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STRATEGIES FOR SUCCESSFUL INVESTING

PORTFOLIO WATCH

Time: An investor's best friend

POWER OF TIME

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MORE THAN ANY OTHER FACTOR, time is a key ingredient to long-term investment success. Time enables companies to grow, earnings to expand, equity values to compound and wealth to accumulate. While we all see aging as a foe to fight, time can be an investor's best friend.

Here's some proof to show the power of time. It may surprise many investors that the S&P/TSX Composite Index has delivered a compound annual growth rate of more than nine percent over the last 10 years (as of August 31, 2014). A $1,000 investment would have grown to roughly $2,431 over that 10-year span.

This impressive growth occurred despite the extremely challenging environment that dominated the investment climate over the past decade. The world faced significant economic shocks, heightened geopolitical events and many major natural disasters. Many individual companies faced both internal successes and challenges as they executed their strategies during this tumultuous period.

But time also allowed management teams to adapt and evolve, build on their successes, occasionally capitalize on the missteps of others and, ultimately, get back on track to strengthen their businesses. Over longer time horizons, stock volatility is muted and longer-term trends become more evident.

Compounding: The eighth wonder of the world

Here's another scenario to demonstrate time's strength. Imagine I present you with the opportunity today to give me $1 million. In exchange, I give you one penny and agree to double that every day for 30 days, and then give you the final sum. Most people would prefer to keep their $1 million. But in reality, the one-penny doubling scenario would be the investment of a lifetime.

Starting with a meager penny, and doubling it everyday for 30 days, grows that one cent to $5.3 million! The magic of compounding! No wonder Einstein reportedly described compounding as the eighth wonder of the world.

This reinforces that investors are most successful when they leverage the power of compounding. Taking a long-term perspective and ignoring short-term volatility is the key to growing wealth.

The importance of dividends and dividend growth

Over time, the long-term benefits of dividends are realized. Numerous historical studies show that dividend-paying and dividend-growing stocks outperform the broader market over the long term. A focus on underlying

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growth and fundamental improvements are built-in to dividend-growing companies. For the S&P/TSX Composite Index, approximately one-third of an investor's total equity returns over the last 10 years came from simply collecting dividends.

Dividend-growing firms are successful businesses ...

A business that wants to continue to generate excess cash flow for dividends must demonstrate many positive improvements. These would likely include market share expansion, sales growth, product innovation and cost containment.

The stocks of dividend-growing companies are simply the profiles of successful, well-managed businesses. In today's low-interest rate environment, many blue-chip businesses, with above-average dividend yields, continue to succeed because they remain focused on delighting their customers and controlling costs. This rewards both the underlying business and its shareholders.

... like TD Bank

Equity investors gain access to a company's ability to grow its earnings over time, which reinforces the power of long-term investing. The Toronto-Dominion Bank (TSX-TD), or "TD," is a terrific example that highlights how a good management team can align with a sound strategy to grow its earnings.

TD's business has grown meaningfully over the last decade. The bank now has 1,164 Canadian branches and 1,306 U.S. "stores" (its name for branches south of the border). By total assets, TD ranks as Canada's largest bank and the fifth-largest in North America. This growth didn't happen overnight, but is the culmination of an ongoing focus on its existing business while also executing several strategic acquisitions. Over the last 10 years, TD's acquisitions include Banknorth, Commerce Bank, Riverside, Chrysler Financial, Epoch, and the credit card portfolios from MBNA and Target. In addition, TD acquired approximately half of CIBC's Aeroplan portfolio.

Consistent momentum produces impressive gains ...

Step by step, TD has grown substantially through unrelenting forward movement. From 2003 to 2013, it more than doubled its revenue to $24.4 billion from $9.9 billion. Net income more than tripled to $6.9 billion from $1.9 billion, and total assets grew to $862 billion from $275 billion. The passage of time enabled seemingly small, consistent momentum to produce strong gains for the bank.

