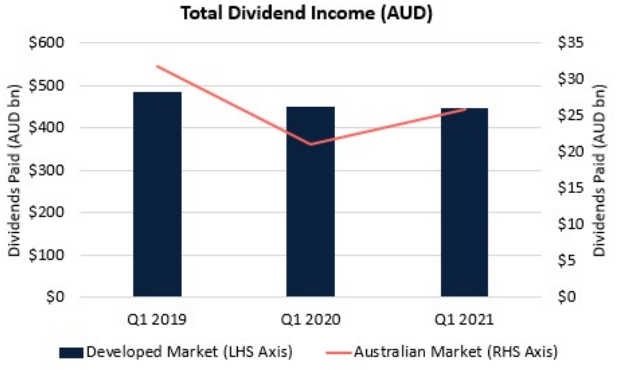
Global Income Quarterly – 2021 Q1 update

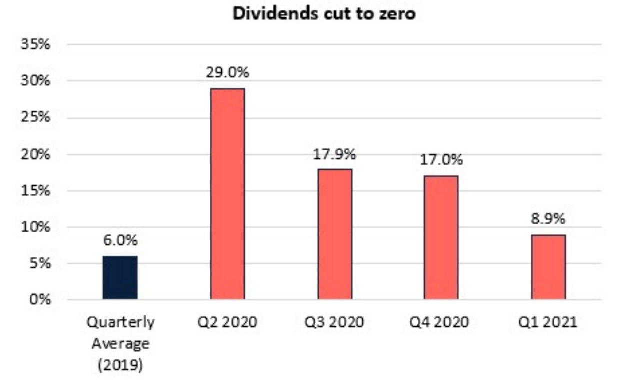
Plato
INVESTMENT MANAGEMENT

What are the major trends in global income?

- In local currency terms income grew substantially (15.1% Q1 2021 v Q1 2020), reflecting the improvement in economies.
- In AUD terms dividends were stable, -0.5%, in Q1 2021 (v Q1 2020). Despite the sustained impact of Covid-19 on company earnings, this reflects a continued improvement in the outlook for dividends (Dividend changes in 2020 were; Q1 -6%, Q2 -28%, Q3 -13%, Q4 -11%).
- The effect of currency on dividends in Q1 was -15.6%, due to a broadly stronger $A compared to the lows in Q1 2020. This large currency effect reduces dividends to Aussie investors and hence the AUD based growth numbers in this report.
- Global developed market companies paid out $A447bn in Q1. After a very weak 2020 we are seeing a much improved picture, inline with our previous forecasts, for the year ahead.
- The number of companies cutting to zero (9%) has fallen substantially when compared the previous quarters, and is more in line with the long term average.
- 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 and avoiding dividend traps.



Source: Factset

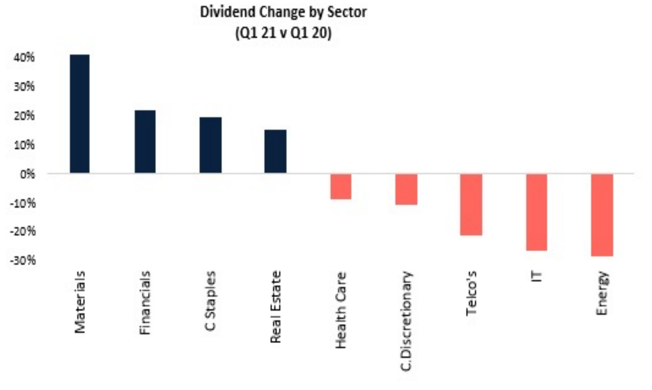


Source: Factset

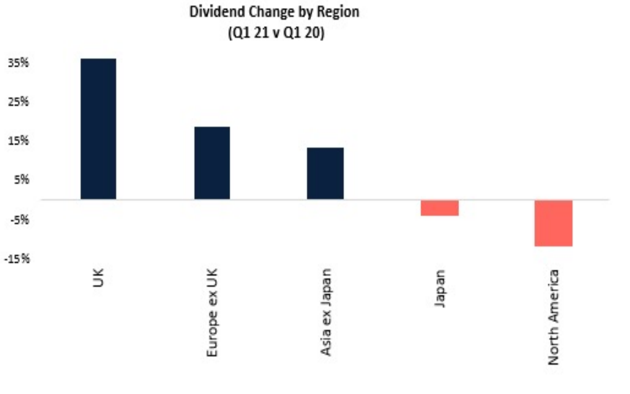
- On the positive side, 37% of dividend paying companies increased or initiated dividends compared to the same quarter last year. However, 18% decreased but still paid a dividend.
- The list of companies that paid dividends in Q1 2020, but not in Q1 2021, included well known companies like EasyJet plc. Many, including Boeing Company and Marriott Intl had actually cut previously in 2020 when the pandemic first impacted earnings.
- Changes in dividends were not uniform. After substantial declines, European dividends rebounded strongly in AUD terms (Europe ex UK +18%, UK +36%). Asian dividends also improved after large falls last year (+1%). In comparison North America fell -12%, the worst of the regions. This was driven by currency moves, US and Canadian dividends were positive in local currency.

