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Dividend payers rule

Cash flow is king

Jonathan Ratner, Financial Post

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The huge rally sectors such as technology saw in 2009 reflects an economic improvement that has yet to materialize, says David MacNicol, president of MacNicol & Associates Asset Management. And he warns that it may not materialize anytime soon given the many problems that still need to be addressed.

The portfolio manager notes that much of the information coming out these days is either optimistic or very dire. For example, the possibility of another credit crunch looms as both the U.S. financial problems and those of smaller European countries threaten the U.S. dollar and the euro.

Meanwhile, the most recent unemployment numbers out of the United States were better than expected, dropping to 9.7% from 10%. However, MacNicol is concerned by the fact that underemployment is still likely around 20%.

Nonetheless, he expects North American markets will feed off of improving fourth-quarter economic data and earnings results out of the United States.

"A very strong snap back in growth occurred as stimulus packages kicked in last quarter," the manager says, noting that he expects U.S. GDP growth to climb to 3% from 2%. "The markets will be riding that wave with stocks that lead out of a recession."

MacNicol anticipates that equity markets will move sideways in the coming years, much as they did during the 1960s and 1970s. But he insists that there are still opportunities to make money owning great companies through strong economic times. For now, the manager is focused on commodities and dividend-yielding stocks.

With cash paying very little and the 25-year bull market for bonds running out of steam, MacNicol is turning to utility-type names so clients can "cash flow their way through this situation" until the economy comes back. "The only reason bonds have done well even at these low levels is because of the quantitative easing that the government has been involved in. It appears that they are trying to turn that off."

While it is no secret that the Fed has been pumping a lot of money into the big U.S. banks, he notes that it is very promising to see that regional banks are just starting to break out.

The manager is overweight precious metals and keeps a close eye on copper, which he notes has turned over recently. Another chart that is causing him some concern is the VIX, or volatility index. While it was getting back to a more normal range of 20 to 25, MacNicol points out that it recently spiked up to the high 20s. He is worried it may be on its way back up to the 40 to 50 range, which we saw in 2007 and 2008.

"That's foreshadowing some very tough times ahead," the manager says. "Hopefully it's just a momentary blip."

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Manager David MacNicol, MacNicol & Associates Asset Management

Portfolio Global balanced

Description Combination of equity, fixed income and alternative asset strategies

Assets under management Approaching $300-million (roughly 250 families)

Style & Process Opportunistic blend of value and growth

BUYS

BMG BULLION FUND

MacNicol continues to add to this position, which was first established in 2002 when he moved out of the U.S. dollar and into hard assets. The open-ended mutual fund holds investment-grade bars of gold, silver and platinum.

"We've seen other precious metals funds come into the market over the past few years, and although we've looked at them, they all seem to want to try to out-manage the underlying assets with currency hedges and other non-physical-metal gimmickry, such as gold certificates, or investments in closed-end funds," the manager says.

"This investment acts the most like its underlying assets of all of the precious metals funds, and the bullion is all there in the vault, unencumbered, and not dependent on anyone's performance."

While gold offers a form of insurance, he notes both silver and platinum have industrial uses and will therefore benefit from a stronger economy.

PAN AMERICAN SILVER CORP. (PAA/TSX)

The manager notes Pan American measures up very favour-ably, with an intrinsic value as high as $75 per share but a stock price below $25. He would add to this long-term position at these levels. "It tracks higher because of the large disparity between the price of gold and silver."

While silver c urrently trades around US$15 per ounce, MacNicol thinks it could jump to US$30. He thinks gold, which is currently hovering around US$1,050 per ounce, may rise to US$1,500. Meanwhile, the manager sees platinum prices climbing to US$1,800 from US$1,500. Pan American has eight operating mines and four development projects in Mexico, Peru, Argentina and Bolivia.

BCE INC. (BCE/TSX)

When BCE's share price collapsed after its privatization failed late in 2008, MacNicol notes it got back to its normalized book value. Before the 1999 technology bubble, it was trading at that level as well.

While the company doesn't have a stake in Nortel Networks as it did back then, the manager feels it does have a great wireless business that is competing well with Rogers Communications Inc.

BCE also offers the potential for appreciation, a safe dividend and a yield of roughly 5.8%.

"They've done everything they said they'd do," says MacNicol. "I think they are a good provider."

He notes that price targets for the stock are anywhere from $34 to $40. As a result, the manager is comfortable adding to this name here.

SELL

SUNTECH POWER HOLDINGS CO. LTD. ADR (STP/NYSE)

MacNicol owned this company for several years and still thinks there will be a wave of money to be made in clean energy, particularly in solar and nuclear. But he feels the space has become too crowded.

"A year ago, we thought [U. S. President Barack] Obama was going to be very supportive of clean energy and solar power industries. It turns out that he was, but now there is too much competition, everyone is doing it. Competition has made the stocks much less worthwhile."

The manager notes that Suntech is one of the largest silicon manufacturers in the world. The China-based company actually got its efficiencies to a level such that the production of their wafers was on par to a unit of oil.