

# **The Case for Dividend Growth**

## THE CASE FOR DIVIDEND GROWTH

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Until 2022, dividend-based strategies lagged for several years primarily due to a combination of unprecedented outperformance from high “long duration” non-dividend paying growth stocks and the lagging performance of the defensive cohort within the dividend paying universe.

### **Catalysts for sustained outperformance:**

- Short term: continued market volatility, recession risks
- Long-term: subdued market returns given the likelihood of prolonged sluggish economic growth, geopolitical risks, and somewhat higher inflation (i.e., absence of Fed “put”)
- Broad increase in capital returns (following COVID-driven pause) over past eighteen months
- Fund flows shift to dividend payers as substitute for bonds
- Rising interest rates, depending on coinciding macro conditions

### **SIA Dividend Strategy**

- High quality emphasis- strong balance sheets, FCF generation, ROIC-focused management teams
- Balance income and capital appreciation through disciplined framework
- Maintain 50-100 bp yield spread over S&P Index
- Manage risks through diversification, quality, valuation discipline, and tactical positions
- Growth-focused. All holdings expected to grow dividends over time

### **Current Fund Positioning**

- Quality and diversification critical given macro cross-currents and cyclical risks
- Barbell most attractive pro-cyclicals (tech hardware, financials) with defensive/ non-cyclicals (P&C insurance, defense, utilities, REITs)
- Increased U.S. exposure given heightened Europe/ China “tail” risks, stronger \$USD
- Significant weightings to most attractive long-term growth sectors: technology, health care, and energy-related

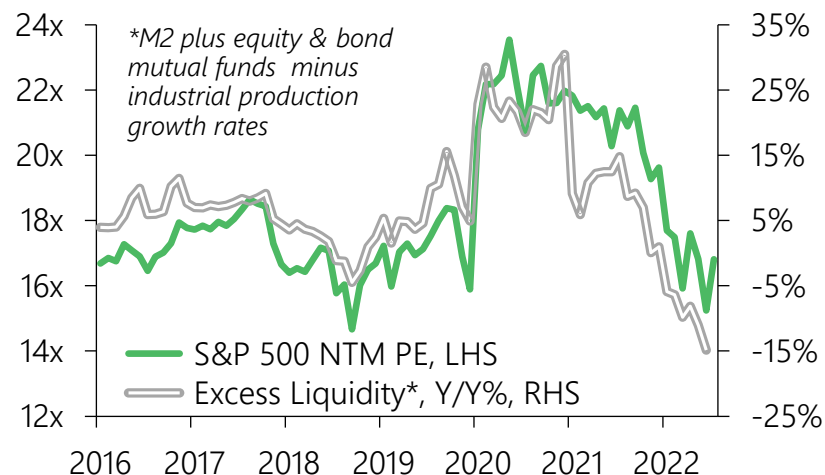
## UNPRECEDENTED STIMULUS AND MARKET IMPACT

### Announced Global Stimulus (Feb. 2020 - Sep. 2022)

	Potential Ctrl. Bank Liquidity Injection		Potential Govt. Fiscal Stimulus	
	\$ Tln	% GDP	\$ Tln	% GDP
U.S.	6.21	27.0%	7.32	31.8%
Euro Area	2.38	16.4%	4.94	34.0%
Japan	1.03	20.8%	3.72	75.3%
U.K.	0.57	17.9%	0.89	29.7%
China	2.11	12.1%	1.10	6.3%
Others*	1.71		3.45	
<b>Total</b>	<b>14.01</b>	<b>14.6%</b>	<b>19.25</b>	<b>22.2%</b>

Source: Piper Sandler

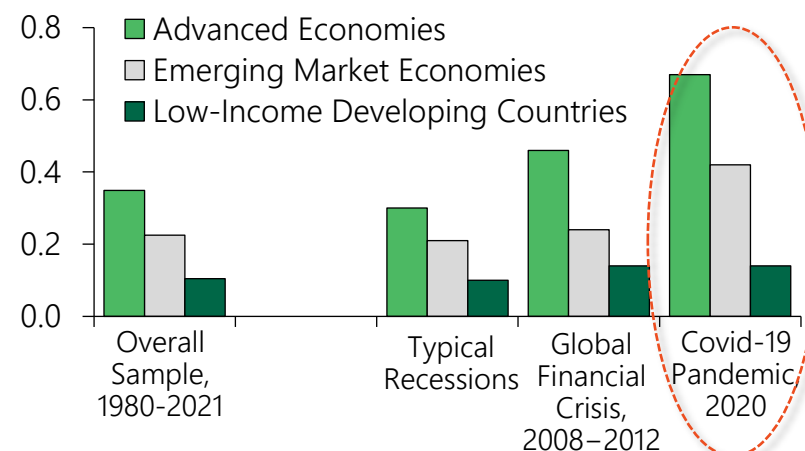
### S&P 500 PE Ratio vs U.S. Excess Liquidity



Source: FactSet

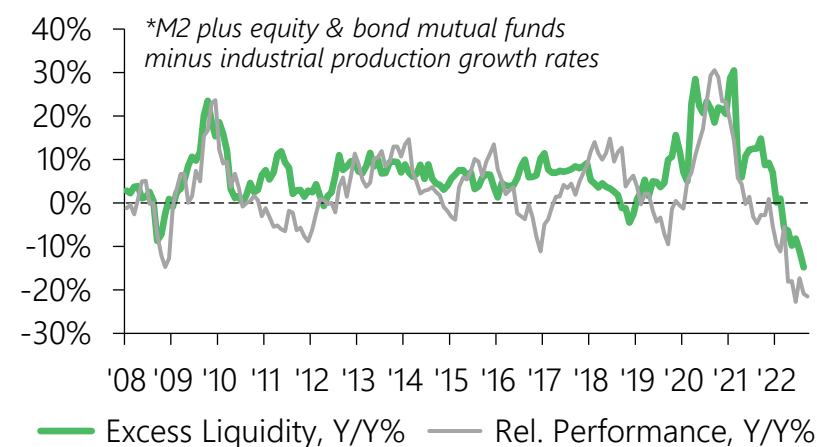
### Fiscal Responses in Large Crises

Estimated Coefficients



Source: International Monetary Fund

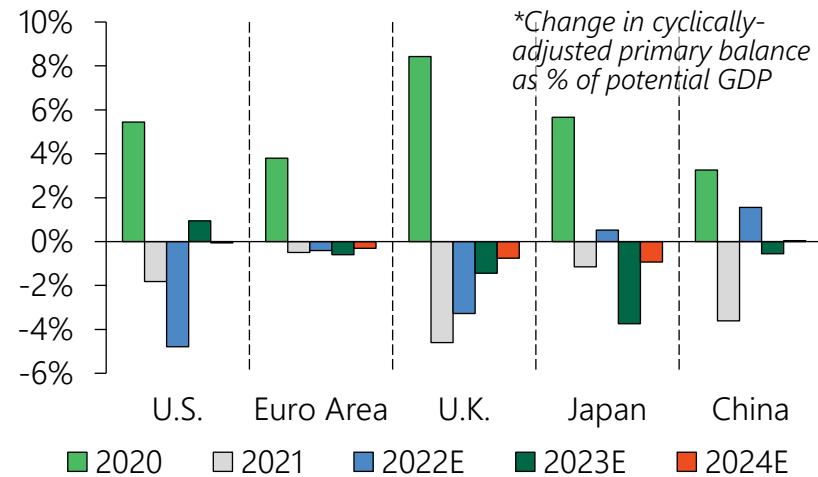
### Non-Dividend/Dividend Payer Relative Performance vs Excess Liquidity\*



Source: Federal Reserve, Investment Company Institute, FactSet

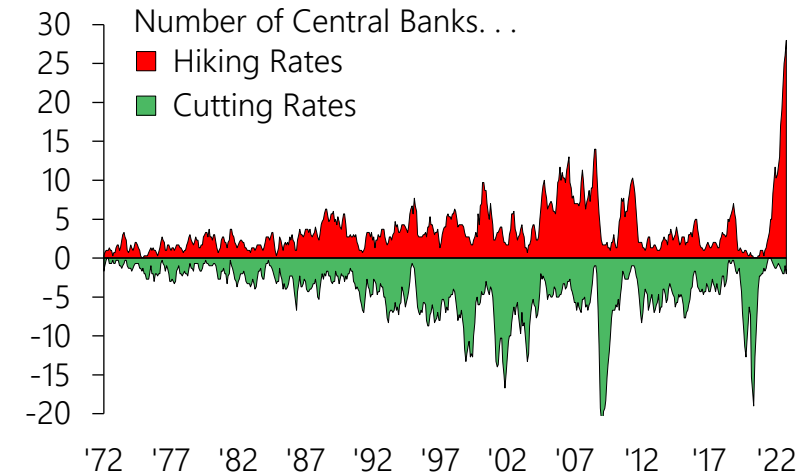
## FISCAL AND MONETARY POLICY TIGHTENING

