DIVIDEND ASSETS CAPITAL, LLC

DIVIDEND ASSETS CAPITAL – INVESTMENT STRATEGIES FOR RISING INCOME & GROWTH

QUARTERLY COMMENTARY **Q2**

NEWSLETTER **July 10, 2014**

AN ENIGMA WRAPPED IN A PARADOX

Winston Churchill, when asked to explain the Soviet Union's foreign policy around 1940, replied, "It is an enigma wrapped in a paradox." To some, this year's stock market is also an enigma. If one were to be an active reader of the financial press or a regular viewer of television business news, one might be confused by the market action of the stock indices. The price-only performance of the S&P 500 in 2013 was up 29.6%, and now the first half of 2014 has continued the upward spiral with an increase year-to-date of 6.1%. The total return for the index was 7.1%. The index performance suggests a favorable investment climate for equities for the past 18 months and yet the press reports suggest something different. We will try to peel away some to the layers of economic and geopolitical news so that a reasonable forecast can be made for the rest of the year. We have not changed our view from the first quarter that 2014 will be another up year for the S&P 500 Index and our rising dividend philosophy.

Perhaps the most perplexing data point was the final first quarter Gross Domestic Product (GDP) report that showed -2.9% growth for the period. Much of the blame for the poor showing was the severe winter weather that kept consumers at home and raised their energy bills. As the second quarter played out, the economic data presented an erratic pattern. Early in the quarter, housing data was disappointed, while employment showed some life. The first estimate of second quarter GDP will come in the last week of July and is forecast to be 3%+ as the weather of the first quarter melted into more seasonal spring temperatures. Both housing and employment data indicate improvement over the winter results. Forecasts by economists for the third and fourth quarters are trending in the low 3%+ range which, when added to the first quarter, would produce an average for the year of around the 2% level.

While we do not always agree with the Federal Reserve's policies, it appears suitable to pay attention to their view of the appropriate actions to be taken. The statement from the Federal Open Market Committee (FOMC) after their June meeting, together with the presentation by Chairman Yellen, suggested that the Fed would continue to be accommodative. Inflation is one of the indicators the Fed is watching. The announced target is 2% and the Consumer Price Index reached that level recently. The Fed's preferred measure of inflation is the Index of Personal Consumption Expenditures (PCE) which is still slightly below the 2% level. As consumer consumption is about 70% of GDP the ability of individuals to spend is very important, which leads to the second point that Ms. Yellen made after the FOMC meeting in June. Wage increases have been lagging behind price increases. Consumer purchases in May adjusted for inflation fell slightly which was the second month in a row. The Fed would like to see more wage growth. At Ms. Yellen's press conference, she stated, "My own expectation is that as the labor market begins to tighten, we will see wage growth pick up some. If we were to fail to see that, frankly I would worry about downside risk to consumer spending." We, too, will be watching wage growth.

The June employment report from the Bureau of Labor Statistics provided some pleasant reading as 288,000 workers were added to US payrolls, which was enough to drop the unemployment rate to 6.1%. Average hourly earnings of employees on nonfarm payroll has risen by 2.0% for the past 12 months, just slightly behind the Consumer Price Index for All Urban Consumers and the labor force participation rate was 62.8%, where it has been for three months in a row.

On the geopolitical front, the news seems only to get worse. The theaters of operation increase almost daily. Domestically, the gridlock has become a constant, as the Congress and the President do not seem to be able to find common ground. As we progress into the fall and the Congressional elections, the rhetoric will probably get more heated. It seems likely that the Republicans will take control of both the Senate and the House, which means that not much will be done until the 2016 elections; and so much needs to be done. On the international front, the hot spots seem to rotate from Syria to Ukraine to Iraq, to

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Palestine/Israel with China, North Korea, Iran, and others waiting their turn. Oil prices have moved higher reflecting concern that supplies might be disrupted at any time.

