A New & Improved Investment Style Emerges:

Enhancement of Div Growth Investing with FCF, S&P Div. Aristocrat indices, & a Tighter, more Analytical DG Methodology

AAII Houston Retirement SIG

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Agenda

➤ Free Cash Flow (FCF) improvements over traditional PE valuation metrics

➤ Dividend Growth aka "The Superior Investment Style"
  ➤ Total Returns vs Yield only – misses stock appreciation & BBs
  ➤ Avoids Value traps like ATT & Verizon

➤ Victory Cap contribution by creating ETFs driven by FCF

➤ S&P upgraded Div Aristocrat Indices w/ FCF valuations

➤ A synergistic combination of investing styles & more selective Stock Selection

The Case for FCF Investing

➢ Price Earnings (PE) remains the main indicator for stock valuation

➢ FCF metrics are more consistent & efficient than PEs

➢ Price to FCF widely used in oil, gas, mining & R&D stocks

    ➢ But PE ratios can be easily manipulated using accounting gimmicks

➢ FCF is the amount of Op Cash Flow before Dividends & Buybacks

    ➢ Implies that S/H returns are primary before deciding upon Capex, M&A $

    ➢ For decades, these extractive industries stressed production & reserve values

    ➢ Markets demanded S/H return goals be made primary

    ➢ Today, Exec comp widely used to make S/H returns the primary motivators for the benefit of shareholders & management alike

Free Cash Flow (FCF) a Key Business Metric

The value of a company is the present value of its _FUTURE_ free cash flow.

- Free cash flow is a crucial metric for assessing the **value** of a company

- Positive free cash flow means a company generates more cash than it needs to cover all expenses – a sign of **quality and operating efficiency**

- We believe free cash flow is a more reliable metric than earnings, which can be impacted by non-cash charges, depreciation, or write-offs

Free cash flow is the cash remaining after a company has covered:

- ☑ Expenses
- ☑ Taxes
- ☑ Interest
- ☑ Long-term investments

Free cash flow can be used to invest in:

- Growing the business
- Buying back stock
- Paying dividends
- Paying down debt

Source: VictoryShares
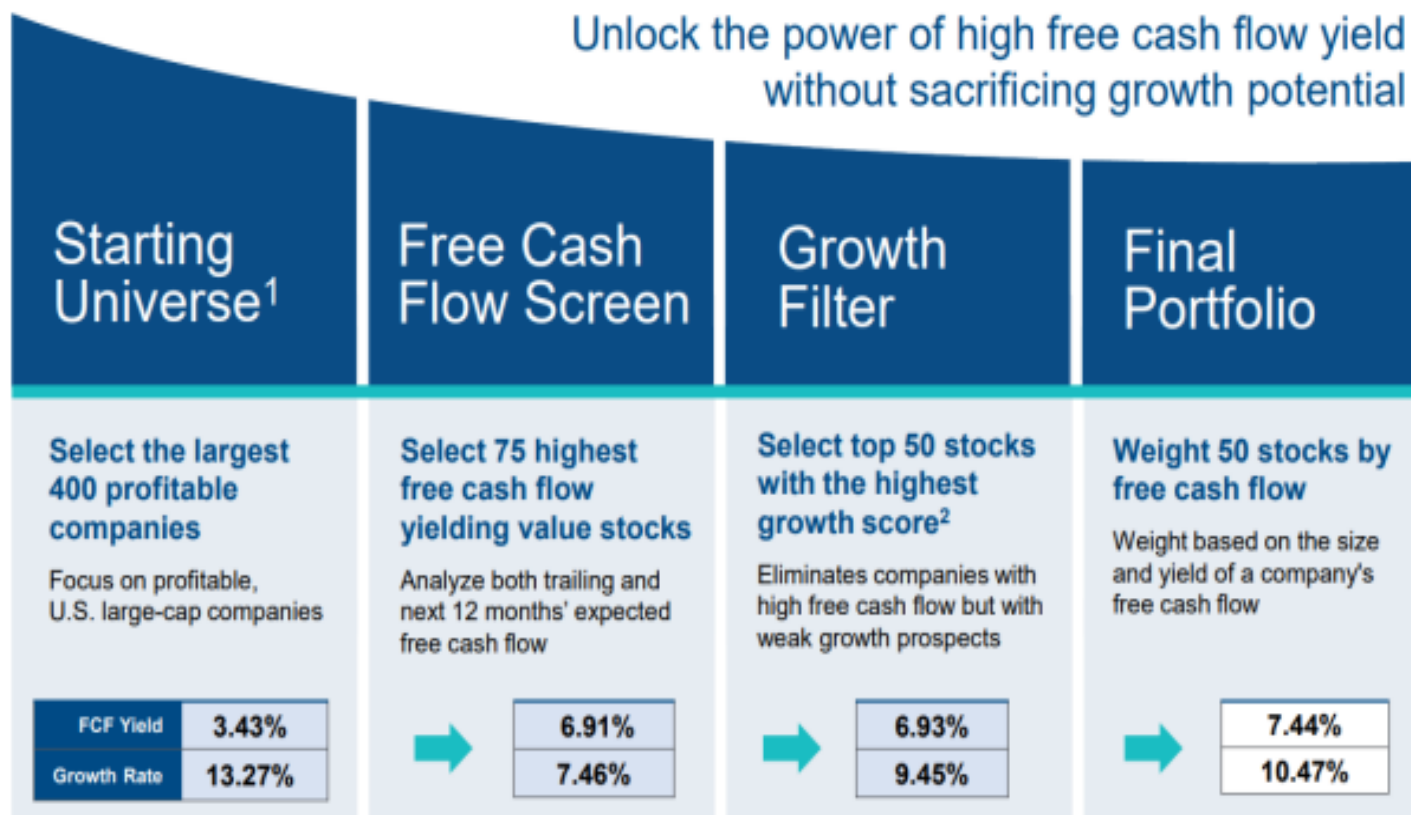
VFLO ETF Highlights