### Fiscal Impulse\*



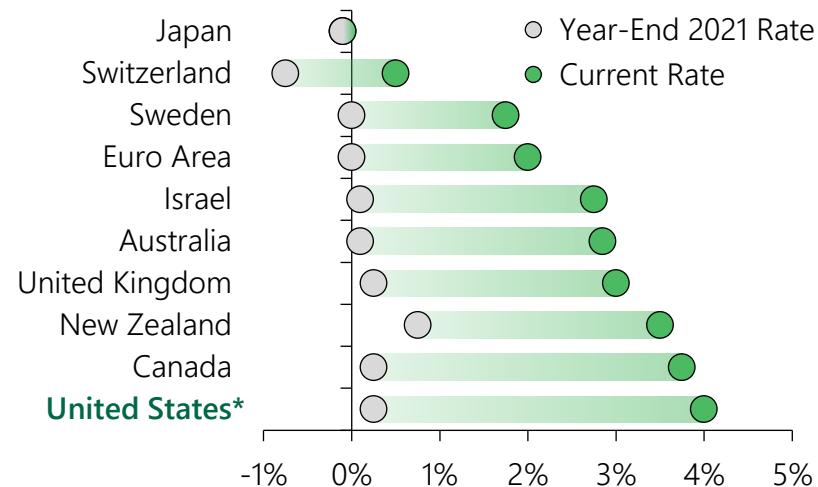
Source: International Monetary Fund

### Global Central Bank Policy Rate Cycles



Source: World Bank, Bank for International Settlements

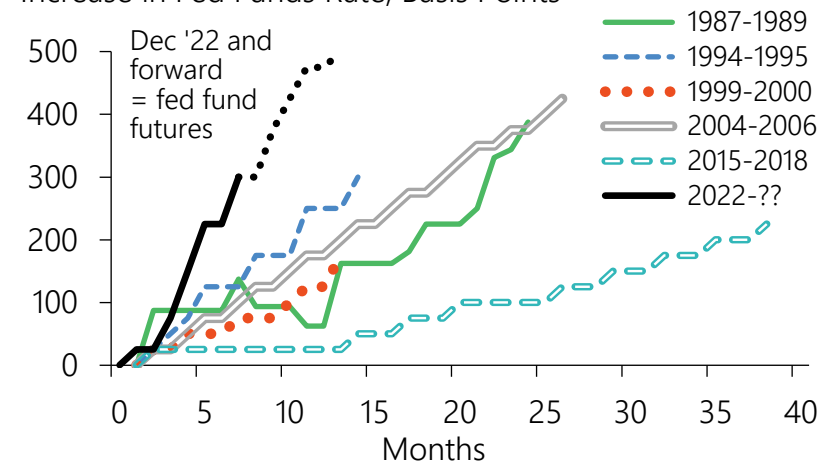
### Policy Rate Changes, Developed Markets, YTD 2022



Source: FactSet

### Pace of U.S. Monetary Tightening Cycles

Increase in Fed Funds Rate, Basis Points



Source: Federal Reserve, CME Group

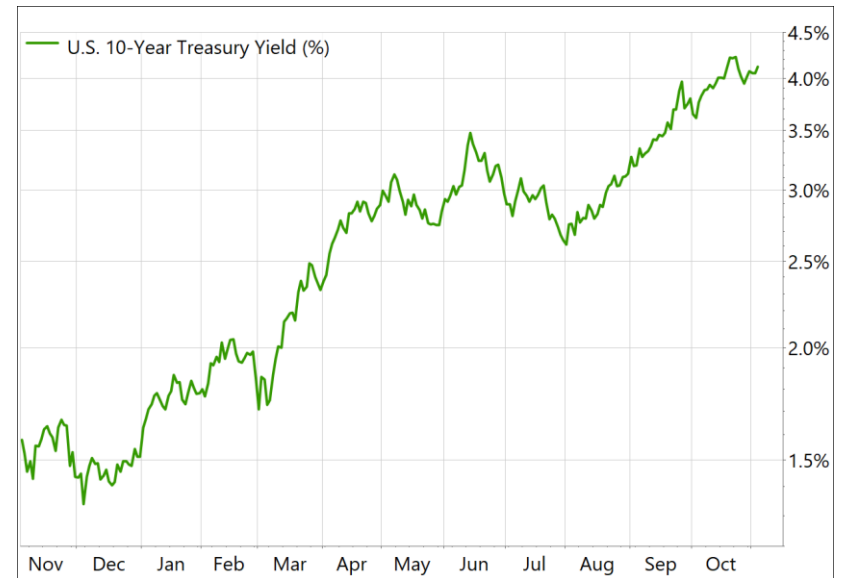
Source: IMF 10/17/22, World Bank, Bank for International Settlements 10/31/22, FactSet, 11/4/22 Federal Reserve, CME Group 11/4/22

