

MARKET OVERVIEW: THE UPSIDE OF DIVIDENDS

THE STRATEGIES

INCOME-EQUITY STRATEGY

A diversified dividend-growth strategy providing high current income, growth of income, and growth of underlying principal. Stocks are high quality, high yield, and are projected to have a rising stream of income.

RISING DIVIDEND PLUS

A portfolio of large- and mid-cap companies in which dividend growth is the key variable. We focus on companies with proven long-term success and special current opportunities and incorporate technical analysis into the portfolio process. RDP should generally be considered a value/momentum strategy.

DISTRIBUTION / MERGING UTILITIES

An opportunistic portfolio of primarily regulated local monopoly distribution utility companies with strategic and financial takeover appeal.

GLOBAL UTILITIES + INFRASTRUCTURE

By focusing on opportunities in the broad, global utilities industry, this portfolio seeks to participate in the dynamic growth potential of the most important economic sector (essential services and infrastructure worldwide).

MLP STRATEGY

A high-yielding portfolio (with tax-deferred income) primarily composed of pipelines and energy facilities we feel have strong prospects for growth of distributions. Revenues are derived from durable and stable business assets that generate attractive yields to the unit holders while allowing for long-term organic growth.

There is considerable hysteria about dividends in the media at the moment, but journalists and investors have not been very diligent about peeking under the headline numbers to see what's really happening. Indeed, the number of dividend decreases has risen sharply, and the increase-to-decrease ratio has declined (though it's still above 3 to 1). But the changes of late have been quite narrowly focused: on financial companies (oh really?), companies that rely on financing, and companies that are most sensitive to declines in economic activity. The "silent majority" continues to pay dividends from current cash flows, and with over 1,700 dividend increases last year there are obviously a good many companies whose straits are hardly as dire as General Motors or the money center banks. The "big name" dividend cuts such as the money center banks, insurance majors, General Electric, Pfizer, and Dow Chemical are testament to the difficult economic conditions we face today. But at the same time, we have seen dividend *increases* across all of our portfolios. Sectors such as health, consumer nondurables, pipelines, telecommunications, and utilities continue a regular course of dividend increases as though existing in a different world, a world of ample cash flow.

Historically, dividend stocks have performed extremely well after bear markets in general and after recession-induced bear markets in particular. To be sure, there are moments when it will seem that the only game in town is reflected in big daily jumps among the stocks most beaten down, but the data tells us this does not last. We reviewed the performance of the higher-yielding deciles after four key bear markets commencing in 1974, using the Fama-French data set. As you can see from the graphs on page 2, historically year 1 of recovery may or may not see excess return from higher dividend stocks. But as the holding period lengthens, so has the excess return of higher dividend stocks versus the broad market. Note that the 10-year period after the October 1990 bottom ends right in the teeth of the tech bubble—one of the few times when dividend-oriented portfolios seriously lagged—though dividend stocks picked up their trend of excess performance almost immediately. If you believe that a new tech bubble is imminent, dividend stocks might not be the way to go, but in most cases they have eventually emerged victorious after market bottoms.

