



Berkshire

DIVIDEND STRATEGY

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"Casual Friday" Commentary

Casual Friday: Back To Business + Growth/Value Inflection? – September, 15th 2017

As summer officially ends, the pace around offices will likely accelerate for most.

Portfolio Change:

Sale of Kohl's (KSS):

Kohl's has rallied sharply after announcing it will partner with Amazon to sell products through select stores and "take private" rumors within the space. Shares are up over 25% from the lows. This sharp rally, coupled with on-going uncertainty within the retail space and too much capacity within mid-tier retailers prompted our exit from the position.

Add to Existing Position - Nucor (NUE):

Nucor is a very well-run company in a very tough business. Historically, they have been extremely disciplined and opportunistic: when steel prices were low and others were closing plants, they increased plant and equipment spending, waiting for prices to turn higher. As prices got high and competition heated up, they started to back off. We have found it takes extremely disciplined management to survive and profit from the boom/bust cycles inherent in the materials sector. Nucor offers a 2.80% dividend yield and is likely to benefit from a global rebound in industrial activity.

Recent Client Question

"Why should I own these lousy value stocks when growth is doing so well?"

Based on some in-bound advisor calls, we suspect client pushback on value stocks may be on the rise. YTD Returns - Russell 1000 Growth Index up 19.88% & Russell 1000 Value Index up 6.31%.

Last week we observed noticeable outperformance of value. The market's advance after IRMA has value up about 1.98% and growth is up only .86%. Forces behind this near term seem to be oil's recovery and a higher treasury yield based in part on geo-political concerns easing. These two forces are good for banks and energy stocks. (Both of which make up a healthy portion of the value index) It's a long way to close the value/growth gap, but we may be seeing the start...

Bigger picture? *Growth is now the most expensive relative to value (on a price to book value basis) going back over 15 years.* While not at March 2000 extremes, valuation charts are starting to look eerily familiar. Charts depicting pretty extreme relative valuation:

[Growth / Value Charts 9.15.17](#)

For the statistically inclined the first chart shows how growth out-trades value on the 'left tail' by over 3 standard deviations, meaning this has only happened less than 1% of the time in 15 years – and that time is now. The recent spike is also dramatic. Growth out-trades value by nearly double the premium we typically observe. (2.5x average vs 4.7x current based on price to book value).

The second chart includes the late 1990's. It is not too much of a stretch to start thinking the valuation gap could be a major inflection point reminiscent of 1999.

More Important Index? – Meeting Client Goals

Advisors allocated to value, core and dividend holdings may now be summoned to impart discipline and remind clients of the attractiveness of these assets long term.

Imagine conversations with two distinct types of clients:

Berkshire is a fee-based, SEC registered advisory firm serving the portfolio management needs of high net worth and institutional clients. Over the past 29 years, we have successfully implemented highly focused equity, fixed income and balanced portfolios. Our guiding principle is a belief that success is achieved by combining rigorous, well-crafted investment processes with an exceptional level of client service and attention to detail. Asset Management with a Difference... Diligence, Integrity, and Focus.

Dividend Highlights

- Dividend growth can often provide transparent insight into a company's fundamentals and vitality.
- Dividend growth can provide an attractive stream of increasing cash flow to satisfy many financial objectives.

Client Profile 1: Pre-Retiree
Current Age: 60
Retirement age: 65
Primary Objective: growing income stream to meet annual retirement expenses
Key Point(s): power of annual dividend growth creates attractive rising income stream, inflation protection
[Power of Enduring Dividend Growth](#)

Client Profile 2: "Young Accumulator"
Current Age: 45
Retirement: 65
Primary Objective: accumulation of wealth
Key Point(s): power of accumulated dividends which potentially match initial investment in year 15; underlying appreciation long term
[Power of Accumulating Dividends](#)

Advisors are using the above charts to simply and directly depict the value of dividend growth. Both are designed to keep clients focused on their long term investment objectives vs. trying to time near term market trends or benchmarks.

Of course its likely clients have multi-asset class portfolios, but these charts are designed to keep clients tuned into the desirability of core holdings even during times of flattish performance.

Have a good weekend.
-Gerry

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