The Sizemore Income Letter

March 2021

Revisiting an Old Friend

By Charles Lewis Sizemore, CFA

I promised last month that I wouldn't drone on about the pandemic anymore. And I won't. I promise.

But let me tell you… that second shot can be a real doozy. I got my second Pfizer shot last week, and ended up spending the better part of two days in bed.

This is why I'm getting the *Sizemore Income Letter* to press a little later than usual. They say the vaccine can create flu-like symptoms for a couple days. I'd liken it to the world's worst hangover. But thankfully, it clears up quickly enough.

The pandemic might not be *over*, per se, as parts of Europe are actually re-imposing lockdowns, and some of the new variants look scary. So, if you're not vaccinated… do try to be careful. It would really be tragic to hold out this long and then get sick with a bad case now, when it's so close to being over.

But as far as the market is concerned, it's a done deal.

The vaccination effort is going remarkably smoothly. 50 million Americans, or 20% of the adult population, are already fully vaccinated, and 36% have gotten at least one shot. In another couple months, the world might actually look normal again.

This month, I'm going to recommend one of my long-time favorite dividend powerhouses. But before I do that, I want to comment on something I read over the weekend in *Barron's*.

***Barron's* List of "Reliable Retirement Returns"**

Company	Ticker	Price	Dividend Yield	Return Since 1/31/2020	5-Year Dividend Growth Rate
AT&T	T	$ 29.99	6.9%	-14.5%	2%
Coca-Cola	KO	$ 51.52	3.3%	-8.0%	5%
Consolidated Edison	ED	$ 73.43	4.2%	-17.9%	3%
IBM	IBM	$ 130.62	5.0%	-3.1%	5%
Johnson & Johnson	JNJ	$ 161.91	2.5%	12.4%	6%
Kellogg	K	$ 61.51	3.7%	-5.7%	3%
Procter & Gamble	PG	$ 132.56	2.4%	9.0%	3%
SL Green Realty	SLG	$ 70.02	5.2%	-18.5%	7%
U.S. Bancorp	USB	$ 53.47	3.1%	5.0%	11%
Verizon Communications	VZ	$ 57.01	4.4%	0.2%	2%

In case you're wondering what I read personally. I really make the effort to get through *Barron's* each Saturday. The biggest problem for an analyst to navigate these days is information overload. *Barron's* has a way of condensing all of the noise of the prior week into what amounts to digestible cliff notes.

At any rate, Barron's put together a list of 10 dividend stocks to "build lasting streams of income for retirement."

As this is right up my alley, I thought I'd compare notes with *Barron's*. You might see a few familiar names here.

You've heard me repeat until I'm blue in the face that income investing is about far more than simply reaching for the highest yield. In fact, doing that is generally a terrible idea and will almost always go poorly. An exceptionally high yield is almost always the sign of an imminent dividend cut or, at a minimum, a sign that the investment is exclusively about income and you shouldn't expect much in the way of capital gains.

I say "almost" because there are clearly exceptions, and I recommend them when I see them. But as a general rule, a stock with a moderate yield of 3% to 5% with regular dividend growth is going to be a better investment than a yield monster paying 10% or more. (Given today's yield environment, even 3% to 5% can be a stretch.)

Barron's feels the same way. Every stock on the list has a respectable current yield (at least by today's standards) and a recent track record of raising its dividend by at least the rate of inflation.

And that's really the key. Any dividend that does not grow at a rate as high or higher than the rate of inflation is a dividend that will actually lose purchasing power over time.

That's the biggest problem with bonds and the biggest reason to depend more on dividend stocks for your retirement needs. Bond investors get poorer every year as their purchasing power shrinks. Dividend growth investors get richer every year, regardless of what the stock price does, because their dividend stream rises.

With that said, let's look at the portfolio.

At the top of the list is **AT&T (NYSE: T)**, which also happens to be one of the original member of our "Forever Portfolio." I'll have more to say about AT&T a little later.