➢Selection based primarily on FCF metrics
- ➢FCF Margin -as % of Operating Margin
- ➢FCF Yield – as % of Invested Capital
- ➢10 years minimum performance
- ➢Slice off bottom quintile for slow growth

➢Mainly Midcap Growth stocks
- ➢A few Large Growth caps

➢FCF has Superior performance to Price Earnings selection
- ➢PE much more variable than FCF so tougher to predict
- ➢PE too easy for accountants to manipulate

Techniques used to Boost Earnings not FCF

➢Timing of Revenue Recognition (sooner)

- ➢At point of sale
- ➢At time of contract execution
- ➢At time of billing or cash receipt
- ➢At time when progress payments received

➢Deferment of LT Asset purchases (later)

- ➢Depreciation & Amortization of all companies
- ➢Recognition of timing of R&D spending in Tech & Medical
- ➢Recognition of Stock Options in Startups & Tech companies
- ➢Capital Leases

➢Overall, a great temptation to cheat on earnings e.g. GE

- ➢FCF is a more consistent & efficient metric (Cash can't lie)

Victory Shares – VFLO Methodology

Unlock the power of high free cash flow yield without sacrificing growth potential

Starting Universe[1]	Free Cash Flow Screen	Growth Filter	Final Portfolio
Select the largest 400 profitable companies	**Select 75 highest free cash flow yielding value stocks**	**Select top 50 stocks with the highest growth score[2]**	**Weight 50 stocks by free cash flow**
Focus on profitable, U.S. large-cap companies	Analyze both trailing and next 12 months' expected free cash flow	Eliminates companies with high free cash flow but with weak growth prospects	Weight based on the size and yield of a company's free cash flow

	FCF Yield	Growth Rate
Starting Universe	3.43%	13.27%
Free Cash Flow Screen	6.91%	7.46%
Growth Filter	6.93%	9.45%
Final Portfolio	7.44%	10.47%

Victory U.S. Large Cap Free Cash Flow Index

- **50 stock portfolio**
- Rebalances and reconstitutes every qtr.
- Holdings capped at 4%
- Sector exposure capped at 45%
- No sector can be 20% greater than starting universe[1]

Source: FactSet. Analysis is shown as of the last rebalancing screening date on 3/13/2025.

FCF yields and growth rates shown above are first those of the Starting Universe, then each subdivision of that universe, and finally of the Victory U.S. Large Cap Free Cash Flow Index—the final portfolio.

Index performance does not represent fund performance.

1 VettaFi 1000 Index.
2 **Growth score** measured by sales trend, EBIDTA growth and long-term earnings growth

FCF yield is measured by the average of trailing 12-month FCF and next 12-month forward FCF over enterprise value.
Growth rate is measured by the average of the long-term sales growth estimates, EBITDA trend and long-term EPS growth estimates. Enterprise value measures a company's total value and is often used as a more comprehensive alternative to equity market capitalization.

Victory Shares – VFLO Growth Filter

- Overlooking growth can lead to missing out on returns

- We believe future growth supports future FCF growth – The Index seeks to remove the slowest growers which may potentially help the index navigate growth regimes more effectively

- The **growth filter** evaluates companies' expected sales growth, EBITDA growth, and long-term growth rate

Growth Filter	75 Stocks Highest Expected FCF/EV	50 Stocks Fastest Growers	25 Stocks Slowest Growers
Sales Growth	5.80%	9.50%	-1.03%
EBITDA Growth	7.08%	12.88%	-3.56%
Long-Term Growth Estimate	9.81%	11.81%	5.75%
Free Cash Flow Yield	9.13%	8.87%	9.57%

Victory Shares Led in FCF investing

➤ One of main Factors used in stock picking is Quality
- ➤ FCF is of higher quality than earnings
- ➤ Pacer had a good ETF using Operating CF in COWZ
- ➤ Ticker suggests "Cash Cows", good FCF but little growth

➤ Victory built upon Factor investing by replacing OCF with FCF thereby enhancing the Quality & Predictability of the individual stock picks
- ➤ Michael Mack was the common denominator at Pacer & Victory

