



## Featured Stock in February's Dividend Growth Model Portfolio

20 new stocks make our [Dividend Growth Stocks Model Portfolio](#) this month, which was made available to members on February 27, 2020.

### Recap from January's Picks

Our Dividend Growth Stocks Model Portfolio underperformed the S&P 500 from January 29, 2020 through February 25, 2020. The Model Portfolio fell 5.4% on a price return basis and 5.2% on a total return basis. The S&P 500 fell 4.3% on a price return and total return basis. The portfolio's best performing stock was up 8%. Overall, nine out of the 25 Dividend Growth Stocks outperformed the S&P 500 from January 29, 2020 through February 25, 2020.

Get the best fundamental research

Only our research utilizes the superior data and earnings adjustments featured by the HBS & MIT Sloan paper, "[Core Earnings: New Data and Evidence](#)." The long-term success of our model portfolio strategies highlights the value of our [Robo-Analyst technology](#)<sup>1</sup>, which scales our forensic accounting expertise ([featured in Barron's](#)) across thousands of stocks<sup>2</sup>.

The methodology for this model portfolio mimics an All Cap Blend style with a focus on dividend growth. Selected stocks earn an [Attractive or Very Attractive rating](#), generate positive free cash flow ([ECF](#)) and [economic earnings](#), offer a current dividend yield >1%, and have a 5+ year track record of consecutive dividend growth. This model portfolio is designed for investors who are more focused on long-term capital appreciation than current income, but still appreciate the power of dividends, especially growing dividends.

### Featured Stock from February: The Allstate Corp (ALL: \$105/share)

The Allstate Corp (ALL) is the featured stock from February's Dividend Growth Stocks Model Portfolio. We first featured ALL as a Long Idea in [June 2015](#) and closed the position in [August 2015](#). Over that time, the stock was up 3% while the S&P 500 was down 1%.

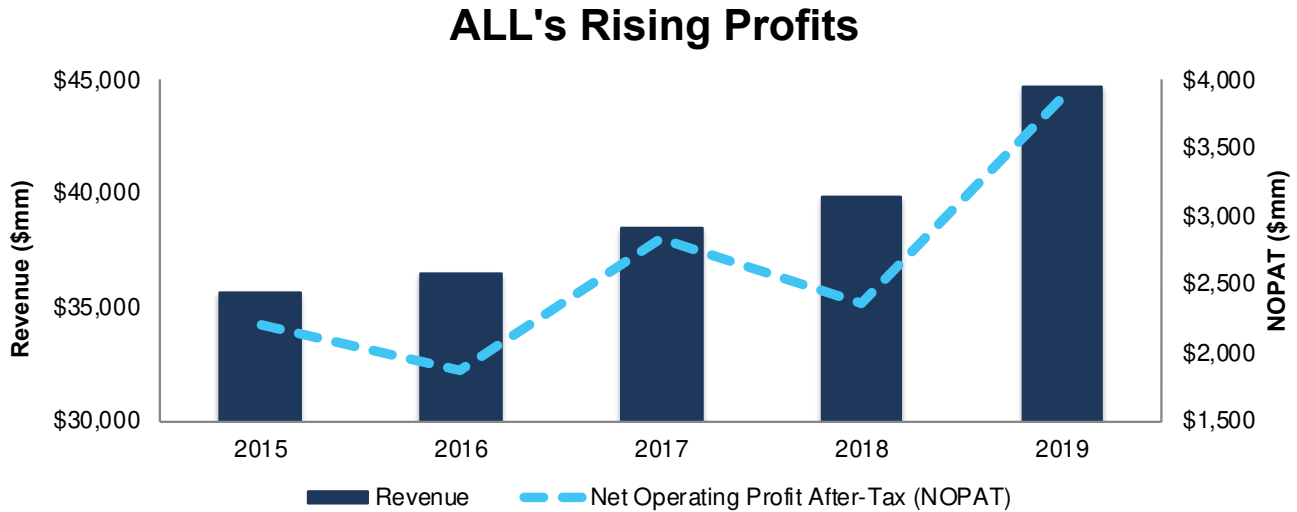
Since 2015, ALL has grown revenue by 6% compounded annually and net operating profit after-tax ([NOPAT](#)) by 15% compounded annually. Longer-term, ALL has grown NOPAT by 15% compounded annually over the last decade. ALL's NOPAT margin increased from 6% in 2015 to 9% in 2019 while its ROIC improved from 9% to 15% over the same time.