The mention of oil prices brings us to a brief discussion of energy, a topic that has graced each of our quarterly letters for the past ten years. Particularly since the development of fracking technologies over the past three or four years, energy independence for the United States is a realistic goal. We see great benefits for the US economy as it takes considerable labor to build the infrastructure, on the one hand. On the other hand, balance of payment deficits have gradually come down, as the US needs to import less energy and in fact can export petroleum and natural gas products. Energy Master Limited Partnerships (MLPs) are a necessary factor in accomplishing energy independence. New infrastructure is needed to develop, process, transport, and store the natural gas and petroleum products that provide the capital base on which higher earnings will be generated. We foresee growth continuing for at least the next three years on a conservative basis and more likely into the next decade.

While we usually concentrate on the impact of energy abundance on the US economy, it is also likely to affect those countries with whom we trade. A recent report from Industrial Info Resources states that their oil and gas production database shows more than 2,500 active capital and maintenance projects are ongoing throughout the world with a combined value of $1.6 trillion. In some cases, this reflects the opportunity to produce energy at home, and in other cases, it reflects to need to develop port facilities to receive energy from abroad. Industrial Info Resources also is tracking $5.7 trillion of projects related to the power industries around the world. This should be energizing to the global economy.

Our market projection for the year remains at a total return of 10-12%, based on the supposition that the current equity market is not over-valued. Bloomberg Finance LP consensus estimate for earnings per share for calendar year 2014 is $118.32, which at quarter-end price generates a price earnings ratio (P/E) of 16.7 times. While this ratio is up from the past few years, it does not appear to be dangerously high. Companies have had many opportunities to feast on low cost fixed debt that has lowered their cost of capital and they have been careful to control costs.

We at Dividend Assets Capital are coming to the end of an era. Tom Cameron, our Chairman and co-Founder, has decided to retire at the end of September. For most of the last seven decades, he has been a vocal investment advisor and is the father of the rising dividend philosophy that he has employed through much of this time. Included in this mailing is a special publication, *A Lasting Legacy: Thomas W.L. Cameron*, a reflection of Tom's life and career. We hope you enjoy it. Our best wishes go with Tom. He will be greatly missed here at DAC.

Additional Sources: Bloomberg, Strategas, RenMac, Bureau of Labor Statistics

IMPORTANT DISCLOSURES

You should carefully consider the investment objectives, potential risks, management fees, and charges and expenses before investing. There are no guarantees that dividend-paying stocks will continue to pay dividends. In addition, dividend-paying stocks may not experience the same capital appreciation potential as non-dividend paying stocks. ***The past performance of the strategy is not an indicator of future performance; and investment results may vary.*** *The Dividend Assets Capital, LLC's Investment Adviser Brochure, Form ADV Part 2, contains this and other information about the Firm, and should be read carefully before investing. You may obtain a current copy of Dividend Assets Capital's Form ADV Part 2 by visiting our website at www.DACapitalSC.com, emailing info@DACapitalSC.com, or by calling us toll free at (866) 348-4769. An investment in a Master Limited Partnership (MLP) unit involves risks that differ from a similar investment in equity securities including ownership controls associated with the limited partnership structure, high debt to equity ratios, and certain tax risks. Investors in Master Limited Partnerships (MLPs) should determine the tax consequences of investing in MLPs based on their specific circumstances and should consult with their tax advisor regarding the tax consequences of an investment in MLPs. Investments in international markets present special risks including currency fluctuation, the potential for diplomatic and political instability, regulatory and liquidity risk, foreign taxation and differences in auditing and other financial standards. Risks of foreign investing are generally intensified for investments in emerging markets. Investors in MLPs may be required to file tax returns and pay tax in each state in which the MLP operates. Individual retirement accounts and retirement plans investing in MLPs may be required to report unrelated business taxable income (UBTI) and pay unrelated business income tax (UBIT). Tax reporting information for MLPs is provided to investors on an annual Schedule K-1 issued by an MLP. Investors may be required to request an extension of time to file their tax returns if an MLP has not issued a Schedule K-1 by April 15. MLPs are generally held in an investor's account to generate income. The S&P500 Index is a widely recognized unmanaged index of equity prices and is representative of a broader market and range of securities than is found in individual client portfolios.*