➤ VFLO (mid/large caps) now outperform COWZ

➤ Endorsed this style as a double position in my portfolio

VFLO vs S&P500 & Excess Returns

Hypothetical index performance data

Index Returns Across Various Market Regimes 12/31/1999– 3/31/2025	S&P 500 Index	Victory U.S. Large Cap Free Cash Flow Index *(Gross of Expenses)*	Excess Return vs. S&P 500 Index
Value	0.91%	15.65%	+14.74%
Growth	15.13%	19.12%	+3.99%
Mega Cap	8.54%	6.88%	-1.66%
Ex-Mega Cap	8.22%	27.06%	+18.84%
Large	-2.54%	-0.96%	+1.58%
Small	19.50%	36.26%	+16.76%
High Quality	2.54%	9.42%	+6.88%
Low Quality	14.32%	25.67%	+11.35%
High Momentum	1.62%	6.66%	+5.04%
Low Momentum	17.73%	32.45%	+14.72%
High Beta	35.13%	47.75%	+12.62%
Low Beta	-22.79%	-17.79%	+5.00%
U.S. Outperforms	12.40%	15.87%	+3.47%
International Outperforms	3.86%	19.25%	+15.39%
Up Market	39.11%	49.62%	+10.51%
Down Market	-47.13%	-40.60%	+6.53%

Past performance does not guarantee future results.
Source: Bloomberg, Analysis Period 12/31/1999 – 3/31/2025

Source: VettaFi data analyzed through Zephyr Reporting. Analysis Period 12/31/1999 – 3/31/2025; Net performance is adjusted for ETF expenses.

Source: Victory Shares

Victory Shares – Metrics

FCF/EV has provided the highest risk-adjusted returns - meaningfully outperforming other valuation metrics.

Risk and Return Profiles for S&P 500 Stocks in the Top Quintile of Valuation Metrics

Free Cash Flow Yield

Enterprise Value to EBIDTA

Price to Book

Price to Sales

Price to Earnings

RETURN

RISK*
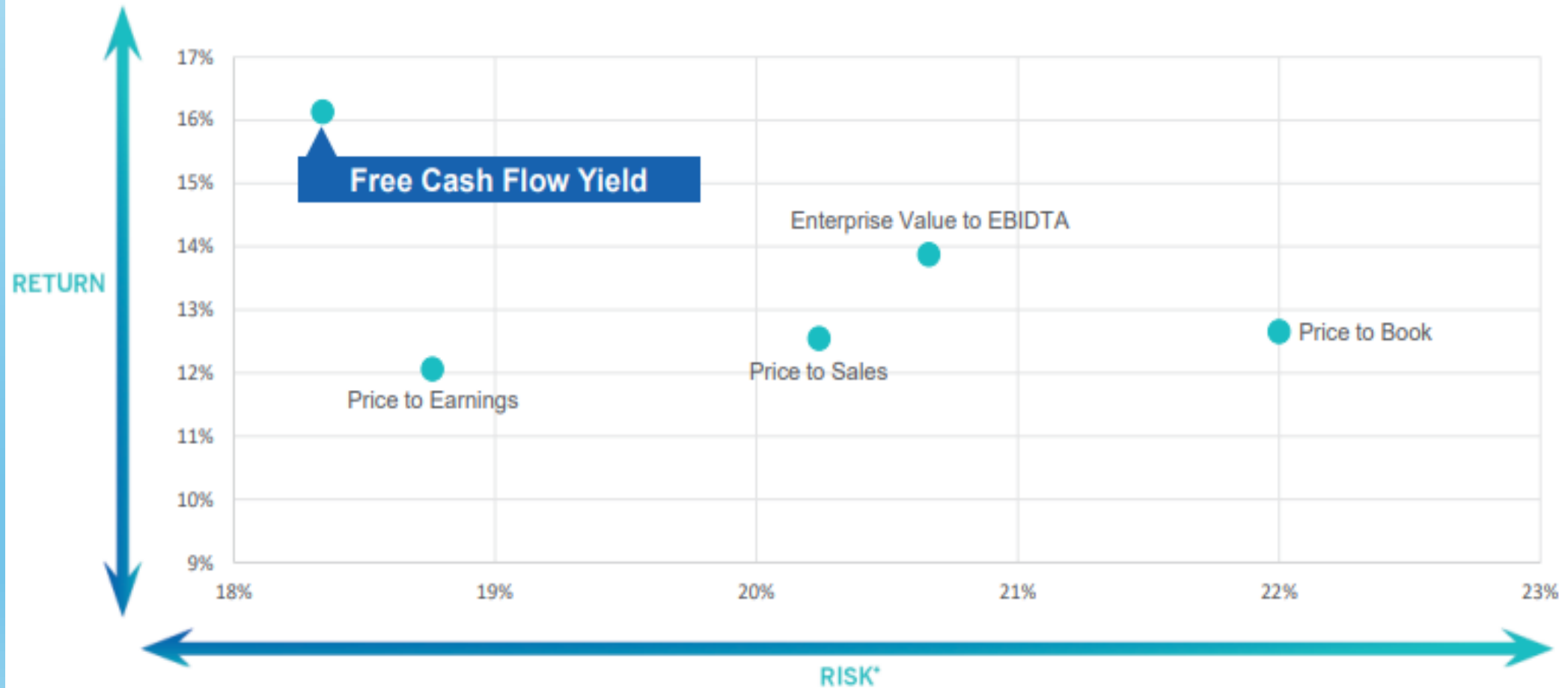
Past performance does not guarantee future results.

