



25th Annual Windy City Summit

Update on Uses of Cash & Subsequent Returns on Share Prices

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2011

Takeaway

- What Use of Cash Strategies Have Paid Off in Total Return Performance
- Provide Insight On What Alternatives May Make More Sense for Your Firm

Topics Covered

- Overview of DeMarche Associates
- Definitions and Background
- Study Results
- Conclusions

DeMarche Associates

Products and Service

Defined Benefit/Endowment/Foundation Consulting

- Asset Allocation
- Investment Policy
- Manager Search and Selection
- Manager Optimization
- Performance Measurement
- Tactical Asset Allocation
- Liability/Spending Policy Analysis
- Fee Analysis

Defined Contribution Consulting

- Investment Policy Development and Review
- DC Analytics
- Supplemental Benefit/COLI Plans
- Investment Funds Analysis
- DC Diversification Tool
- Provider Search
- Fee Analysis

Programs in Finance and Investments

- Topics Critical to Investment, Corporate Finance, and Investor Relations Practitioners
- Access to Renowned Academics

Tactical Advisory Services

- Portfolio Rebalancing
- Market Outlook
- Phase Analysis of Market Cycle

Corporate Finance Consulting

- Total Equity Management
- P/E Analysis and Valuation
- Cost of Equity Capital
- Supplemental Benefit/COLI Plans
- Dividend Policy Review

Investor Relations Consulting

- Peer Group & Clone Analysis
- Manager Targeting & Intelligence
- Treasury Buyback Analysis
- P/E Analysis
- Trading Liquidity Analysis
- Message Central

Stock Rating Services

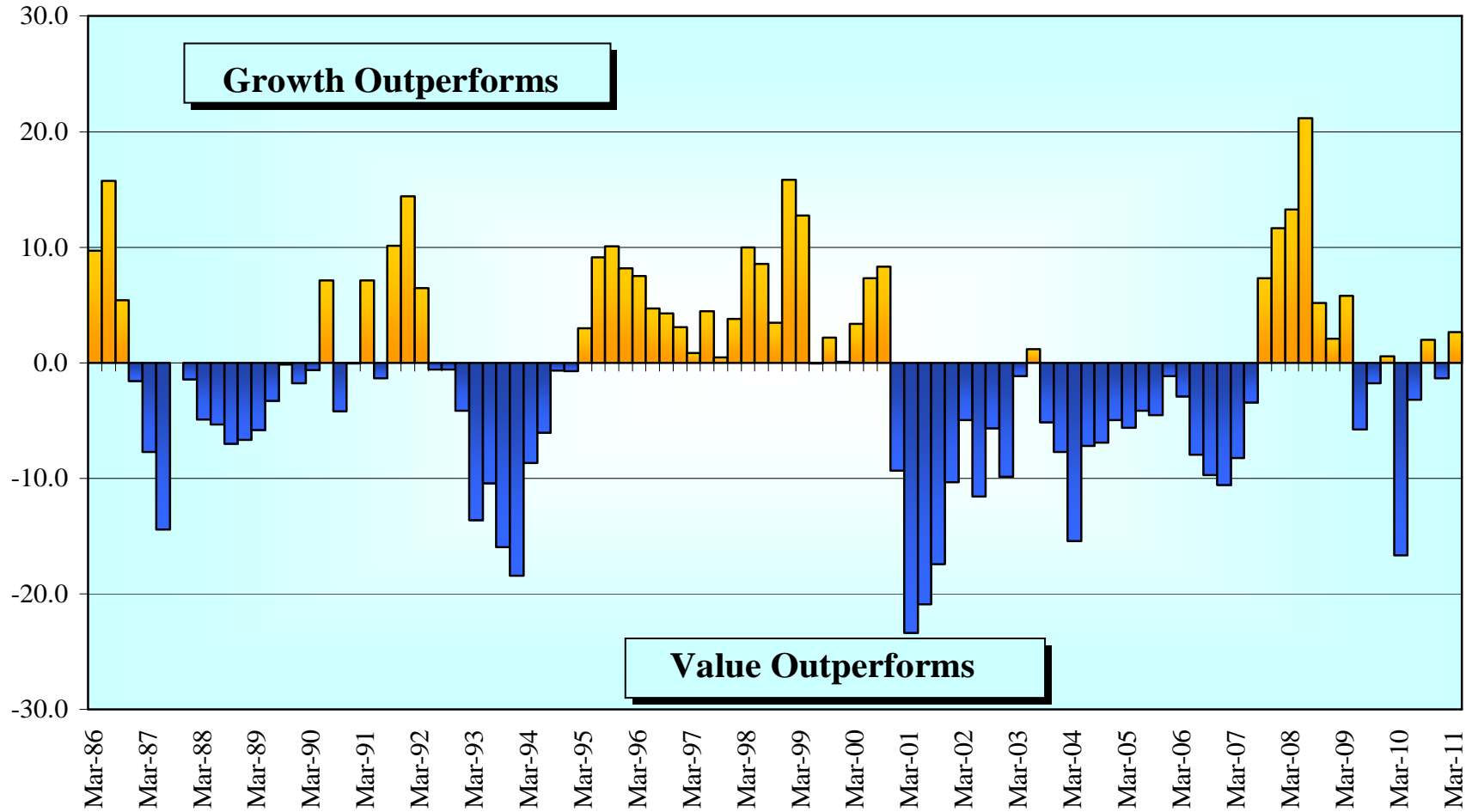
- Insight into Factors Affecting Stock Price
- Identify Competitors for Capital, Peer Group
- Enhanced S&P 500 Index

The Genesis of DeMarche's Research

- Absence of Academic or Practitioner Studies
 - Long-term Time Frame
 - Multi-Cap & Style Differentiated
 - Multiple Use of Cash Strategies
 - Segregated by Economic Sector & Industry