Moving on, I really like **Coca-Cola (NYSE: KO)**, **Johnson & Johnson (NYSE: JNJ)**, **Kellogg (NYSE: K)**, **Procter & Gamble (NYSE: PG)** and **Verizon (NYSE: VZ)** as long-term dividend payers.

You're not likely to see me recommend any of these in this newsletter, as they are just a little too conservative and low-yielding to make that cut. But I would gladly take an income portfolio made out of these four companies over a bond portfolio. These are companies that sell basic consumer staples and services and, in the case of JNJ, health products. They're about as "future proof" as you can get.

I still believe we can do a lot better in the *Sizemore Income Letter*. But these stocks definitely deserve a home in a comprehensive income portfolio. If you're looking for stocks to round out a dividend strategy, these should make the cut.

I'm a little less enthusiastic about the rest of the portfolio.

I've never been a fan of electric utilities like **Consolidated Edison (NYSE: ED)**. They offer better inflation protection than bonds, but they are also overregulated, slow-growth dinosaurs. I'd prefer to get my yield elsewhere.

I love REITs. But I'm not a fan of **SL Green Realty (NYSE: SLG)**. It's just too concentrated in New York City offices. If we're looking for something safe for a retirement portfolio, that's not it.

Including **IBM (NYSE: IBM)** in a retirement portfolio is madness. If we're looking for a portfolio of stocks you can buy, drop in a drawer, and hold forever, what would ever possess you to buy shares of a legacy tech company that's seeing its core businesses get ravaged by Amazon.com's AWS?

And finally, while I like **U.S. Bancorp (NYSE: USB)**, I don't consider any bank at the safety level I'd want to see in a forever portfolio. It's decent, and you could definitely do a lot worse. I actually expect the stock to do really well over the coming year or two. But I wouldn't consider it a "forever stock."

So, there you have it. *Barron's* had a few good recommendations. But I think you can find better.

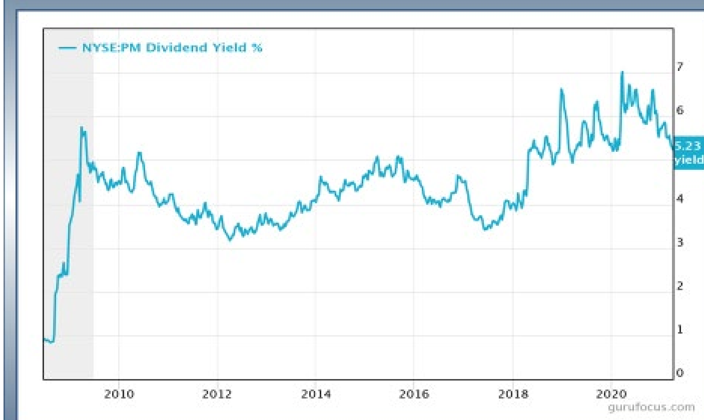
A Durable 5% Yielder

And speaking of that, let's jump right in to this month's new recommendation. **Philip Morris International (NYSE: PM)** has been a mainstay in income portfolios since its spinoff from **Altria (NYSE: MO)** in 2008.

Philip Morris International (NYSE: PM)

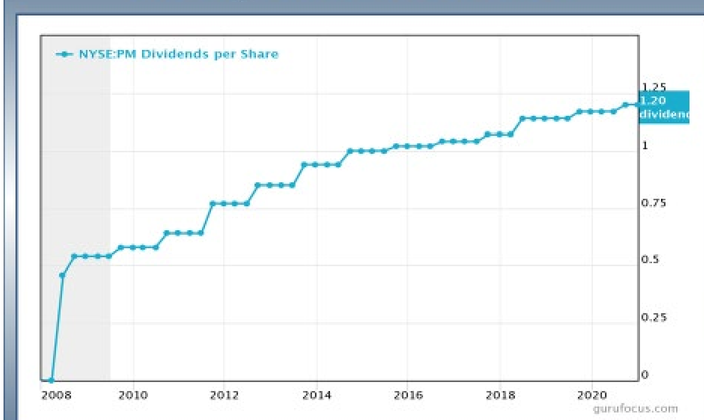
Source: GuruFocus.com *Figure 2*

Dividend Yield



Source: GuruFocus.com *Figure 3*

Steady Dividend Growth



Source: GuruFocus.com *Figure 4*

Philip Morris International sells tobacco and other nicotine products outside of the U.S.

