February 3, 2016

Hello everyone,

This is the monthly advisor update of the **AlphaDelta Growth of Dividend Income Class** ("ADGoDIC" or the "Fund") from SciVest Capital Management Inc. (the sub-advisor to the Fund).

Before delving into our regularly formatted monthly commentary, we want to look at two investment themes that we believe may be approaching extremes: (i) the collapse in the Canadian dollar; and (ii) the wide and positive yield spread between stocks and bonds.

First, the Canadian dollar hit a 13-year closing low against the US dollar of 0.6859 on January 19, 2016. We want to determine how unusual this level of the Canadian dollar is relative to the 45-year history of fully floating exchange rates – Appendix I shows the weekly closing USD/CAD exchange rate for this 45-year time period. The graph shows that the average exchange rate during this time period was 0.8387. The graph also shows that the Canadian dollar has rarely traded below 0.70 – in fact, during the 45-year time period, the Canadian dollar has only traded below 0.70 for approximately 5 years from early 1998 to early 2003. The Canadian dollar bounced off the 0.70 level once during the mid-1980's and once during the mid-1990's – never trading below 0.70 until 1998. In addition, the all-time closing low of 0.62 was not much lower than 0.70, and is not much lower than what it achieved in mid-January 2016. To put a shorter-term context on the current exchange rate, we have also plotted the 20-year and 10-year daily graphs in Appendix I. The average exchange rate over the past 20 years was 0.8178, while the average over the past 10 years was 0.8481. It appears that the low-to-mid 80 cent range is a reasonable assumption for a long-term average.

Many have recognized a correlation between the USD/CAD exchange rate and the price of oil. In the final graph of Appendix I, we plot the Bloomberg West Texas Intermediate Cushing spot price of crude oil (in USD) overlaid against the USD/CAD exchange rate for the past 30 years. There indeed does appear to be a reasonably high positive correlation between the price of oil and the Canadian dollar, at least over the past 17 years (not as much prior). Oil too (like the Canadian dollar) is trading at roughly 13 years lows. However, note that the oil price time series is not adjusted for inflation – thus, oil would likely be trading near 30-year lows in real inflation-adjusted terms.

No matter how you look at the history of the Canadian dollar, it has rarely traded at the current low levels. While we are not calling for a near-term bottom in the dollar (or oil), if history is any guide then the Canadian dollar is likely at the lower side of its long-term forward-looking trading range. Moreover, while many ***un***hedged US equity portfolios have benefited greatly in Canadian dollar terms over the past several years from the collapse in the Canadian dollar, these unhedged portfolios may unwind many of these gains if and when the Canadian dollar reverts towards more "normal" levels. Consequently, **we remind all readers that the ADGoDIC is by policy fully hedged to moves in the Canadian dollar relative to the US dollar. Thus, the Fund's substantial US holdings are expected to be fully insulated from adverse**

**exchange rate conversion returns if and when the Canadian dollar does indeed revert towards its long-term averages.**

The second investment theme we examine is the wide and positive yield spread between stocks and bonds. In the past 6 months, we have seen the gross dividend yield on our Fund holdings increase from approximately 3.5% to 4.0% while at the same time US Government Bond Yields have fallen from approximately 2.4% to 1.8%. Here too we want to determine how unusual this is relative to a longer-term history. The first graph of Appendix II shows the gross 12-month trailing dividend yield of the Dow Jones Industrial Average Index ("DJIA") (in white) plotted against the US Government 10-Year Bond yield (in orange) for the past 20 years. Not unexpectedly, the yield on the US 10-Year Bond prior to the Great Recession was always much *higher* than the dividend yield of the DJIA. During the 1990's, it appears that the spread between stock and bond yields averaged approximately -4.5% per annum (i.e., bond yields were 4.5% per annum higher than the DJIA dividend yield), while during the 2000's until the Great Recession it appears to have averaged approximately -2.5% per annum. Dividend yields for baskets of common stocks of the quality within the DJIA are generally (and should be in the long-term) lower than Government Bond yields because (a) stock dividends per share tend to go up through time with dividend growth and (b) stock prices themselves tend to go up through time providing capital gains – Government Bonds possess neither of these growth features (i.e., bond coupons and redemption prices are fixed). However, during and since the Great Recession the yield spread between the DJIA and the US 10-Year Bond has surprisingly been both negative and positive, averaging close to 0% per annum.

