

# Value Ideas

A Research Publication by DZ BANK AG

## Basic principles

### Methodology dividend aristocrats

Dividend aristocrats are companies which have consistently paid, and increased the dividend to their shareholders. This can be regarded as indicative of a successful and established business model. The S&P Dividend Aristocrats is the best known dividend aristocrats index and it invests in stocks whose dividends have been raised on an annual basis for at least 25 successive years.

The criteria used in the DZ BANK dividend aristocrats approach differ from those of the S&P Dividend Aristocrats. Firstly, because there are virtually no companies in Germany in particular with such a long and positive dividend history. Secondly, from a risk/return perspective we have used other quantitative and qualitative data in our selection process.

Various studies have shown that dividends contribute a significant proportion of total return in the longer term. This is true of the equity markets in both the USA and Europe, and is reflected, for example, in historical price and performance trends.

Based on the stability and high degree of reliability of dividend payments, dividend aristocrats are also referred to colloquially as “the new bonds”, and are of particular interest in the current climate of low or zero interest rates. Dividend aristocrat stocks are suitable for fairly defensive and long-term investors, and for investors who are reliant on steady cash flows.

This publication is intended, inter alia, for Volks- und Raiffeisenbank and institutional customers at home and abroad.

## EQUITIES

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## DIVIDEND ARISTOCRATS

### What are dividend aristocrats?

The dividend is the main focus of the dividend aristocrats approach. Dividend aristocrats are companies (stocks) which have paid and raised dividends on a regular basis.

If companies have consistently paid and increased dividends, this can be regarded as indicative of a successful and established business model. Dividend aristocrats show signs of leading market positions and competitive advantages with the prospect of sustainable payouts.

Based on steady dividend growth, the returns of dividend aristocrats also continue to grow continuously over time.

**Dividend aristocrats pay regular dividends which they also raise on a continuous basis**

**Dividend continuity, indicative of a stable and sustainable business model**

**Attractions of dividend aristocrats evident in medium to long term**

### Theoretical basis

The theoretical basis and the best known example of this approach is the “S&P Dividend Aristocrats”. This index consists of stocks from the S&P 500 which have raised their dividends on an annual basis for at least the last 25 years. Bloomberg Ticker: SPDAUDT Index

Financial literature also frequently refers to the fact that stocks from defensive sectors with high dividend yields – which often include dividend aristocrats - tend to react more strongly to changes in interest rates.

### Stock selection essential

Various studies have shown that active management combined with a high degree of diversification produces better results for dividend investments. A structured investment and stock selection process is therefore crucial.

An investment decision which is based solely on the dividend return falls short of the mark. On the one hand, dividend payments are directly associated with a fall in the share price. On the other hand, share prices are driven in the longer term by a company's operating performance.

The sustainable dividend policy of a company therefore plays a particularly crucial role for the longer-term success of an investment. Otherwise, there is a risk of both cuts in the dividend and share price losses in the medium term.

**Active management and diversification important**

**Dividend yield not recommended as sole investment criterion**

**Dividend must be sustainable**

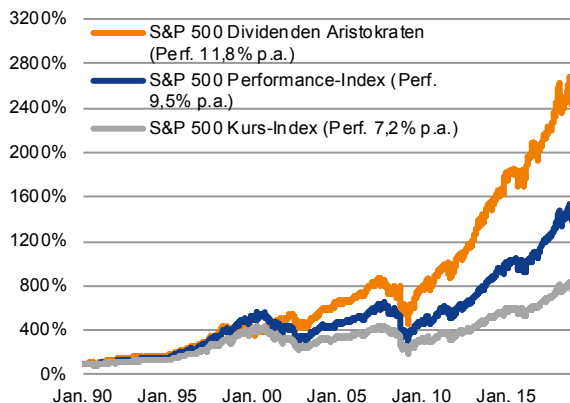
## Historical performance

Various studies have shown that dividends contribute a significant proportion of total return in the longer term. This is true of the equity markets in both the USA and Europe, and is reflected, for example, in historical price and performance trends. The charts below show the trend in the price index, the performance index (e.g. including reinvested dividends) and the dividend aristocrats index for the respective regions. The periods covered correspond to the respective maximum data series available.