But it's been a rough stock to hold. PM enjoyed a nice run from 2008 to 2012… and then proceeded to trade in a range for the next nine years. The stock price today was first seen in 2012.

The dividend yield was also a little less than impressive for most of that time, bouncing around between 3% and 5%.

Earlier, I said that a dividend in that range was good. And it is… usually.

But remember that tobacco is an industry in decline. Yes, there are pockets of growth, such as in vaping products. And Philip Morris International competes well in this space. Already, vaping and other safer alternative to traditional cigarettes make up about a quarter of sales. By 2025, PM expects a majority of its sales to be from smoke-free products.

But let's face it. As the seller of a controversial and addictive product, Philip Morris has issues that a company like Coca-Cola simply doesn't have.

I'm ok with that, of course. But I have to be paid for that extra risk I'm taking. I might be happy to own Coca-Cola at a 2% to 3% yield. But for a tobacco stock, I really need a higher yield than that. And with a dividend yield of about 5.2%, PM makes the grade.

Philip Morris raised its dividend only slightly last year, which is understandable given how chaotic 2020 was. But over the past decade, PM doubled its dividend payout.

That's a big deal. A company capable of doubling its dividend in a decade is a company that should have no trouble at all keeping ahead of inflation.

Let's talk a little more about Philip Morris' product portfolio. Most of us will be most familiar with is traditional iconic brands like Marlboro. But it is also the owner of the IQOS and HEETS smoke-free line of vaping products, which the company views as its future.

IQOS is the world's #1 smoke-free brand and the #5 nicotine brand overall.

To give an idea of the growth potential here, there were 17.6 million IQOS users as of the end of last year. There are 250 million addressable tobacco users in the markets in which Philip Morris International operates and around 600 million nicotine users outside of the U.S. and China.

So, even while traditional tobacco is an industry in decline, PM has fantastic growth potential in the markets in which it operates.

I've always loved Philip Morris International. Unfortunately, the stock has been a no-go zone for me for most of the past decade because the stock was too expensive and in a downtrend.

Well, that's no longer the case. After years of trading sideways, its real-world businesses have more than caught up with its share price. And after bottoming last year during the March selloff, the stock has been trending higher. We're no longer catching a falling knife.

Rather than add Philip Morris International to our regular portfolio, I'm going to do something a little different this month. I'm going to add it to our "forever" portfolio.

The Forever Portfolio												
Stock	Ticker	Entry Date	Buy	Price		Recent Price	Stop Loss	Yield		Cumulative Dividends	Total Return	IRA Friendly?
Philip Morris International	PM	3/30/2021	$	89.35	$	89.35	None	5.28%	$	-	0.00%	Yes
Altria Group	MO	3/19/2020	$	37.10	$	51.26	None	6.55%	$	4.26	49.65%	Yes
Realty Income	O	3/19/2020	$	48.08	$	64.12	None	4.39%	$	2.81	39.20%	Yes
AT&T	T	3/19/2020	$	31.15	$	30.73	None	6.91%	$	2.08	5.33%	Yes
Enterprise Products Partners	EPD	3/19/2020	$	14.52	$	22.36	None	7.83%	$	1.79	66.29%	No
Kinder Morgan	KMI	3/19/2020	$	11.20	$	16.62	None	6.25%	$	1.05	57.79%	Yes
Ventas	VTR	3/19/2020	$	19.98	$	54.72	None	3.28%	$	2.14	184.60%	Yes
Public Storage	PSA	3/19/2020	$	187.60	$	247.03	None	3.27%	$	8.00	35.94%	Yes
International Paper	IP	3/19/2020	$	30.13	$	55.00	None	3.72%	$	2.05	89.35%	Yes
STAG Industrial	STAG	3/19/2020	$	21.71	$	33.92	None	4.24%	$	1.44	62.88%	Yes
Retail Opportunity Investments	ROIC	3/19/2020	$	7.25	$	16.27	None	1.88%	$	0.31	128.69%	Yes
Average								**4.87%**			**71.97%**	

As you might remember, in the very first issue of the Sizemore Income Letter, I created a list of 10 stocks that I considered strong enough to buy and hold forever.

