YIELD HOG- What three portfolio managers are doing right now with their dividend investments

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It's often said that stock markets climb a wall of worry. Lately, the wall's been greased with Crisco and strewn with booby traps.

The price of crude has been cut in half. The Canadian dollar has plunged to about 80 cents (U.S.). And government of Canada bond yields have collapsed to record lows – the five-year bond yields just 0.65 per cent – amid worries about slowing growth and the Bank of Canada's recent rate cut.

Those razor-thin yields, in turn, have sparked a rally in interest-sensitive sectors such as utilities, power producers and real estate investment trusts (REITs), even as bank stocks have been clobbered.

In such a volatile environment, many investors feel paralyzed. Is energy the deal of the century, or a value trap? Should they buy U.S. stocks, or avoid them lest the loonie recover? Will the gains in interest-sensitive stocks be wiped out if bond yields rebound?

To help dividend investors navigate through these unusual times, Yield Hog asked three portfolio managers to discuss what they've been doing. Their responses have been edited for brevity and clarity.

Greg Newman, Associate Portfolio Manager, ScotiaMcLeod

While these may be strange investing times, I find they usually are. I find they usually only appear easy when looking backward.

I am still buying utilities and interest sensitives where we believe they have a catalyst or have been overlooked. Capital Power (CPX), for example, is well hedged to lower Alberta power prices for the next couple of years, at a time when major developments are set to come on line in 2015. It trades at an estimated 2015 free cash flow yield of 11.5 per cent and its dividend is secured by a low payout ratio.

While the REITs have had a big move, there are still some with good value. Crombie REIT (CRR.UN) boasts a dividend of about 6.7 per cent, which is underpinned by what we believe is an improving payout ratio. I don't think there is too much risk in buying interest sensitives as long as you buy names at a good price and where you can see a catalyst for growth even if bond yields spike.

As well, with a balanced portfolio, we also own positions that should benefit from rising bond yields such as banks and insurance companies.

While the Canadian dollar's move has been big, I do not believe it is too late to convert to U.S. dollars, assuming you can find really a compelling idea in the United States. While the Bank of Canada may not say it, the effects of $50 oil are less catastrophic for Canadian oil producers if they are amplified by a 1.25 (Canadian dollars per U.S. dollar) exchange rate. Better still if they are amplified by 1.35, for example.

Tony Demarin, President, BCV Asset Management

Overall, we believe we are in a multiyear bull market for equities. Strong corporate profit fundamentals, low interest rates, cheap oil and gas prices and a soft labour market will allow businesses to operate, hire and borrow cheaply. The U.S. economy, driven by consumer consumption and housing, will pull Canada along with its lower dollar, which we feel will bottom at 75 cents (U.S.), giving Canadian investors a further lift with a U.S. stock allocation.

We focus a great deal on dividend growth, both past and expected. Investors will continue to gravitate to dividend stocks as interest-bearing investments will only satisfy the most risk-averse savers.

Sectors such as utilities and pipelines – for example, Fortis Inc. (FTS) and TransCanada Corp. (TRP), respectively – will provide positive returns due to this trend.

In Canada, we also favour the railways – Canadian National Railway Co. (CNR) recently increased its dividend by 25 per cent. We also like the telecoms – Rogers Communications Inc. (RCI.B) increased its dividend by 5 per cent, with BCE Inc. (BCE) and Telus Corp. (T) soon to follow. We believe the Canadian banks offer value with the recent pullback in their share price, and the dividend yields are too attractive to pass up.

We remain underweight in energy and will be patient. Energy will require six months before supply bottoms and stocks can begin to discount higher spot prices.

John Stephenson, Chief Executive Officer, Stephenson & Co. Capital Management

It's important for investors to consider the long term when investing, and our view is that the U.S. is unquestionably the best house on the block. The Canadian economy and the Canadian dollar look vulnerable over the next few years, as oil, our principal export, is likely to remain under pressure. The Canadian dollar is overwhelmingly viewed as a petro currency and the surprise rate cut from the Bank of Canada has only hastened the slide in our dollar as investors correctly perceive that the Bank of Canada has a weak dollar policy.

Because the slide in oil prices represents a structural shift rather than a temporal one, and materials are also undergoing a structural change with very weak demand from China, both sectors should be avoided by investors.

The economic data in the United States is overwhelmingly positive and, unlike the Canadian consumer whose personal balance sheet is in tatters with the highest-ever debt to disposable income levels, the U.S. consumer's personal balance sheet is in the best position it's been in for more than two decades. Canadian investors should consider large, liquid U.S. equities that have limited exposure to overseas markets where the foreign exchange with a surging U.S. dollar could erode returns.