

Euro Dividend Aristocrats

Playing the Recovery in 2021

Ryan Reardon

Senior Smart Beta ETF Strategist

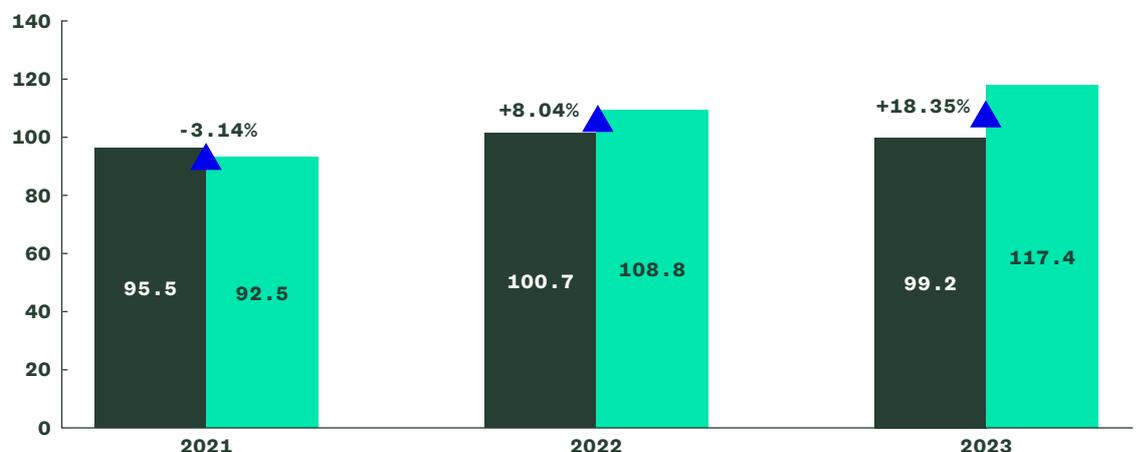
- Market sentiment continues to favour an economic recovery in 2021, as vaccination programs help support a pickup in business activity
- Companies are keen to renew their commitments on returning capital to shareholders through dividends
- A stable dividend strategy, such as the Dividend Aristocrats index tracked by SPDR ETFs, aims to offer investors strong yield factor exposure through higher quality stocks from a diverse range of sectors

The change in economic sentiment at the end of 2020 provides a supportive case for dividend stocks as we look forward to a continued economic recovery in 2021. Analysts remain positive that the stabilisation of cash flows will support dividend growth. This extension of the recovery should see investors considering an allocation to dividend strategies, using Smart Beta ETFs, in order to play this theme.

In this note, we highlight the potential opportunity to benefit in this environment from a Dividend Aristocrats approach, the leading dividend index in European Smart Beta ETFs.

Figure 1
**EURO STOXX 50
Annual Dividend
Outlook**

■ Current Dividend Level (Futures)
■ JPM/Consensus Bottom-up Estimates
▲ Upside (Downside) Potential



Source: JP Morgan Global Dividend Review as of 23 March 2021. JPM/Consensus bottom-up estimates are based on aggregated J.P. Morgan analyst dividend per share estimates, where available, or IBES/Bloomberg consensus estimates.