Well, I feel the same way about Philip Morris International. So, with no further ado…

Action to take: Buy Shares of Philip Morris International at market. Plan to hold it for the rest of your life.

While we're at it, why don't we give the Forever Portfolio a deeper look. I don't discuss this portfolio every month because, frankly, I don't have to. It's designed to be an autopilot portfolio that requires absolutely no maintenance. But that doesn't mean that we shouldn't give it a good look every now and then.

Including dividends, we're up an average of 72% over the past year in this portfolio. The two biggest standouts have been health and senior living REIT **Ventas (NYSE: VTR)**, up 184.6%, and neighborhood retail REIT **Retail Opportunity Investments (NYSE: ROIC)**.

It's the latter that I find the most interesting. If I am to be honest with myself, I really botched this recommendation. At the onset of the pandemic, I believed that a REIT specializing in neighborhood strip malls, generally anchored by a grocery store, would be a fantastic place to ride out the storm.

Well, I was right about grocery stores. They had a banner year in 2020 as people were forced to eat more at home. But mom-and-pop retail in general had an awful year, and ROIC had to suspend its dividend shortly after I recommended it so that it could assess the damage.

Thankfully, we've come a long way since then. The damage to the retail economy, while massive, has long ago been done. ROIC investors are looking beyond the pandemic and seeing a rosier future for the neighborhood strip mall.

Oh, and it's worth mentioning that ROIC reinstituted its dividend, albeit at a lower rate for now.

As the world gets closer and closer to normal, I expect ROIC to raise its dividend accordingly.

Every stock on this list remains a buy. But if you're looking to deploy new cash, I would focus on a handful of these first.

Energy stocks have been on fire in 2021, and I expect that to continue for a while. So, I'd put **Kinder Morgan (NYSE: KMI)** and **Enterprise Products Partners (NYSE: EPD)** at the very top of your list.

Investors really fretted that President Biden would be less friendly to the energy industry than former president Donald Trump. And thus far, that's been the case. Biden's administration is committed to renewable energy, and pipeline operators are going to be facing a tougher regulatory climate for the foreseeable future.

But what of it? The Obama Administration was also hard on pipeline operators, and KMI and EPD both did really well for the first six years of his presidency. It was collapse in the price of oil that hurt these stocks starting in 2014, not heavy-handed government.

So, if you don't already own these, it's not too late. Both pay extremely competitive yields, even after their recent run-ups in price.

I'd also recommend you give **Realty Income (NYSE: O)** a look. Realty Income owns a sprawling portfolio of high-traffic retail properties like pharmacies and convenience stores.

This is a phenomenally well-run REIT, and it's trading at 2016 prices. It managed to maintain and even raise its dividend in 2020. If that doesn't prove how bullet-proof its business model is, I don't know what will. The REIT has made 608 consecutive monthly dividend payments and has raised its payout for 94 consecutive quarters. There's really no way you can be an income investor and not love this stock.

Portfolio Review

Let's also give the main portfolio a good look before we call it a month.

The S&P 500 has essentially gone nowhere in March, and the Nasdaq is actually down for the month. I don't necessarily believe this is the beginning of a major bear market. But it does look like some significant rotation is afoot. Investors are taking profits in a lot of the major winners of 2020 – such as technology and media – and are buying more economically sensitive stocks that should benefit most from the world returning to normal.

This isn't bad for our portfolio. The stocks getting dumped are generally stocks that don't pay dividends and are thus stocks we'd never own in this newsletter.

If you're looking to put new capital to work, I might make **Magellan Midstream Partners (NYSE: MMP)** one of your first choices. Magellan hasn't performed as well as some of its peers in the pipeline space this year, but I expect that it will catch up soon enough. This is a best-in-class pipeline operator, and it yields an almost ridiculous 9.5% yield.