DeMarche Growth vs. DeMarche Value

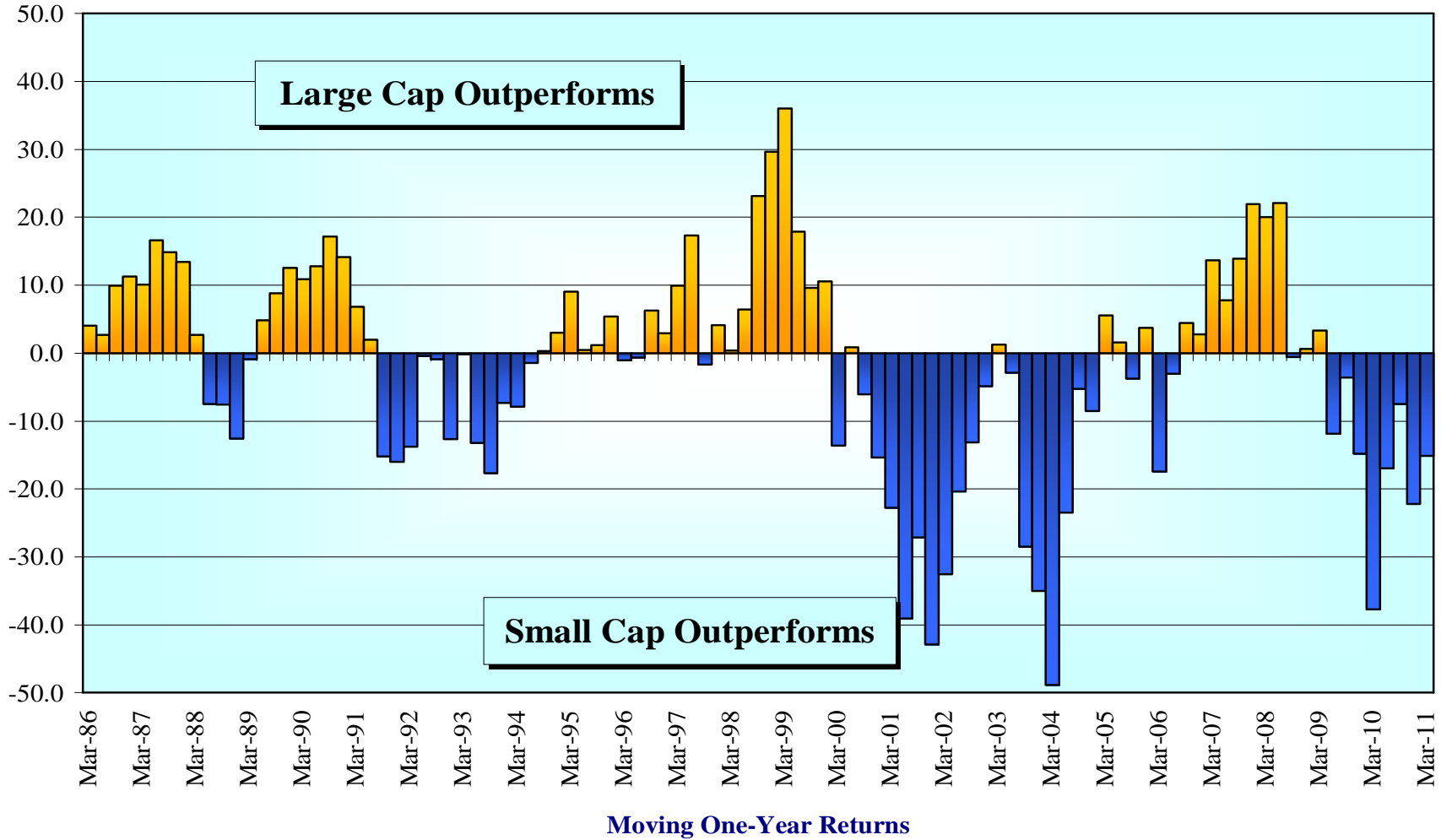
Percent Spread



Moving One-Year Returns

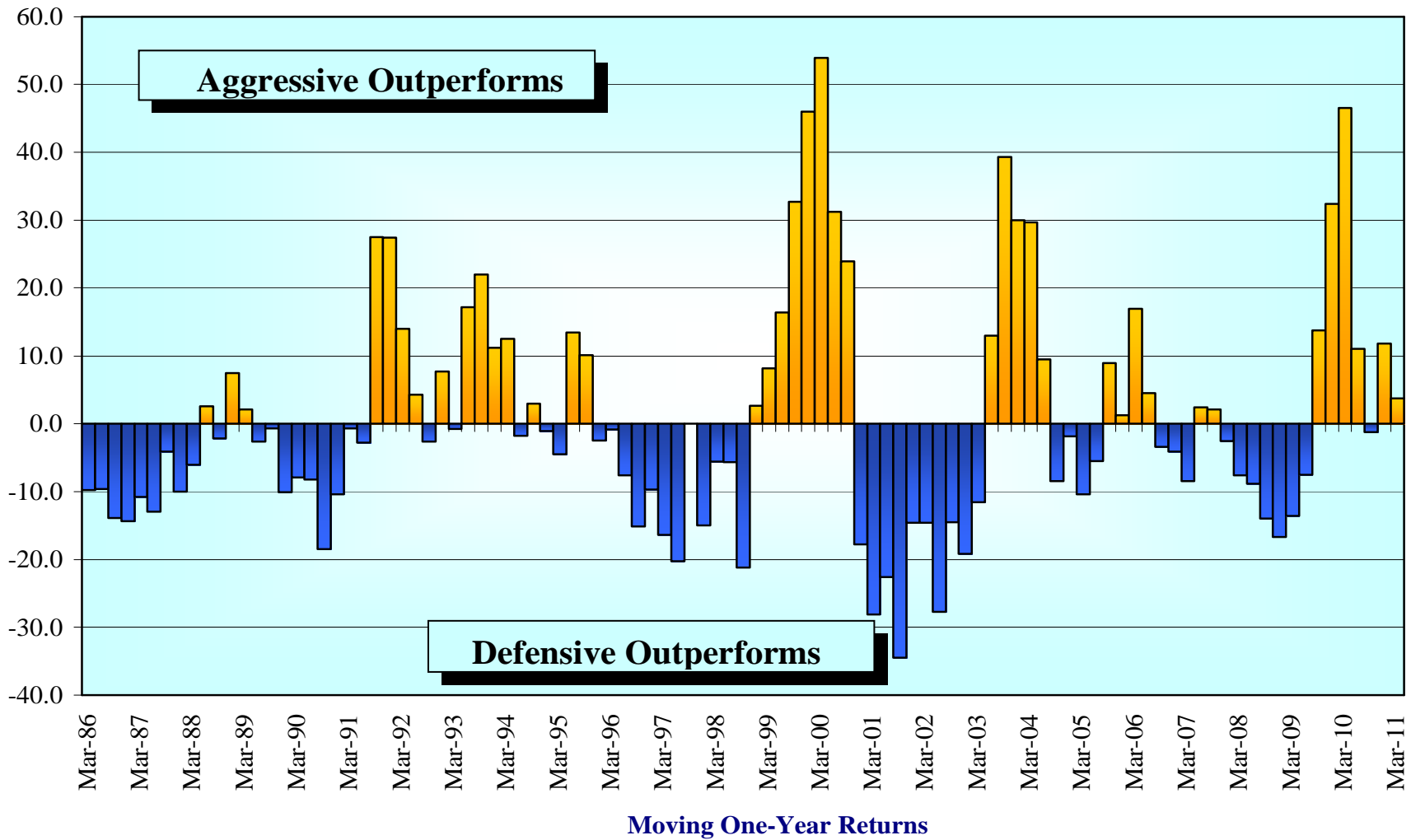
DeMarche Large Cap vs. DeMarche Small Cap

Percent Spread



DeMarche Aggressive vs. DeMarche Defensive

Percent Spread

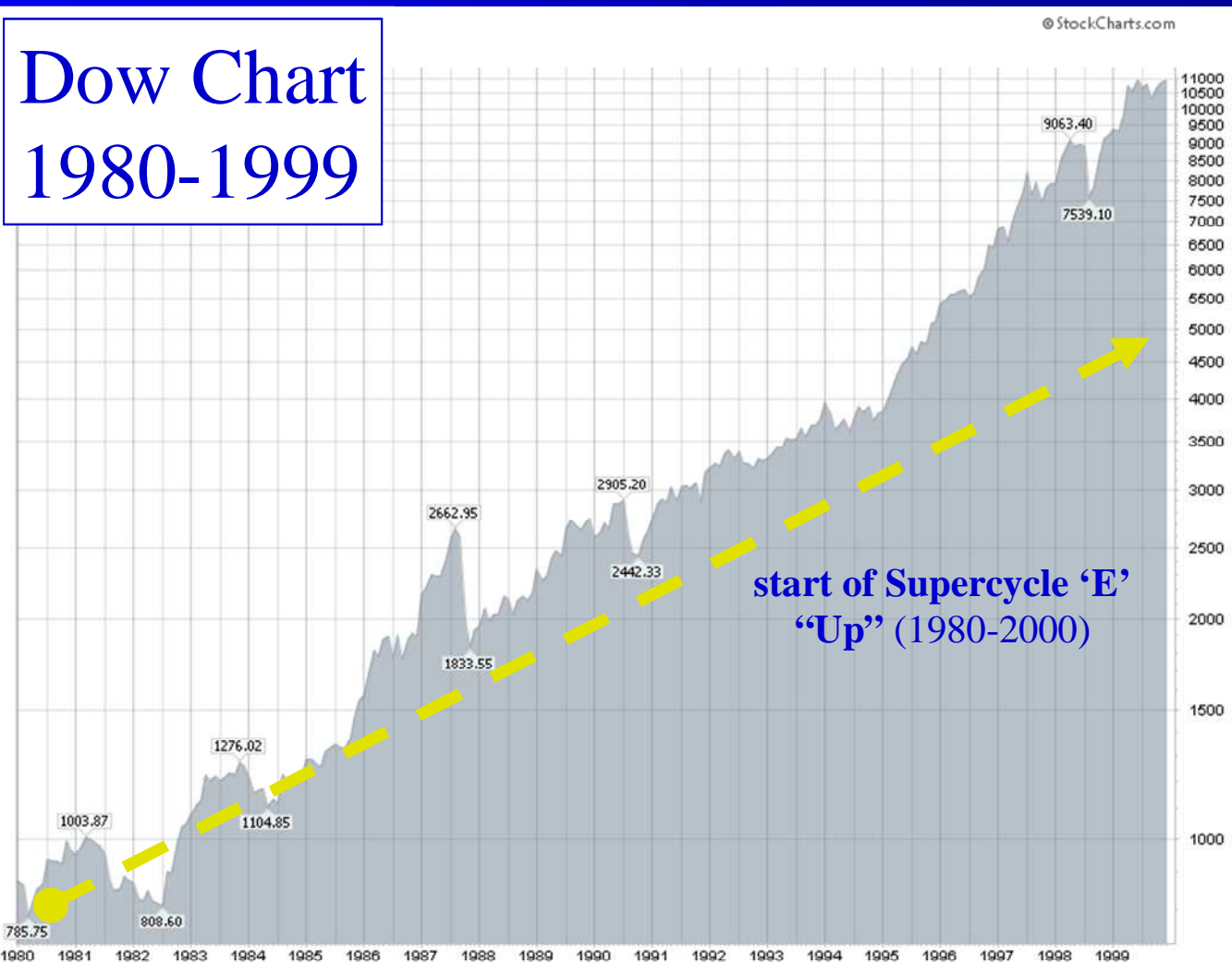


DeMarche Associates

Introduction to Supercycles

Past markets had bulls & bears, but also were part of “Supercycles” with longer upward & downward trends

DeMarche Associates



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Dow Chart 2000-2010



start of Supercycle 'F'
"Down" (2000 - ?)

Where & when
does this one end?

Uses of Cash Study

Definitions and Background

- Date of Study: 1990 – 2010
- 4,000+ stocks
- Subsequent annualized returns analyzed
- (for one, **three**, and five years)
- Minimum Liquidity Requirement

Uses of Cash Study

Metrics (Distributing to Shareholders)

1. Dividend Policy (Primarily Increases)
2. Stock Buy-Backs
(Avg. Annual Repurchases Over Past 5 Years)

Uses of Cash Study

Metrics (cont.)