# LASTING REVERSAL IN DISINFLATIONARY BACKDROP WOULD BE PAINFUL

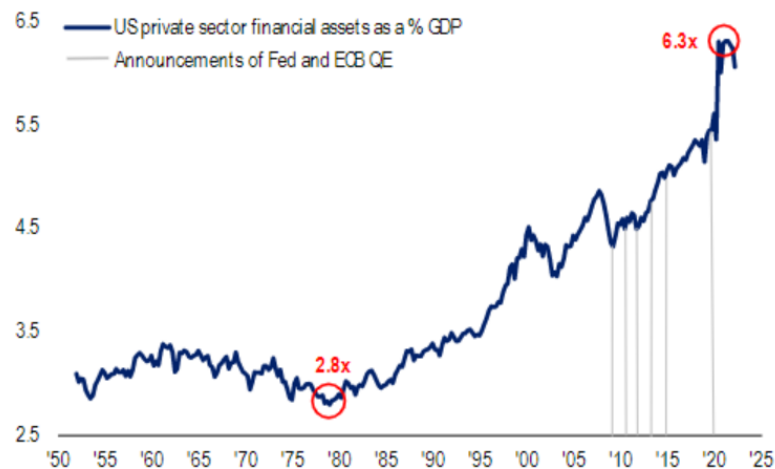
The End of the “Lowflation” Era



Source: Bloomberg, Evercore ISI Research

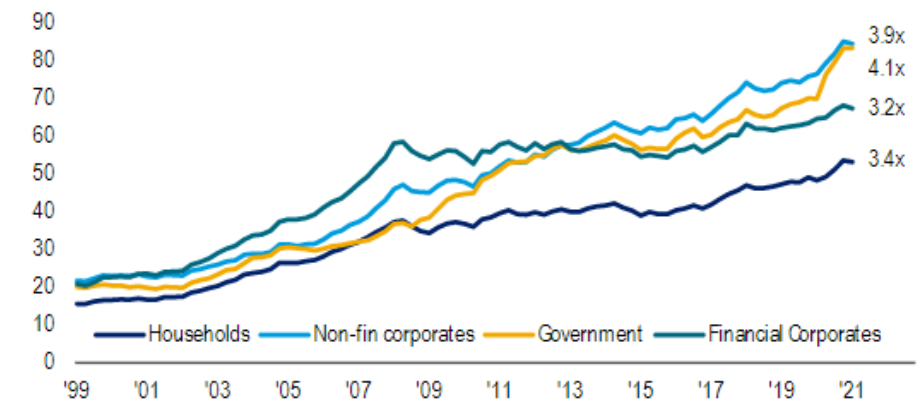


US private sector financial assets % of GDP



Large rise in leverage over the past decade

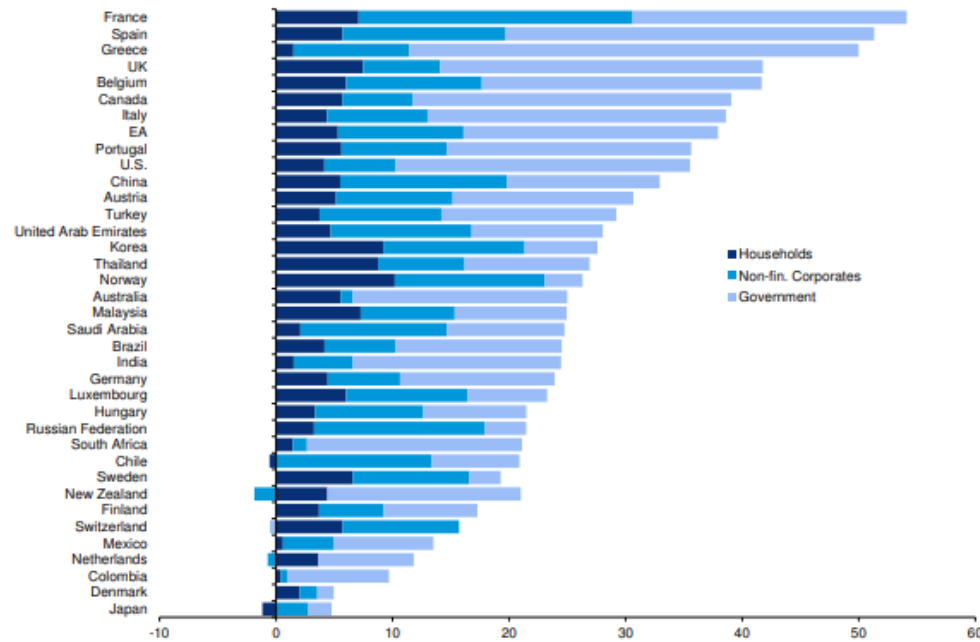
Change in global debt by sector, \$tn



Source: Bank of America/Merrill Lynch 7/28/22 & 7/19/21, Wall Street Journal 6/25/22  
Factset Research Systems 11/3/22

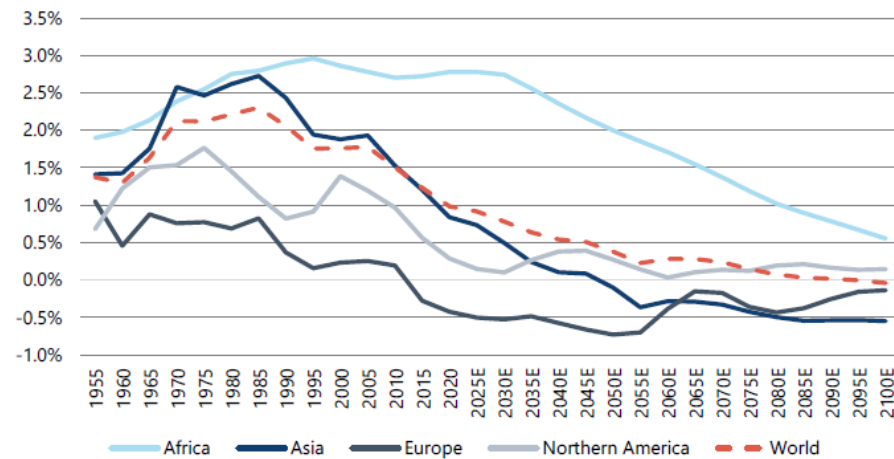
# DEBT BURDENS AND DEMOGRAPHICS TO PRESSURE GLOBAL GROWTH FOR YEARS TO COME

Change in debt-GDP, between Q4-2019 and Q4-2020 (pp)



Source : IIF, BIS, IMF, National Sources, Deutsche Bank

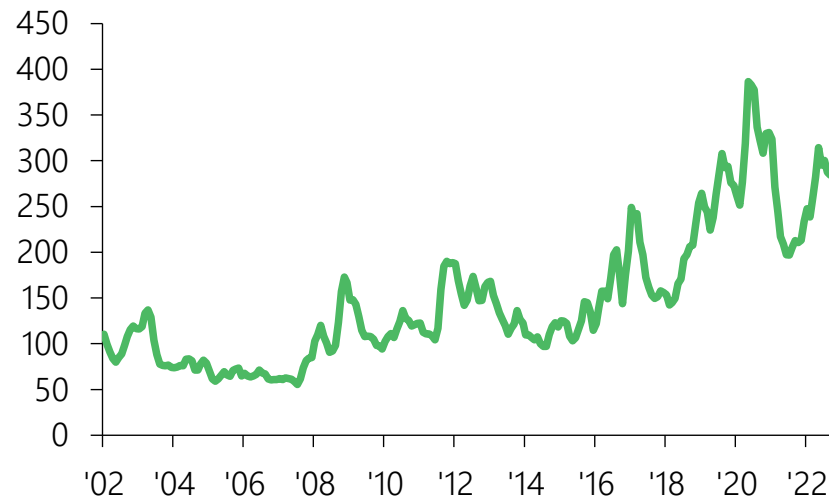
Annual change in working age population, 1955-2100



Source: Deutsche Bank Research 5/7/21, Jeffries 1/17/22

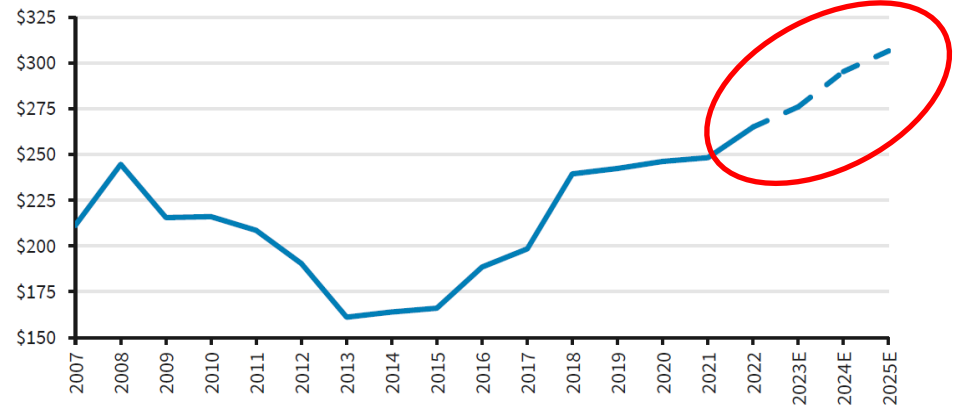
## GEOPOLITICAL RISKS LIKELY TO REMAIN HIGH

