of following your plan and sticking to your investment strategy.

No matter what happened in 2022 and no matter what will happen in 2023, my investment strategy will remain the same. 2022 just reminded me to focus on dividend growers and ensure they have everything in place to continue growing those payments.

2022 Stock Pick Results

2022 was a very frustrating year for the markets. Here are the results as of November 18th compared to their respective sector ETFs. We used iShares sector ETFs for our U.S. benchmark and BMO sector ETFs for our Canadian benchmark (when available).

Stock	Return	ETF	Δ	Stock	Return	ETF	Δ
DIS	-40.8%	-35.6%	-5.2%	T.TO	0.6%	-22.8%	23.4%
GRMN	-31.3%	-30.7%	-0.6%	MG.TO	-15.7%	-23.9%	8.2%
MKC	-12.8%	-2.4%	-10.4%	JWEL.TO	-16.6%	-1.6%	-15.0%
MMP	19.6%	71.6%	-52.0%	CNQ.TO	54.6%	48.3%	6.4%
JPM	-13.1%	-8.9%	-4.2%	GSY.TO	-32.9%	-5.4%	-27.5%
PFE	-15.4%	-4.6%	-10.8%	TFII.TO	-1.7%	-7.7%	6.1%
ABT	-25.5%	-4.6%	-20.9%	OTEX.TO	-33.7%	-38.6%	4.9%
LMT	37.2%	-5.6%	42.7%	ITP.TO	54.7%	-10.9%	65.6%
AVGO	-20.9%	-23.6%	2.7%	GRT.UN	-24.2%	-17.7%	-6.5%
APD	-1.1%	-10.9%	9.8%	AQN.TO	-42.1%	-7.8%	-34.3%
IIPR	-54.3%	-25.8%	-28.5%				
XEL	2.6%	-3.8%	6.4%				
Avg	-13.0%	-7.1%	-5.9%	Avg	-5.7%	-8.8%	3.1%
SPY	-16.0%		3.1%	XIU.TO	-3.7%		-2.0%
VIG	-9.9%		-3.1%	XDV.TO	-7.1%		1.4%

Here are my conclusions:

- 10 out of 22 companies did better than their sector.
- 4 companies produced major negative returns (DIS, IIPR, GSY.TO, AQN.TO)
- On average, U.S. stocks underperformed their sector and the dividend grower benchmark but beat the S&P 500.
- On average, Canadian stocks underperformed the TSX, but beat their sector and the dividend grower benchmark.
- The year was marked by heavy misses (DIS, IIPR, GSY.TO, AQN.TO) and homeruns (LMT, CNQ.TO, ITP.TO, T.TO (considering the differences vs the sector).

As I mentioned, 2022 was a year of humbleness. Last year, I also added a section to my favorite picks. That was called the "speculative plays". It was a suggestion made by many members. They wanted more spice in their portfolio. Well, they have been served… both ways!

Stock	Return	ETF	Δ
ATVI	11.8%	-35.6%	47.4%
XTC.TO	-25.0%	-23.9%	-1.1%
ADW.A.TO	-39.4%	-1.6%	-37.8%
TPZ.TO	41.3%	48.3%	-6.9%
OZK	2.8%	-8.9%	11.7%
MDT	-20.6%	-4.6%	-16.1%
NFI.TO	-48.8%	-7.7%	-41.1%
SYZ.TO	-64.8%	-38.6%	-26.1%
BTO.TO	-6.5%	-2.6%	-4.0%
VICI	10.9%	-25.8%	36.7%
PNW	8.8%	-3.8%	12.6%
Average	-11.77%	-9.50%	-2.77%