SWITCH FROM FCF TO DG

The Dividend Growth Business Model

➢Div Aristocrats have been growing dividends for >25 yrs while Div Kings have been growing >50 yrs; many for 100 yrs+
  ➢Spanning all industry sectors but all enjoying a wide economic moat (MS)

➢The management culture is to exploit their moat on a LT sustainable path & growing the dividend before ever deciding on, capex, M&A,BBs, or debt reduction

➢This differentiates them from the vast unwashed who chase M&A, R&D projects, or the next big find in Oil & Gas to name a few

➢New CEOs rarely need to tweak the ultimate Corp. business model
  ➢Growing dividends & stock appreciation for investors

Dividend Growth - "Premier Investing Style"

➢ David Bahnsen talked to us earlier in 2025 (sans slides)
  ➢ DG the only style he will use himself or recommend to others
  ➢ Manages multi-$B DG funds & provides daily market commentary

➢ ST Traders probably have higher returns vs Buy & Hold investors
  ➢ At risk levels unacceptable to such LT investors

➢ Simply the best stocks to own for Retirees & Long-term investors
  ➢ LT players attracted by Growing Income but also Stock Appreciation
  ➢ Track records over 25, 50 &100 years of consistent Total Return growth
  ➢ Superior to Div Yield & Div Value styles in RARs & in avoiding Value Traps endemic in riskier Yield plays
  ➢ Market highly efficient for Aristocrats & Kings so expectations of Hi-Rewards & Lo-Risk are prevalent thx to decades of corporate excellence
  ➢ Aristocrats & Kings tend to be "first stocks to go up & the last to go down"

Highlights of LeBris Methodology - RARs

➢ Thorough definition & reconciliation of key financial metrics with ratio formulae - Key metric is RARs

➢ Generates Hi-graded prospects from thorough review & practice w/several proprietary data feeds

➢ Data screened from a universe of 855 to 495 Economic Moat Cos to 61 Kings & Aristocrats to 9 Prospects

    ➢ High reliance on FCF generation & Perpetuity growth (PG)

    ➢ Timing also critical since Initial Value is "the most controllable variable"

➢ Lots of "What if" & "Sensitivity analytics" to find your personal preferences within the prospect list

RARs = Risk-adjusted Total Returns

LeBris Engagement with Frank & John

➢ Informal discussion over Frank's Income SIG database vs LeBris model

➢ Desire to compare & simplify the data sources & compilation process

➢ Both data sets improved & led LeBris to create a Stock Selection presentation, using DG investing style & lots of financial analysis

➢ Frank was looking to value companies & LeBris did with Analyst predictions but also Perpetuity Growth (PG)

    ➢ DCF analysis of future FCF using PG for the years beyond Yr 5

DG Stock Selection Tenet *(Framework)*

Seek **Excess Return** from balanced **Dividend Yield**, **Dividend Growth** and **Rising Valuation**.

D   **A**   **B**   **C**

B Sustainable Dividend Growth is the main engine underpinning Dividend Yield return and Valuation expansion over time.

$$S = \left(\frac{R_p - R_f}{\sigma_p}\right)$$

5-Year T-Bond Yield	**D**	Excess Return	Volatility	SHARPE Ratio

TOTAL RETURN

A   **B**   **C**

DIVIDEND YIELD	DIVIDEND GROWTH	VALUATION GROWTH

Minimal Risk-Adjustment   Perpetuity Dividend Growth >0.5%   Market Cap < Fair Value

- ❏ Financial Leverage
- ❏ Payout Ratio
- ❏ Dividend / FCF
- ❏ Dividend History

- ❏ Competitive Advantage
- ❏ Operating Leverage
- ❏ Sustainable Growth
- ❏ Return on Capital

- ❏ Market Cap / FCF
- ❏ (Market Cap / Yield) / Growth
- ❏ Yield / Last 5-Yrs > 1
- ❏ EV / EBITDA