Global Economic Policy Uncertainty Index

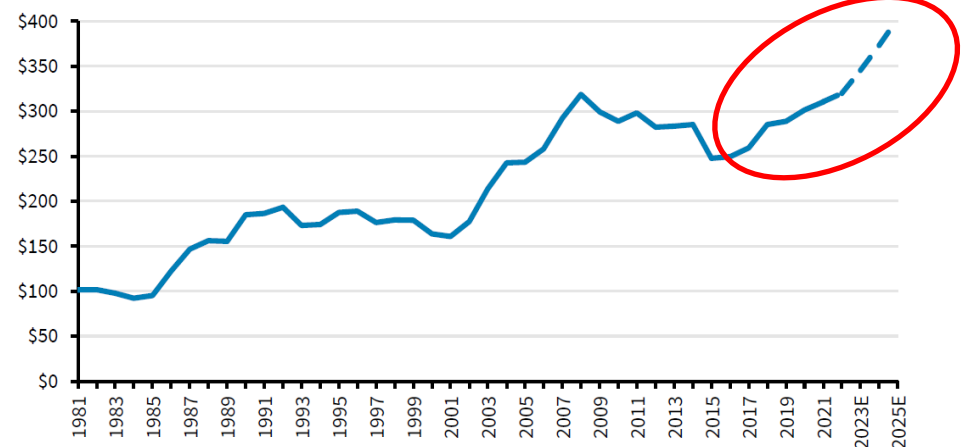


Source: Baker, Bloom & Davis

U.S. Modernization Budget Forecast FY23-25

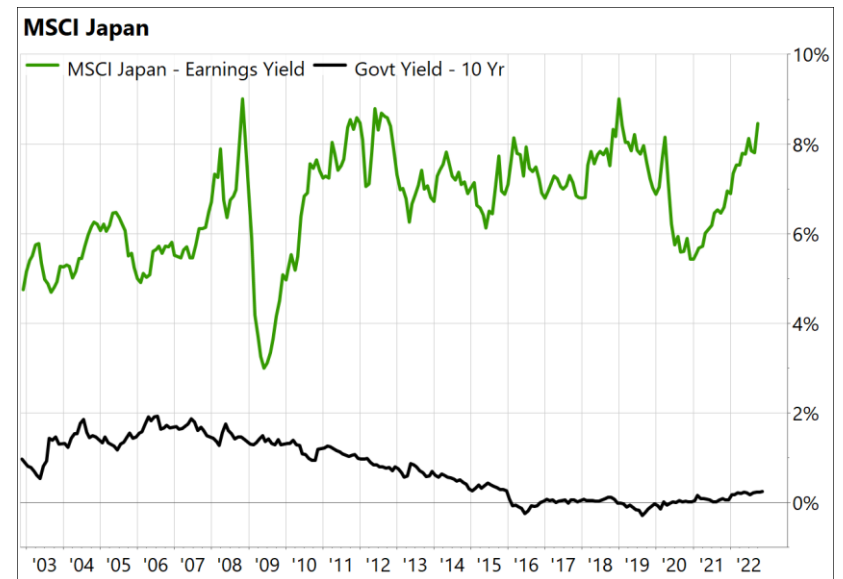
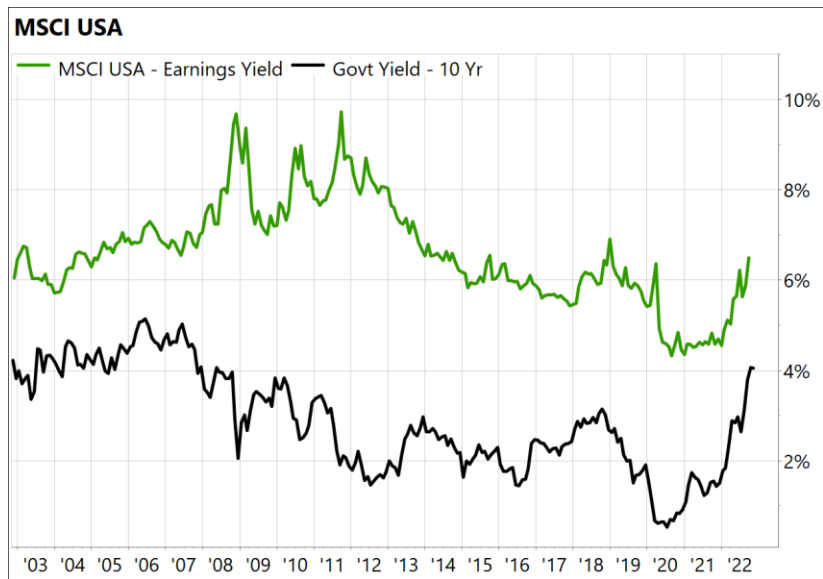
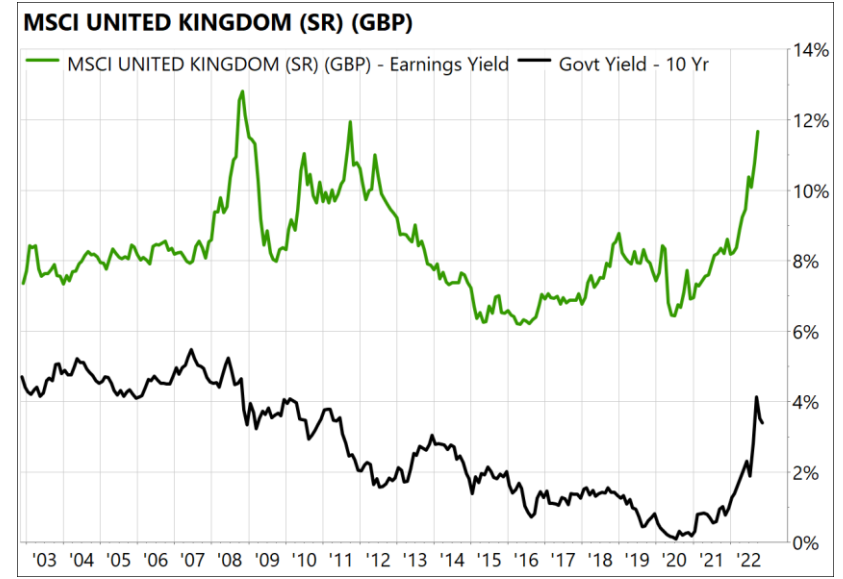
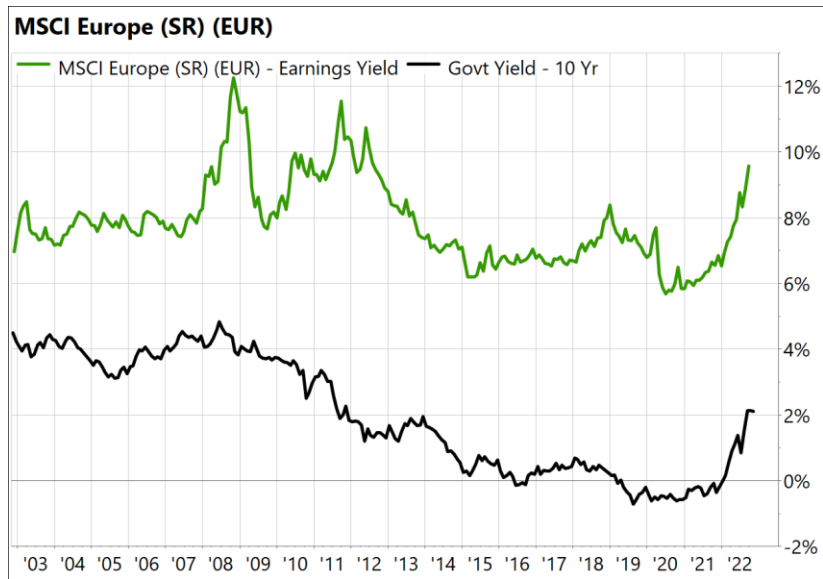


Europe NATO Members Nations – Defense Spending (Current \$)



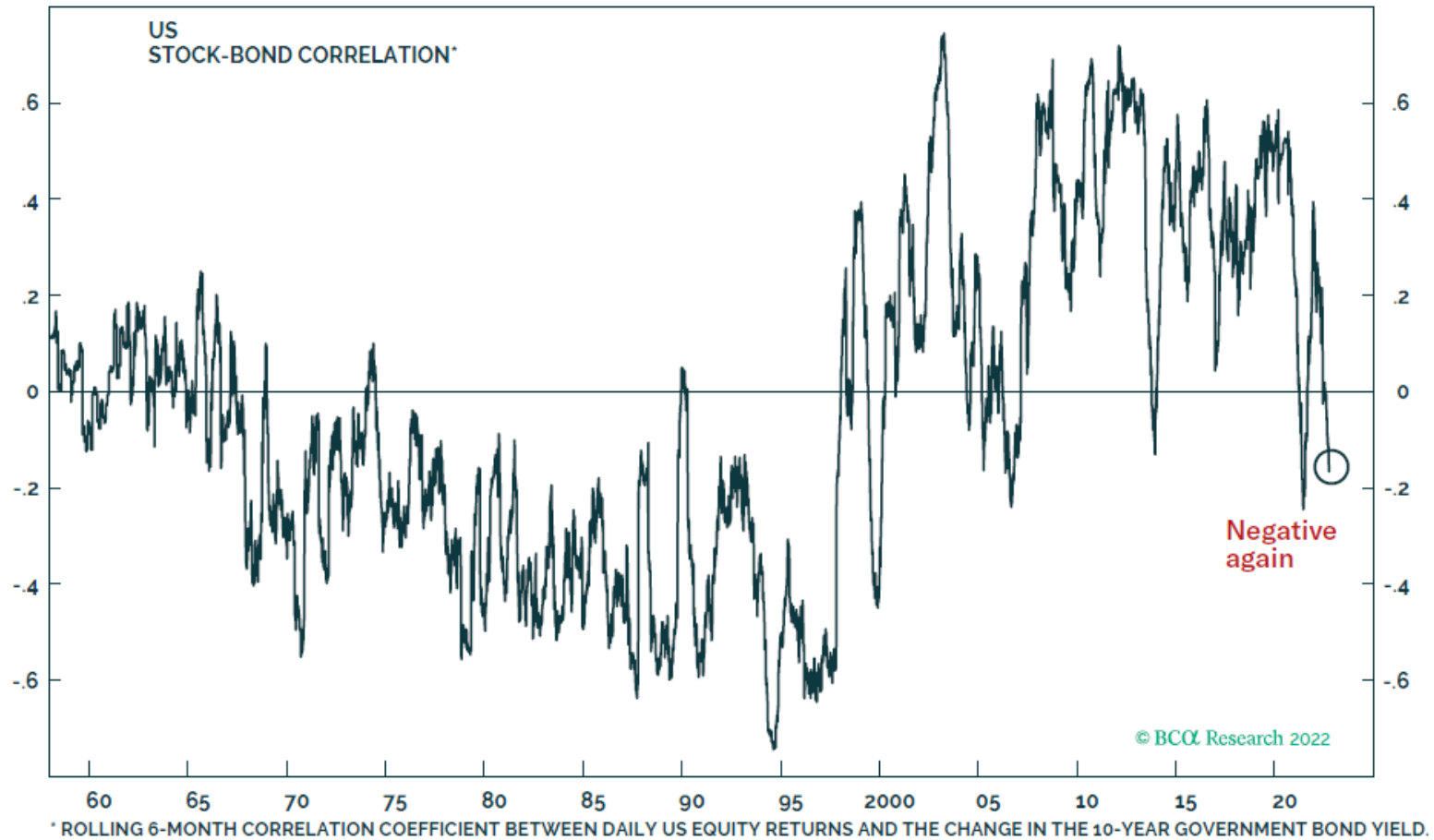
Source: Baker, Bloom & Davis 9/30/22, Barclays 7/14/22