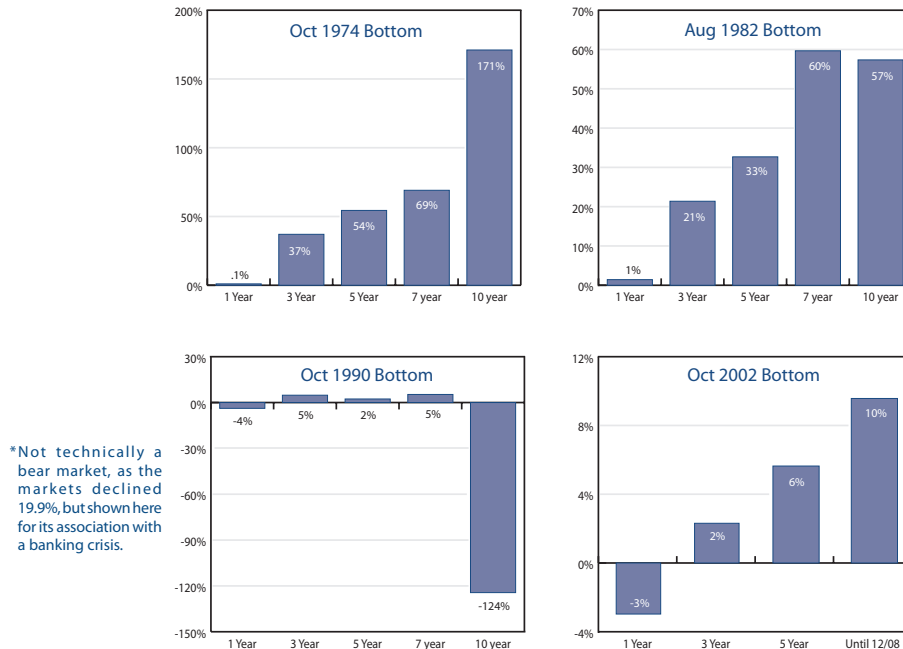
DIVIDEND STABILITY AND DIVIDEND GROWTH

Obviously, in order to replicate these kinds of results in a less inimical future, we need to insure dividend stability now, in these difficult times, as well as seeking the dividend growth that creates the sort of long-term compounding we strive to generate in our portfolios. Below we review some of the principles we have in place to evaluate dividend stability in our portfolios. Thresholds may vary somewhat depending on market conditions, but the principles have stood the test of time.

[more ▶](#)

“...as the holding period lengthens, so has the excess return of higher dividend stocks versus the broad market.”

Cumulative “Excess” Return of High Yield Stocks vs. S&P 500 (1, 3, 5, 7 & 10 Years from Bear Market Bottom)



Returns for both High Yield Stocks and S&P 500 are total returns. “High Yield Stocks” comprises deciles 6 to 10 from the data set created by Eugene Fama and Kenneth French called “Portfolios Formed on Dividend Yield,” in which they separate stocks into deciles based on their dividend yield. Their file was created by CMPT_DP_RETs using the 200901 CRSP database. We have utilized the value-weighted returns for this study. They compute D/P (in percent) breakpoints at the end of each June.

SELECTED INDICES

	1 st Qtr 09	1 Yr
S&P 500	(11.0)%	(38.1)%
Equity Inc	(10.6)%	(37.5)%
Util Fund	(10.7)%	(34.3)%
BC Long	(5.3)%	13.1%
R3UTIL	(9.5)%	(27.0)%
R1000	(10.5)%	(38.3)%
R3000	(10.8)%	(38.2)%
R3000Val	(17.0)%	(42.1)%
DVY	(23.1)%	(41.9)%

S&P 500 = Standard & Poor’s Index
 Equity Inc = Avg Equity Income Fund (Lipper)
 Util Fund = Avg Utility Fund (Morning Star)
 BC Long = Barclays Capital US Treasury Long
 R3UTIL = Russell 3000 Utilities
 R1000 = Russell 1000
 R3000 = Russell 3000
 R3000Val = Russel 3000 Value
 DVY = iShares Dow Jones Select Dividend ETF

Cash Flow. Dividends are paid from a company’s cash flow, so we need to be sure that cash flow after all necessary expenses adequately covers the dividend, with a margin of error to accommodate contracting economic times. With some exceptions, we’d like to see cash flow covering the dividend by about 3 to 1.

Interest Coverage. No company is going to pay a dividend if they’re having trouble paying fixed charges such as interest on debt, so coverage here must be ample. We prefer that interest charges are covered at least 4 to 1 by EBITDA.

Payout Ratios. The analysis for some companies, especially those with high depreciation, focuses on cash flow. But ultimately most companies pay dividends out of earnings. Except for utilities and a few others, we hope to see earnings at 2 to 1 relative to dividends.

Future Debt Obligations. The world has changed in this way: Companies that used to rely on refinancing of debt as part of the normal course of business can’t necessarily do that today. If substantial debt is due soon,

the company may be inclined to hoard cash—including cash that would otherwise be paid as a dividend—as a tool to pay off debt or make refinancing easier. Now, more than ever before, we need to know the schedule of debt due and the current resources available to pay it.

Reliability of Earnings and Cash Flow. This entails an evaluation of the basic business premise or model. How sensitive is it to economic conditions? Does the company make parts for domestic auto companies or does it sell groceries?

Herding. Some sectors, especially those with heavy financing needs such as REITs, have begun to withhold or reduce dividends prophylactically. As we’ve seen with the banks, in any given industry there always seems to exist pressure to manage in the way that your competitor is managing. Some companies may cut if all those around them are cutting.