Best to Worst Strategies
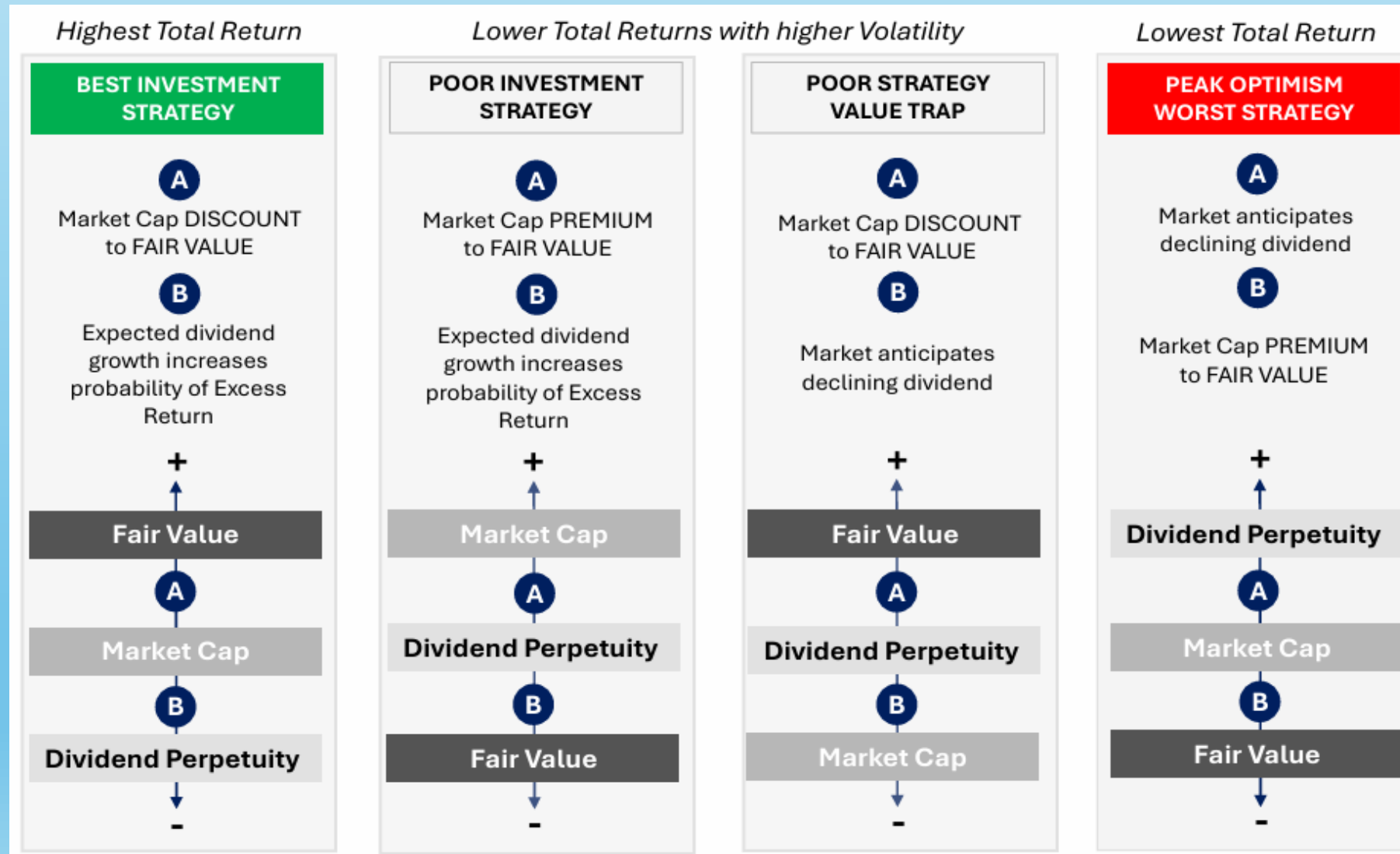
Div Stock Selection – Back Testing/Analysis

61 DIVIDEND KINGS & ARISTOCRATS

5-Year Back Testing of Required Perpetuity Growth

(A) DOUBLE DIGIT RETURN - Stocks with Perpetuity Growth rates exceeding **0.5%** in April 2019 delivered **11.7%** total returns over the subsequent 5-year period ending April 2024.

(B) GREATER SHARPE RATIO - These stocks delivered total returns **2.2x** greater than those from stocks with **<0.5%** Perpetuity growth, and a **3x** higher SHARPE ratio.

KINGS & ARISTOCRATS DIVIDEND STOCKS
Pepertuity Growth and subsequent 5-Year Total Return