Macroeconomic Outlook for Dividends

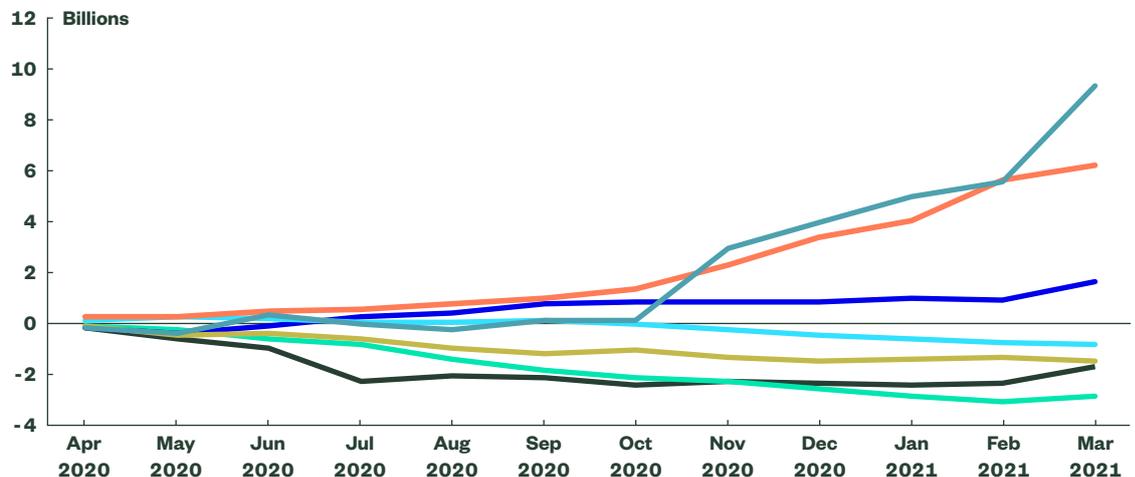
The change in economic sentiment at the end of 2020 laid the foundation for companies to reflect a more positive outlook in their 2021 earnings guidance. One of the most profound areas where this impact was felt was in dividend expectations. This earnings season, dividend investors heard a number of positive themes that helped shape the future estimates on forward dividends, as displayed in Figure 1 (previous page). In eurozone equities, three major tailwinds support the ongoing case for investors to consider increasing yield factor exposure by allocating to dividend stocks:

- Analyst estimates reflect significant upside potential for dividends, compared to the present value of dividend futures
- As business activity resumes, further improvement to fundamentals and earnings expectations could provide additional momentum for analyst revisions to go even higher
- Dividend strategies — such as Dividend Aristocrats — offer significant exposure to sectors which maintain relatively attractive valuations and should benefit from further economic reflation

Many companies that faced cash flow challenges as a result of the global pandemic were forced to *'take their medicine'* by cutting or suspending dividends in 2020. These firms will be keen to renew their commitment of returning capital to shareholders through dividends. This should benefit the relative valuations of dividend stocks, which were heavily discounted and under-owned in 2020.

While investor sentiment has become more positive on dividend stocks, investor flows have yet to follow at the same rate seen for other recovery exposures, such as Size and Value. As Figure 2 demonstrates, European Smart Beta investors have been pouring money into Size and Value ETFs since Q4 2020, when news on the deployment of vaccines affected asset prices. Dividend ETFs have yet to experience similar inflows but can likely expect to see investors return to these exposures as the economic recovery persists. This further supports the valuation case for dividend stocks.

Figure 2
European-Listed Smart Beta Flows
(Last 12 Months, USD)



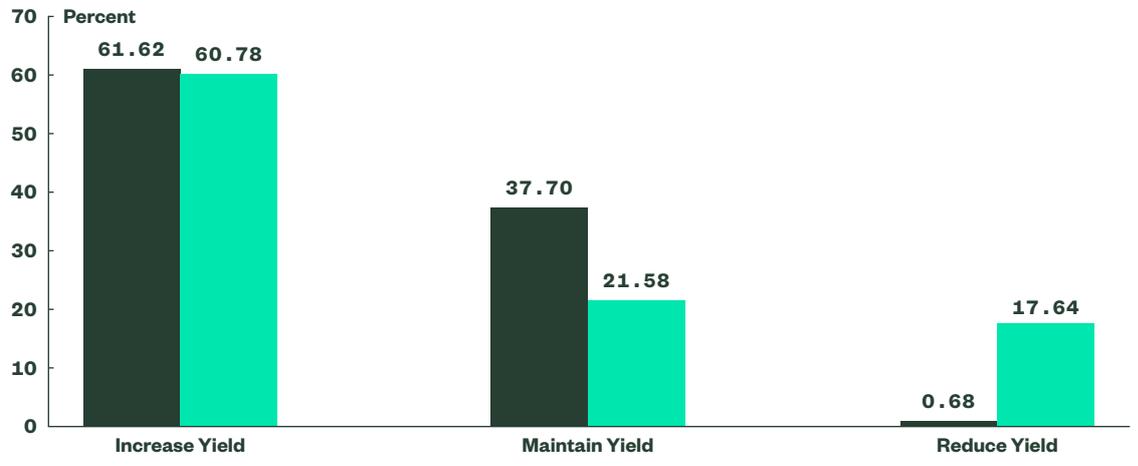
Source: State Street Global Advisors, Bloomberg Finance L.P., as of 26 March 2021. Flows are as of date indicated and shouldn't be relied thereafter.