The second graph in Appendix II shows the gross estimated dividend yield of the DJIA (in white) plotted against the US Government 10-Year Bond yield (in orange) for the past 3 years. The yield spread has been positive and negative over the past 3 years with an average spread of close to zero (at +7 basis points per annum). Interestingly, the yield spread hit its 3-year high in the past couple of weeks at +1.04% per annum. The current DJIA dividend yield of 2.92% per annum compares to the current US Government Bond yield of 1.88%. We chose the DJIA for comparison because every one of the 30 stocks within the DJIA is large-cap, high quality, and pays a dividend. Comparatively, the ADGoDIC has over 60 stocks (i.e., more diversification than the DJIA), has an average gross indicated dividend yield of 4.0% per annum (i.e., 37% higher yield than the DJIA), and much higher dividend growth than the DJIA. **The current spread between the ADGoDIC's indicated gross dividend yield and the US Government 10-Year Bond yield is an outsized +2.2% per annum – against the Canadian Government 1-Year Bond yield, the Fund's yield spread is +2.9% per annum.**

Spreads that are this positive, let alone positive at all, between stock dividend yields and bond yields may not persist for lengthy periods into the future. In the long-term, for these spreads to revert towards more "normal" levels, one or more of the following would need to happen: (i) bond yields increase through bond prices falling; (ii) dividend yields fall through stock prices rising; and/or (iii) dividend yields fall through dividends per share falling. **Therefore, given current stock-to-bond yield spreads, under most scenarios being moderately more long growth of dividend stocks relative to bonds may make medium term tactical sense.**

**Attached is the ADGoDIC Portfolio Disclosure Page**. The front-side of the Portfolio Disclosure Page shows all of the current stock holdings of the ADGoDIC, as well as some descriptive, dividend and valuation characteristics for each portfolio holding – plus overall portfolio averages. The back-side of the Page shows a number of relevant pie charts depicting overall ADGoDIC portfolio exposures and characteristics such as sector, market capitalization, dividend yield and dividend growth "bucket" exposures.

As shown on the front of the Portfolio Disclosure Page, **across the Fund's current holdings the weighted average gross dividend yield is 4.0% per annum with impressive double-digit trailing 1, 3 and 5 year dividend growth rates (12.6%, 15.5% and 16.9%, respectively)**. The 4.0% average dividend yield compares to a portfolio weighted average forward earnings per share yield of 8.2% (205% dividend coverage) and forward cashflow yield of 11.7% (293% dividend coverage). Regarding valuation, the portfolio weighted average twelve-month forward price-to-earnings ratio is 14.8x and the average twelve-month forward price-to-cash-flow ratio is 10.2x.

As always, the ADGoDIC portfolio is well diversified across sectors and industry groups with no sector allocation currently exceeding 14.0% (note that we break REITs out of the overall Financial Sector in the sector exposures pie chart, given their unique risk characteristics). In order of size, we have the following exposures to the Bloomberg defined Sectors (plus REITs): 14.0% Consumer Discretionary, 13.9% Financials, 12.1% Technology, 11.9% Industrials, 8.3% Health Care, 8.3% Materials, 7.7% Communications, 7.4% Consumer Staples, 7.2% Energy, 7.1% REITs, and 0% Utilities.

On an individual stock holding basis, we currently hold a diversified portfolio of 67 equity positions. During the month of January, we initiated new positions in Discover Financial Services (DFS), Johnson Controls Inc (JCI), Magna International Inc (MG), Polaris Industries Inc (PII) and Valero Energy Corp (VLO). Other than these new positions, we did not materially increase (by more than 0.5%) any existing positions. During January, we eliminated positions in BHP Billiton PLC (BBL), Corus Entertainment Inc (CJR.B), DineEquity Inc (DIN), KLA-Tencor Corp (KLAC) and Williams Cos Inc (WMB). In addition, during January, we decreased (by more than 0.5%) our positions in CI Financial Corp (CIX) and General Electric Co (GE).