Legend: ☐ Perpetuity Growth < 0.5% ◼ Perpetuity Growth > 0.5%
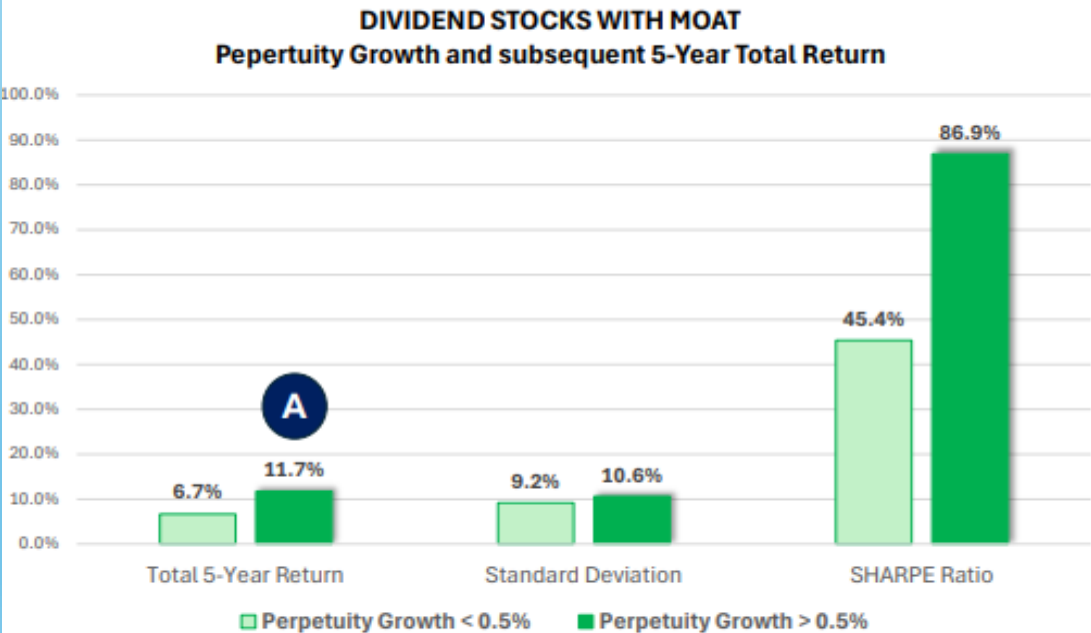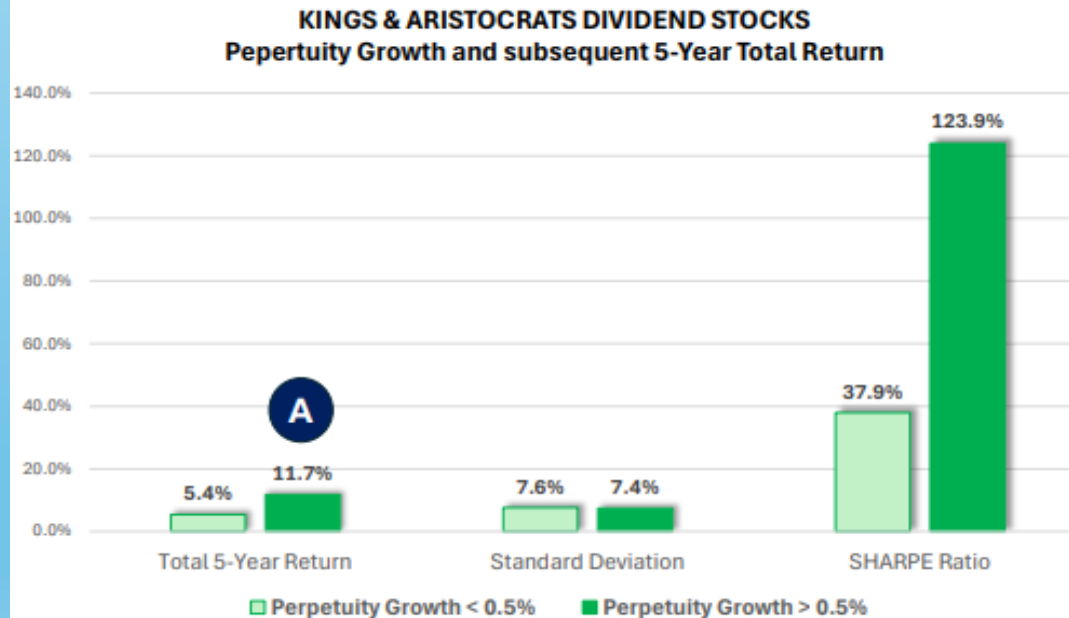
G Tier (Perpetuity required growth to Mkt Cap)	% Population with Return > 0%	Average Total Return	Return Standard Deviation	SHARPE RATIO
Below -20%	0%	0.0%	0.0%	0.0%
-10% to -20%	0%	0.0%	0.0%	0.0%
-5% to -10%	100%	2.0%	0.0%	0.0%
0% to -5%	78%	6.0%	7.5%	46.9%
0% to 0.5%	92%	8.1%	8.4%	66.7%
0.5% to 1%	100%	10.5%	6.2%	130.0%
1% to 2%	100%	14.5%	10.9%	110.7%
TOTAL	**85%**	**7.3%**	**7.8%**	**61.8%**
<0.5%	82%	5.4%	7.6%	37.9%
> 0.5%	100%	11.7%	7.4%	123.9%
Variance X	**1.21X**	**2.17X**	**0.98X**	**3.27X**

Source: PlB

Dividend Growth Selection Strategy

855 Dividend Stocks
(updated April 19, 2024)

Safety Segment	Required PERPETUITY GROWTH	Projected DIVIDEND Return	Projected VALUATION Return	Projected TOTAL Return	Projected EXCESS Return	Market Cap / FCF	Price / FV (Average)
A+	3.0%	2.1%	0.3%	2.5%	-2.4%	13.9X	102%
A-	2.8%	2.1%	0.8%	2.9%	-1.7%	27.3X	99%
B+	2.0%	2.5%	1.5%	4.0%	-1.2%	18.7X	97%
B-	1.8%	2.3%	2.2%	4.5%	-0.3%	17.7X	94%
C+	1.3%	2.3%	4.3%	6.7%	1.3%	1.6X	87%
Poor	-2.4%	2.6%	7.8%	10.4%	5.4%	13.5X	75%
TOTAL	**0.5%**	**2.4%**	**4.1%**	**6.5%**	**1.6%**	**14.3X**	**88%**

61 Dividend Kings & Aristocrats
(updated April 19, 2024)

Safety Segment	Required PERPETUITY GROWTH	Projected DIVIDEND Return	Projected VALUATION Return	Projected TOTAL Return	Projected EXCESS Return	Market Cap / FCF	Price / FV (Average)
A+	3.0%	2.2%	-1.2%	1.0%	-3.9%	22.1X	108%
A-	2.4%	2.5%	-0.1%	2.4%	-0.9%	15.0X	102%
B+	2.1%	2.5%	-0.6%	1.9%	-2.4%	40.7X	104%
B-	1.2%	2.9%	0.0%	2.9%	-1.9%	11.4X	101%
C+	-1.6%	3.9%	-0.4%	3.6%	-2.1%	10.1X	103%
Poor	-2.6%	3.2%	3.8%	7.0%	-3.5%	10.6X	82%
TOTAL	**2.1%**	**2.5%**	**-0.5%**	**2.0%**	**-2.9%**	**21.0X**	**104%**