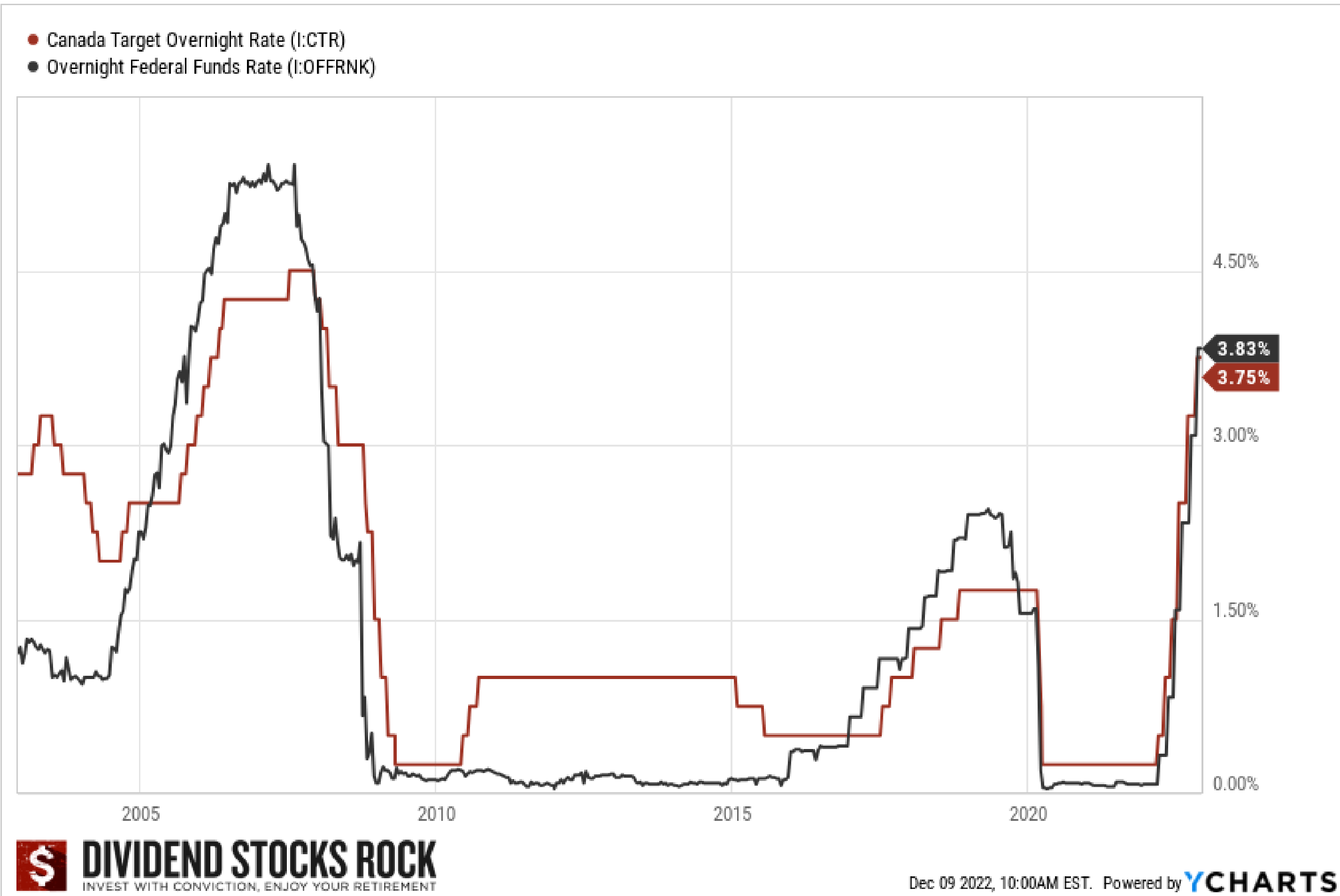
I made 11 speculative plays and got four "right", two were "draws" (-1.1% and -4% vs the sector) and five were "bad" picks. Besides bringing a high volume of volatility, I don't think these picks brought much in the way of value. Therefore, you should not be surprised that I will not repeat that experience in 2023.

Now, let's see what each sector has in store for us next year. Each sector will be reviewed, and I'll provide my favorite company within each sector.

The top 23 is expected to beat the market in 2023. As you well know, I can't promise anything 😉. The selections in this letter have been made assuming a tough economic environment with high inflation, higher interest rates, and the possibility of a recession rearing its ugly head. **Today, I'm sharing 6 of them freely with you.**

FINANCIAL SERVICES

Last year, I wrote about how 2022 the year of higher interest rates would be. I'm sorry, I didn't want to be THAT right about interest rate hikes! Both BoC and the FED have jumped in an MMA ring and they are ready to fight until inflation is KO'ed. They went from "inflation is transitory" to "we hope recession will be transitory too".