<sup>1</sup> Harvard Business School features the powerful impact of our research automation technology in the case [New Constructs: Disrupting Fundamental Analysis with Robo-Analysts](#).

<sup>2</sup> This [paper](#) compares our analytics on a mega cap company to Bloomberg and Capital IQ (SPGI) in a detailed appendix.



Figure 1: ALL's Revenue & NOPAT Since 2015



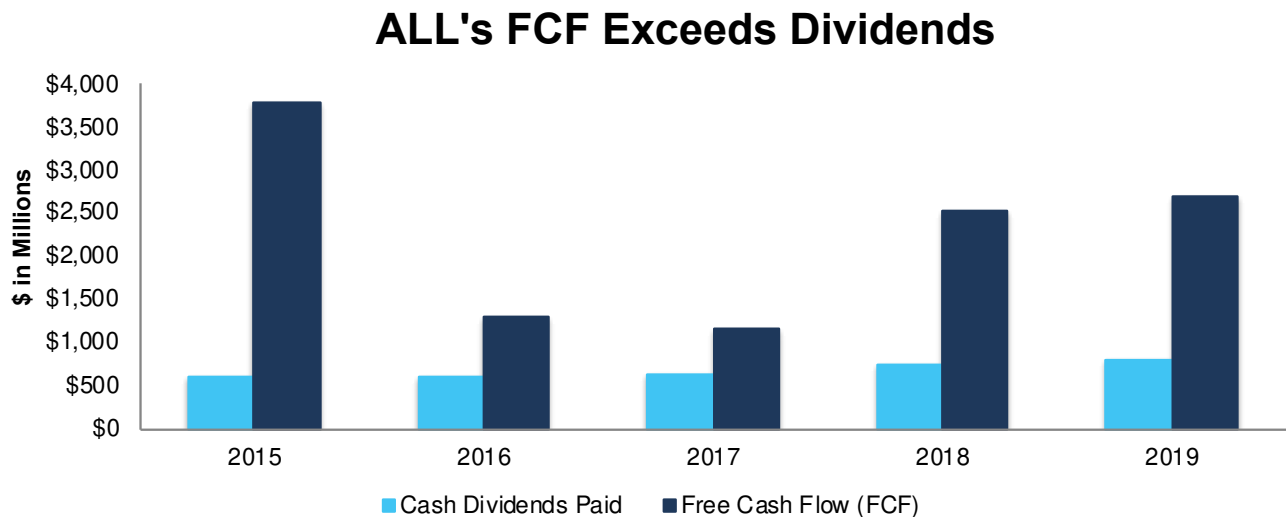
Sources: New Constructs, LLC and company filings

#### Steady Dividend Growth Supported by FCF

ALL has increased its dividend on common stock in each of the past nine years. The company increased its annualized dividend from \$1.20/share in 2015 to \$2.00/share in 2019, or 14% compounded annually. Its current quarterly dividend, \$0.54/share equates to \$2.16/share annually. More importantly, ALL easily generates the cash flow needed to continue paying and growing its dividend. Over the past five years, ALL has generated a cumulative \$11.5 billion in FCF (33% of market cap) while paying \$3.4 billion in dividends.

Companies with FCF well in excess of dividend payments provide higher quality dividend growth opportunities because we know the firm generates the cash to support a higher dividend. On the other hand, the dividend of a company where FCF falls short of the dividend payment over time cannot be trusted to grow or even maintain its dividend because of inadequate free cash flow.