495 Moat Companies
(updated April 19, 2024)

Safety Segment	Required PERPETUITY GROWTH	Projected DIVIDEND Return	Projected VALUATION Return	Projected TOTAL Return	Projected EXCESS Return	Market Cap / FCF	Price / FV (Average)
A+	3.2%	2.0%	-0.3%	1.7%	-3.2%	24.3X	105%
A-	3.0%	1.9%	0.7%	2.7%	-1.6%	28.6X	101%
B+	2.4%	2.2%	1.5%	3.7%	0.5%	21.9X	96%
B-	2.1%	2.1%	2.2%	4.3%	-0.7%	15.3X	95%
C+	1.6%	2.1%	3.5%	5.6%	-0.7%	2.7X	89%
Poor	-0.6%	2.2%	5.7%	7.9%	0.7%	14.7X	80%
TOTAL	**1.9%**	**2.1%**	**2.3%**	**4.4%**	**-0.5%**	**17.8X**	**94%**

Source: PLB

Dividend Growth Prospect Summary

➢ For each of the 9 Prospects generated, a single page summary is produced with all the most important variables delineated

➢ With a combo of the Prospect summary sheets & all the key sensitivities/analyses run, the system will generate 9 excellent quality stocks to buy immediately

➢ However, if the decision maker believes the market has significant downside risk, they will defer the decision

    ➢ Most controllable variable in this mix is the stock price paid (Initial Value)

➢ Have historically high market valuations, which leaves us to watch those Prospects until we judge "time is right" e.g. a drawdown

SWITCH FROM DG INVESTING TO DIVIDEND INDICES

S&P redefine DG Aristocrats with Indices

➢S&P has used a Dividend Aristocrats Index (DAI) for decades

   ➢To qualify dividends must have grown at least 25 years

➢Several years ago, they introduced a FCF screen to the DAI with great performance in Risk-Adj returns (RARs)

➢In 2025, they brought out a more refined version called the Developed Quality FCF index

   ➢ Even better Risk-Adj Total Returns

   ➢Here are a few S&P slides on index performance

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Performance & Risk vs Benchmarks

Performance

INDEX LEVEL	RETURNS			ANNUALIZED RETURNS			
	1 MO	3 MOS	YTD	1 YR	3 YRS	5 YRS	10 YRS
Total Return							
9,154.04	2.25%	-2.41%	1.28%	16.32%	16.68%	17.55%	14.12%
Price Return							
6,078.96	2.15%	-3.01%	0.61%	14.48%	14.78%	15.68%	12.03%
Net Total Return							
8,361.43	2.23%	-2.58%	1.12%	15.92%	16.21%	17.08%	13.6%
BENCHMARK* Total Return							
1,579.19	1.11%	-3.78%	-0.39%	12.65%	11.51%	14.26%	9.74%
BENCHMARK* Price Return							
764.31	0.92%	-4.35%	-1.05%	10.59%	9.26%	12.01%	7.32%

* The index benchmark is the S&P Developed LargeMidCap (USD)

Risk

	ANNUALIZED RISK			ANNUALIZED RISK-ADJUSTED RETURNS		
	3 YRS	5 YRS	10 YRS	3 YRS	5 YRS	10 YRS
Total Return						
	17.05%	16.81%	15.34%	0.98	1.04	0.92
Price Return						
	17.09%	16.81%	15.37%	0.86	0.93	0.78
Net Total Return						
	17.05%	16.8%	15.35%	0.95	1.02	0.89
BENCHMARK* Total Return						
	15.82%	15.73%	14.99%	0.73	0.91	0.65
BENCHMARK* Price Return						
	15.84%	15.73%	15.02%	0.58	0.76	0.49

Risk is defined as standard deviation calculated using monthly values.

* The index benchmark is the S&P Developed LargeMidCap (USD)

S&P Index Sectors & Constituents

Sector* Breakdown

- Information Technology 38.9%
- Financials 16.9%
- Health Care 16.1%
- Communication Services 10.3%
- Consumer Discretionary 6%
- Consumer Staples 4.6%
- Materials 4.3%
- Industrials 2.7%
- Utilities 0.3%
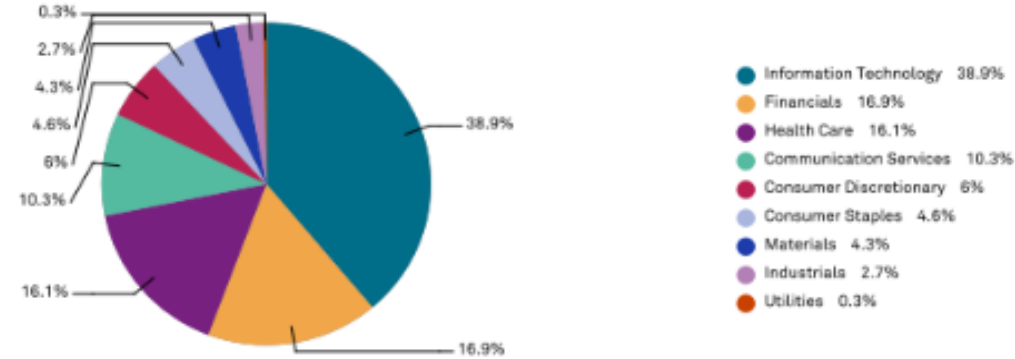
*Based on GICS® sectors

The weightings for each sector of the index are rounded to the nearest tenth of a percent; therefore, the aggregate weights for the index may not equal 100%.

