Bristol Gate
Dividend Report 2023

As of December 31, 2023

The Dividend Information You Need, From Those Who Know It

Throughout 2023 there were 405 dividend payers in the S&P 500®, delivering a median dividend growth rate of 6.67%. Despite a strong year for the stock market, the economic implications of inflation coupled with a rising rate environment did have an impact. During 2023 we saw 14 S&P 500® companies cut their dividends. This compares to just 5 dividend cutters in 2022. Within this report we explore the misconception of high yielding stocks and the potential peril of a dividend cut.

DIVIDEND STATISTICS THROUGH THE CALENDAR YEAR OF 2023

S&P 500® Dividend Statistics 2023	
Total Dividend Payers	405
Median Dividend Growth	6.67%
Dividend Cutters	14
Dividend Maintainers	53
Dividend Growers	328
Dividend Suspenders	1
Inadequate # of Payments (<2yrs)	10
Median Grower Dividend Growth	7.68%

S&P TSX Dividend Statistics	
Total Dividend Payers	175
Median Dividend Growth	5.40%
Dividend Cutters	7
Dividend Maintainers	48
Dividend Growers	117
Dividend Suspenders	0
Inadequate # of Payments (<2yrs)	3
Median Grower Dividend Growth	8.70%

Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023.

CASE STUDY – LOOKING AT YIELD IS NOT LOOKING DEEP ENOUGH

When it comes to investing, investors generate returns through various sources, including interest income, capital appreciation, and dividends. When building a portfolio, investors often count on dividends as a relatively reliable component of their expected total return.

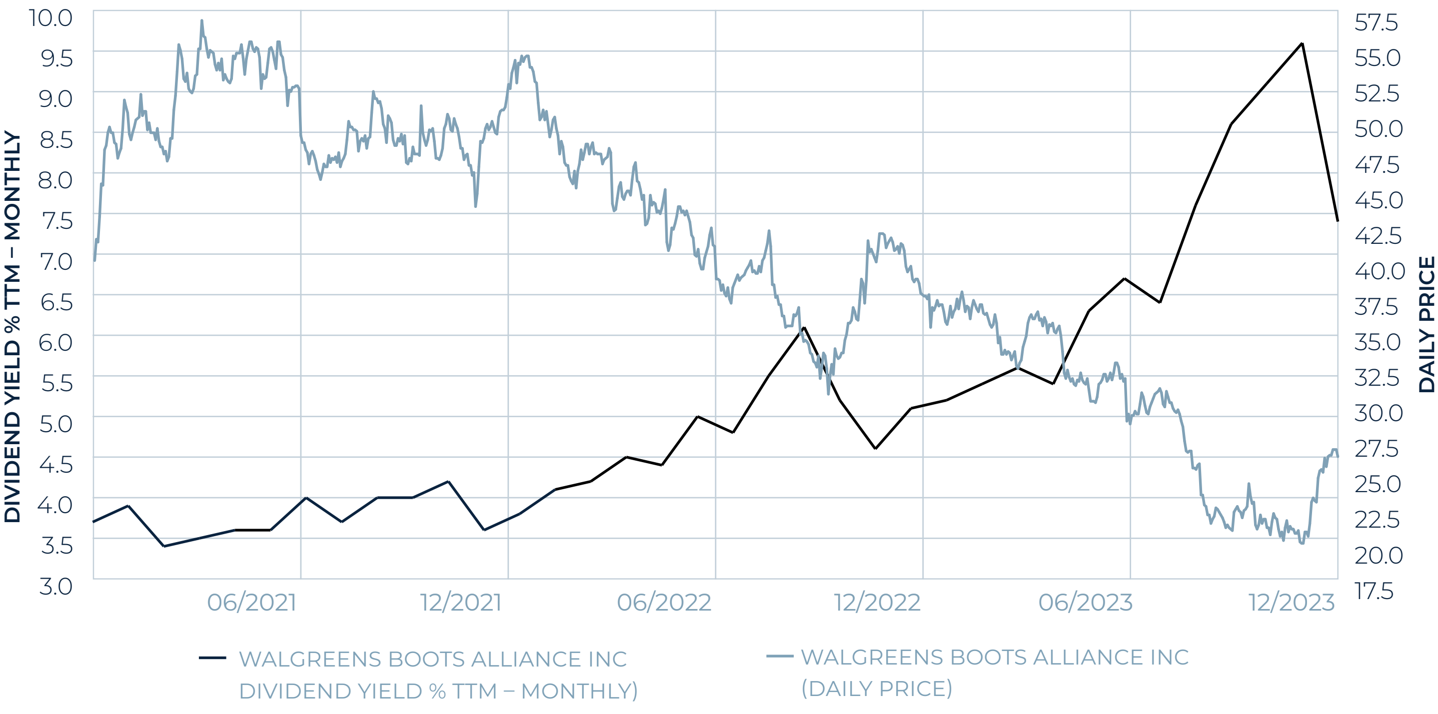
When investors rely on dividends for income, stocks with high dividend yields can often appear attractive. But how reliable are dividends? A company's management has discretion on dividend policy and is often incentivized to maintain payouts to shareholders, particularly given market reaction to a dividend cut. Maintaining a certain dividend level, however, can cause a company's payout ratio to increase. This is the dollar amount of dividends paid relative to their net income. In a case where net income is declining, but dividends remain steady – there is less cash to allocate to other priorities such as R&D, expansions, or paying down debt. Poor capital allocation decisions by management can ultimately lead a company into a downward spiral. What could be considered the last line of defense would be the decision to then cut the dividend.