Management Commitment. Many companies have an established formal dividend policy; others periodically affirm their commitment to their dividends. Would they cut dividends in order to acquire a weaker competitor

Bear Markets Since 1950

■ Recession-Induced Bear Markets highlighted

Top	Bottom	Decline	Months
8/2/56	10/22/57	-22%	14
12/12/61	6/26/62	-28%	6
2/9/66	10/7/66	-22%	8
11/29/68	5/26/70	-36%	18
1/11/73	10/3/74	-48%	21
11/28/80	8/12/82	-27%	21
8/25/87	12/4/87	-34%	4
3/24/00	10/9/02	-49%	31
Avg of All Bear Markets		-33%	15
Avg of Recession-Induced Bear Markets		-40%	20

Recoveries from Bear Markets Since 1950

Bottom	Top	Rise	Months
10/22/57	12/12/61	86%	50
6/26/62	2/9/66	80%	44
10/7/66	11/29/68	48%	25
5/26/70	1/11/73	74%	32
10/3/74	11/28/80	126%	73
8/12/82	8/25/87	229%	60
12/4/87	3/24/00	582%	147
10/9/02	10/9/07	102%	60
Avg of Bear Market Recoveries		166%	61

Price return only. Bear markets are identified as periods during which the market declined 20% or more. Recession-induced bear markets are defined as periods where generally recognized "recession" periods overlapped the bear markets we've identified. Source: Commodity Systems, Inc. (CSI) and Bloomberg

"...when a company raises dividends today, in an environment where there is so little competitive or peer pressure to raise, we think it speaks volumes about the company's true situation, its true prospects, its true view of shareholders, and the decisiveness and boldness of management."

in these unique times? Would they rather buy their own discounted debt? Can they afford to pay the dividend and also expand? Do they have a long history of paying? Increasing? We look and listen carefully to what management says and how they say it.

Special Factors. We keep abreast of how government regulations such as those under TARP may cause companies to cut dividends and to refrain from increasing them. Unrealized (book) losses on investments may require companies to increase reserves to make up for mark-to-market charges. New tax rulings may influence how a company views its dividends.

Dividend Growth. Last but far from least, we are alert as never before to companies that offer increasing dividends. These have always been the companies we favor, but today they are simply rarer—they are "standouts." Dividend increases tell us more about how business is going and how management feels about its prospects than any analyst or journalist ever can. Managements and boards hate to cut dividends—it is a kind of defeat—so increasing a dividend always involves a measure of bravery (as well as a recognition that the shareholders own the company and deserve some of the current profits). But when a company raises

dividends today, in an environment where there is so little competitive or peer pressure to raise, we think it speaks volumes about the company's true situation, its true prospects, its true view of shareholders, and the decisiveness and boldness of management. It is only the genuine Bravehearts that raise today.

GIPS Disclosure Information

Results are shown in US dollars. Included in the results are all unrestricted portfolios that have been managed for at least one full quarter, including those accounts no longer with the firm. Past performance is not indicative of future results. All composites contain fully discretionary accounts. Gross returns have been reduced by transaction costs and include the reinvestment of all income. Net return assumes a 3% annual advisory fee, charged quarterly, which includes wrap program fees. Other than brokerage commissions, this fee may also include portfolio monitoring, consulting services, custodial services, and investment management fees. Actual investment advisory fees incurred by clients may vary. Actual returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Miller/Howard Investments Inc. is an independently registered investment advisor specializing in multi-cap, core equity management and dividend strategies.

Miller/Howard Investments Inc. claims compliance with the Global Investment Performance Standards (GIPS®). Compliance with the GIPS standards has been verified for the period of January 1, 2000, through December 31, 2006, by Ashland Partners & Company LLP. To receive a complete list and description of Miller/Howard Investments' composites and/or a presentation that adheres to the GIPS standards, contact Marilyn Marecek at 845-679-9166, or write Miller/Howard Investments, PO Box 549, Woodstock, NY 12498, or marilyn@mhinvest.com.

Annual ADV Update

If you would like a copy of our current ADV Part II, please contact Marilyn at:

(845) 679-9166

or

marilyn@mhinvest.com.

The ADV will be mailed to you, free of charge.

Miller/Howard
I N V E S T M E N T S , I N C

PO Box 549
Woodstock, NY 12498

Contact Information:
Steve Chun
schun@mhinvest.com
www.mhinvest.com
(888) 282-8845