Top 10 Constituents By Index Weight

CONSTITUENT	SYMBOL	SECTOR*
Roche Hldgs AG Ptg Genus	ROG	Health Care
Novo Nordisk AS B	NOVO B	Health Care
ASML Holding NV	ASML	Information Technology
Apple Inc.	AAPL	Information Technology
Broadcom Inc	AVGO	Information Technology
Microsoft Corp	MSFT	Information Technology
Nvidia Corp	NVDA	Information Technology
Meta Platforms, Inc. Class A	META	Communication Services
Visa Inc A	V	Financials
Mastercard Inc A	MA	Financials

*Based on GICS® sectors

Country/Region Breakdown

COUNTRY/REGION	NUMBER OF CONSTITUENTS	TOTAL MARKET CAP [USD MILLION]	INDEX WEIGHT [%]
United States	60	17,677,174.53	57.6
Netherlands	2	311,521.78	7.7
Switzerland	4	299,699.66	6.6
Denmark	2	238,680.46	5.6

S&P Index Performance

Historical Performance

Depending on index launch date, all charts below may include back-tested data.

* Data has been re-based at 100

Chart y-axis values: 390, 325, 260, 195, 130

Chart x-axis values: 2016, 2017, 2018, 2019, 2020, 2021, 2022, 2023, 2024, 2025

Legend:
■ S&P Developed Quality FCF Aristocrats Index (USD) TR
■ S&P Developed LargeMidCap (USD) TR
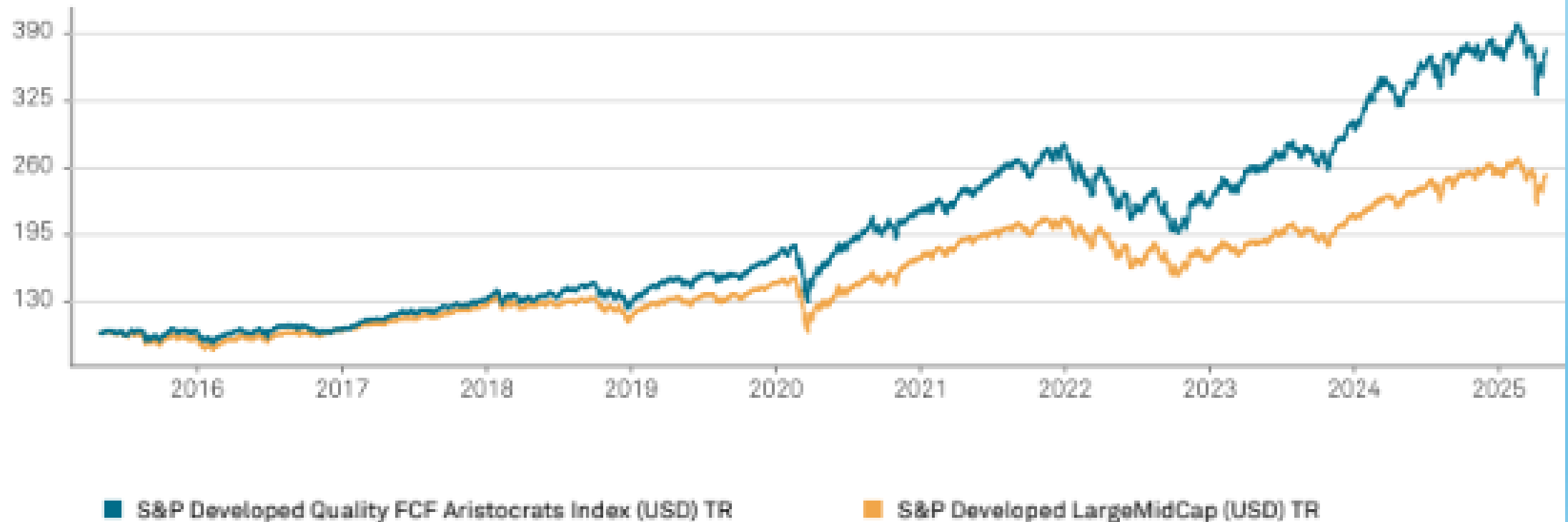
CONCLUSIONS & CREDITS

A New & Improved Retiree Investing Style Emerges

➢ From recognition of superiority of DG investing to all other styles
  ➢ LeBris Methodology pulls theory & practice together in a rigorous way

➢ From replacement of PE metrics by FCF Valuations (COWZ to VFLO)
  ➢ Road map for companies to select best business models to follow
  ➢ Improvements in predictability of FCF vs earnings valuations
  ➢ Upgrading valuation consistency & efficiency in stock valuation & selection
  ➢ Eliminating noise from misleading accounting gimmicks

➢ Value added from refinement of FCF Quality metrics to S&P Aristocrat Indices
  ➢ Creating excellent candidates for title of Aristocrats
  ➢ Adding Quality, Value & better RARs to stock selection process

➢ From application of FCF metrics to DG investing
  ➢ Combination synergizes two superior Investing Styles

Credits

➢ Phillip LeBris, a private investor, in enhancing the quality of DG methodology well beyond any Wall Streets offerings

➢ Michael Mack of Victory Capital for educating investors & attracting significant $ to FCF Investing thru targeted ETFs

➢ S&P Global, themselves a Div. Aristocrat/King stock, to the creation & refinement of these indices to include FCF & greater rigor on Div stock picking

➢ To Frank Erzinger in developing his own data feeds & analysis that opened the door to engaging Phillip in this exciting new Inv style

Questions….

Comments…

Concerns..

Div Stock Selection – Example of 4%Yield Sensitivity

Source: PlB