(Reinvesting in the Business)

3. Mergers and Acquisitions (M&A)
(Cash M&A/Assets Over Past 5 Years)
4. Research and Development (R&D)
(Total 5-Year R&D/Total Sales)
5. Capital Expenditure (CapEx)
(Total 5-Year CapEx/Assets)

Uses of Cash Study

Cap Size Ranges

- Large Cap: \geq \$20 Billion
- \$2 Billion \leq Mid Cap $<$ \$20 Billion
- \$600 Million \leq Small $<$ \$2 Billion
- Micro: $<$ \$600 Million

DeMarche Style Factors

VALUE TO GROWTH SPECTRUM



Value Stocks	Factor	Growth Stocks
High	Book-to-Price	Low
High	Sales-to-Price	Low
High	Dividend Yield	Low
High	Cash Flow Yield	Low
Low	Dividend Growth	High
Low	Asset Growth	High
Low	Earnings Growth	High
Low	Relative Price Strength	High

Uses of Cash Study

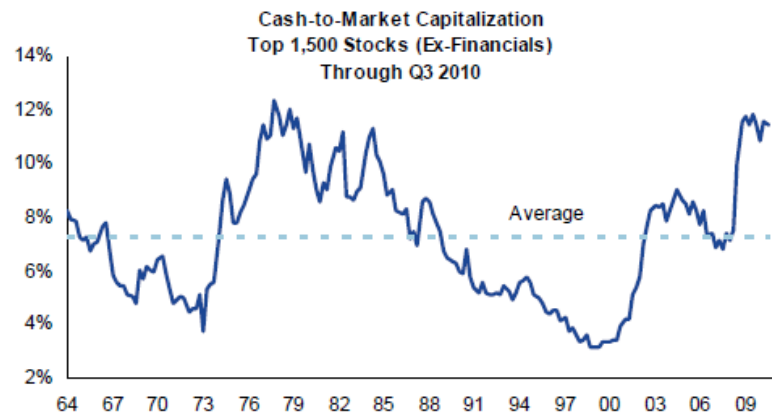
Other Metrics Included

- Degree of Leverage
- What about P/E?
- Does Free Cash Flow Matter?

Company Fundamentals-Corporate America is Strong As Ever!

Exhibit 37

**Cash Relative to Market Capitalization Is Near
Historic Highs**



Source: Factset, Morgan Stanley Research

Exhibit 39

Corporate Debt Levels Are Also Healthy



Source: Factset, Morgan Stanley Research

Uses of Cash

Increase Dividends?

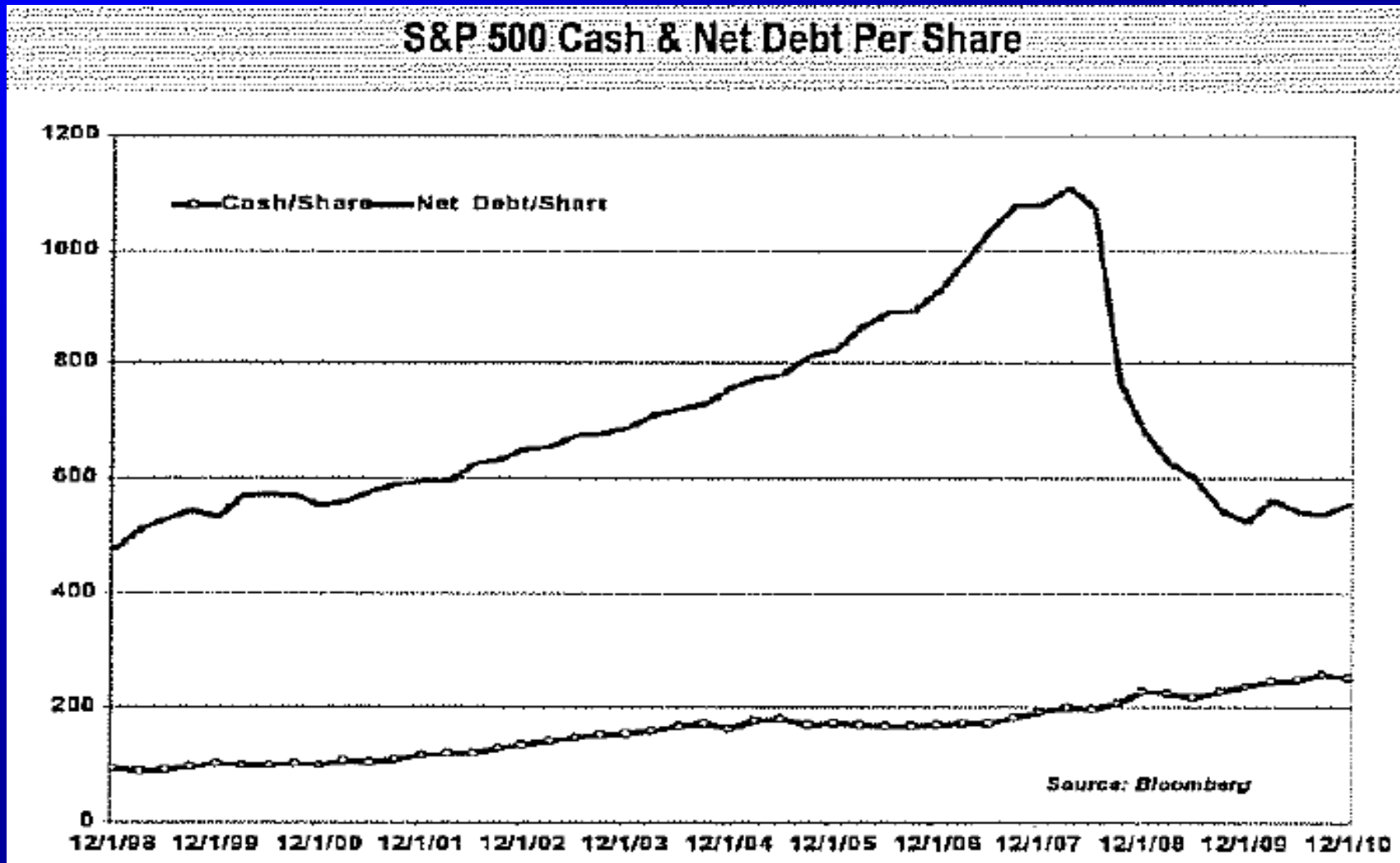
Share Repurchases?

Mergers & Acquisitions?

Capital Expenditures?

Hire Workers/Increase Compensation?

Debt Levels Much Lower



2010 Study Findings

Review of Total Returns by Cap Size & Style

Three-Year Annualized Returns (1990-2010)

Total Universe of Stocks	6.26%
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Large Cap Stocks	7.51%
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Small Cap Stocks	7.28%
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Value Stocks	7.07%
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Growth Stocks	5.39%
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All Stocks

Uses of Cash Return Rankings

Use of Cash	Return Ranks	
	1 Year	3 Year
Dividend Increases	1	1
Buy-Backs	2	2
M&A	3	3
R&D	4	4
CAPEX	5	5

Large-Cap Stocks

Uses of Cash Return Rankings

Use of Cash	Return Ranks	
	1 Year	3 Year
Dividend Increases	1	1
Buy-Backs	3	2
M&A	4	4
CAPEX	5	5
R&D	2	3

Small-Cap Stocks

Uses of Cash Return Rankings

Use of Cash	Return Ranks	
	1 Year	3 Year
Dividend Increases	1	1
Buy-Backs	2	2
M&A	4	3
CAPEX	3	4
R&D	5	5

Growth Stocks

Uses of Cash Return Rankings

Use of Cash	Return Ranks	
	1 Year	3 Year
Dividend Increases	1	1
Buy-Backs	2	2
M&A	3	3
CAPEX	4	4
R&D	5	5

Value Stocks

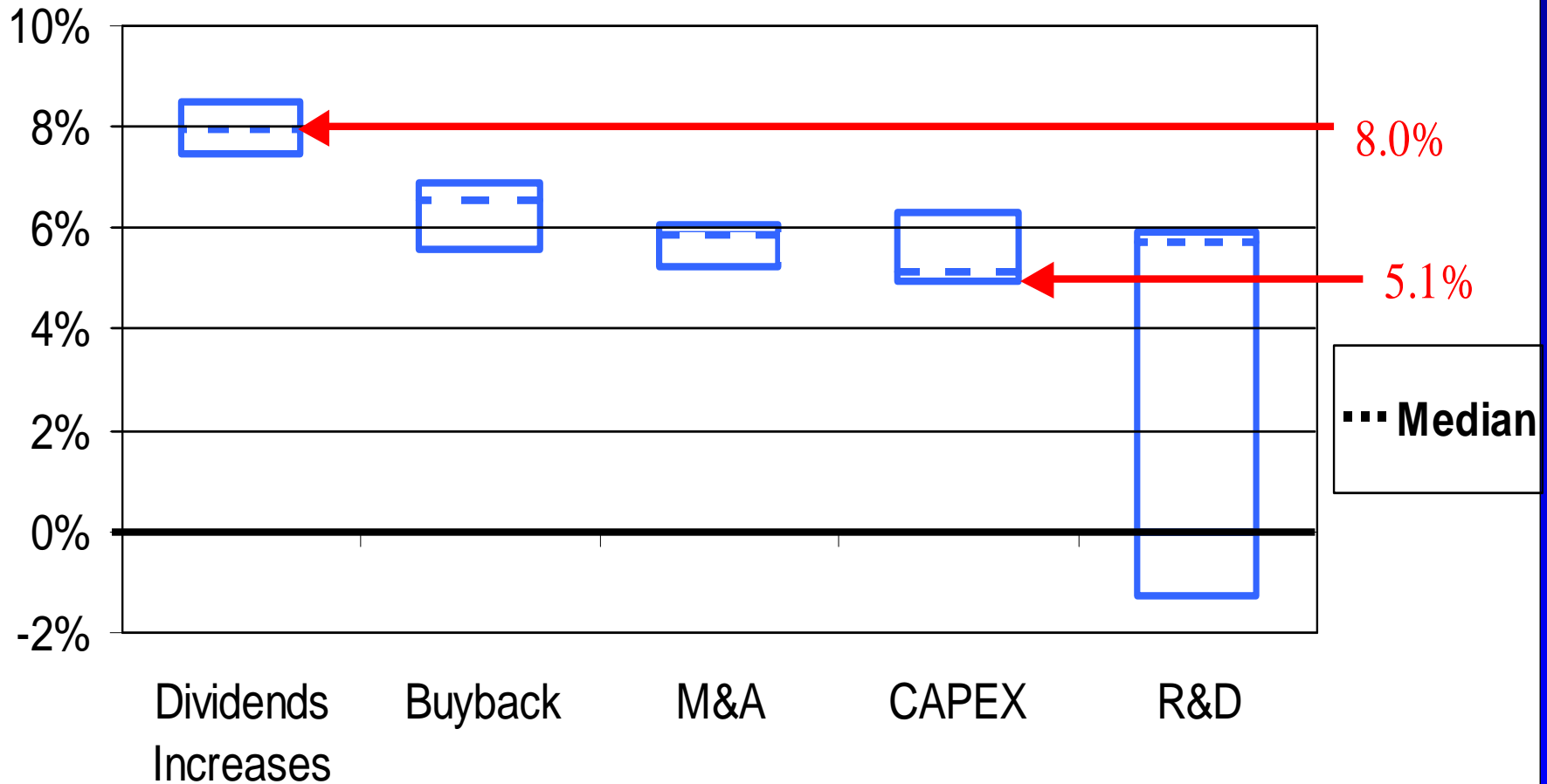
Uses of Cash Return Rankings

Use of Cash	Return Ranks	
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Buy-Backs	2	2
M&A	3	3
CAPEX	4	4
R&D	5	5