Since our objective within the ADGoDIC is income/distribution growth, our monthly notes focus on growth of dividends amongst Fund holdings as opposed to short-term capital returns. In particular, each month we report those Fund holdings which declared dividend increases during the prior month, as well as those holdings we expect to declare dividend increases in the next month. Recall that one of our fundamental beliefs is that, if we can select stocks which consistently increase their dividends into the future, then price appreciation must eventually follow – that is, long-term price appreciation is a *consequence* of consistent earnings and dividend growth.

Amongst our current ADGoDIC holdings, **during the month of January 2016 we had six (6) declared dividend increases averaging an announced increase of 7.9% quarter-over-quarter** ("QoQ") **and 17.7% year-over-year** ("YoY"), relative to those already known at the end of the prior calendar month.

| No. | Name | Ticker Symbol | Current Ind Div Yld (% p.a.) | QoQ Div Increase (%) | YoY Div Increase (%) |
|---|---|---|---|---|---|
| 1 | Diageo PLC | DEO | 3.1 | 5.1 | 7.5 |
| 2 | General Motors Co. | GM | 5.1 | 5.6 | 26.7 |
| 3 | Las Vegas Sands Corp. | LVS | 6.4 | 10.8 | 10.8 |
| 4 | Omega Healthcare Invstrs | OHI | 7.2 | 1.8 | 7.5 |
| 5 | Polaris Industries Inc. | PII | 3.0 | 3.8 | 3.8 |
| 6 | Valero Energy Corp. | VLO | 3.5 | 20.0 | 50.0 |
| | **Average** | | **4.7** | **7.9** | **17.7** |

Diageo PLC, the large-cap alcoholic drink producer, increased its interim semi-annual dividend by almost exactly what we had expected at 5.1% (in local currency), or 7.5% year-over-year. Diageo has now increased its dividend every year for 27 consecutive years.

General Motors announced an unexpected early dividend increase of 5.6%, only three fiscal quarters after its last dividend increase. At the same time, GM announced a large incremental share buy-back. GM continues to generate enormous cash-flows, and is returning a lot of it to shareholders. Year-over-year, GM has increased its dividend by 26.7% – not bad, considering it currently has a 5.1% dividend yield.

Despite well-publicized issues in Macau China, Las Vegas Sands Corp delivered a 10.8% dividend increase in late January. This is a positive signal from the company, given the Macau risks and recent poor stock price performance. The 10.8% dividend increase takes Las Vegas Sands' dividend yield from 5.8% to an attractive 6.4%.

Omega Healthcare Investors, a US-based long-term healthcare REIT and serial dividend increaser, increased its quarterly dividend by our expected 1.8% – or 7.5% year-over-year. Omega also has a very attractive dividend yield of 7.2%, given its reasonably strong dividend growth rate.

We added Polaris Industries to the portfolio during January. Polaris produces off-road vehicles, as well as motorcycles. While Polaris has increased its dividend for 21 consecutive years, it did produce a moderately disappointing 3.8% dividend increase in January.

We also added Valero Energy Corp to the portfolio during January. Valero is a large-cap refiner of petroleum and thus is theoretically somewhat insulated from falling oil prices, as it relies on refining spreads for profitability. Valero provided an unexpected 20% dividend increase in January, after providing a 25% dividend increase last quarter. Year-over-year, Valero has produced a 50% dividend increase, and yet still generates significantly more cash-flow than it distributes to shareholders – potentially leading to further significant dividend increases in the future.

Last month we wrote that we expected 3M Co. (MMM) and Dunkin' Brands Group Inc (DNKN) to increase their dividend in January. Both are still expected to announce dividend increases (6%-9% and 8%-12%, respectively) – just now in February.

Finally, last month we had also expected two of Canada's media stocks to announce dividend increases in January – Corus Entertainment (CJR/B) and Shaw Communications (SJR.B). The companies announced a deal with each other in January whereby Shaw Communications is selling its media group to Corus Entertainment. This divestiture is related to Shaw's announcement in December that it plans to purchase Wind Mobile. Given this deal flow, and other business uncertainties, independently both companies decided to keep their dividends unchanged for the coming quarter despite being due to increase their respective dividends – in both cases (coincidentally) halting 13 consecutive years of dividend increases. As Corus Entertainment was already on our negative watch list, we eliminated it from the portfolio.