As interest rates kept going up, the market got scared, banks increased their provisions for credit losses, but both country's GDP's and unemployment rates are still in good standing. Will Central Banks reach their unachievable goal of a smooth landing? Labor shortages and the ability of many companies to adapt quickly to this new environment should support the economy. However, it's clear that rate increases have a lagging effect on all economic metrics, and we haven't seen the worst of the story yet. I expect more pain to come in 2023 as we will feel the full consequences of those many rate hikes. Not to mentioned that it seems we will get a few more in the first half of the new year. Brace yourself for impact – new debt will be very expensive for everyone.

U.S Pick: BlackRock (BLK) (Core Holding)

The purpose of this excerpt is to provide you with stock ideas that should beat their respective sectors in 2023. This forces me to start the tracking on January 1st. For BLK, I would probably wait a little as I expect more volatility in the beginning of the year. If I could pick a date in March or April, I'd be even more confident. If the market anticipates more interest rate hikes (which is expected to continue in the first half of 2023), it will be a tough market. Bear markets are bad for asset managers since they make money on fees charged on the assets they manage. Lower valuations then equal lower fees. We have seen BLK's dividend triangle (revenue and EPS) slowing down in the second half of 2022. Chances are this will continue in early 2023. This should put more pressure on BLK's stock price and open the door for a great buying opportunity. If BLK hits a 3% yield again, it would be a great buy signal.

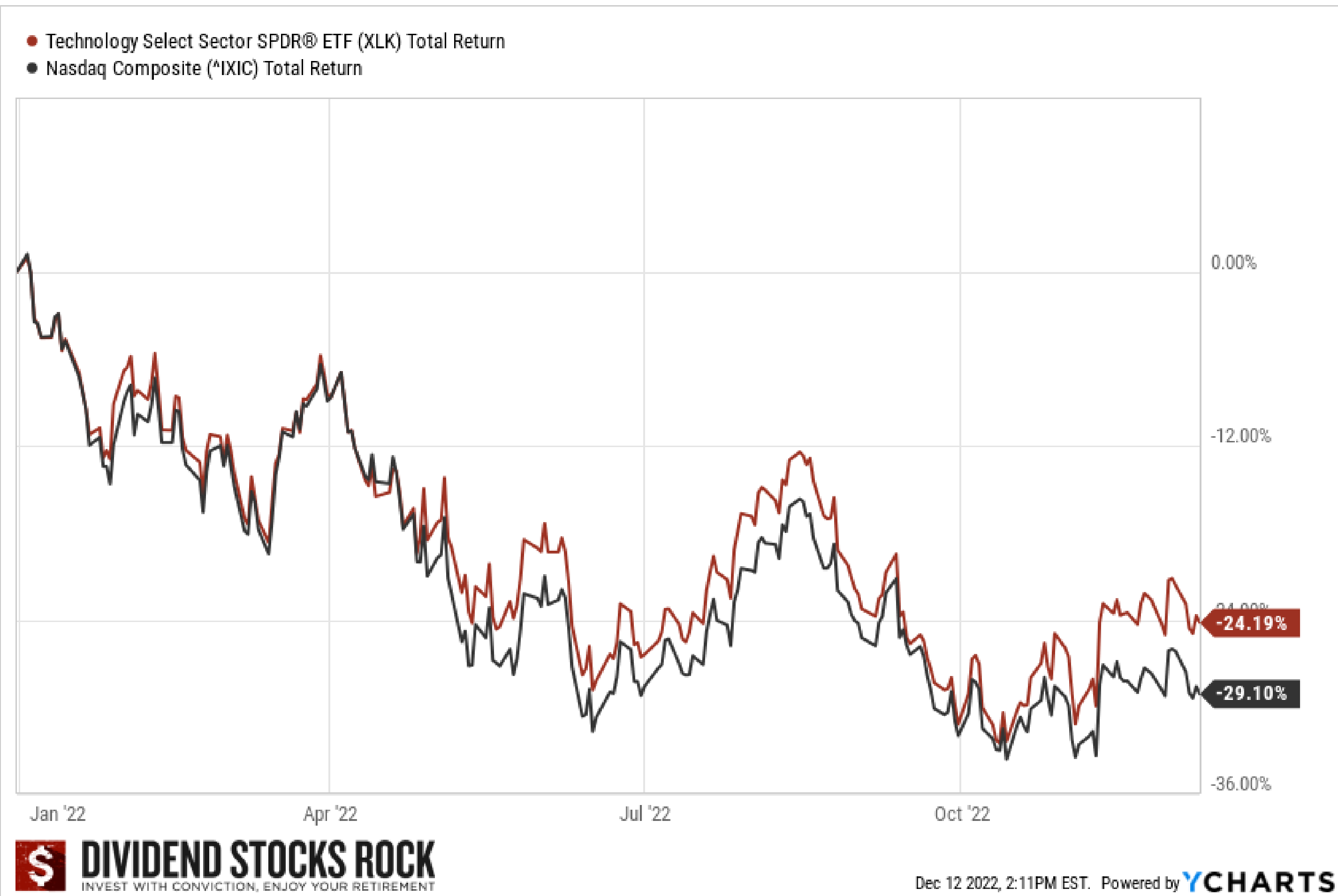
As opposed to many asset managers in the U.S., BlackRock will surf on the passive investment trend with its iShares ETFs. The company offers pretty much every type of investment solution for every type of investor. BLK's wide variety of products will provide a solid base of income and support dividend growth.