## EARNINGS YIELD GREATER THAN BOND YIELDS GLOBALLY



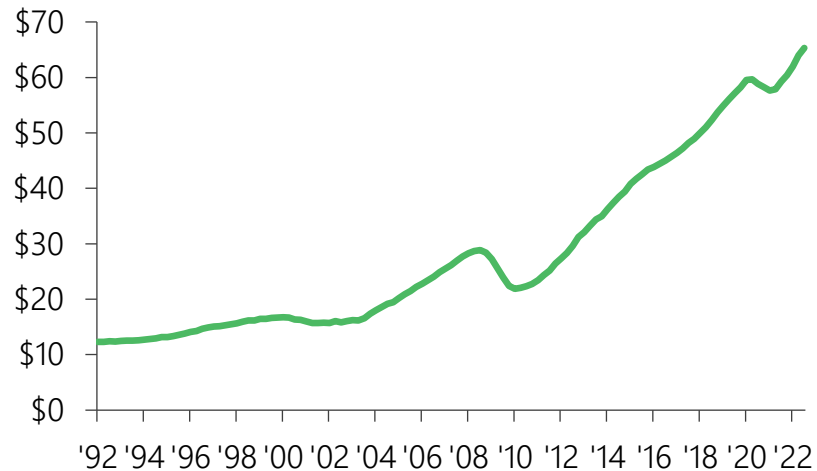


## BONDS ARE NOT INSULATING INVESTORS AS THEY ONCE DID



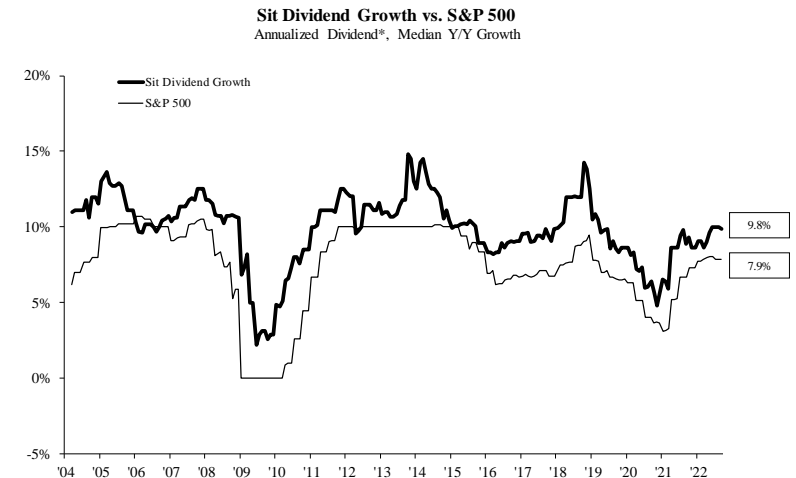
# DIVIDENDS AND SHARE BUYBACKS ACCELERATING

## S&P 500 Cash Dividends per Share



Source: S&P Global

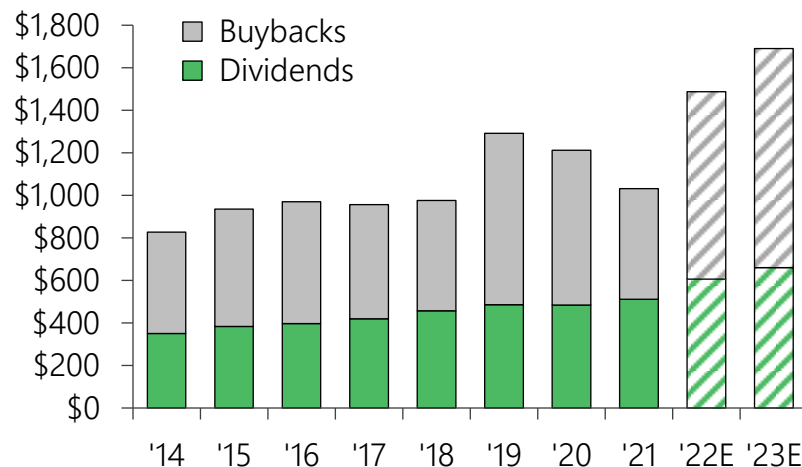
## S&P 500 dividend payout ratio vs. Forward P/E



Source: FactSet & Compustat

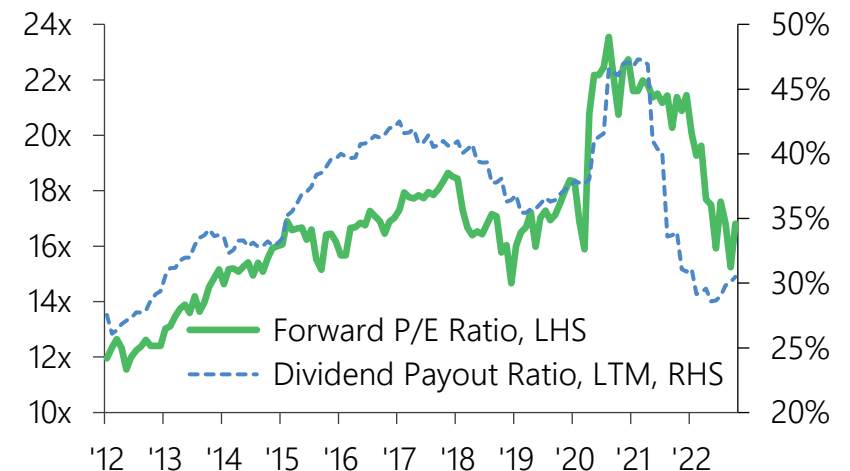
\* Methodology: Annualized dividend payment based on quarterly dividend paid/announced in local currency, including the local currency dividend for ADR parent securities where applicable.