All Stocks

Three-Year Annualized Return Spreads (1990-2010)

Median Return



* Median 3-Year Return For All Stocks: 6.26%

“Drill-Down” on Buybacks

- By Cap Size & Style
- By Sector

Buyback Background

2007 - \$589 bb

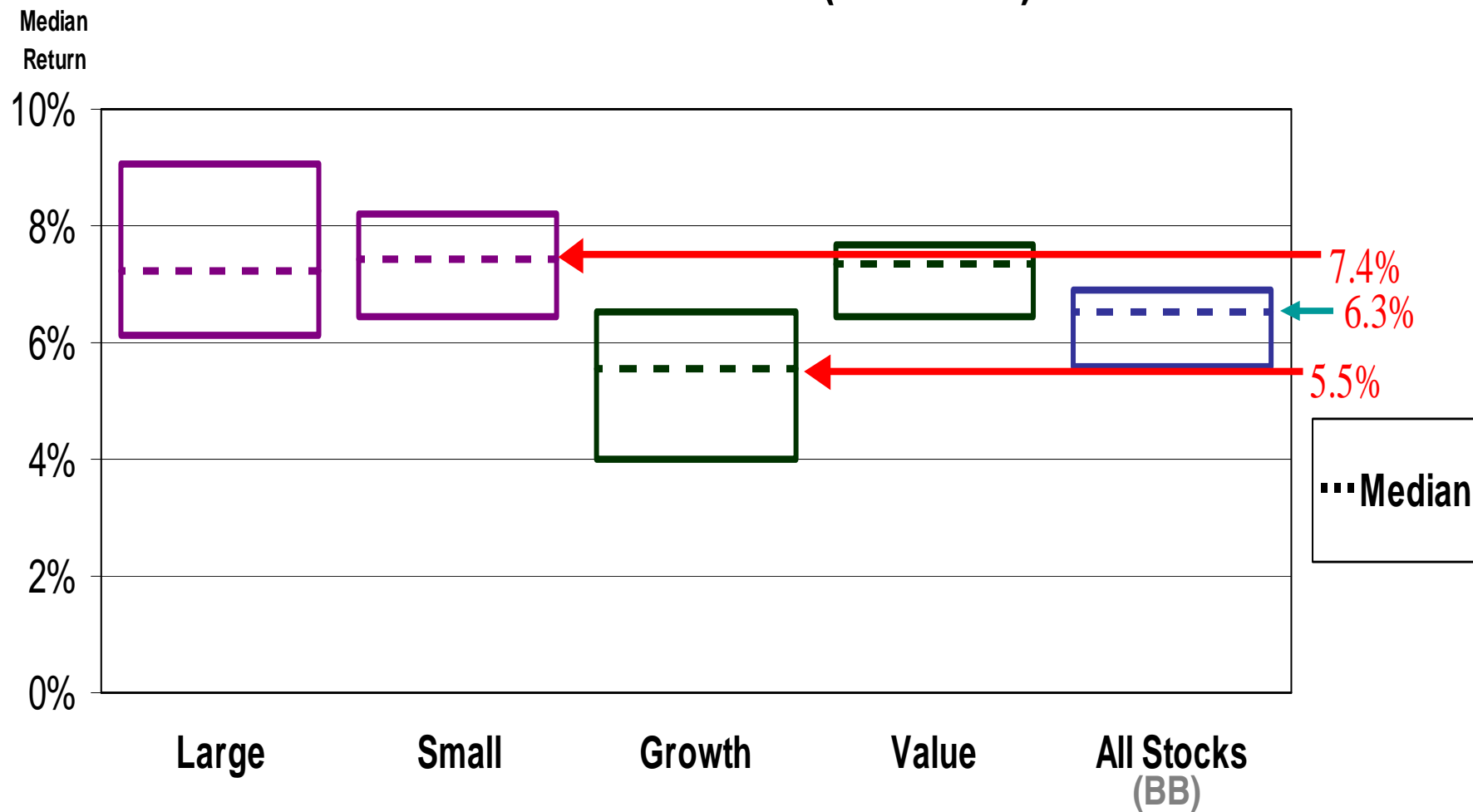
2008 - \$340 bb

2009 - \$200 bb

2010 - \$299 bb

Source: NY Times

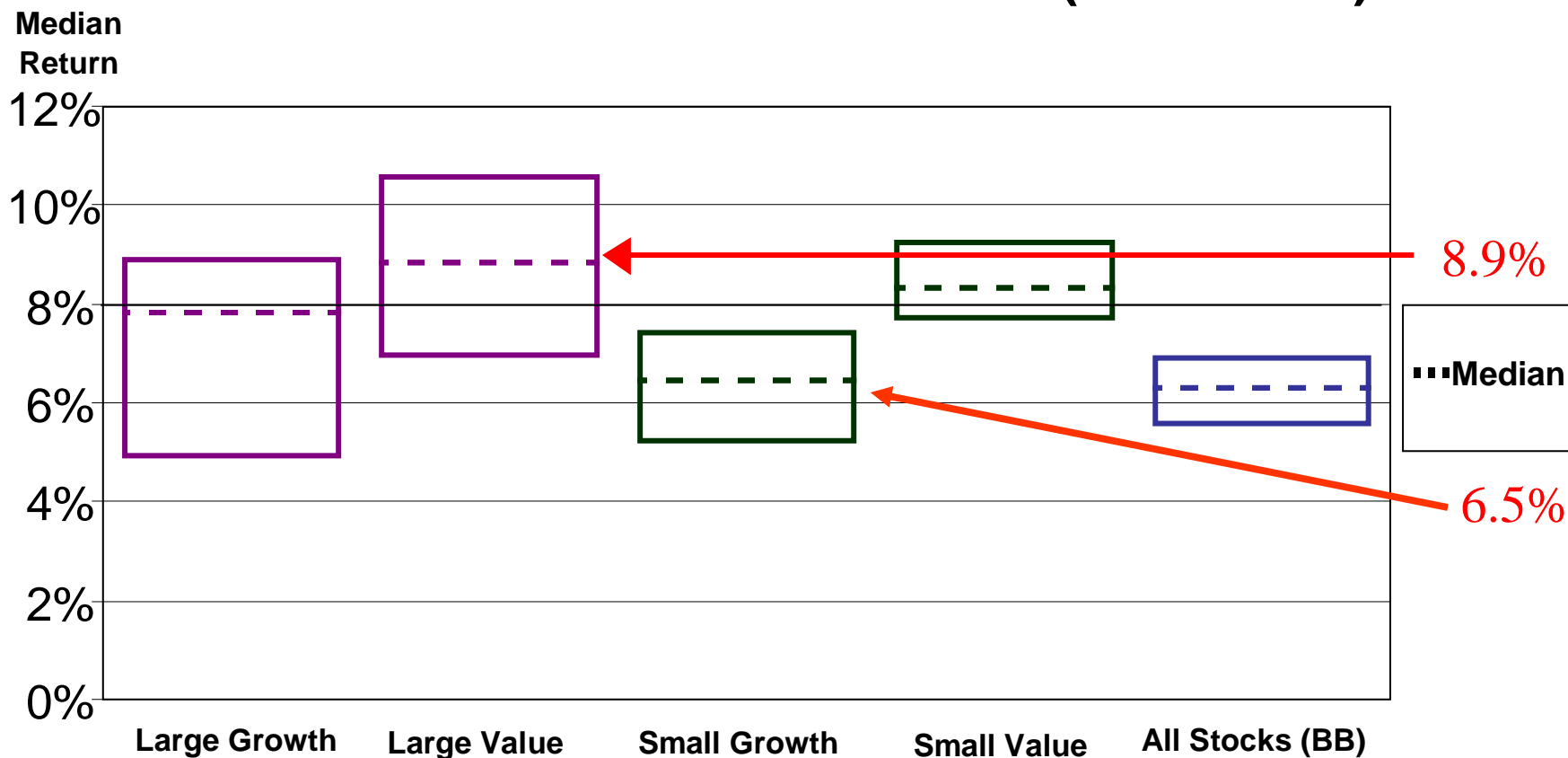
Treasury Stock Buybacks by Cap Size & Style Three-Year Annualized Returns (1990-2010)