Canadian Pick: National Bank (NA.TO) (Core Holding)

After seeing NA out of the top 10 most popular stocks at DSR, I had to bring it back to the best stock for 2023! National Bank is the second most generous bank in terms of dividend increases over the past 10 years (right behind TD), and the most generous in the past 5- and 3-year periods. It also shows one of the lowest payout ratios of the group. What does this tell me? More generous dividend increases to come. The name of the game in 2023 for all Canadian banks will be PCLs (Provision for Credit Losses). Last quarter, it hurt most banks to various degrees. NA was hurt by stronger PCLs but kept showing double-digit growth (before PCLs).

INFORMATION TECHNOLOGY

Tech stocks have entered its winter season after being the darling sector for more than a decade. Several factors explain this technology crash. First, higher interest rates have forced the market to review their investment model. Higher rates come with higher expected rates of return (as the free-risk return increases with interest rates). Since the market was ready to pay large multiples on tech companies' earnings, the contraction in valuation was also larger. The sub-sector that took the largest hit was semiconductors (chip makers). Intel (-45%), Nvidia (-42%), AMD (-52%), and Taiwan Semiconductors (-34%) contributed greatly to the bearish views. Supply Chain disruptions, delays in conception and innovation along with a down investment cycle from many customers forced many companies to cut their guidance for 2022 and 2023.



Semiconductors have become our new "industrial stocks". 50 years ago, the best jobs were found in industrial businesses operating large manufacturing facilities. Today, semiconductors also offer great jobs, are capital intensive, and must follow economic cycles. Since we are talking about cyclicality, it does mean that it is the right time to invest when a key industry is down!

U.S Pick: Broadcom (AVGO) (Educated Guess)

Broadcom was my pick for 2022 and it is similarly my pick for 2023. I could have picked Apple (AAPL) or Microsoft (MSFT), but AVGO is currently trading at a PE of 23.7 (vs 23.3 for ALPL and 27 for MSFT), but also at a forward PE of 13.4 (vs 23 for AAPL and 26 for MSFT). It's generous yield for this sector (3.35%) helps AVGO stand out from the crowd. Please also note that AVGO has grown its dividend by double-digit increases for the past year, 3 years, 5 years, and 10 years.

Broadcom counts on multiple revenue streams. While demand for wireless chips may be hurt by weaker smartphone sales in 2023, AVGO can count on healthy networking demand led by cloud and enterprise data center spending. The company also counts on networking, storage, and broadband business units which have proven resilient.

Expect AVGO to benefit from higher spending from cloud customers and telecom providers that are looking to upgrade their infrastructure and networks. We're very confident in management's execution and expect AVGO to benefit from higher spending from cloud customers looking to upgrade their infrastructure and networks.