During February 2016, we are expecting at least fifteen (15) dividend increase announcements from our current holdings – that is to say, incredibly, we are expecting over 22% of our current holdings to increase their dividends this month:

| No. | Name | Ticker Symbol | Current Ind Div Yld (% p.a.) | Est. Announce Date | Est. Div Increase (%) |
|---|---|---|---|---|---|
| 1 | 3M Co. | MMM | 2.8 | Feb 9 | 6-9 |
| 2 | Analog Devices Inc. | ADI | 3.1 | Feb 16 | 7-13 |
| 3 | BCE Inc. | BCE | 4.6 | Feb 4 | 3-6 |
| 4 | Coca-Cola Co. | KO | 3.1 | Feb 18 | 7-9 |
| 5 | Dunkin' Brands Group Inc. | DNKN | 2.6 | Feb 4 | 8-12 |
| 6 | Eaton Corp. PLC | ETN | 4.5 | Feb 24 | 5-9 |
| 7 | Gap Inc. | GPS | 3.8 | Feb 29 | 2-6 |
| 8 | Magna International Inc. | MG | 2.4 | Feb 25 | 10-14 |
| 9 | National Health Investors | NHI | 5.6 | Feb 18 | 7-11 |
| 10 | Reliance Steel & Aluminum | RS | 2.9 | Feb 22 | 7-13 |
| 11 | T Rowe Price Group Inc. | TROW | 3.0 | Feb 22 | 6-10 |
| 12 | Time Warner Inc. | TWX | 2.0 | Feb 11 | 10-12 |
| 13 | Toronto-Dominion Bank | TD | 3.9 | Feb 25 | 6-8 |
| 14 | Union Pacific Corp. | UNP | 3.0 | Feb 4 | 7-11 |
| 15 | United Parcel Service | UPS | 3.1 | Feb 11 | 6-10 |

With so many expected dividend increases this month, we have created the above table with our stock-by-stock dividend increase estimates. We have also included the estimated dividend increase announcement dates.

Given all the uncertainty surrounding today's investment environment, there are a number of announcements that should prove interesting. For example, 3M Co will be interesting because of its size, global breadth, US dollar exposure and product mix. We would view any dividend increase above our 6% to 9% range as a significant positive. Moreover, any increase would represent 3M's 58th consecutive year of dividend increases and an increase of this magnitude would push 3M's dividend yield above 3% – putting 3M the same rarified air as Johnson & Johnson, Coca-Cola and Proctor & Gamble (all mega-cap 3% yielders with more than 50 consecutive years of dividend increases).

Eaton Corp., a large industrial that produces electrical and hydraulic components, will also be interesting given the widely reported "global industrial recession". Eaton's stock price performance has been extremely weak pushing its dividend yield up to 4.5%. A significant dividend increase would push Eaton's yield towards 5.0%.

Similarly, Union Pacific, the large west coast rail company, has had a very poor year as well, with their shipping volumes down dramatically. A significant dividend increase would go a long way towards conveying some confidence in the long-term future of the company and the North American economy in general.

Overall, given the large volume of expected dividend increases, and given the perceived slowdown in the global economy, this month's dividend announcements may shed some light on the long-term business

health of a number of diverse businesses and industries. Note that we believe that dividend announcements likely convey even more information about the *long-term* forward-looking expectations of management teams than do quarterly earnings announcements.

Always remember our primary message: **"Growing income", as opposed to "fixed income", is the only means of maintaining the purchasing power of your and your client's income stream over the years to come**.

If you would like more information regarding the **AlphaDelta Growth of Dividend Income Class** and its current portfolio (including the up-to-date presentation piece), please feel free to contact me directly or alternatively contact AlphaDelta Management Corp. ( www.AlphaDelta.com ).