Dividend Aristocrats Targets Stocks Increasing Dividends

The S&P® Euro High Yield Dividend Aristocrats Index (“Euro Dividend Aristocrats”) — which is the eurozone regional exposure of the Dividend Aristocrats family — selects stocks that have increased or maintained a stable total dividend per share amount every year for at least 10 consecutive years.¹ By adding Euro Dividend Aristocrats to the portfolio, investors can increase exposure to stocks forecasting an increase in dividend yields, both in terms of portfolio weight (Figure 3) and nominal stock exposure (Figure 4), as compared to a benchmark MSCI EMU Index.

Figure 3
**Total Portfolio
Exposure by
Forecast Action**

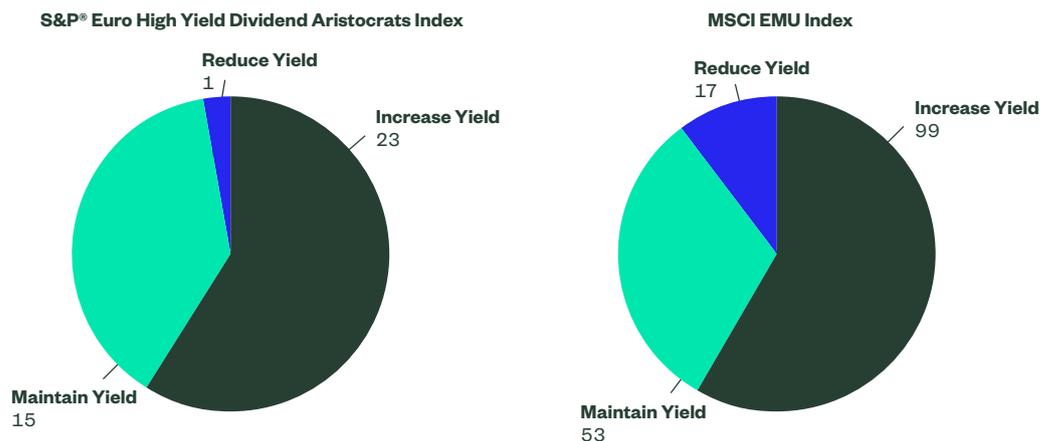
■ S&P® Euro High Yield
Dividend Aristocrats
Index
■ MSCI EMU Index



Source: State Street Global Advisors, Bloomberg Finance LP as of 26 March 2021.

Figure 4
**Total Number
of Stocks by
Forecast Action**

■ Increase Yield
■ Maintain Yield
■ Reduce Yield



Source: State Street Global Advisors, Bloomberg Finance LP as of 26 March 2021.

The relative increase in exposure to stocks increasing and maintaining yields may seem lower than expected, given the selection criteria of Euro Dividend Aristocrats. This further emphasises the point made in Figure 1 that eurozone equity dividend expectations are positive for 2021.

Increase Quality by Focusing on Stability

The Dividend Aristocrats indices produce ‘quality’ income for investors by focusing, and selecting, on a long-term track record of dividend stability. This is unique from other eurozone dividend indices, which may focus primarily on high dividend payers or a high concentration select approach. Pure high dividend indices may increase the risk of exposure to ‘dividend traps’. High concentration select dividend indices may expose investors to higher leverage, with respect to both fundamentals and factor risk. Figure 5 highlights some of the key distinctions between these construction methodologies.