## S&P 500 Share Buybacks and Dividends (\$ Billions)



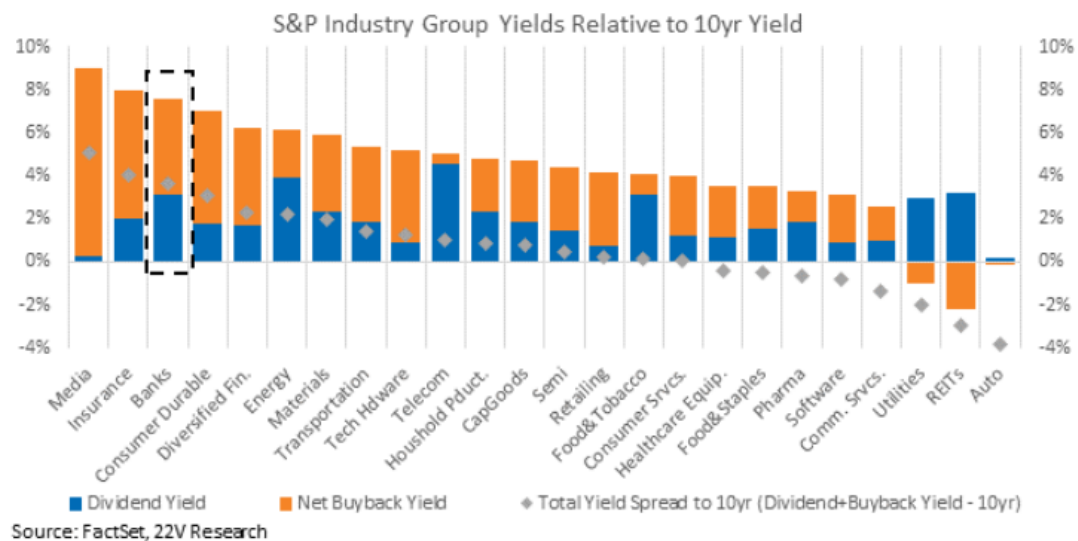
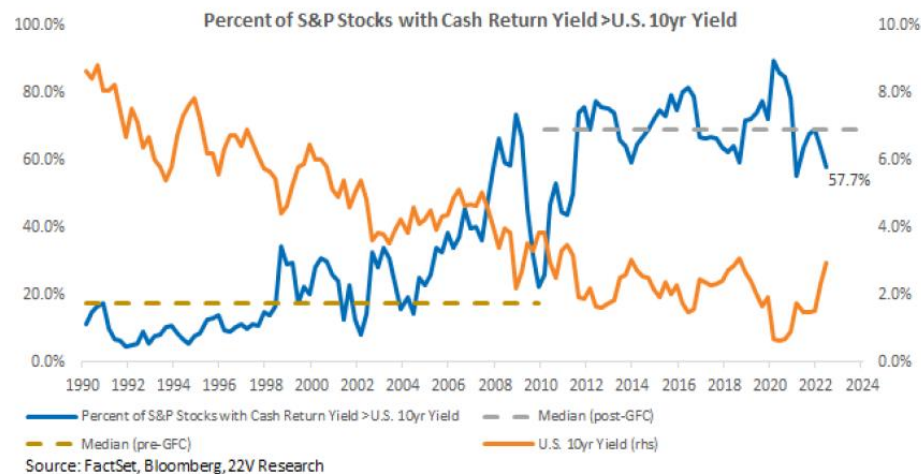
Source: FactSet, Goldman Sachs

## S&P 500 Forward P/E Ratio vs Dividend Payout Ratio



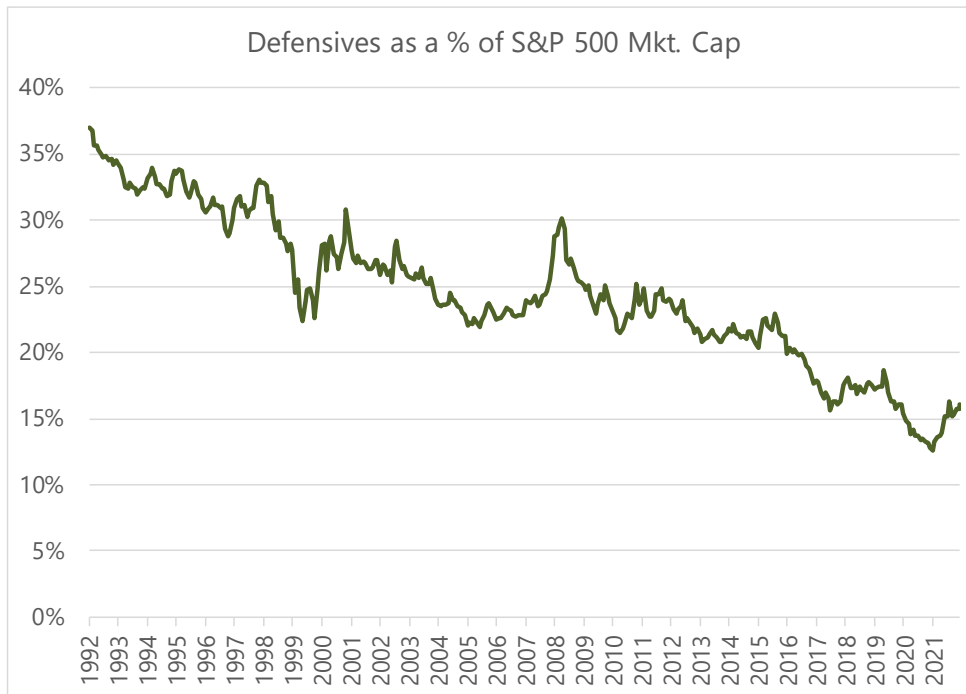
Source: FactSet

## DESPITE HIGHER RATES, CAPITAL RETURN STRATEGIES REMAIN ATTRACTIVE



Source: 22V Research 7/2022 & 10/16/22

## MASSIVE UNDERPERFORMANCE IN DEFENSIVE SECTORS AND NON-DIVIDEND PAYERS



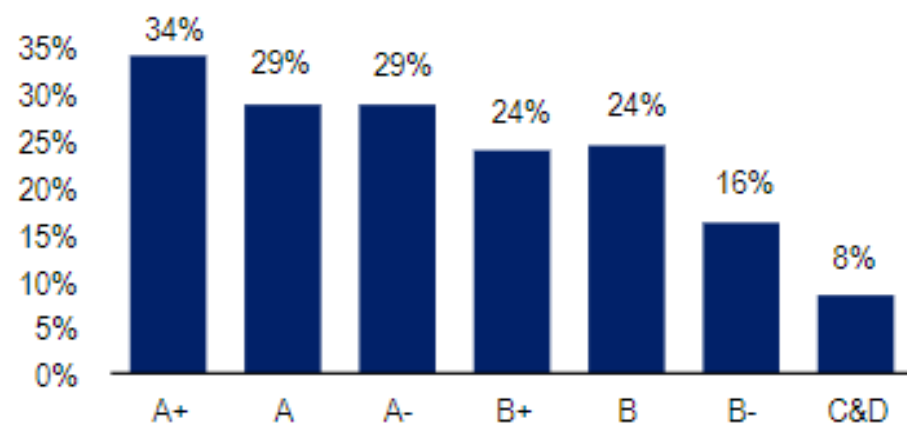
Defensives include: Telecommunication Services, Consumer Staples, Utilities, and Pharmaceuticals

### Attribution Dividend Payers vs. Non Dividend Payers 6/29/2012 to 10/31/2022

S&P 500		
	Average Weight	Total Return
<b>DIVIDEND</b>	<b>82.02</b>	<b>240.14</b>
<b>NO DIVIDEND</b>	<b>17.98</b>	<b>345.40</b>
<b>Total</b>	<b>100.00</b>	<b>247.56</b>

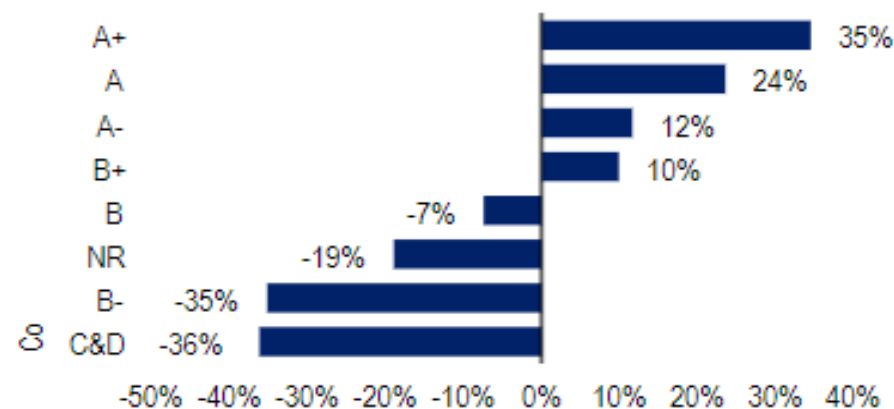
## DECELERATING PROFIT CYCLE AND INCREASING VOLATILITY FAVORS QUALITY ORIENTATION

Average performance by S&P 500 Quality Ranks when the profits cycle decelerated (last seven cycles, 1988-present)