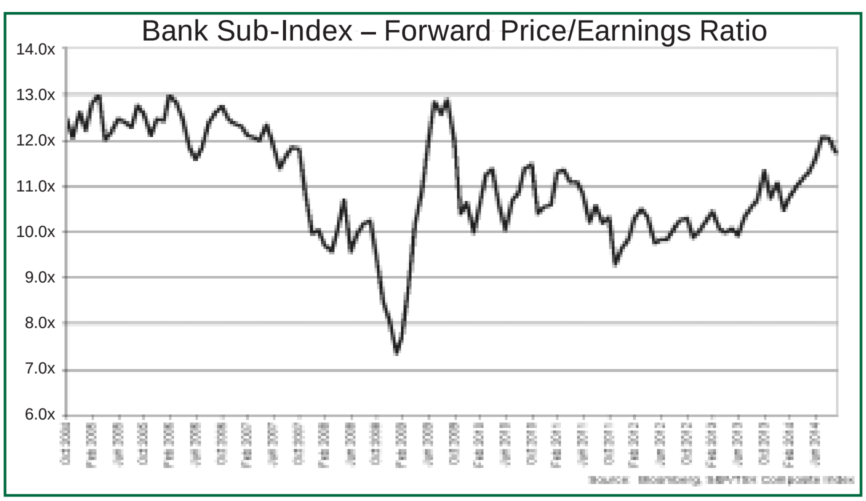
Despite TD's impressive evolution, its journey had bumps along the way. Management made tough choices to exit profitable businesses such as "structured products." In addition, the financial crisis affected TD's performance and stock price. But strong companies such as TD can navigate the turbulence and take the opportunity to execute strategic choices that strengthen and improve the franchise. The passage of time allows that value to be recognized in the stock price.

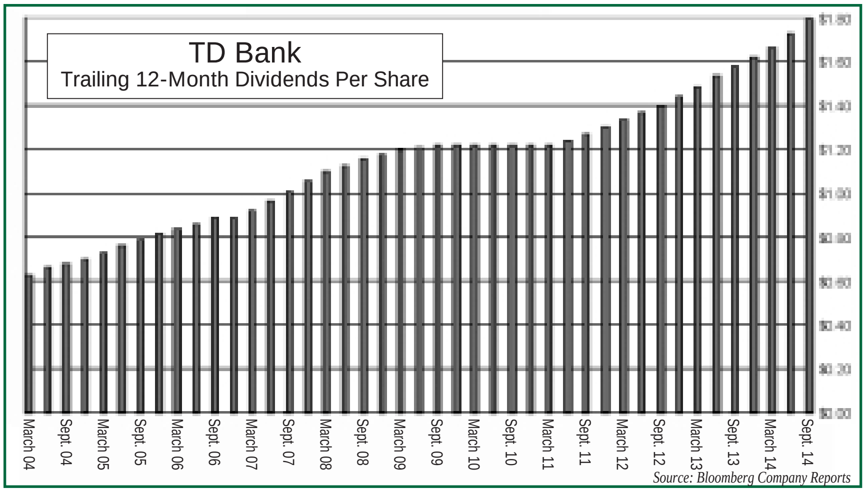
... and rising dividends

Investors have been well served by this growth. Dividends per share for TD have grown from $0.58 in 2003 to $1.62 in 2013. Including dividends, TD's compound annual growth rate for its stock price is 13.5 percent over the past decade, again reinforcing the benefit of earnings growth over time.

Why we're overweight on Canadian banks

Our funds remain overweight in their exposure to Canadian banks. While some investors focus on near-term fears, we view the banks as well-managed businesses with strong capital positions. They offer attractive yields and the potential for strong dividend growth over the coming years. In addition, while





Source: Bloomberg Company Reports

bank stock prices have performed well, valuations have only returned to long-term averages.

What we look for in choosing investments

Our focus remains investments in well-managed businesses with clearly defined strategic direction. Over time, these businesses have a track record of enhancing their franchise, growing their earnings and rewarding investors with dividend increases that have helped to fuel higher stock prices. This is why we continue to search for companies poised to compound their earnings over the long term.

We like to buy these stocks when they're inexpensive, and take advantage of short-term volatility. When we choose wisely and invest with a long-term perspective, compounding over time becomes a powerfully ally in growing wealth. ▼

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