Figure 5
Main Index Methodologies Targeting Dividend Stocks in Eurozone Equities

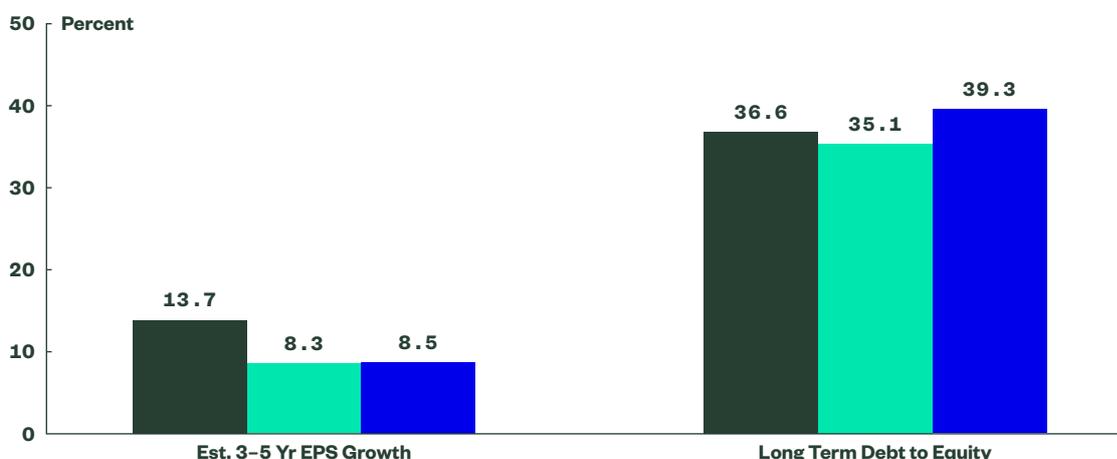
	S&P® Euro High Yield Dividend Aristocrats Index	MSCI EMU High Dividend Yield Index	EURO STOXX® Select Dividend 30 Index
Ticker	SPEUHDAN Index	M4EMHDVD Index	SD3T Index
Selection Universe	S&P® Eurozone BM Index	MSCI EMU Index	EURO STOXX® Index
Construction	Select stocks which have maintained increasing or stable dividends every year for at least 10 consecutive years	Select stocks with at least a 30% higher dividend yield, relative to the selection universe, and pass dividend sustainability screens	Select 30 stocks which have the highest dividend yield relative to their home market
Weighting Scheme	Price-weighted with a weighting factor based on the indicated annual dividend yield	Market-capitalization weighted after selection	Price-weighted with a weighting factor based on the indicated annual dividend yield
Constraints	5% single stock weight cap 30% sector weight cap 30% country weight cap	5% single stock weight cap	15% single stock weight cap
No. of Holdings	Target 40	Floating	Target 30
Rebalance Frequency	<i>Annual</i> reconstitution (June) with a <i>Quarterly</i> review and conditional <i>Monthly</i> review	<i>Semi-Annual</i> review (May and November)	<i>Annual</i> review (March) with a conditional <i>Fast exit</i>

Source: S&P Dow Jones Indices, MSCI, STOXX. The information contained above is for illustrative purposes only.

While the Dividend Aristocrats strategy does not explicitly target fundamental quality metrics in stock selection, it is not surprising that the Euro Dividend Aristocrats can result in superior quality metrics (Figure 6) compared to a pure high yield index. Dividend indices are inherently biased toward value stocks and away from growth, but the Euro Dividend Aristocrats Index provides similar expected earnings growth (3–5 years) to a pure high dividend index, with lower leverage (long-term debt to equity) than both the pure high dividend strategy and a benchmark EURO STOXX® Index.

Figure 6
Dividend Aristocrats Quality Exposure (vs. High Dividend)

■ EURO STOXX® Index
■ S&P® Euro High Yield Dividend Aristocrats Index
■ MSCI EMU High Dividend Yield Index