I also still believe that emerging markets are going to be the biggest growth story of the next several years. The **WisdomTree Emerging Markets High Dividend Fund (NYSE: DEM)** gives us broad access to emerging markets while also paying us an attractive 4% yield.

One of my latest additions – blue-chip miner **BHP Group (NYSE: BHP)** – is off to a slow start. We're down a little over 10%.

This is just something that comes with the turf. BHP is a volatile stock. I expect us to make a lot of money in BHP, and I'd consider this little pullback a fantastic opportunity to buy the dip.

And finally, I still really like the **Tortoise Essential Assets Income Term Fund (NYSE: TEAF)**. It trades at a 13% discount to net asset value, which means you're getting a dollar's worth of high-quality assets for just 87 cents. And because this is a term fund that liquidates in 2030, that gap has to close.

Until that happens, we'll just keep collecting the monthly dividends.

That's going to wrap it up for this month. We'll pick this up in April. Until then, keep cashing those dividend checks!

P.S.: Apart from writing this newsletter, I run a full-service wealth management firm along with my colleagues. At **Sizemore Capital Management**, we build income portfolios like those I write about in the *Sizemore Income Letter*. But we also do a lot more than that. We manage a suite of low-volatility strategies offering low correlation to the S&P 500. If you think your portfolio is a little too exposed to the stock market right now, let's talk. I may have some alternatives that can offer competitive returns without the heartburn.

If you'd like for me to take a look at your portfolio and offer some recommendations, contact me at info@sizemorecapital.com.

The Sizemore Income Letter Portfolio

Stock	Ticker	Entry Date	Buy Price	Recent Price	Stop Loss	Yield	Cumulative Dividends	Total Return	IRA Friendly?
BHP Group	BHP	2/25/2021	$78.04	$ 69.70	$60.94	4.10%	$ -	-10.69%	Yes
Vale SA	VALE	2/25/2021	$17.40	$ 17.02	$12.06	3.00%	$ -	-2.18%	Yes
Magellan Midstream Partners	MMP	1/29/2021	$44.41	$ 42.79	$34.74	9.10%	$ 1.03	-1.33%	No
WisdomTree Emerging Markets High Dividend Fund	DEM	12/31/2020	$41.22	$ 44.22	$37.02	4.70%	$ -	7.28%	Yes
Healthcare Trust of America	HTA	11/20/2020	$26.80	$ 28.26	$23.14	4.75%	$ 0.32	6.64%	Yes
Physicians Realty Trust	DOC	11/20/2020	$17.80	$ 17.95	$14.53	5.12%	$ 0.23	2.13%	Yes
AllianceBernstein Holding, LP	AB	11/6/2020	$30.85	$ 39.74	$28.16	9.12%	$ 0.97	31.96%	No
Main Street Capital	MAIN	9/25/2020	$29.74	$ 39.56	$24.36	8.46%	$ 0.82	35.78%	Yes
Iron Mountain	IRM	8/25/2020	$30.22	$ 37.16	$23.53	8.15%	$ 1.24	27.06%	Yes
Starwood Property Trust	STWD	8/25/2020	$15.70	$ 24.91	$15.87	12.05%	$ 0.96	64.78%	Yes
Dow Inc.	DOW	6/24/2020	$38.45	$ 64.61	$41.05	6.62%	$ 0.70	69.86%	Yes
Tortoise Essential Assets Income Term Fund	TEAF	6/24/2020	$10.73	$ 14.24	$11.07	8.19%	$ 0.60	38.30%	Yes
LyondellBasell Industries	LYB	5/22/2020	$60.39	$ 105.03	$73.29	6.17%	$ 1.05	75.66%	Yes
Invesco Adv. Municipal Income Trust II	VKI	4/23/2020	$10.12	$ 11.87	$10.87	4.76%	$ 0.51	22.28%	No
Ares Capital Corporation	ARCC	4/23/2020	$11.35	$ 18.85	$15.02	11.44%	$ 1.20	76.65%	Yes