* Median 3-Year Return For All Stocks: 6.26%

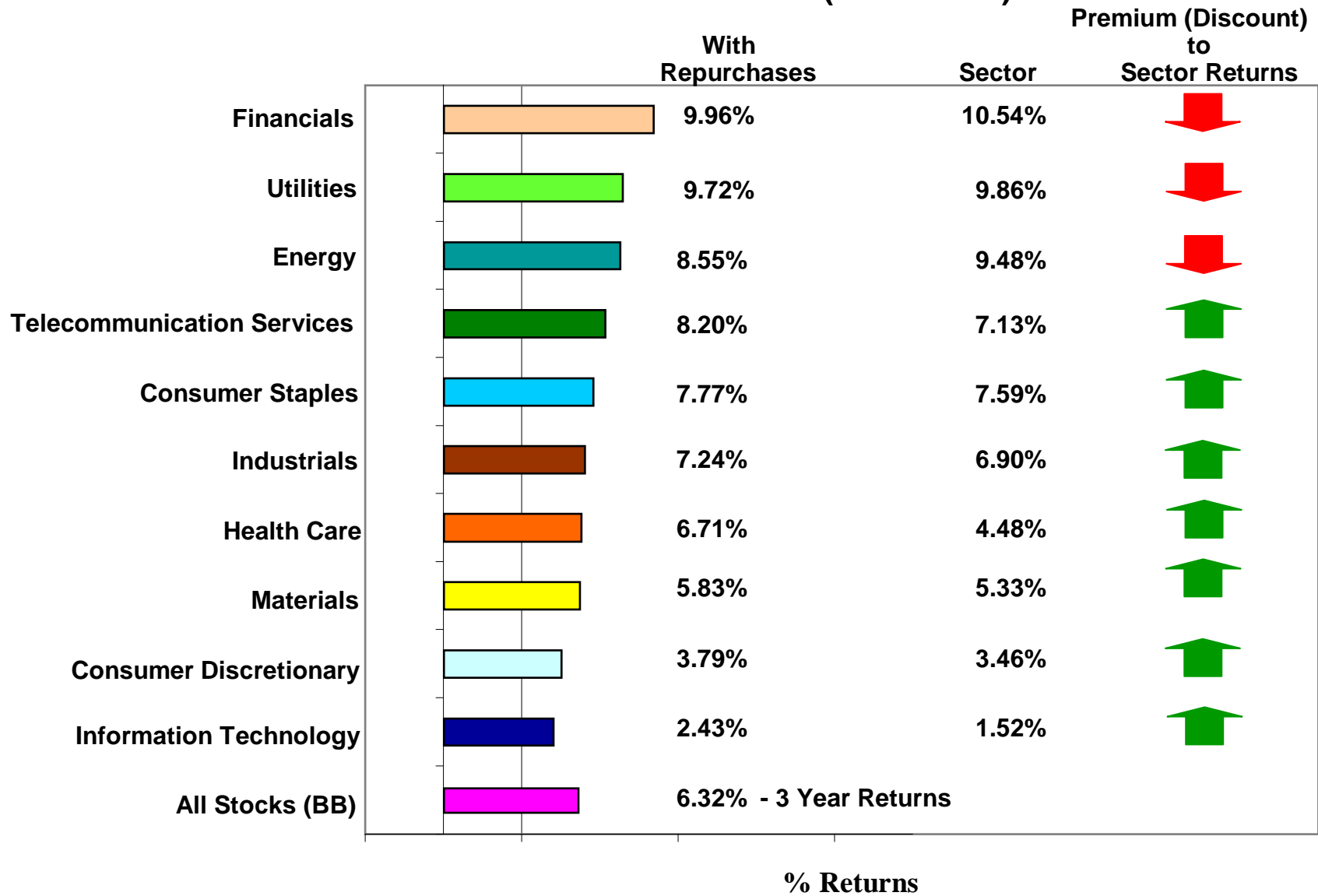
Treasury Stock Buybacks by Cap Size & Style

Three-Year Annualized Returns (1990-2010)



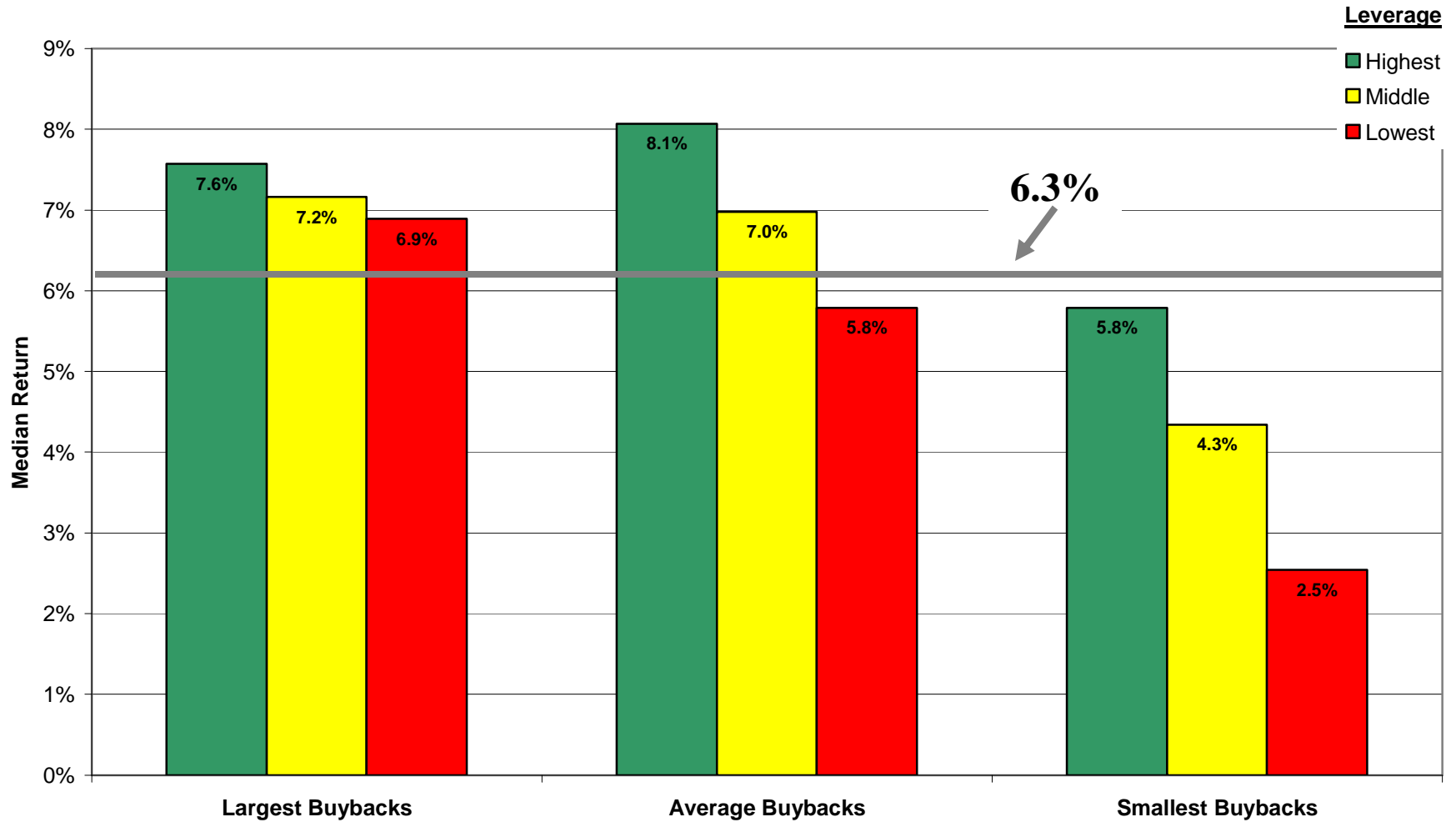
* Median 3-Year Return For All Stocks: 6.26%

Stock Repurchases 1990-2010 Three-Year Annualized Return (10 Sectors)



* Median 3-Year Return For All Stocks: 6.26%

Effects of Leverage on Buybacks Annualized Three Year Returns (1990 - 2010)