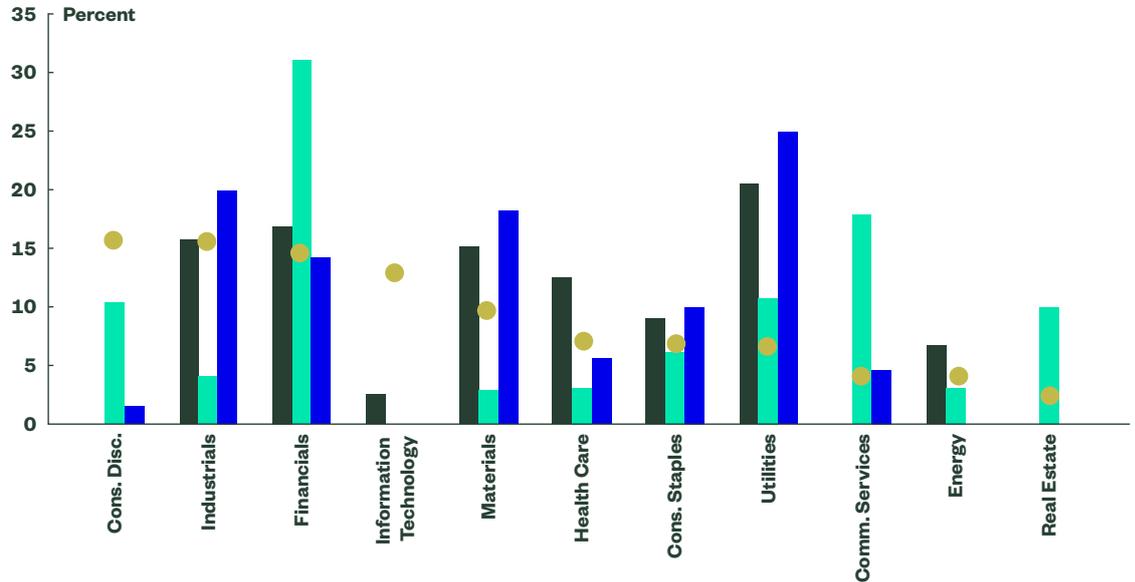


Source: State Street Global Advisors, FactSet, BarraOne as of 29 March 2021.

A Balanced Sector Approach to Quality Income

The Euro Dividend Aristocrats Index uses a balanced approach to targeting quality income. The strategy does restrict index exposure to a maximum weight of 5% (single stock), 30% (sector) and 30% (country) at each quarterly rebalancing. This allows the strategy flexibility to go *'wherever it needs'* to find quality income, while also promoting adequate diversification. Historically, this has created significant sector biases. Ultimately, investors tend to favour this feature as it offers a balanced diversification from the benchmark, whereas other strategies may provide investors too strong of a concentrated exposure.

Figure 7
Sector Allocation of Dividend Strategies (vs. S&P® 500 Index)



Source: State Street Global Advisors, FactSet, BarraOne as of 29 March 2021.

If we take a deeper dive into the dividend estimates for the EURO STOXX® 50 Index, we can see that all sectors are expected to deliver positive dividend growth in the coming years. In 2021, the 12-month forward dividend expectations are highest +41.9% in Financials and +40.6% in Consumer Discretionary. While this is encouraging, such high expectations also carry an increased risk if growth is slower than expected emerging from the global pandemic. As seen in Figure 7, Dividend Aristocrats offers a modest overweight to Financials, with no exposure to the risk of a slow consumer (discretionary) recovery. This may strike a good balance for investors seeking to play the recovery, but cautious of being over-levered.

Figure 8
Sector Distribution of Dividend Estimates (EURO STOXX® 50)



Source: JP Morgan Global Dividend Review as of 23 March 2021. JPM/Consensus bottom-up estimates are based on aggregated J.P. Morgan analyst dividend per share estimates, where available, or IBES/Bloomberg consensus estimates.