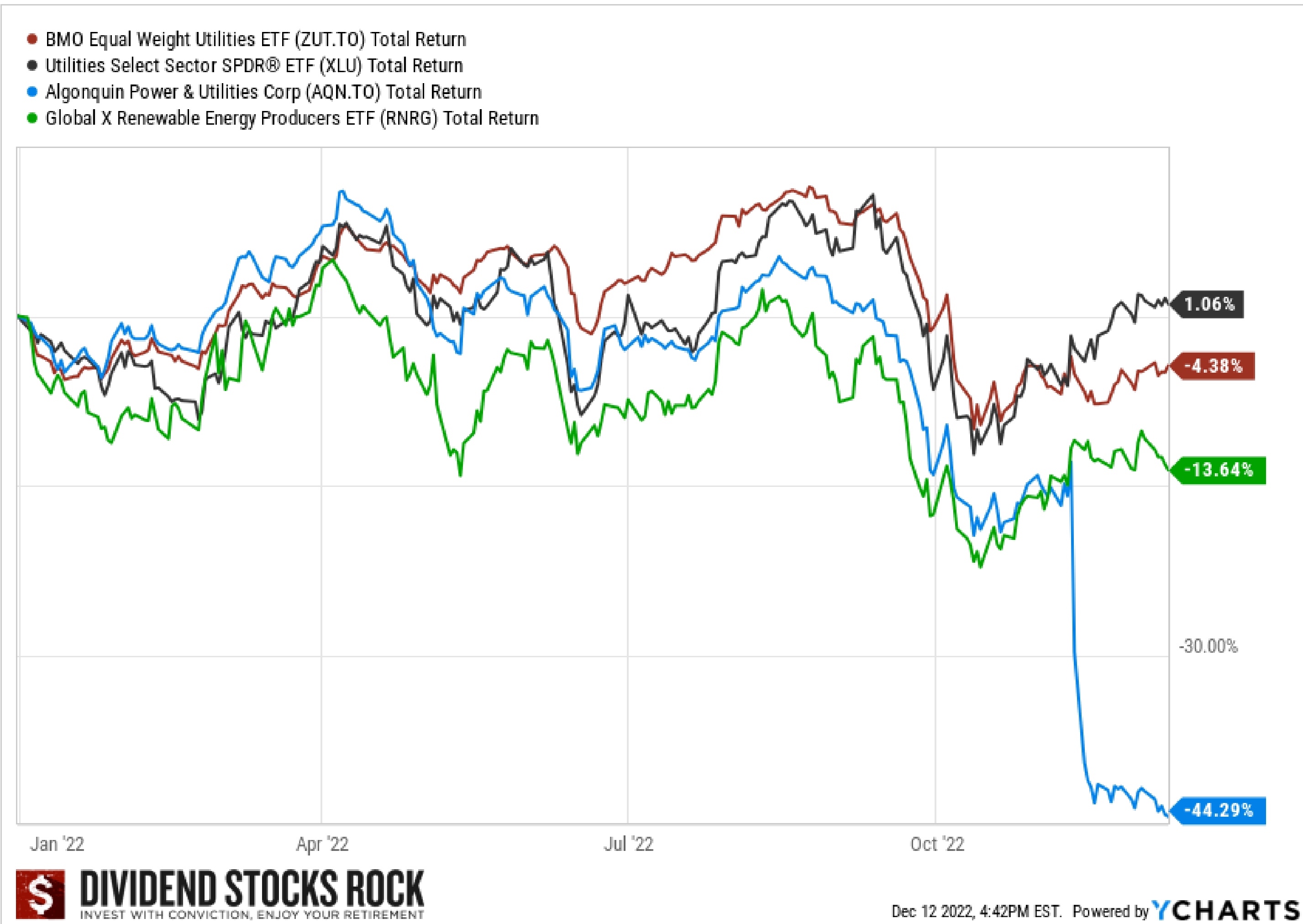
Canadian Pick: Constellation Software (CSU.TO) (Core Holdings)

We don't talk enough about Constellation Software. CSU's CEO Mark Leonard is one of the most brilliant minds in Canada and has built a fantastic money-making machine. Unfortunately, as Mr. Leonard enjoys flying under the radar, so to does CSU. The stock will be ignored by dividend investors since CSU pays a 0.25% yield with no dividend increases. Between you and me, I purposely ignored this one for several years due to this fact. However, some DSR members kept bringing CSU back on to my radar. Since the tech stocks paying dividends is very small number of companies in Canada, I finally decided to look under the hood.

Constellation Software operates a unique business model. It's not uncommon to find a tech stock focused on growth by acquisition (Broadcom (AVGO) in the U.S. is a great example). What makes CSU unique is its target: most acquisitions are small software companies generating between $5M and $10M in revenue. By making small acquisitions, it flies under the radar of most venture capitalist firms. CSU adds new companies that are dominating niche markets across the world. It has a unique expertise and reputation to close deals and improve profitability while keeping management in place. Today, CSU has hundreds of companies under its 6 business segments. It keeps increasing its revenue, EPS, and cash from operations year after year.