Source: BofA US Equity and Quant Strategy, S&P

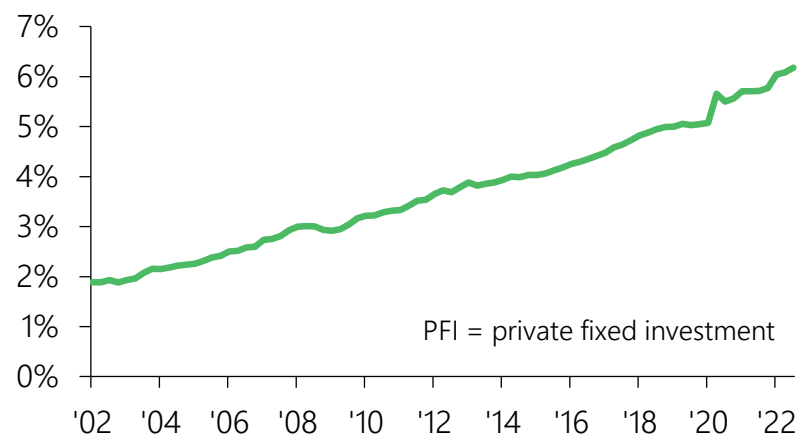
BofA Quality Indices 12m Performance Correlation to 12m Changes in CBOE VIX (1986-4/30/2022)



Source: BofA US Equity and Quant Strategy, Standard & Poor's

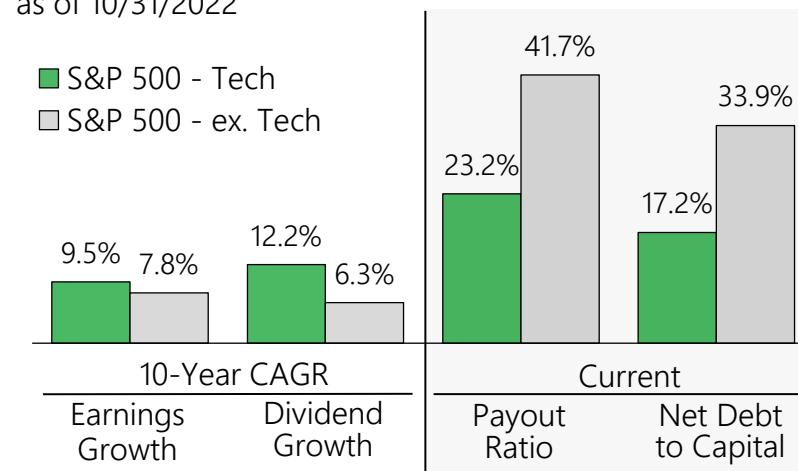
## TECHNOLOGY SECTOR ATTRACTIVE FOR DIVIDEND GROWTH INVESTORS

**Real PFI: Information Processing Equipment & Software**  
Percent of Real GDP



Source: Bureau of Economic Analysis

**S&P 500: Information Tech vs Non-Information Tech**  
as of 10/31/2022



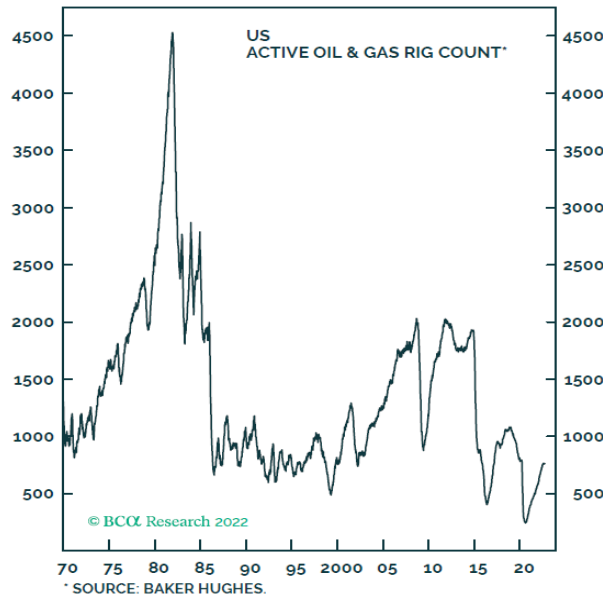
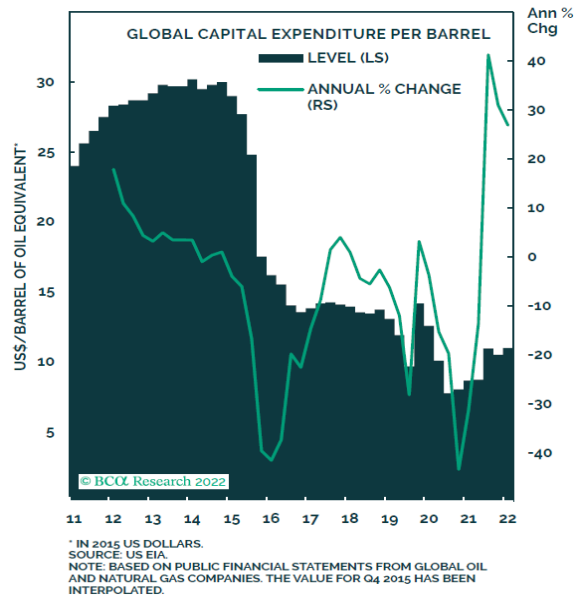
Source: FactSet

### Attractive Tech Dividend Payers

COMPANY NAME	DIV. YIELD	10-YR CAGR		NTM P/E (11/4/22)	NTM P/E (12/31/21)
		DPS	EPS		
Accenture Plc	1.7%	11%	11%	22.5x	38.0x
Genpact Limited	1.1%	n/a	8%	15.4x	19.8x
Broadcom Inc.	3.5%	40%	26%	11.4x	19.8x
Oracle Corporation	1.7%	18%	1%	14.6x	17.2x
Microsoft Corporation	1.2%	12%	18%	21.9x	34.0x
Analog Devices, Inc.	2.1%	10%	5%	15.1x	22.8x
Skyworks Solutions, Inc.	2.8%	n/a	22%	8.8x	13.1x
TE Connectivity Ltd.	1.9%	11%	11%	16.5x	22.1x
Tech Group (Median)	1.8%	11%	11%	15.2x	21.0x
S&P 500 (Median)	1.6%	9%	8%	17.0x	20.2x

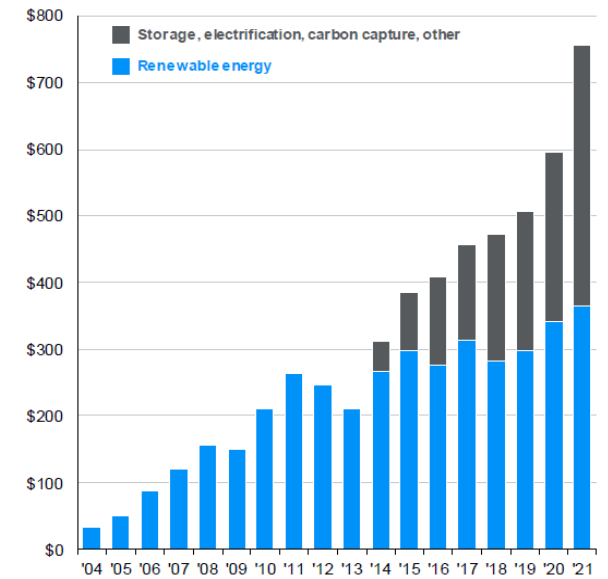
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# UNDERINVESTMENT IN OIL AND GAS, WITH RENEWABLES SURGING



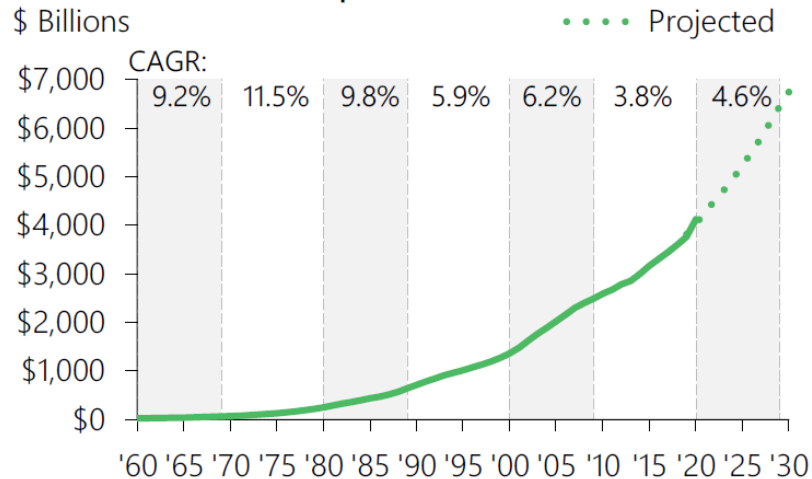
## Global investment in energy transition