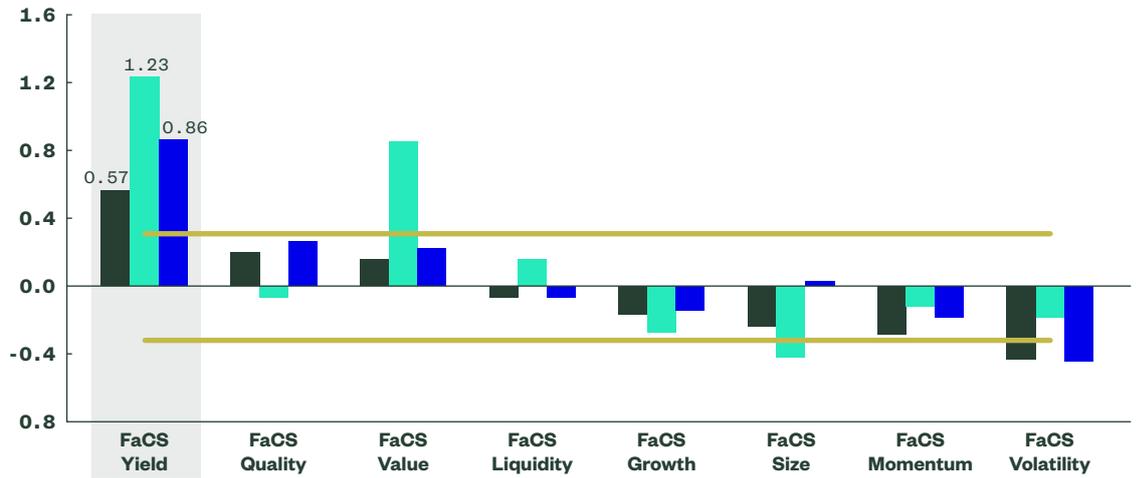
A Balanced Yield Factor Approach to Quality Income

In addition to the sector flexibility offered by the Dividend Aristocrats approach, the yield-weighted strategy is also balanced in seeking yield factor exposure from the basket of highly stable (by historical standards) dividend-paying stocks. In Figure 9, we see Euro Dividend Aristocrats has a significantly strong, but not over-levered active exposure to the Yield factor.

Construction of the Euro Dividend Aristocrats strategy starts with a broad market index (S&P Eurozone) selection universe, but is ultimately a yield-weighted strategy. Despite this, the strategy does not have a strong negative Size factor exposure, but is a slightly significant low volatility play compared to the market-capitalisation weighted EURO STOXX® Index. Figure 10 demonstrates how Euro Dividend Aristocrats is able to offer significant yield factor exposure while maintaining a balanced country risk profile.

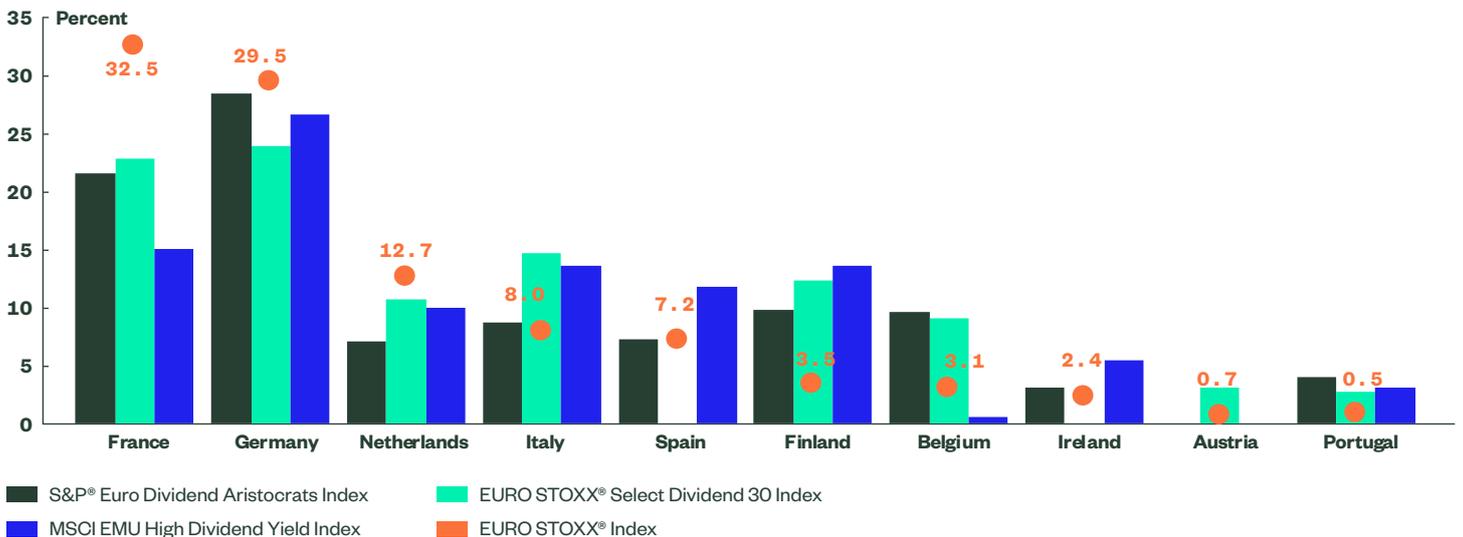
Figure 9
FaCS Active Exposure Comparison
(vs. EURO STOXX® Index)

