



BLUE CURRENT GLOBAL DIVIDEND

**2015 – Q4  
Quarterly  
Letter**



Prepared by:

**EDGE ADVISORS**

Blue Current SMA Strategy

December 31, 2015

## BLUE CURRENT GLOBAL DIVIDEND

Dear Investors:

The Blue Current Global Dividend Strategy returned +4.30% (net) during the fourth quarter of 2015. We remind investors that our strategy is not managed to any specific equity index, but instead we focus on identifying companies that will pay a stable and increasing dividend and generate an attractive total return for our investors. For comparison, the MSCI World High Dividend Yield Index returned +4.61% and the MSCI World Index returned +5.50% during the quarter. For the full year 2015, the strategy returned -2.00% (net)<sup>1</sup>, which compares to the MSCI World High Dividend Yield Index return of -3.20% and the MSCI World Index return of -0.87%. For 2015, we estimate the portfolio's dividend growth rate was 10%.

Despite the strong fourth-quarter headline print for both Blue Current and the comparable index, the year ended on a sour note due to weakening U.S. and Asia economic data and plummeting energy prices. A strong rebound in October was responsible for all of the quarterly return and was followed by negative cumulative returns during the final two months of the year. The net impact reduced full-year 2015 returns into negative territory. The year was especially challenging for the intersection of the two investment styles that define our Blue Current process: value and dividend investing. Within the U.S., value-style indices underperformed growth by nearly 10% last year, an exceptionally wide spread given how low absolute returns were.



As depicted above, growth has been in the driver's seat since 2009 and has meaningfully outperformed value – to an extent approaching 2 standard deviations. Also impacting returns, popular yield sectors such as utilities and master limited partnerships (MLPs) were decidedly negative – MLPs experienced declines inline with crude oil. Unfortunately, even hopeful New Year's resolutions have not lightened investor sentiment, and January is off to what the popular media has labeled the worst start on record for financial markets.

<sup>1</sup> Net of the strategy's highest annualized management fee of 1%

## **BLUE CURRENT GLOBAL DIVIDEND**

---

If investor confidence was mixed in 2015, market perception has fully transitioned to a glass-half-empty view and for explainable reasons. Economic growth clearly slowed during the second half of the year; a recent forecast by the Atlanta Federal Reserve estimates fourth-quarter real GDP growth of 0.6%. As a reminder, the third-quarter final GDP growth rate was 2.0%, down from 3.9% in the second quarter. In addition to slowing GDP, continued export weakness and declining energy capital expenditures are two more reasons to be cautious. Countering the bears, trends such as unemployment, job quits, retail spending, and consumer sentiment are either heading in a bullish direction or stable despite what GDP estimates would suggest. The Fed's interest rate liftoff in December would also suggest confidence in the economy – supported by strong private sector payroll growth of 257,000 in December. The latter information is being significantly discounted by highly correlated global equity markets, all of which are following persistent declines in energy through mid-January.

Where is the truth? Probably somewhere between the bulls and the bears. We are stating the obvious by saying that 2016 is likely to be another volatile year for investors, and in this environment we like cash flow and dividend growth investing even more. In low-return environments, dividends and buybacks can represent the majority of shareholder returns. This was the case during the 1960s and 1970s when more than half of investor returns were generated by dividends and buybacks.

## **BLUE CURRENT PHILOSOPHY & OBJECTIVES**

The Blue Current investment team utilizes its expertise in growing cash flow to invest in what we believe is a niche universe of high-quality, dividend-paying companies with sustainable business models and dividend policies. The primary objectives are to pay a stable and increasing dividend each quarter and to deliver attractive long-term capital appreciation to investors.

The portfolio is concentrated and invests in 25 to 50 companies across developed markets that meet our stringent quality requirements. We focus on companies that we believe have a strong history of rewarding shareholders and have the financial ability to continue to increase the dividend over time. We also focus on the future earnings potential of each company and strive to purchase those businesses when they are trading at a discount to their true value.

## **PORTFOLIO COMMENTARY**

Blue Current's global diversification rewarded investors in 2015. Led by PartnerRe, Syngenta, and Unilever, our international investments contributed positive 0.5% (gross) to portfolio performance, compared with a -1.5% contribution (gross) from our U.S. domiciled positions. When viewed in U.S. dollar terms, the performance of our international companies outperformed comparable regional benchmarks. For example, the MSCI Eurozone generated a -2.2% U.S. dollar return last year. During the fourth quarter, both the U.S. and international allocations generated positive returns.