While high dividend payouts may seem more attractive, they could actually be a signal of larger problems within the company. For this reason, investors are encouraged to take a closer look when considering investing in higher yielding companies. Investors looking to maximize dividend income by investing in stocks offering a high yield may end up facing a dividend cut, which not only reduces their future dividend income but is also often associated with a significant decline in the price of the stock as well.

How does a company end up with a high dividend yield? One way is for the company's share price to tumble without any reduction in dividend. The second way is an increase in dividend payout without a corresponding increase in the share price. In either case, an investor should question whether the dividends being paid are supported by the earnings and free cash flow being generated by the business. In some cases, management may even resort to using debt to help facilitate dividend increases. This can create a problem for the company and its cash flow, especially in an environment where borrowing money is no longer cheap.

A recent example in the US market of a high yield stock resulting in a dividend cut is Walgreens Boots Alliance (ticker: WBA). Walgreens, which was a constituent of the S&P 500® Dividend Aristocrats Index, meaning it had delivered 25 years of consecutive dividend increases to shareholders. For context, there are only 66 other companies that also met the criteria to be included in the Aristocrats, making such consistent divided increases a rare feat. As such, investors may have felt more comfortable chasing the yield that was on offer. Early in January 2024, Walgreens cut its dividend by 48% to shore up cashflow as they were facing lower consumer spending, intense competition, and a larger debt load due to its investment in the UK pharmacy chain Boots. The announcement of the dividend cut sent the stock down 11%, after the company's share price had fallen 25% in 2023.

Below is a chart plotting WBA's stock price as well as its dividend yield. As you'll note, WBA was yielding 9.5% towards the end of 2023.