Thank you for your continued interest in the Fund,

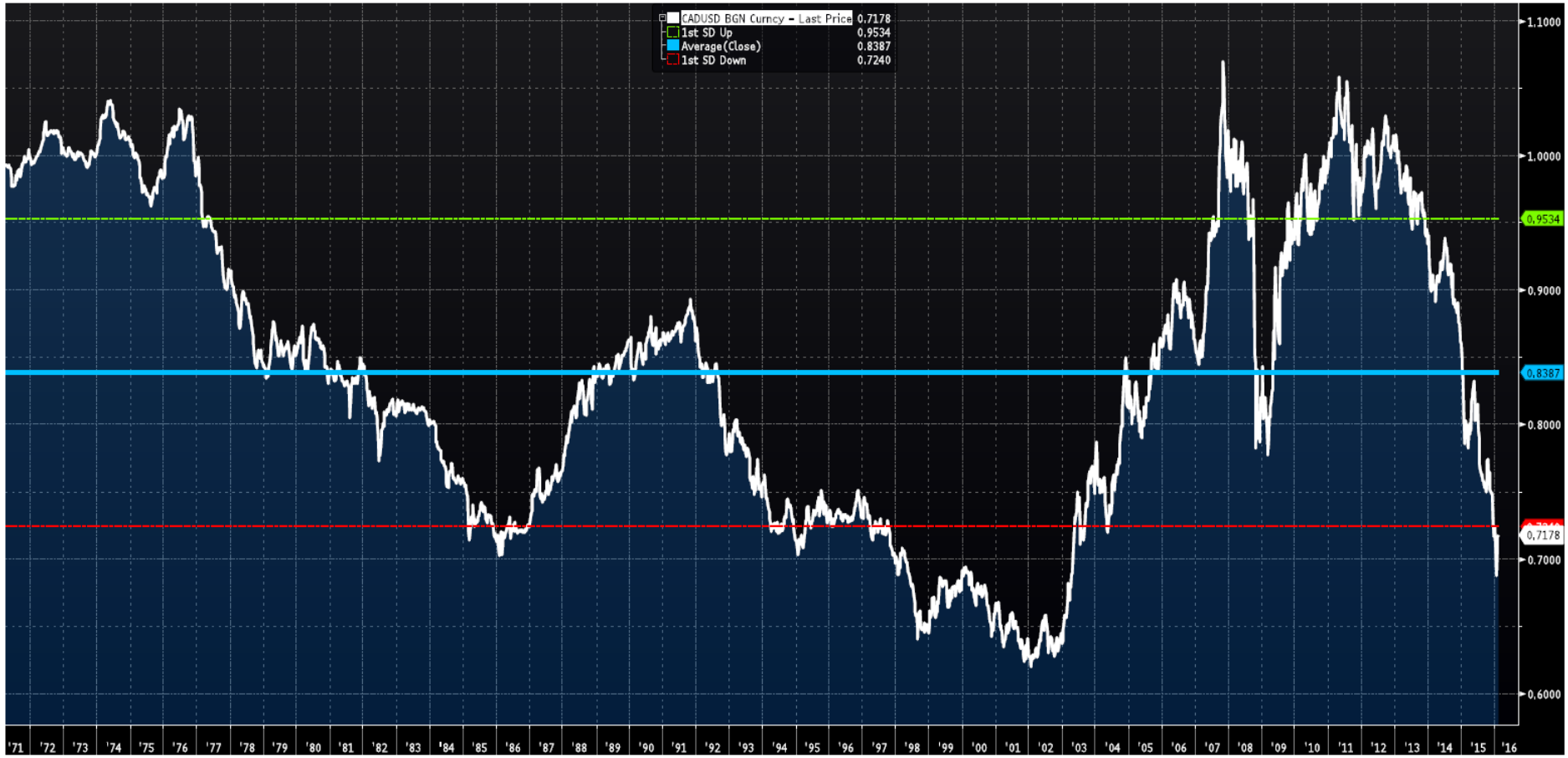
John J. Schmitz, Ph.D., CFA

# APPENDIX I: Canadian Dollar