For the second year in a row, the technology sector was our top performer in 2015, returning +20% and contributing +1.6% to strategy performance. Gains were led by Accenture, Microsoft, and Apple. Of the three, two dominant cloud-computing franchises (Accenture and Microsoft) remain in the portfolio, while Apple was liquidated in June within several dollars of the company's all time high stock price. Accenture and Microsoft announced dividend increases of 9% and 12%, respectively, during the year. On a single-

## BLUE CURRENT GLOBAL DIVIDEND

---

name basis, PartnerRe was our top contributor and returned +23%; Exor Spa of Italy tendered an offer for the company during the year.

For the fourth quarter, the financial sector was our largest contributor, adding 1.3% to strategy performance. Our top performer during the quarter, ACE, appreciated 14% and received full regulatory approval to complete its merger with Chubb, creating a diverse insurance juggernaut with improved scale and pricing across business lines. ACE has been a core holding for several years. Other financials, including Allianz and Wells Fargo, generated attractive returns. As a sector, financials generated a +9.8% return during the quarter, significantly outperforming the S&P 500 Financials Index.

Top Contributors			
Fourth Quarter	2015		
ACE (Switzerland)	0.60%	PartnerRe (Bermuda)	0.72%
Kimberly Clark	0.55%	Hasbro	0.70%
Microsoft	0.54%	Accenture (Ireland)	0.67%

For the full-year, the energy sector (including the portfolio's MLP exposure) detracted 1.7% from strategy performance. Our emphasis on high-quality MLPs with modest leverage and identifiable distribution growth did not protect capital during the year to the extent we expected. If there was a silver lining, it's that we limited our exposure to MLPs to an average weight of 5.5% in 2015. Two of the three MLPs that we currently own in the portfolio, Enterprise Products and Magellan Midstream, recently announced 2016 distribution growth of 5.5% and 12%, respectively. In addition, late in the year we invested in Spectra Energy Partners, which recently announced it would increase distributions by double digits.

Declining commodity prices, increasing counter-party risk, leverage, and hedge fund shorting continue to pressure midstream partnerships. Our framework to evaluate MLPs relies on many of the same qualities we use to analyze tax-paying C-corporations – leverage, quality of the assets, identifiable cost advantages, valuation, and dividend coverage ratio, to list a few. One of the pressures facing midstream partnerships is determining how to value future cash flow given the uncertainty from energy prices and capital access. Whether we use EBITDA or yield to value the business, we think investors are under-estimating the replacement value of the assets.

For example, Magellan Midstream owns the longest refined product pipeline system in the country (9,500 miles of pipeline across 15 states) with access to more than 50% of the country's refining capacity.

Magellan's refined pipeline network represents close to 14% of the total refined product pipeline infrastructure in the U.S. The market today is assigning an enterprise value of \$15 billion to Magellan, which also rewards shareholders with an annual 5% yield that will increase by double-digits in 2016. We can make the valuation argument for Magellan using the typical tools, EV-to-EBITDA, dividend yield (relative and absolute), etc. - but what if we asked two questions instead: Would you build this company today, and what would it cost to build it? We would argue that a single business responsible for 15% of the country's gasoline, diesel, and jet fuel transportation plays a critical role. If the answer is yes to the question of whether you would build this company, could you build it for less than \$15bn? Consider this example to help guide you: the deeply contested Keystone XL pipeline project, recently declined by

## BLUE CURRENT GLOBAL DIVIDEND

---

Washington DC and being appealed by TransCanada, was expected to stretch 1,200 miles and cross three states to carry crude from Alberta, Canada, to Steele City, Nebraska. The capacity was estimated at 830,000 barrels per day or roughly 9% of U.S. crude production. **The project cost prior to shovels in the ground is currently over \$8bn for those 1,200 miles.** The project was rejected for more reasons than we can highlight, but landowners refusing to either sell land or allow right-of-way for construction played a role – in other words, it is hard to build a pipeline in someone’s backyard. The Keystone XL pipeline is just one example, and we believe it is highly unlikely that Magellan’s asset base can be constructed for less than its current enterprise value of \$15 billion. Did we mention that Magellan also owns 1,600 miles of crude pipelines (larger than the Keystone XL proposal) and 21 million barrels of crude storage in Cushing, Oklahoma? All that for \$15bn.

We are thankful to be able to share with you that our energy investments (including MLPs) generated positive gains for the strategy in the fourth quarter. Not to be forgotten, Marathon Petroleum generated positive returns during the year as refiners benefited from strong gasoline demand and declining input costs.

Bottom Contributors		
Fourth Quarter	2015	
Kingfisher (France)	-0.24%	Alliance Resources -1.22%
CH Robinson	-0.18%	Volkswagen (Germany) -0.78%
Hasbro	-0.15%	Norfolk Southern -0.73%

At a 22% weighting, consumer discretionary continues to represent our largest sector exposure within Blue Current, however; our exposure declined through the course of the year. We liquidated positions such as Ford and Michelin that are tied to the global auto cycle, which we believe is at or near peak levels. The majority of the decline has been to the benefit of the consumer staples sector that now represents 14% of the portfolio. Positions that were initiated during the second half of the year include Wal-Mart, Danone, and Diageo.