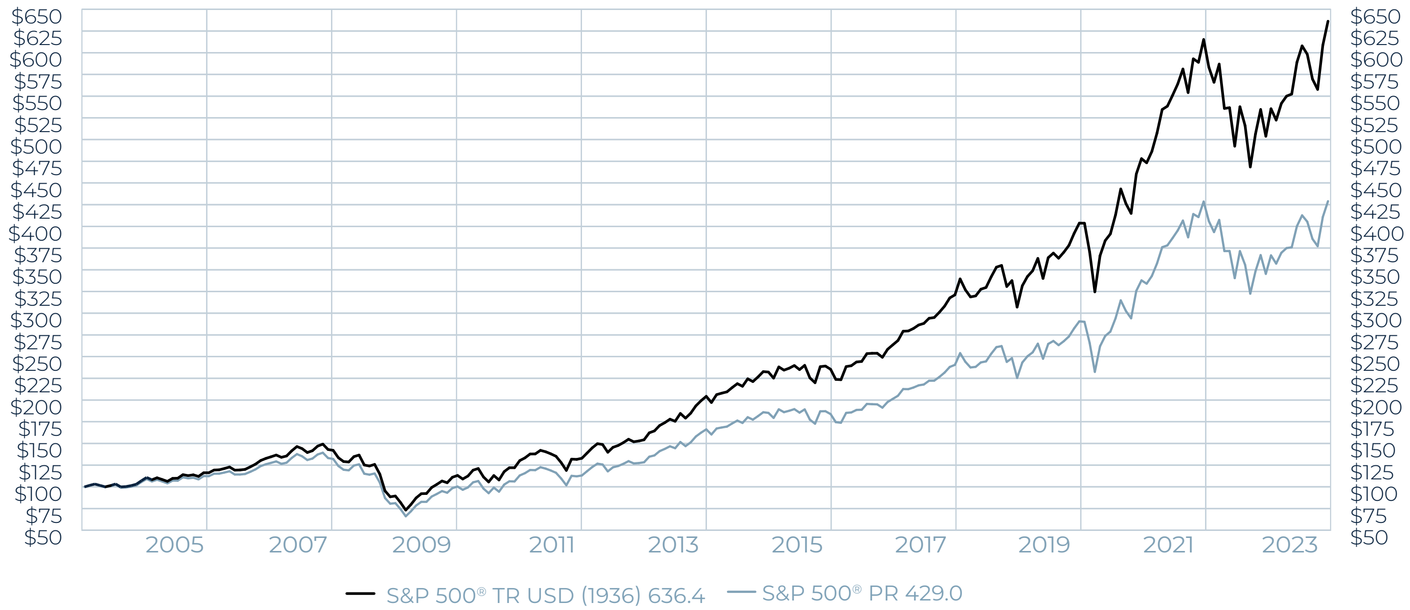
Source: Morningstar, Bristol Gate Capital Partners Inc January 31, 2021 – Dec 31, 2023

Investors should be wary of allocating investment capital by simply buying high yield stocks. It is worth taking the time to fully understand the driving forces of a company.