Billions USD, nominal



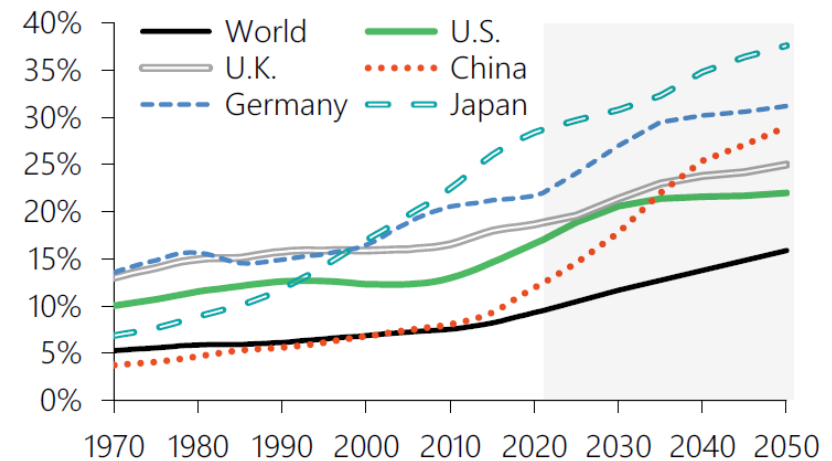
## SECULAR CASE INTACT FOR HEALTH CARE

### U.S. National Health Expenditures



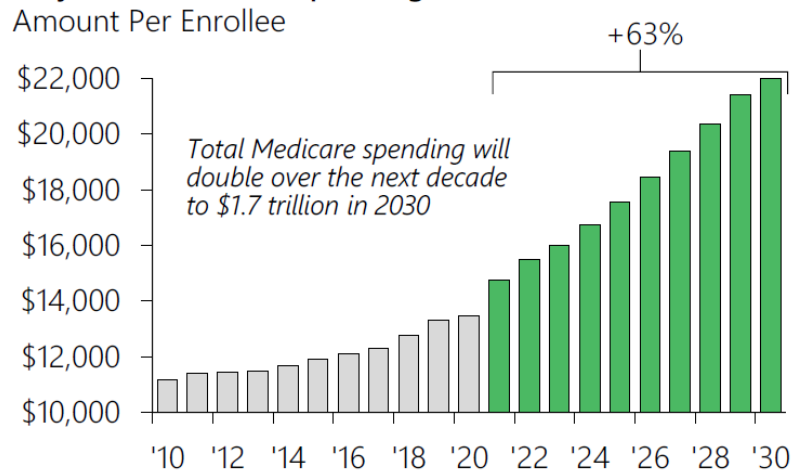
Source: Centers for Medicare & Medicaid Services

### Population Age 65+



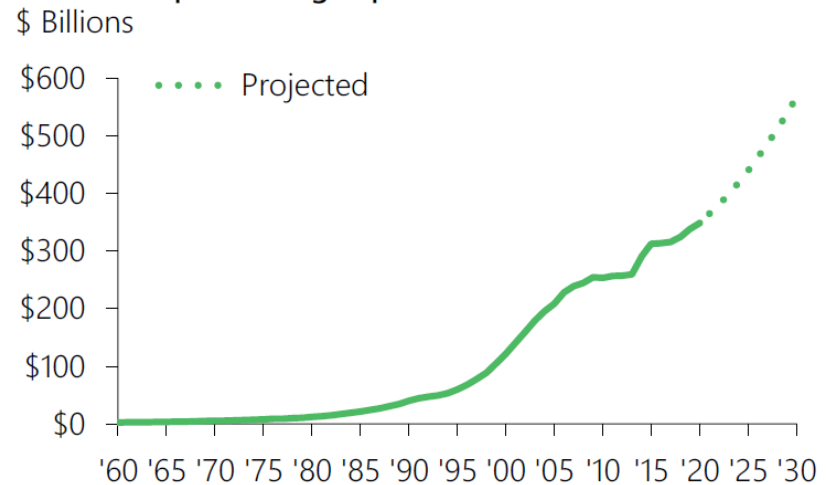
Source: World Bank, U.S. Census International DB (Projections)

### Projected Medicare Spending



Source: U.S. Department of Health & Human Services

### U.S. Prescription Drug Expenditures



Source: Centers for Medicare & Medicaid Services

Source: Centers for Medicare & Medicaid Services, World Bank, U.S. Census International DB, U.S. Department of Health & Human Services 11/2022



## SIT DIVIDEND GROWTH – SECTOR STRATEGY

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### PRO-CYCLICAL GROUPS

- **Financials/Credit Sensitive:** *Overweight.* Valuations reflect recession risks more than any other sector. Credit trends stable, loan growth and NIM improving, with most banks increasing dividends post capital review. Higher rates support life insurers and the P&C sector, which is in midst of multi-year pricing cycle. Regardless of sub-industry, favor firms with strong capital positions and conservative investment portfolios.
- **Materials/Energy:** *Overweight.* Structural underinvestment in virtually all commodities amplified by Russia-Ukraine conflict; prefer energy to metals/materials given macro risks. Attractive as inflation/geopolitical hedge.
- **Technology – Hardware/Semiconductors:** *Overweight.* Earnings risk largely discounted as valuations have compressed. Favor diversified semiconductor (outside of PCs) names growing via ever-increasing “content” stories in *everything*. Emphasizing exposure to cloud/5G exposure, auto/electric vehicles, industrial, defense.
- **Industrials:** *Equal weight.* Peaking fundamentals, but backlogs support near-term growth. Supply chain pressures largely offset by pricing. Emphasizing infrastructure, “electrification”, commercial aerospace, and automation plays. Slowdown in Europe and China are key risks.
- **Transports:** *Equal weight.* Pricing beginning to erode in some modes (i.e., air freight, truck) just as goods spending is decelerating as consumer shift to service spending. Favor rail as re-opening/commodity export beneficiary.
- **Consumer Cyclical:** *Underweight.* Consumer balance sheets healthy (in aggregate) as job growth accelerates, but risk from “mean reversion” as spending shifts from goods to services as economy normalizes. Labor, energy, and transport costs are major headwinds for many sub-groups.
- **Technology – Software/Services/Internet:** *Underweight.* Lack of dividends and elevated valuations are primary factors driving underweight. Prefer IT service firms and select software. Higher interest rates remain a challenge to valuations via “duration effect,” while growth is slowing in formerly “hot” areas (AI, cloud, etc.)

## SIT DIVIDEND GROWTH – SECTOR STRATEGY

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### NON-CYCLICAL/DEFENSIVE GROUPS

- **Healthcare:** *Overweight.* Valuations attractive on achievable expectations; favor US based service companies (HMO's/hospitals) and med-tech over bio/pharma given drug pricing risks. Sector trading at 30% discount to consumer staples and overall markets despite much stronger growth prospects. Minimal "rotation risk" due to interest rates or if market sentiment improves (i.e., to "risk on").
- **Utilities:** *Overweight.* Valuations high but best hedge (by far) against macro "tail" risk given EPS visibility, immune to U.S. dollar swings, inflation/supply chain pressures. Growth (5-8%) supported by rate base and underappreciated renewables (wind, solar, T&D) growth, boosted by recently passed IRA.
- **P&C Insurance:** *Overweight.* Pricing improving following significant catastrophe and COVID-related losses. Higher interest rates boosting investment income. Favor commercial over personal lines.
- **Defense:** *Overweight.* Russia-Ukraine will likely mark an inflection point in defense budgets, with Europe the key driver.
- **REITS:** *Equal weight.* Valuations generally attractive (including 3-5% dividend yields), fundamentals broadly improving for most subsectors with limited new supply pressure. Rising rates and persistent inflation a key risk.
- **Consumer Staples:** *Equal Weight.* High valuations and slow growth, margin pressure from price/input costs, substitution risk from private label. Beverages and consolidation stories attractive.
- **Telecommunications:** *Underweight.* Defensive with modest growth, high dividend yields, and attractive valuations. Underweight telco providers given debt and competitive concerns; favor 5G exposure via tower companies.

## IMPORTANT DISCLOSURES

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