## INVESTMENT OUTLOOK

The recent American Association of Individual Investor sentiment survey indicates that nearly 49% of investors are bearish on stock returns over the next six months. The reading is nearly two standard deviations to the extreme, but still 10 percentage points away from the third standard deviation which is considered to be the strongest of contrarian indicators. According to historical results and using the current reading as a guide, 60% of the time, markets are higher six months later. Should pessimism stretch another 10 points, markets are on average 25% higher 100% of the time. What does that mean? If history repeats and the data to be believed, we are probably in the later innings of the current correction and we would agree. From our vantage point, the world is in decent shape today - not perfect (it never is), but sound to the point that earnings and multiples should hold. We are in the early innings of fourth-quarter earnings releases, and we believe the consumer sectors will be the ones to watch this quarter. The consumer represents two-thirds of the U.S. economy and has been the tent pole for recent economic growth. We believe the consumer, aided

## BLUE CURRENT GLOBAL DIVIDEND

by falling gasoline prices and rising wages, is doing well and will help carry the U.S. economy through the year.

We expect our portfolio companies will continue to grow revenue and free cash flow in 2016, rewarding shareholders with dividend increases and share buybacks. As of December 31<sup>st</sup>, the portfolio was invested in 38 companies with an average yield of 3.2%, and a 2016 average P/E of 15.8x.

Sincerely,



**Henry "Harry" M. T. Jones**

Co-Portfolio Manager  
Blue Current Global Dividend



**Dennis Sabo, CFA**

Co-Portfolio Manager  
Blue Current Global Dividend

EQUITY PERFORMANCE				
	Blue Current Equity Composite (net of fees)	Cumulative	MSCI World High Dividend Yield Index (no transaction costs or fees)	Cumulative
2009	15.0	115.0	32.9	132.9
2010	12.7	129.6	6.3	141.3
2011	8.6	140.8	3.9	146.8
2012	11.4	156.8	12.2	164.7
2013	28.9	202.1	21.9	200.8
2014	3.4	209.0	2.5	205.8
2015	-2.0	204.8	-3.2	199.2
CAGR (since inception)	<b>10.8</b>		<b>10.3</b>	
CAGR (trailing 3 years)	<b>9.3</b>		<b>6.5</b>	

Source: Blue Current Investment Management. 2015 performance has not been verified by our independent verification service provider, Ashland Partners & Company. See GIPS disclosure at the end of this report.

## BLUE CURRENT GLOBAL DIVIDEND

### BLUE CURRENT INVESTMENT MANAGEMENT EQUITY ONLY COMPOSITE Annual Disclosure Presentation 1/1/2009 to 6/30/2015

Year	Blue Current Gross Return	Blue Current Net Return	MSCI World High Div Yield	MSCI World Net Index Return	Blue Current Standard Deviation	MSCI World High Div Yield	MSCI World Index Net Standard Deviation	Internal Dispersion	Number of Portfolios	End of Period Assets	End of Period Firm Assets
2009	16.11%	14.97%	32.48%	29.99%	NA 2	24.23%	21.70%	NA 1	< 6	\$1,565,376	\$10,970,324
2010	13.85%	12.71%	6.29%	11.76%	NA 2	25.89%	24.05%	NA 1	< 6	\$2,363,654	\$32,789,983
2011	9.67%	8.58%	3.89%	-5.54%	14.98%	21.81%	20.44%	NA 1	< 6	\$19,499,442	\$115,089,166
2012	12.50%	11.40%	12.24%	15.83%	12.58%	15.33%	16.98%	0.49%	16	\$30,917,548	\$192,572,153
2013	30.14%	28.88%	21.91%	26.68%	10.53%	11.88%	13.73%	0.29%	46	\$71,025,142	\$291,321,586
2014	4.40%	3.35%	2.48%	4.94%	8.84%	10.44%	10.37%	0.31%	57	\$115,318,155	\$425,601,341
6/30/2015	1.58%	1.07%	-0.63%	2.63%	8.72%	9.43%	8.71%	NA	60	\$118,152,568	\$402,219,248

N.A.1 - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

N.A.2 - The three-year annualized standard deviation measures the variability of the composite and the benchmark returns over the preceding 36-month period. The three-year annualized standard deviation is not presented for periods with less than 36 months of data.