Exchange Rate Analysis

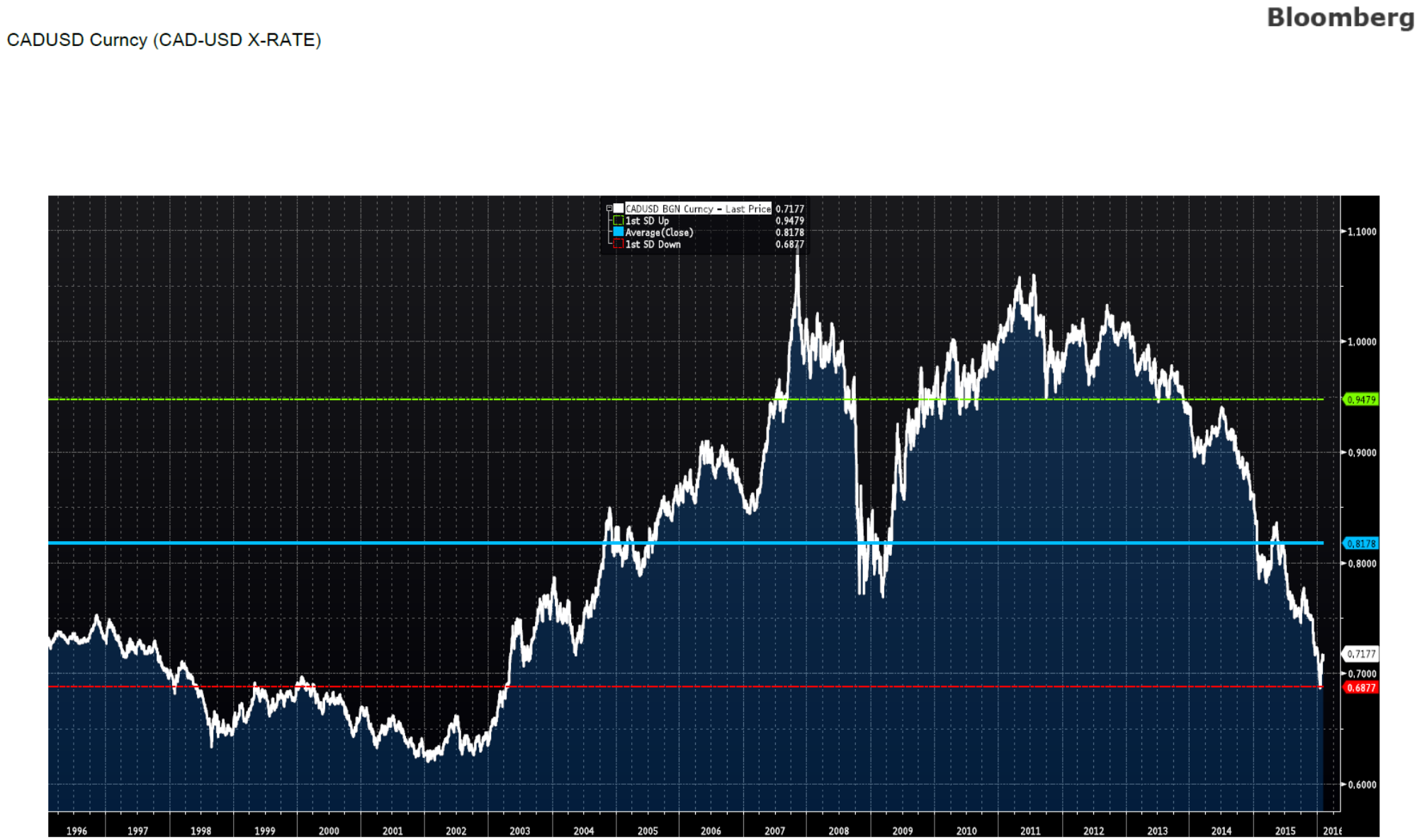
## Graph 1: CAD/USD Exchange Rate, Daily Data, 45 Years Through Current (source: Bloomberg)