UTILITIES

The utility sector followed the similar trend that started in 2022. Regulated utilities are relatively stable while renewable energy utilities took another hit this year. The “energy money” didn’t come back in 2022 as oil and natural gas remained strong. Rising interest rates convinced investors that future projects may be less profitable than expected on top of eventually increased interest on current debt. We had a great reminder that growth through more debt and share issuance has its limit with Algonquin Power (AQN.TO).



At this point, AQN is either a fantastic bet, or a dead money trap. There are several factors that will influence this stock in 2023. Early in 2023, management will discuss their capital allocation (investment in new projects, debt repayment and dividend policy) during their investors presentation (Investors Day). AQN could decide to sell more green assets to concentrate on regulated utilities and pay off debts at the same time. There is also the possibility that interest rates won’t stay high for a long time. Keep in mind that Governments also see their interest payments going up accordingly.

U.S Pick: NextEra Energy (NEE) (Core Holding)

NextEra Energy offers investors the best of both worlds: a high-quality regulated utility in Florida and fast-growing renewable energy business. This is a good example of a company using a cash cow (regulated utilities) to fund fast growing assets (renewable energy). NEE is also investing massively in its regulated utility business. The utility plans to invest up to $34B through 2025, supporting a 9% rate base growth rate.

On the other hand, NEE is also known to be the world's largest renewable energy operator. It has developed a strong expertise in wind and solar energy and benefits from economies of scale. Like it or not, Governments will continue to invest massively in renewable energy going forward. For example, the Inflation Reduction Act provides significant economic benefits to renewable energy operators. I would rather stick with the leader in the industry.

If you want more yield and less total return, you can also select NEE's Yieldco: NextEra Energy Partners LP (NEP). Keep in mind it's a limited partnership which inevitably means more complicated taxes.

Canadian Pick: Brookfield Infrastructure (BIPC.TO) (Core Holding)

For this final selection, I'm going for diversification! Brookfield Infrastructure is everything in the utility world under one company. Investing in BIPC is investing in pipelines, electric transmission lines, natural gas storage, railroads, data centers, ports and more! It's like an infomercial of utility businesses! The company is also well diversified geographically as it generates maximum revenues from Brazil and has a presence in Australia, Colombia, United Kingdom, Canada, the United States of America, Chile, Peru, India, and other countries.

BIPC comes with a decent yield and a target dividend growth rate of 5 to 9% annually. That's enough to support your retirement and fight inflation.

Please note that the ticker BIPC is a corporate class share which should make your life easier when it's time to do your taxes. The trust units (BIP.UN.TO) currently offers a higher yield, but you are better off holding it in a tax-sheltered account to avoid tax calculations charged by your accountant!

FINAL THOUGHTS

Many factors will have an influence on the market in 2023. However, the best way to invest remains the same: having a straightforward strategy.

Invest with More Confidence and Less Stress

If you are like most investors, you constantly struggle with the right time to invest in the right assets. When you have losing investments, you get stuck by paralysis by analysis. This confusion hurt your portfolio and prevent you from enjoying your retirement.

Just look at how Rick solved his investing struggles and reached investing peace:

> *"One thing that I, struggle with is knowing when to let go of a losing investment when it makes sense to do so. DSR provides quarterly updates of each subscriber's portfolio (PRO feature) that provide value and dividend safety ratings for each individual holding. This is a really helpful guide as to whether it is time to consider selling a loser. Another very useful feature is that his report also provides potential replacements with better ratings. This gives me an independent viewpoint of whether my holdings are the best ones to keep going forward.*
>
> *One great part of the DSR service is Mike's inter-activeness with his subscribers. He does this regularly through both newsletters and webinars. His webinars are highly interactive, with subscribers able to make comments and input questions as it goes. Each and every time I have sent a separate email to Mike's service he has personally responded with helpful input. I recommend this service to anyone who is focused on dividend stocks and values a separate analysis of their holdings to help verify their portfolio's value and safety."*

Rick Urquhart, DSR PRO members since September 25th, 2017.

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