Which countries are leading the charge?

- European countries were certainly leading the charge on dividends in Q1.
- After substantial falls, some European countries more than doubled dividends, albeit from a small dollar base. Increases included Finland 216%, Italy 166% and Norway 101%.
- The change in dividends versus the previous corresponding quarter was very mixed. There were obvious winners, including the UK which was also up strongly. Two large countries, with low payout ratios, had underlying dividend growth but fell when translated into AUD (US -13%, Japan -4%).
- The companies contributing to the increase in income included Tesco PLC, HSBC Holdings and ING Groep. None of these names paid in Q1 2020.
- After a weak 2020, dividends rebounded strongly (+23%) in Australia. This was led by large increases from the miners, RIO, BHP and Fortescue Metals. APRA announcements and write-backs of Covid related bad debt provisions continue to fuel our expectations for an increase in bank dividends.



Source: Factset



Source: Factset

What happened in global sectors?

- COVID-19, and the associated economic risks, continue to impact sectors differently. In 2020 IT & Healthcare increased dividends the most, with Consumer Discretionary and Financial names hurting. The story in Q1 has changed somewhat. Materials, Financials and Staples have posted strong increases, leaving IT and Energy to trail behind. Many energy companies are repairing their balance sheets, but the dominance of US IT companies creates a substantial currency impact in IT. For example, Microsoft and Apple increased DPS, but paid far less in AUD.
- Whilst we still see the defensive nature of staples, discretionary continues to cut dividends. The lower level of cuts reflects large previous decreases to income. Large dollar payers in consumer staples include Procter & Gamble and Walmart. Discretionary names, hit by the pandemic, that have cut include Marriott, Ford and Carnival Plc.
- Materials (+41%) had the largest increase in Q1, driven by companies including Anglo American and Rio Tinto. In contrast Energy continues to reflect the weak 2020 for the sector, paying out -28% less income than in Q1 2020. Businesses that reduced their payout to shareholders include Royal Dutch Shell and BP.
- Financials (+21%) continued to be the largest dividend payer in AUD terms ($84.7bn AUD), contributing 19% of the total income in the quarter.

Global Income Quarterly – 2021 Q1 update

Interesting facts in global income

- When incorporating dividend cuts and initiations, 1.6 companies increased or initiated dividends for every one company that reduced or completely cut dividends versus the previous corresponding period. Although still significantly below pre pandemic levels, this ratio has increased since Q2 2020 due to companies that had deferred now paying and the slowing pace of dividend reductions.
- Just under half (47%) of US companies that pay dividends increased or initiated in Q1 (v Q1 2020), versus under a third that remained unchanged. 49% of US companies paid out a dividend in Q1.
- In 2019 65% of companies paid dividends. This fell substantially to 52% in 2020 and is down below half for the first quarter of 2021. Only 3 countries had a payer ratio over 50%, Australia, Canada and Japan.

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.

As the challenges to companies from the Coronavirus become more clear, our model predicts fewer stocks cutting dividends. After the May 2020 high of almost 30%, cuts in Q1 continue to fall. After such significant cuts, we currently predict the chance of global developed market dividends being cut further, is below the long term average of 12%.

Unsurprisingly, industries with a high risk of dividend cuts still include, Transportation Infrastructure, Apparel and luxury goods. Airlines have improved slightly.

In conclusion

- The dividend cut model has been very accurate in predicting the magnitude of the dividend cuts through 2020. The Plato proprietary model is signalling a more positive outlook for 2021.
- Yields, especially in Europe, are showing signs of recovery and markets have seen better performance from the more yield heavy value sectors. Local currency dividends are greatly improved versus Q1 2020. As economies begin to show renewed strength we see an improving story for 2021.
- Our dividend outlook is certainly brightening, but given the fluid environment it is important to look forwards rather than backwards. Stock selection, and avoiding dividend traps, remains key.

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 e.g. Q3 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.