3 Important Lessons From 2015 That Investors Should Heed in 2016

Description

Last year was tough for investors; the sharp collapse in oil, China's rapid economic deceleration, and the commodities crunch all took their toll on financial markets. The outlook for 2016 doesn't appear to be any better with the TSX down by 14% compared with a year ago and fears over China's slowing growth creating further market instability.

Now what?

This makes now an important time for investors to reflect on 2015, lessons learned, and how they can be applied in 2016. Let's cast our gaze back and look at three virtually timeless lessons that all investors would do well to remember.

Firstly, booms always end in bust.

Whether it be the oil boom that made the oil patch responsible for generating over 6% of Canada's GDP, the commodities boom, or the U.S. housing bubble, all good things must come to an end.

This makes it important to recognize that investing for the long term in companies with solid economic moats and timeless businesses is far more important than following the latest market trend.

Secondly, dividends still matter, but not every dividend is created equal.

Dividend investing forms an important part of long-term wealth creation; dividends account for around 40% of the total returns of the TSX since 1956.

However, not all dividends are the same.

During 2015 we saw this with the deepening crisis surrounding the energy patch. Not only did weak crude force energy companies to slash costs, but a number of dividend stalwarts such as **Crescent Point Energy Corp.** (TSX:CPG)(NYSE:CPG) and **Canadian Oil Sands Ltd.** (TSX:COS) cut their dividends.

This highlights why it is important to identify stocks with sustainable dividends. A key way of doing so is by examining a company's dividend-payout ratio.

This represents the amount of dividend payments made in proportion to net income. The lower the ratio, the more sustainable the dividend. One dividend stalwart that has a low ratio, yet has hiked its dividend every year for the last 20 years straight is **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI).

Its dividend may only yield a modest 1.7%, but it has an impressive compound annual growth rate of over 15%. This impressive rate of growth will continue when the low payout ratio of 28% and its solid economic moat are considered.

Finally, it never hurts to take profits.

As a long-term contrarian investor, I typically take a buy-and-hold strategy, ignoring the sensational headlines and market gyrations.

Nonetheless, there is one thing I can't stress enough: don't be afraid to take profits. This may appear to be contrary to the ethos of long-term investing, but a key tenet is the preservation of capital.

Let's face it, there are times when secular trends cause industries to fall into disfavour.

An example from 2015 is the trend towards cleaner renewable energy and the move to eliminate coal-fired electricity generation. This saw the Alberta government introduce a new carbon tax and regulations aimed at eventually eliminating coal-fired electricity from the province's energy mix.

This will impact electric utility **TransAlta Corporation** (TSX:TA)(NYSE:TAC) because it earns almost half of its EBITDA from coal-fired electricity generation in the province. As a result, over the last year its share price has plunged by 60% with no sign of a bottom in sight. After completing a costly update of its plants to meet clean coal technology and now having to meet the new regulations, it will remain under considerable financial pressure.

So what?

These lessons may be easy to see in hindsight, but what is most important is for investors to apply them now and use them as tools to manage their portfolios.

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1. Dividend Stocks
2. Energy Stocks
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2. NYSE:TAC (TransAlta Corporation)
3. NYSE:VRN (Veren)
4. TSX:CNR (Canadian National Railway Company)
5. TSX:TA (TransAlta Corporation)
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