Figure 2: Free Cash Flow (FCF) vs. Regular Dividend Payments



Sources: New Constructs, LLC and company filings



## ALL Is Undervalued

At its current price of \$105/share, ALL has a price-to-economic book value ([PEBV](#)) ratio of 0.5. This ratio means the market expects ALL's NOPAT to permanently decline by 50% over its remaining corporate life. This expectation seems overly pessimistic for a firm that has grown NOPAT by 2% compounded annually since 1999 and 15% compounded annually over the past decade.

If ALL can maintain NOPAT margins at its 5-year average of 7% and grow NOPAT by only 2% compounded annually over the next decade, the stock is worth \$226/share today – a 115% upside. [See the math behind this reverse DCF scenario](#). Add in Allstate's 1.8% dividend yield and history of dividend growth, and it's clear why this stock is in February's Dividend Growth Stocks Model Portfolio.

## Critical Details Found in Financial Filings by Our [Robo-Analyst Technology](#)

As investors [focus more](#) on fundamental research, research automation technology is needed to analyze all the critical financial [details in financial filings](#) as shown in the Harvard Business School and MIT Sloan paper, "[Core Earnings: New Data and Evidence](#)".

Below are specifics on the adjustments we make based on Robo-Analyst findings in The Allstate Corp's 2019 10-K:

Income Statement: we made \$2.3 billion of adjustments with a net effect of removing \$812 million in [non-operating income](#) (2% of revenue). See all adjustments made to ALL's income statement [here](#).

Balance Sheet: we made \$5.2 billion of adjustments to calculate invested capital with a net decrease of \$555 million. The most notable adjustment was \$2.6 billion (10% of reported net assets) in [other comprehensive income](#). See all adjustments to ALL's balance sheet [here](#).

Valuation: we made \$5.7 billion of adjustments with a net effect of decreasing shareholder value by \$5.7 billion. There were no adjustments that increased shareholder value. The most notable adjustment was \$2.2 billion in the [fair value of preferred stock](#). This adjustment represents 6% of ALL's market value. See all adjustments to ALL's valuation [here](#). Despite these subtractions from shareholder value, ALL remains undervalued.

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*Disclosure: David Trainer, Kyle Guske II, and Matt Shuler receive no compensation to write about any specific stock, style, or theme.*

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## ***Footnotes adjustments matter. We are the ONLY source.***

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We provide ratings, models, reports & screeners on U.S. 3,000 stocks, 700 ETFs and 7,000 mutual funds.

**HBS & MIT Sloan research** reveals that:

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The HBS & MIT Sloan paper, [Core Earnings: New Data and Evidence](#), shows how our superior data drives uniquely comprehensive and independent debt and equity research.

This [paper](#) compares our analytics on a mega cap company to other major providers. The Appendix details exactly how we stack up.

**Learn [more](#).**

Quotes from HBS & MIT Sloan professors on our research:

### **Get better research:**

*“...the NC dataset provides a novel opportunity to study the properties of non-operating items disclosed in 10-Ks, and to examine the extent to which the market impounds their implications.” – page 20*

### **Pick better stocks:**

*“Trading strategies that exploit cross-sectional differences in firms’ transitory earnings produce abnormal returns of 7-to-10% per year.” – Abstract*

### **Avoid losses from using other firms’ data:**

*“...many of the income-statement-relevant quantitative disclosures collected by NC do not appear to be easily identifiable in Compustat...” – page 14*

### **Build better models:**

*“Core Earnings [calculated using New Constructs’ novel dataset] provides predictive power for various measures of one-year-ahead performance...that is incremental to their current-period counterparts.” – page 4*

### **Exploit market inefficiencies:**

*“These results ... suggest that the adjustments made by analysts and Compustat to better capture core earnings are incomplete. Moreover, the non-core items identified by NC produce a measure of core earnings that is incremental to alternative measures of operating performance in predicting an array of future income measures.” – page 26*

### **Fulfill fiduciary duties:**

*“An appropriate measure of accounting performance for purposes of forecasting future performance requires detailed analysis of all quantitative performance disclosures detailed in the annual report, including those reported only in the footnotes and in the MD&A.” – page 33-34*



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