* Median 3-Year Return For All Stocks: 6.26%

“Drill-Down” on Dividends

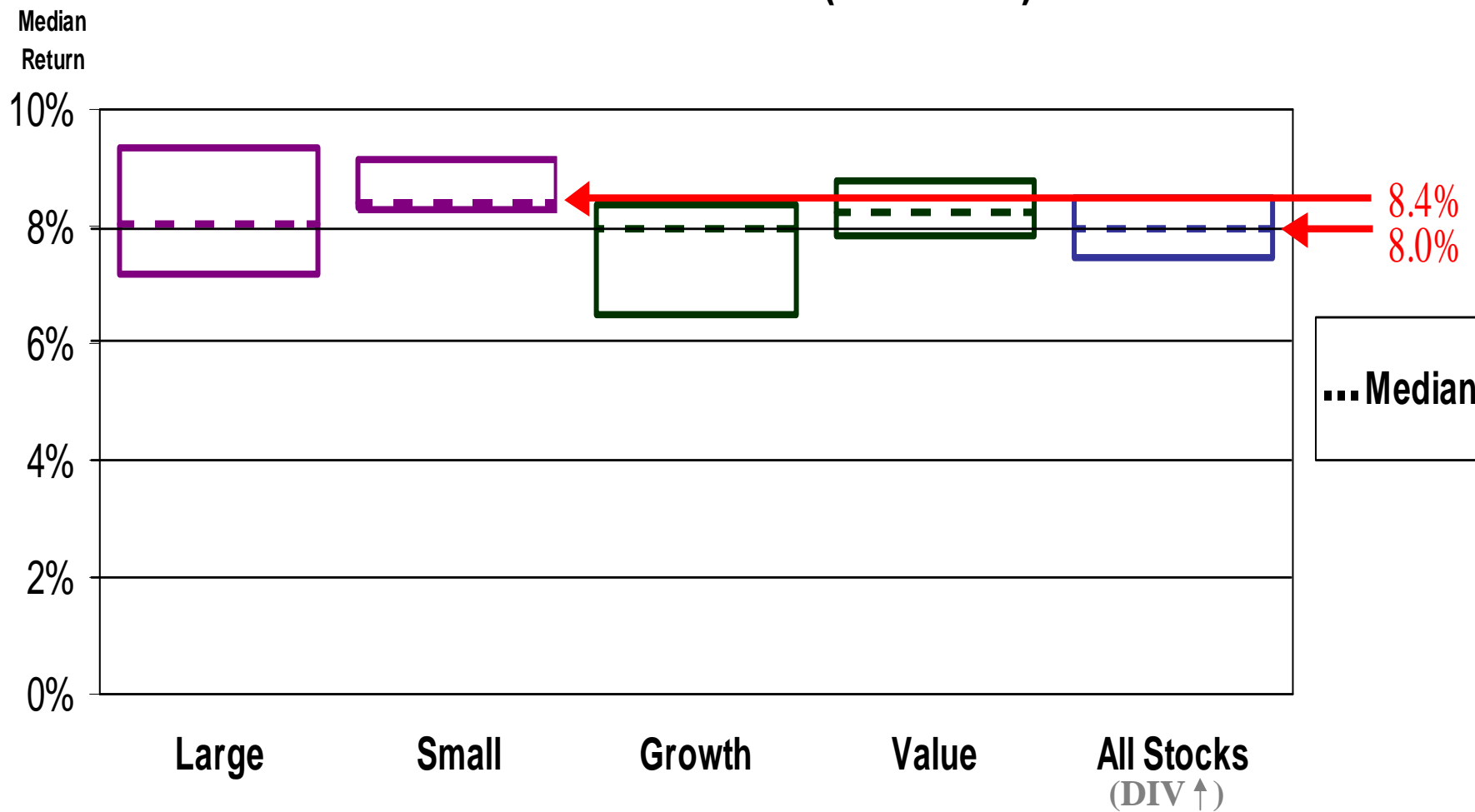
- By Cap Size & Investment Style
- By Sector
- Stratify by P/E
- Summary of Various Dividend Strategies

Dividend Background

S&P 500 Companies

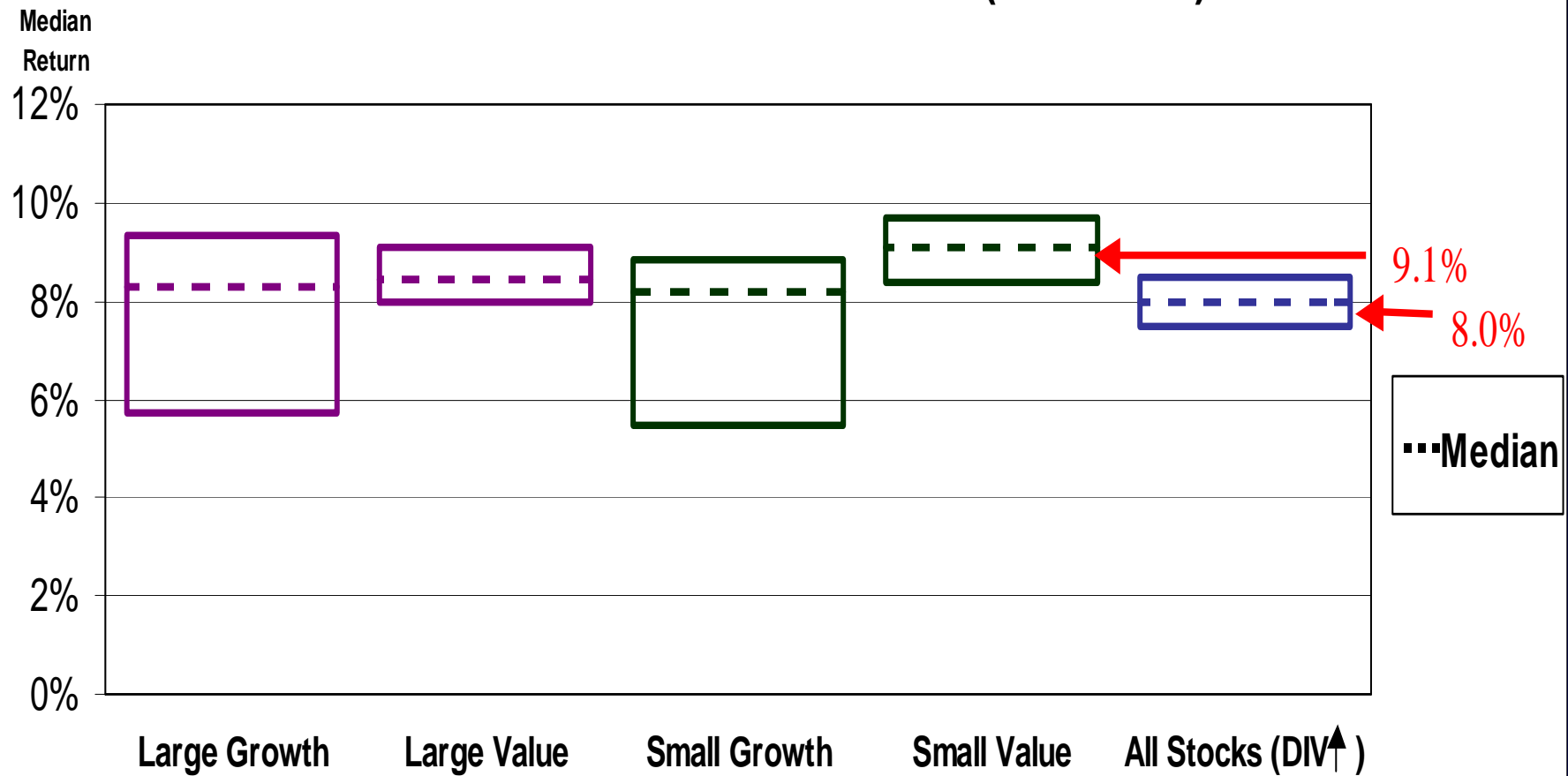
	<u>2008</u>	<u>2009</u>	<u>2010</u>
Dividend \$s Paid	n/a	n/a	n/a
Companies Paying Dividends	372	363	370
Dividend Increases	241	247	247
Dividend Reductions	62	78	4

Dividend Increases by Cap Size & Style Three-Year Annualized Returns (1990-2010)



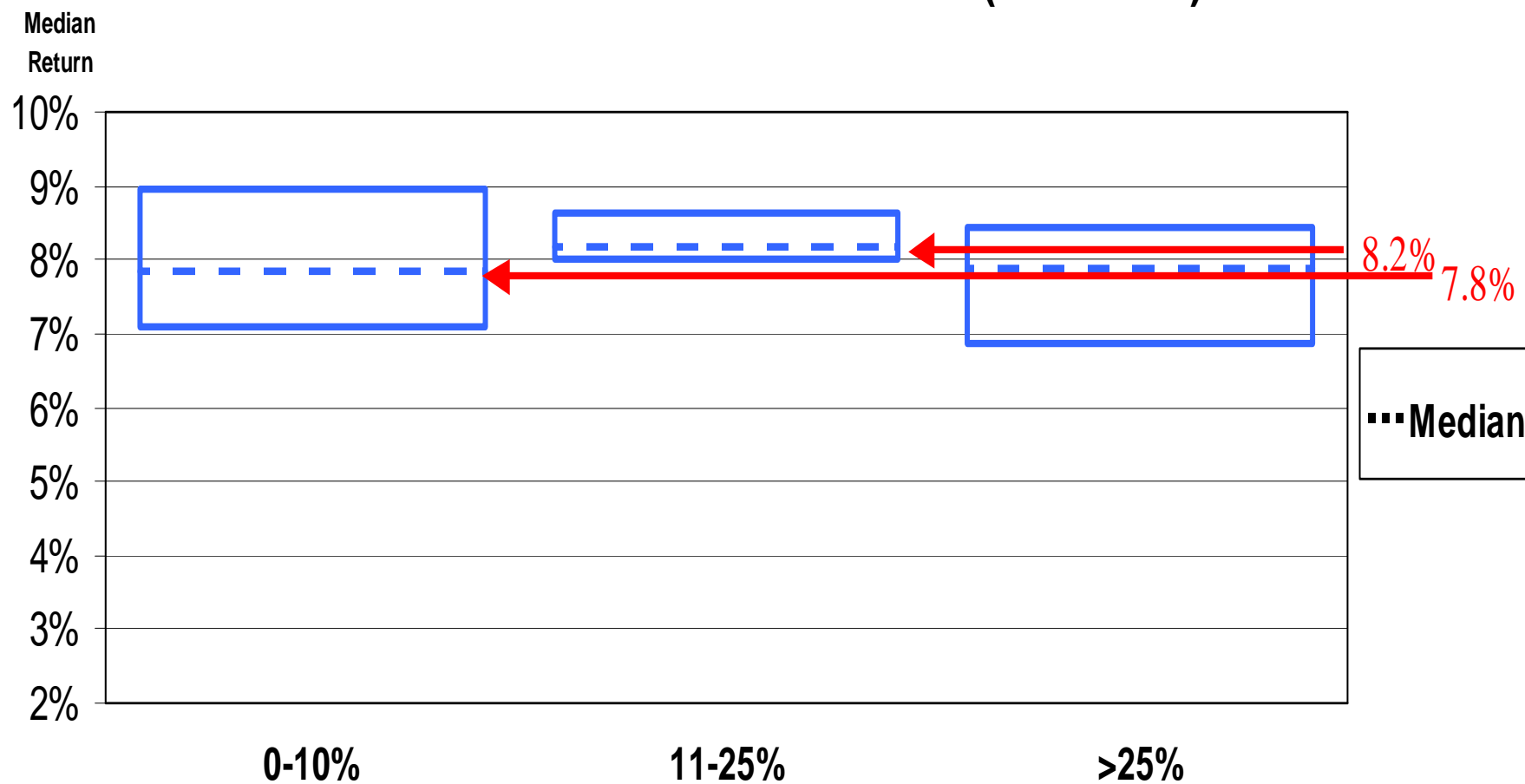
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Dividend Increases by Cap Size & Style Three-Year Annualized Returns (1990-2010)