■ S&P® Euro Dividend Aristocrats Index
■ EURO STOXX® Select Dividend 30 Index
■ MSCI EMU High Dividend Yield Index
■ Significance Level (± 0.31)



Source: State Street Global Advisors, FactSet, BarraOne as of 29 March 2021.

Figure 10
Country Allocation of Dividend Strategies
(vs. EURO STOXX® Index)



Source: State Street Global Advisors, FactSet, BarraOne as of 29 March 2021.

Conclusion

Current economic sentiment provides a supportive case for dividend stocks based on recent earnings guidance, analyst projections and general optimism towards a continued economic recovery. This environment could present an opportunity for European ETF investors to return to dividend strategies, following momentum seen in other recovery plays.

The S&P® Euro High Yield Dividend Aristocrats Index is a stable dividend strategy that selects stocks that have increased or maintained a stable total dividend per share amount every year for at least 10 consecutive years. By adding Euro Dividend Aristocrats to the portfolio, investors can increase exposure to stocks forecasting an increase in dividend yields. In addition, the strategy can provide investors with positive quality bias, less concentration and lower leverage, through a balanced approach to strong yield factor exposure.

SPDR® ETFs

The investment objective of the SPDR® family of Dividend Aristocrats indices is to track the performance of equities that historically have exhibited stable dividend growth.

- **SPDR® S&P® Euro Dividend Aristocrats UCITS ETF (Dist)**

The SPDR® S&P® Euro Dividend Aristocrats UCITS ETF seeks to replicate the S&P® Euro High Yield Dividend Aristocrats Index, which consists of the 40 highest dividend-yielding stocks in the S&P® Eurozone Broad Market Index (“BMI”) that have increased or maintained stable dividends every year for at least 10 consecutive years. These stocks have both capital growth and dividend income characteristics, as opposed to stocks that are pure yield or pure capital oriented.

Figure 11
Standard Performance

Fund/Index Name	1 Month	3 Months	6 Months	Year to Date	1 Year	3 Years	5 Years	Since Inception
Inception Date 14/10/2011								
SPDR® S&P® Euro Dividend Aristocrats UCITS ETF	7.13	7.44	15.51	7.44	30.31	3.44	5.15	7.94
S&P® Euro High Yield Dividend Aristocrats Index	7.10	7.39	15.56	7.39	29.75	3.03	4.75	7.59
Difference	0.03	0.05	-0.05	0.05	0.56	0.41	0.40	0.35
MSCI EMU Index†	6.59	8.96	22.83	8.96	43.96	6.72	8.24	8.67
Difference	0.54	-1.52	-7.32	-1.52	-13.65	-3.28	-3.09	-0.73

Source: State Street Global Advisors, †Morningstar and Bloomberg, as of 31 March 2021.

Performance is net of fees. **Performance quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate, so you may have a gain or loss when shares are sold. Current performance may be higher or lower than that quoted. All results are historical and assume the reinvestment of dividends and capital gains. The performance data do not take account of the commissions and costs incurred on the issue and redemption, or purchases and sale, of units. Visit spdrs.com for most recent month-end performance.** Performance returns for periods of less than one year are not annualised. Index returns are unmanaged and do not reflect the deduction of any fees or expenses.

Endnote

1 Full index methodology is available at spglobal.com.

ssga.com/etfs

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