BRISTOL GATE DIVIDEND CHART BOOK

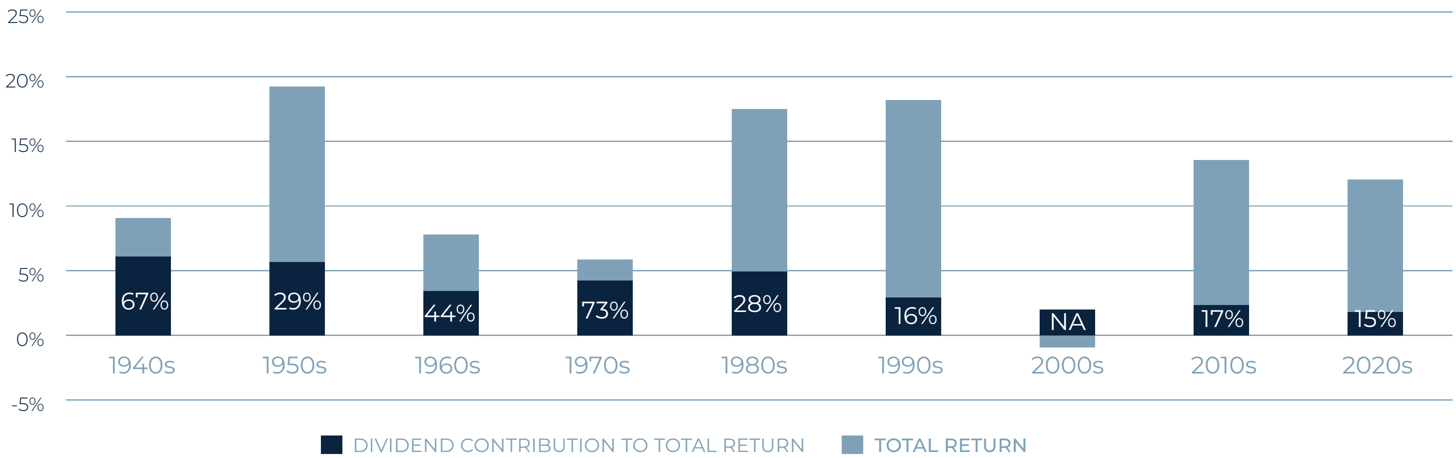
WHY DIVIDENDS MATTER

TOTAL RETURN VS. PRICE RETURN OF THE S&P 500®



Source: Morningstar, Bristol Gate. Dec 31, 2003 – Dec 31, 2023.

CONTRIBUTION OF DIVIDENDS TO TOTAL RETURN BY DECADE



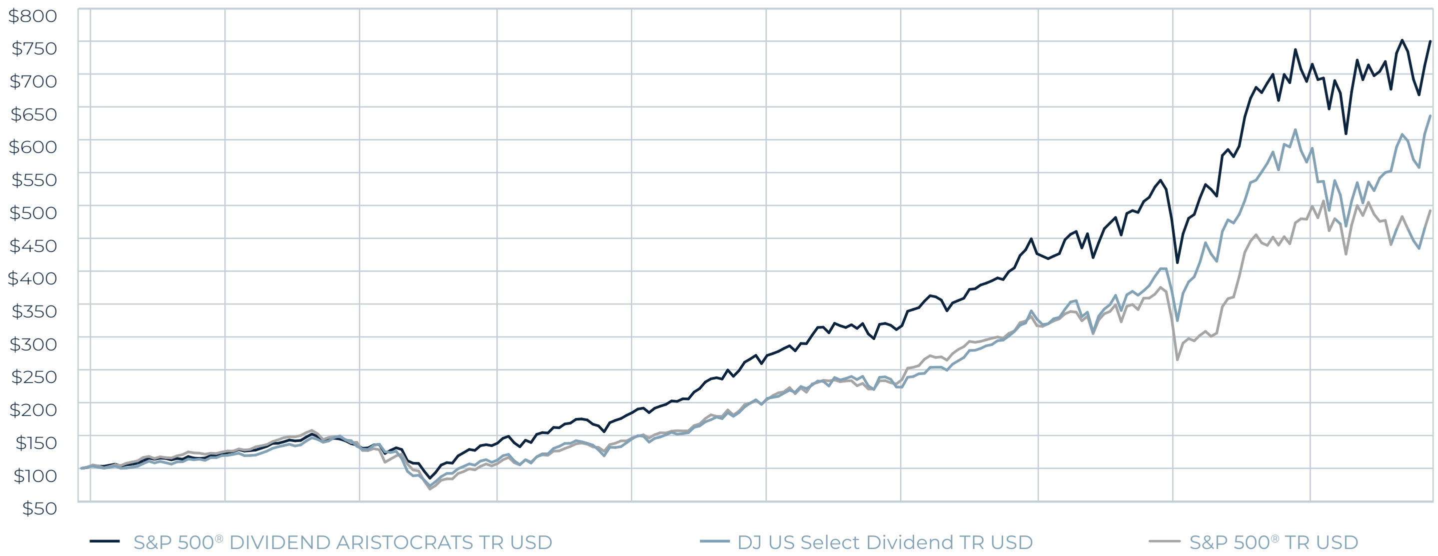
Source: Morningstar, Bristol Gate

Reinvestment of dividends have contributed to significant wealth creation opportunities.