**Dividend an important element of performance**

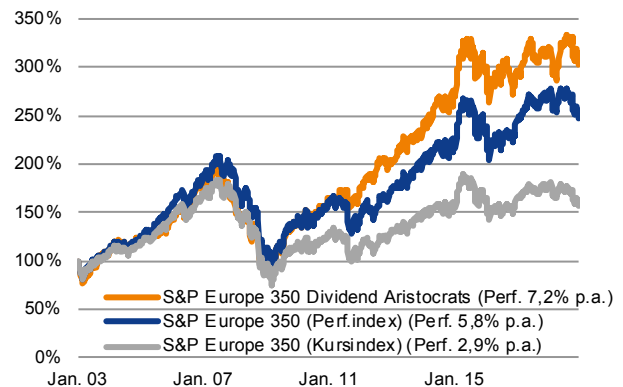
**Dividend indices clearly outperform in longer term**

**USA: S&P 500 VS. S&P DIVIDEND ARISTOCRATS**



Source: Bloomberg, DZ BANK

**S&P EUROPE VS. S&P EUROPE DIVIDEND ARISTOCRATS**



Source: Bloomberg, DZ BANK

## DZ BANK dividend aristocrats approach

The USA has a much larger stock universe than Europe, and Germany in particular, and thus has recourse to a significantly larger number of stocks with a long dividend history.

To enable us to also show a selection of dividend aristocrats for the German and European universe we have softened the criteria slightly, and the stocks included in our selection lists are not therefore required to demonstrate a history of 25 years of steady dividend growth.

In fact, we have established the following criteria for our selection process, which we have extended to include parameters other than merely an annual dividend increase.

We have selected the following criteria for our dividend aristocrat favourites:

- **Dividend continuity:**
  - o Dividend paid in 10 out of 10 years
  - o Dividend raised or stable for at least 8 out of 10 years
  - o No significant cut in dividend
  - o Payout ratio < 85%

**DZ BANK**  
dividend aristocrats

We also factor in a minimum dividend yield and a high quality balance sheet for our dividend aristocrats as well as a positive recommendation from the DZ BANK equity analysts.

- **Expected dividend yield:**
  - o expected dividend yield of at least 3%
  
- **Balance sheet quality & valuation:**
  - o Equity ratio > 30%  
resp. net debt/ EBITDA < 3
  - o EV/EBIT < 20
  - o Investment recommendation Hold or Buy

We reserve the right to adjust the criteria accordingly in line with current general and market conditions.

The DZ BANK dividend aristocrat approach thus represents a purely quantitative evaluation. We do not therefore make any estimates of our own in relation to the future performance of companies.

### Target group

Based on the stability and high degree of reliability of dividend payments, these securities are also referred to colloquially as “the new bonds“, and are of particular interest in the current interest rate climate. Dividend aristocrat stocks are suitable for fairly defensive and long-term oriented investors, as well as investors reliant on steady cash flows.

This publication is intended, inter alia, for Volks- und Raiffeisenbank and institutional customers at home and abroad.

### Sources: data, studies and information

We have based our evaluations on data supplied by Reuters. It includes both historical company information and also estimated consensus data for the expected dividend yield and estimated payout ratios.

Our analysis also draws on the investment recommendations of DZ BANK equity analysts. For details of the processes used, please see the basic principles report produced by the equity analysts.

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"**Neutral weighting**" refers to the expectation that a sub-segment will not deliver any significant performance differences compared with all the sub-segments as a whole.

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"**Upward arrow (↑)**" means that the absolute price increase expected in the next twelve months is greater than 10%.

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"Arrow pointing to the right (➔)" means that the absolute price change expected in the next twelve months will lie between +10% and -10%.

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"Negative" is given if the agencies S&P, Moody's and Fitch are expected to make a rating downgrade in the next twelve months,

"Stable" is given if the agencies S&P, Moody's and Fitch are expected to leave their ratings unchanged in the next twelve months

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|                                                                  |                      |
|------------------------------------------------------------------|----------------------|
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| Euro Stoxx Sector Strategy ( <b>DZ BANK Sector Favourites</b> ): | one month            |
| Dividends ( <b>DZ BANK Dividend Aristocrats</b> ):               | three months         |
| <b>Credit trend issuers</b>                                      | twelve months        |
| <b>Share indices (fundamental):</b>                              | three months         |
| <b>Share indices (technical / chart analysis):</b>               | one week             |
| <b>Share indices (technical daily):</b>                          | publication day      |
| <b>Currency areas:</b>                                           | six to twelve months |
| <b>Allocation of market segments</b>                             | one month            |
| <b>Country weightings for covered bonds:</b>                     | six months           |
| <b>Derivatives</b>                                               |                      |
| (Bund futures, Bobl futures, treasury futures, Buxl futures):    | one month            |
| <b>Commodities:</b>                                              | one month            |

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