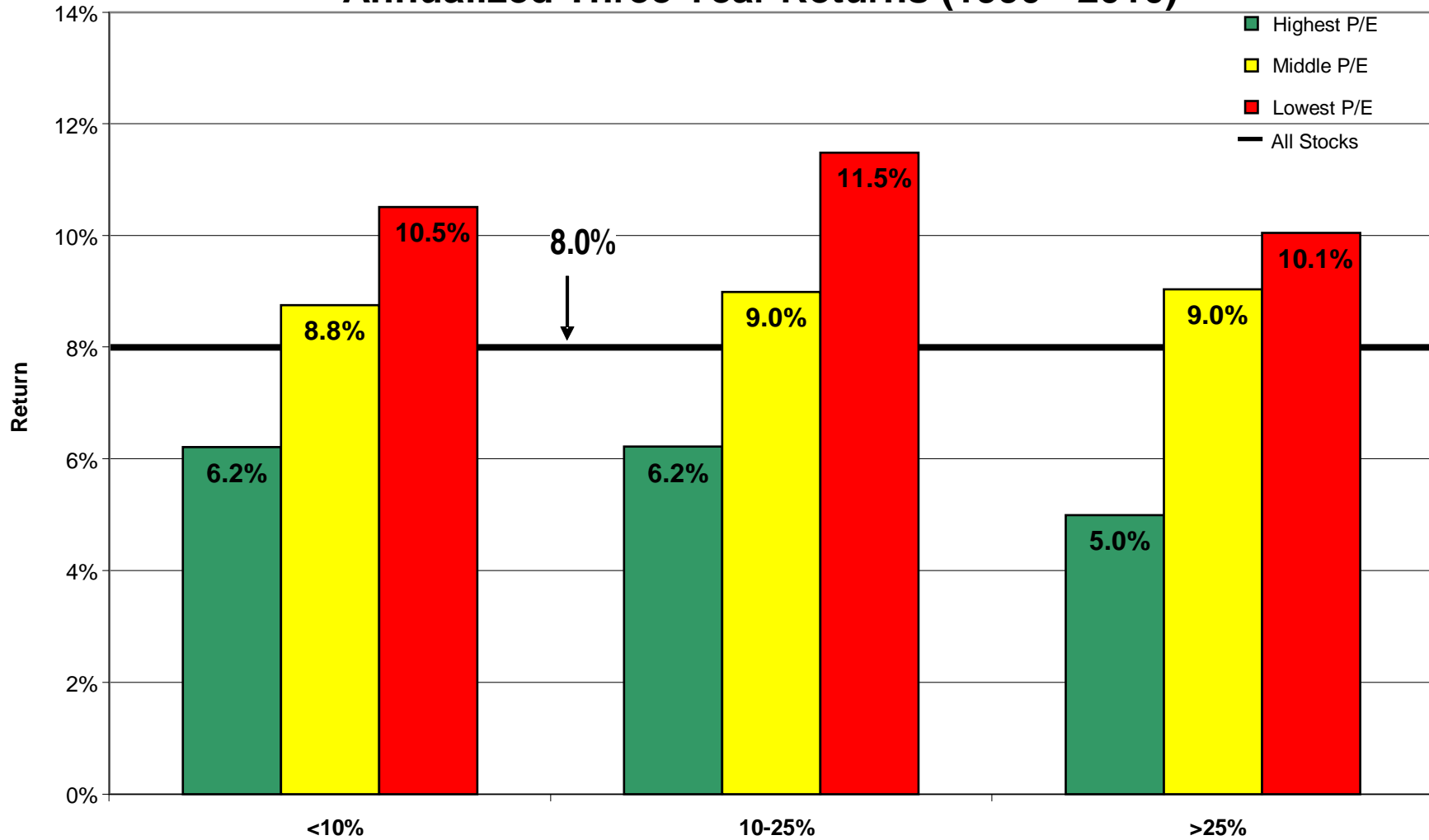


* Median 3-Year Return For All Stocks: 6.26%

Level of Dividend Increases Three-Year Annualized Returns- (1990-2010)

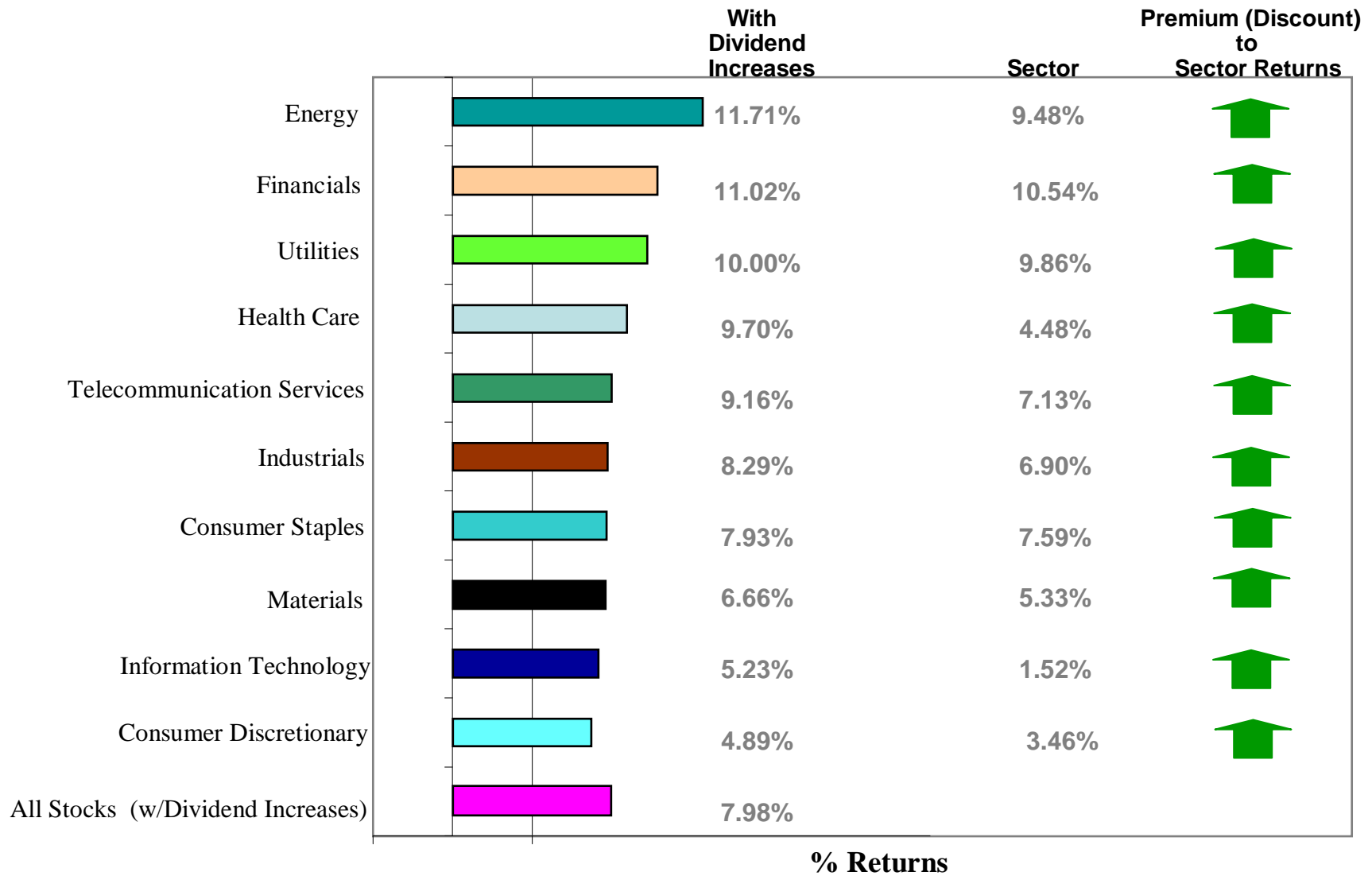


Subsequent Returns Dividend Increases Segregated by P/E - All Stocks Annualized Three Year Returns (1990 - 2010)



* Median 3-Year Return For All Stocks: 6.26%

Dividend Increases (By Economic Sector) 1990-2010 Three-Year Annualized Return (10 Sectors)



* Median 3-Year Return For All Stocks: 6.26%

Summary of Different Dividend Strategies

Three-Year Annualized Returns

1990-2010

Pay Dividends/ No Change	7.82%
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Initiations	5.64%
Terminations	5.52%

Increases	7.98%
Decreases	8.06%

Ranking Dividend Policy Decisions (Top 5)