Bloomberg

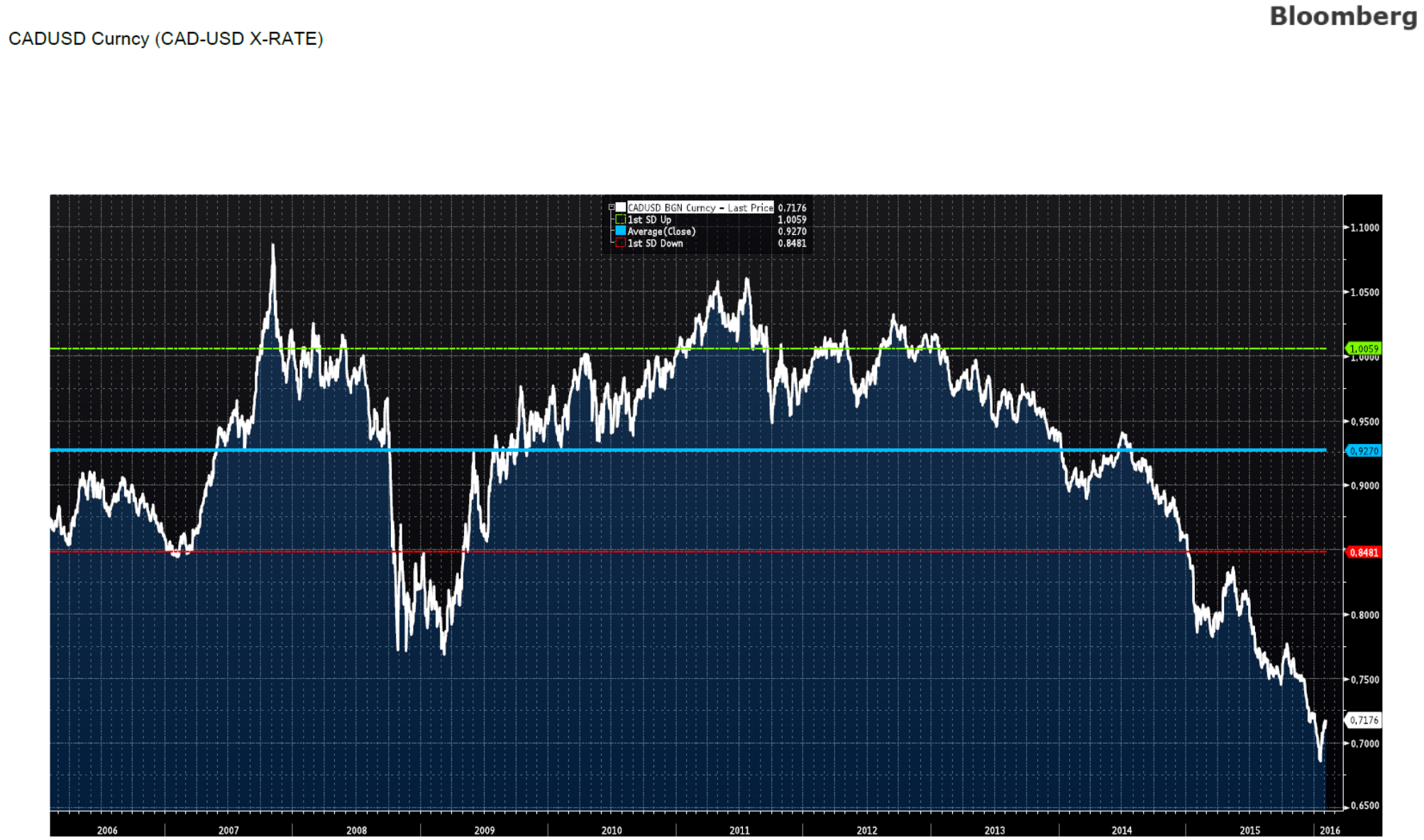
CADUSD Curncy (CAD-USD X-RATE)



## Graph 2: CAD/USD Exchange Rate, Daily Data, 20 Years Through Current (source: Bloomberg)



## Graph 3: CAD/USD Exchange Rate, Daily Data, 10 Years Through Current (source: Bloomberg)



## Graph 4: CAD/USD Exchange Rate Against Bloomberg West Texas Cushing Oil Price (in USD), Daily Data, 30 Years Through Current (source: Bloomberg)

# APPENDIX II: Common Stock Dividend Yield Versus US Government Bond Yield Spread Analysis

## Graph 1: Dow Jones industrial Average Index Gross 12-Month Trailing Dividend Yield versus the US Government 10-Year Bond Yield, Daily Data, 20 Years Through Current (source: Bloomberg)

Bloomberg

INDU Index (Dow Jones Industrial Average)
USGG10YR Index (US Generic Govt 10 Year Yield)
INDU Index - USGG10YR Index

## Graph 2: Dow Jones industrial Average Index Gross Estimated Dividend Yield versus the US Government 10-Year Bond Yield, Daily Data, 3 Years Through Current (source: Bloomberg)