**Blue Current Global Dividend Composite** includes all fully discretionary, fee paying accounts under management following a common investment objective, including those accounts no longer with the firm. The Composite invests primarily in domestic or international securities the portfolio manager feels have the potential to deliver outperformance due to a combination of price appreciation and current income in the form of a dividend. The composite will typically invest in securities with a current dividend yield in excess of the broad equity markets with a history of consistently increasing the dividend rate and with what we believe to be strong fundamentals at an attractive price (i.e. low use of leverage, operating margins in excess of 5%, free positive cash flow yield, a price to earnings ratio at or below the market average, and earnings growth). The Global Dividend Equity Composite was created on 1 January 2009. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year.

The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of management fees and include the reinvestment of all income. Net of fee performance was calculated using the highest allowable annual management fee of 1% applied monthly. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

Past performance is not indicative of future results.

The investment management fee schedule for the composite is 1% on the first \$5 million, .7% on the next \$5 million, 0.65% on the next \$10 million, .55% on the next \$30 million, .45 on the next \$50 million. Fees for assets over \$100 million are at a rate customized to the client. Actual investment advisory fees incurred by clients may vary.

*The benchmark MSCI World Index includes 1611 stocks located across 24 developed countries and captures approximately 84% of the free float-adjusted market capitalization in each country. MSCI uses the maximum withholding tax rate applicable to institutional investors in calculating MSCI net dividends*

## **BLUE CURRENT GLOBAL DIVIDEND**

---

The MSCI World High Dividend Yield Index is based on the MSCI World Index, its parent index, and includes large and mid-cap stocks across 23 Developed Markets countries. The index is designed to reflect the performance of equities in the parent index (excluding REITs) with higher dividend income and quality characteristics than average dividend yields that are both sustainable and persistent. The index also applies quality screens and reviews 12-month past performance to omit stocks with potentially deteriorating fundamentals that could force them to cut or reduce dividends. MSCI uses the maximum withholding tax rate applicable to institutional investors in calculating MSCI net dividends.

Blue Current claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Blue Current has been independently verified for the periods January, 2009 to June, 2015 by Ashland Partners. & Company. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The Blue Current Global Dividend composite has been examined for the periods January, 2009 to June, 2015, by Ashland Partners & Company. The verification and performance examination reports are available upon request.

Blue Current Investments is a subsidiary of Edge Advisors, LLC ("Edge"). Edge is an independent registered investment adviser based in Atlanta, Georgia. Blue Current manages separate account strategies with defined investment objectives styles. Edge's total firm assets of approximately \$2.7B (as of July 31, 2015) include the assets manager by the Blue Current division of Edge (\$295.98M) as well as those managed by Edge but not by the Blue Current division. All employees who work within the Blue Current division of Edge may also manage assets for Edge outside of the Blue Current division. The firm's list of composite descriptions is available upon request.

Withholding taxes may vary according to the investor's domicile. Composite returns are gross of withholding tax and represent investors domiciled primarily in the United States. The MSCI Indices uses withholding tax rates applicable to GHI Country holding companies.

### **Disclosure and Risk Summary**

The opinions expressed herein are those of Edge Capital Partners, LLC, and the report is not meant as legal, tax, or financial advice. You should consult your own professional advisors as to the legal, tax, financial, or other matters relevant to the suitability of investing. The external data presented in this report have been obtained from independent sources (as noted) and are believed to be accurate, but no independent verification has been made and accuracy is not guaranteed. The information contained in this report is not intended to address the needs of any particular investor.

The information contained in this document does not constitute an offer to sell any securities nor a solicitation to purchase any securities. Index returns reflect the reinvestment of dividends.

PAST PERFORMANCE CANNOT BE CONSTRUED AS AN INDICATOR OF FUTURE RESULTS BECAUSE OF, AMONG OTHER THINGS, POSSIBLE DIFFERENCES IN MARKET CONDITIONS, INVESTMENT STRATEGY, AND REGULATORY CLIMATE. THERE IS NO ASSURANCE THAT THE FUND WILL ACHIEVE ITS INVESTMENT OBJECTIVE. INDEX INFORMATION (I) IS INCLUDED MERELY TO SHOW THE GENERAL TREND IN THE EQUITY MARKETS FOR THE PERIODS INDICATED AND IS NOT INTENDED TO IMPLY THAT THE FUND'S PORTFOLIO WILL BE SIMILAR TO THE INDICES EITHER IN COMPOSITION OR RISK AND (II) HAS BEEN OBTAINED FROM SOURCES BELIEVED TO BE ACCURATE.

This presentation is solely for the recipient. By accepting this report, the recipient acknowledges that distribution to any other person is unauthorized and any reproduction of this report, in whole or in part, without the prior consent of Edge Capital Partners, LLC, is strictly prohibited.