What are the major trends in global income?

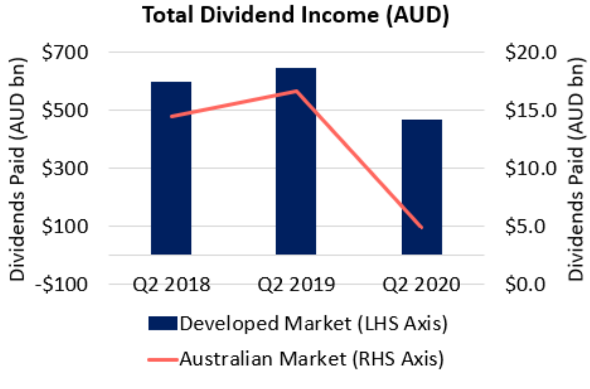
- In AUD terms dividends fell 28% in Q2 2020 (v Q2 2019), the second fall in dividends in 3 years, as companies continue to be impacted by the Covid pandemic. Despite this, Global developed market companies still paid out $A465bn in Q2, slightly more than Q1 2020.

- On the positive side, 40% of dividend paying companies increased or initiated dividends compared to the same quarter last year. However, 13% decreased dividends and 29% cut to zero. Substantial dividends exist, but clients must take increasing care in how they access them.

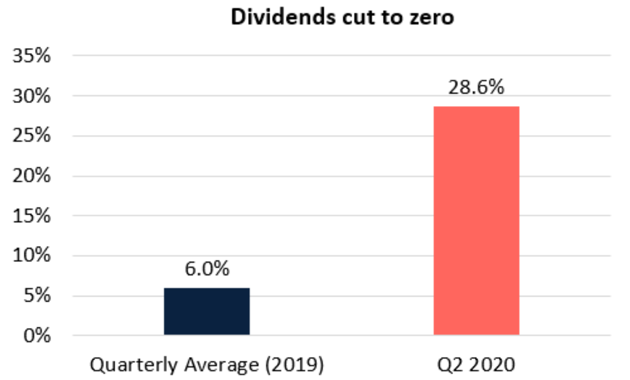
- The increase in the number of companies cutting to zero (29%) is stark when compared to the 2019 quarterly average of 6%, illustrated in the chart below. Investors now need to be more careful than ever in avoiding dividend traps.

- Despite such weakness, the Plato Global Equity fund continues to distribute 6% p.a. yield since inception. This highlights the continued importance of active management in income generation.

- The list of companies completely cutting dividends to zero in Q2 included large, well known companies like Boeing, HSBC bank and Adidas.



Source: Factset



Source: Factset

- The effect of currency on dividends in Q2 2020 was +4%, due to a broadly weaker $A versus Q2 2019, highlighting a benefit from not hedging currency. This slightly offset a fall of over -30% in local currency terms.

- Changes in dividends were not uniform. North America (+0.9%) displayed growth versus the previous corresponding quarter. In stark contrast European (-47%) and Asian (-27.4%) dividends fell substantially, in a quarter usually driven by annual paying European firms.

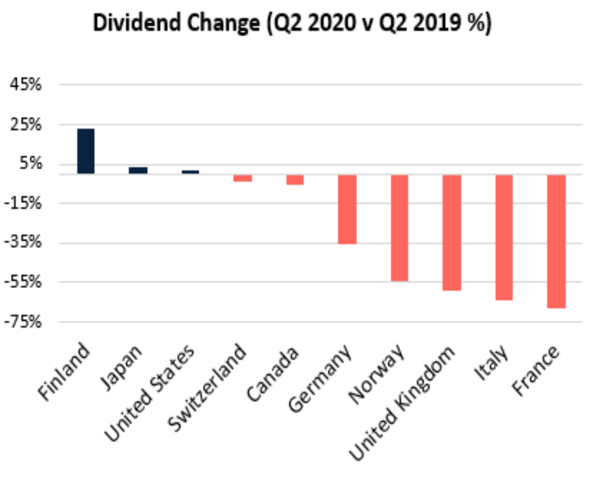
- However, US dividends were also negative in local currency terms, boosted just into positive territory by a relatively weaker Aussie dollar.

- It is interesting to note that some banking regulators discouraged (Australia), or outright banned companies from paying dividends (UK, NZ) or in some cases suggested deferring dividends.

Plato INVESTMENT MANAGEMENT Global Income Quarterly – **Covid Update** (Q2 2020)

Which countries are leading the charge?

- Some large countries, who have low payout ratios, had positive percentage increases (US +1.6%, Japan +3.4%). These gains in Japan and the US, when translated into AUD paid, were mainly due to currency strength versus the domestic dollar.
- However, the US tends to return money to shareholders in the form of stock buybacks which did reduce substantially in Q2.
- Dividends fell across most developed market countries. This included France (-68.3%) and the UK (-58.5%).
- In local currency terms only one country, Finland, grew its dividends.
- Dividends contracted -70.7% in Australia, although Q2 is a small dividend quarter domestically. Examples of companies that decreased dividends were Westpac Banking Corp., ANZ banking Group and Sydney Airport. These companies cut their distributions to zero.
- This fall is largely caused by bank dividend deferrals and cuts. It is important to note that if a company deferred a dividend, such as Westpac, we consider that a cut in this period. This may overestimate the reduction in yield.