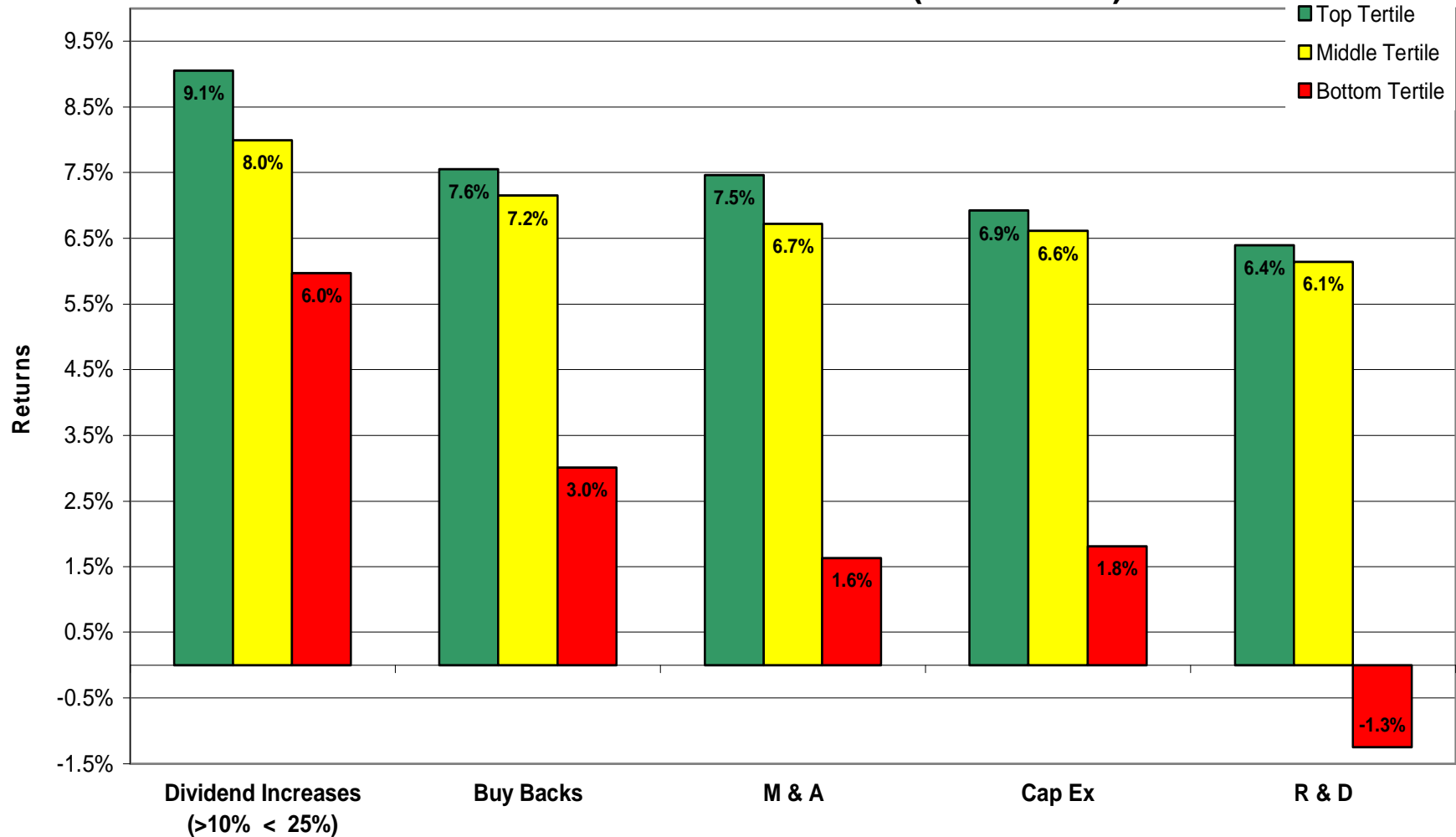
3 Year Annualized Returns (1990-2010)

Increasing Dividends (11-25%)	8.2%
Decreasing Dividends (11-25%)	8.1%
Increasing Dividends (>25%)	7.9%
Increasing Dividends (0-10%)	7.8%
Keeping Dividends Stable	7.8%

Free Cash Flow

Does Free Cash Flow
Make a Difference?

Free Cash Flow / Assets (Results For All Stocks) Returns By Use Of Cash Category Annualized Three Year Returns (1990 - 2011)



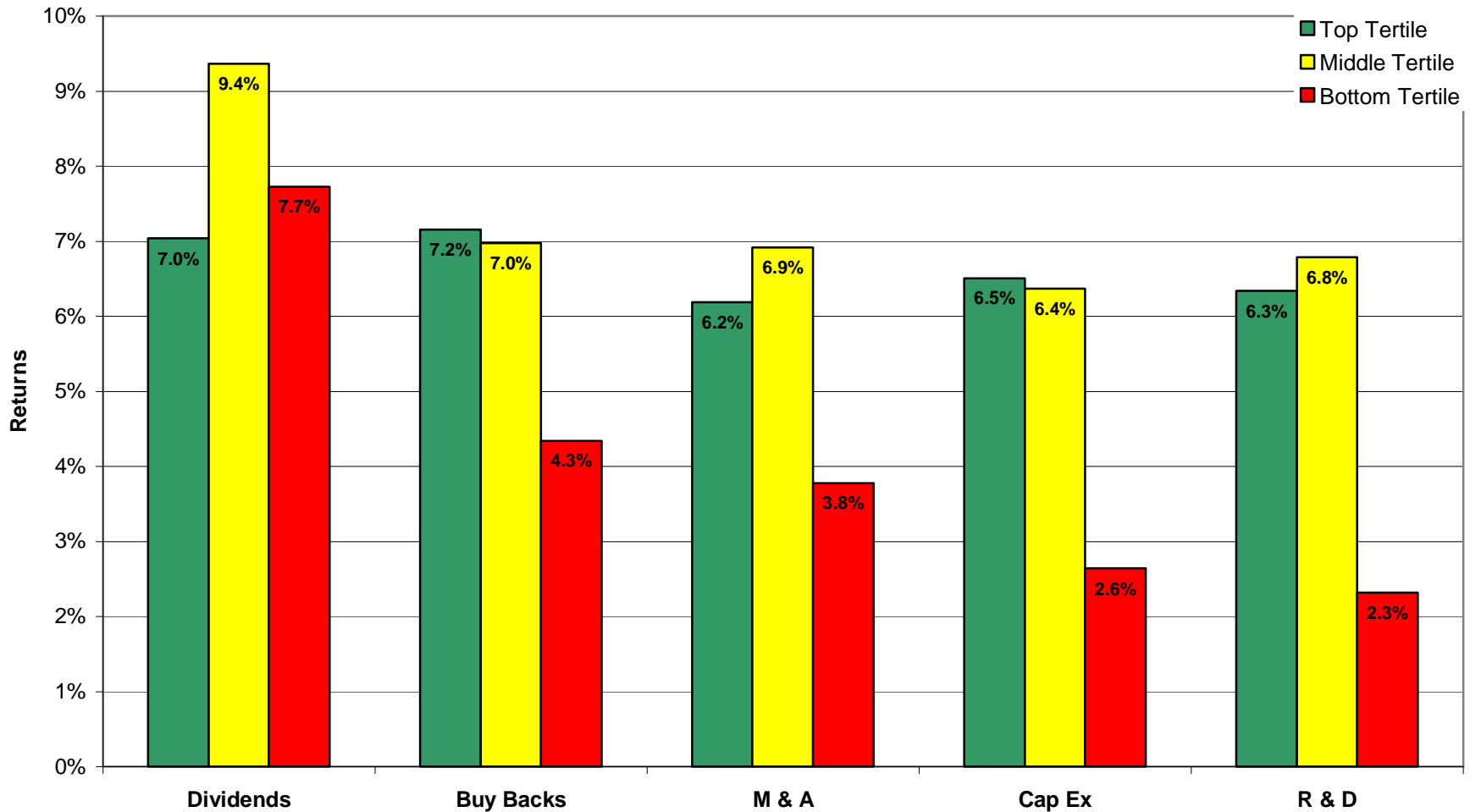
* Median 3-Year Return For All Stocks: 6.26%

Does Debt Matter?

Debt to Total Capital (Results For All Stocks)

Returns By Use Of Cash Strategy

Annualized Three Year Returns (1990 - 2010)



* Median 3-Year Return For All Stocks: 6.26%

Conclusions

In General (When Ranking 4,000+ Stocks)

- Maintaining dividends is the best use of cash
- Increasing dividends is the second best use of cash
- Buy-Backs are the third best use of cash
- M&A in number four spot
- CapEx and R/D rank in the bottom

Conclusions

- Returns Depend On Company's "DNA"
 - Large outperformed Small
 - Value outperformed Growth
 - Dividend Increases had biggest + effect on Growth stocks (238 bps)
 - Buy-Backs had biggest + effect on Value stocks (18 bps)

Conclusions

		<u>Growth Stocks</u>	<u>Value Stocks</u>
Universe 3-Year Annualized Return	→	5.39%	7.07%
Dividend Increases 3-Year Annualized Return	→	7.78%	8.25%
Premium Added		238bps	118bps

Conclusions

		<u>Growth Stocks</u>	<u>Value Stocks</u>
Universe 3-Year Annualized Return	→	5.39%	7.07%
Buyback 3-Year Annualized Return	→	5.50%	7.25%
Premium Added		11bps	18bps

Conclusions

- High Leverage doesn't appear to negatively impact returns
- High Free Cash Flow appears to positively impact returns

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