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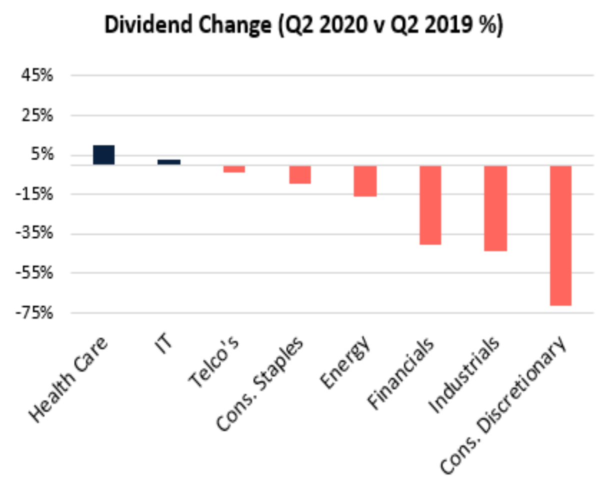


Source: Factset

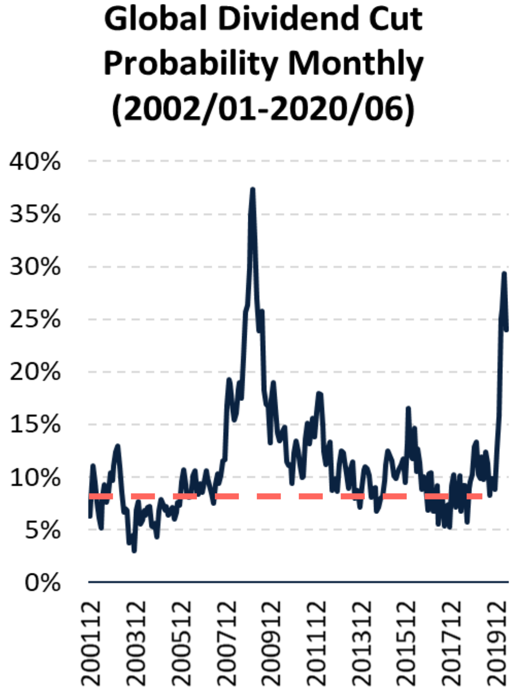
What happened in global sectors?

- COVID-19, and the associated economic risks, continue to impact sectors differently.
- Health care continued its recent dividend growth, up 9.2%. IT (+2%) was the only other sector to record positive growth in Q2. Telco's did hold up relatively well, down only -3.8%. Lockdowns and the trend to work from home in the pandemic have benefitted both the IT and Telco sectors. Healthcare was another obvious beneficiary in a health driven pandemic.
- In stark contrast the Consumer Discretionary sector posted the worst fall in income, down over -70%, when compared to Q2 2019. As unemployment rose and household budgets tightened, discretionary spending became increasingly challenged.
- Despite a -40.1% fall in dividends, Financials continued to be the largest dividend payer in AUD terms ($97bn AUD), contributing over 20% of the total income in Q2.

Plato INVESTMENT MANAGEMENT — Global Income Quarterly – **Covid Update** (Q2 2020)

Interesting facts in global income

- When incorporating dividend cuts and initiations, 1 company increased or initiated dividends for every one company that reduced or completely cut dividends versus the previous corresponding quarter. This illustrates that the number of dividend cuts is much larger than previous periods.
- 3.7% initiated a dividend in Q2 2020, compared to 3% in Q1 2020.
- 51% of US companies that pay dividends increased or initiated them in Q2 (v Q2 2019), versus 24.5% that cut or decreased. Just under half of all US companies paid out in the last 12 months.
- 35% of the companies in the universe covered paid dividends in Q2 2020. At the country level Canada (58%) and Switzerland (60%) had the highest number of dividend payers in Q2 by number of companies.



Source: Plato Investment Management

What's the outlook for global income?

Plato's proprietary dividend cut model provides insights into future dividends. It represents Plato's macro view regarding the likelihood that global developed markets will cut their income.

Coronavirus continues to create a challenging backdrop for global companies and has resulted in a further reduction in dividends. Plato's aggregated dividend cut model predicts an elevated chance of future dividend cuts (24%). On a positive note there has been a small pull back from recent highs.

Remaining high risk with respect to dividend cuts are predictable industries, significantly challenged by the virus. These include Transportation infrastructure, Automobiles and Airlines. Interestingly Hotels, Restaurants and Leisure has seen a small pull back, although it still remains elevated.

In conclusion;

- The dividend cut model was very accurate in predicting the magnitude of the dividend cuts in Q2. Thankfully our model has come back a bit, signalling possible respite from the recent surge in companies cutting dividends.
- Lower yielding countries (US, Japan) had stronger relative growth in yield. The traditional areas that provide income for yield investors were the ones cutting. Growth stocks in sectors like IT and Healthcare have outperformed in recent times and consequently seen less pressure on yield when compared to some of the underperforming value sectors.
- In this challenging environment investors need to be remain cautious where they look for income. Stock selection will be very important. Separating the wheat from the chaff is key... Or in this case separating strong dividend payers from “dividend traps”.

Methodology

1. The methodology uses dividends paid, in AUD, however the ex dividend date is used to allocate the dividends in the relevant time period i.e. Q2 2020.
2. Dividend paid ($) for each stock in each calendar quarter is calculated as the shares outstanding as of quarter end multiplied by the total gross dividend per share (DPS) paid out in the calendar quarter. The DPS paid excludes spin offs but includes capital returns and special dividends. Conversion to AUD is done using the prevailing WM/Reuters London exchange rates at the time of dividend payment.
3. Full year dividend paid ($) is the summation of dividend paid ($) from Q1 to Q4 using the methodology (1).
4. DPS movement is based on total DPS paid out (in local currencies) over each calendar quarter. DPS movement from quarter to quarter is then categorised as initiating, increasing, unchanged, decreasing or cut to zero.
5. Secondary issues are removed from the calculations to prevent double counting of income.