From the start of 1940 to the end of 2023, the reinvestment of dividends has contributed a staggering 94.4% to the S&P 500®'s total return, gross of fees. If an individual were to have invested $1,000 in the S&P 500® on January 1, 1940 – their ending portfolio balance on December 31, 2023, including the reinvestment of dividends, would have been $6,367,942. This compares to the portfolio balance without of the inclusion of dividends, over the same time frame, of $354,694.

DIVIDEND GROWTH VS. HIGH DIVIDEND YIELD

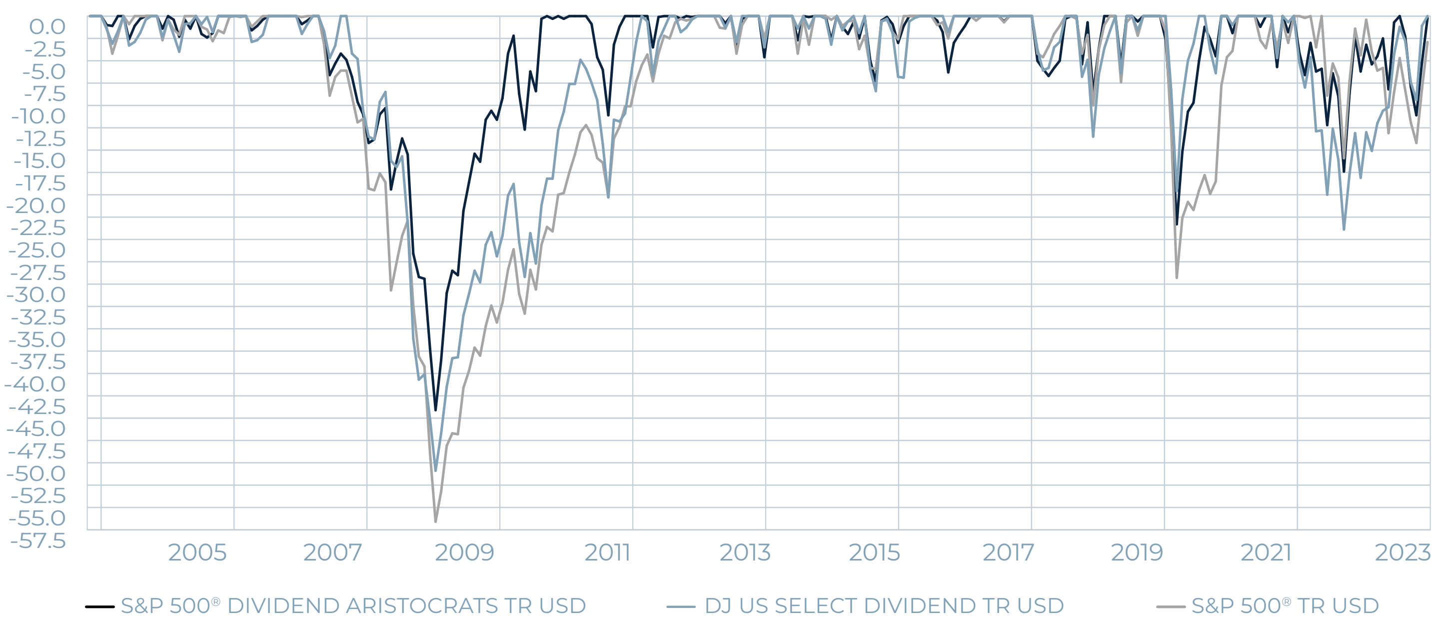
PERFORMANCE OF DIVIDEND GROWERS VS. DIVIDEND YIELDERS



Source: Morningstar, Bristol Gate. Dec 31, 2003 – Dec 31, 2023

Going back 20 years, the S&P 500® Dividend Aristocrats (a proxy for a dividend growth portfolio) has substantially outperformed both the market and also the Dow Jones US Select Dividend index (a proxy for a high yield-oriented portfolio). Over the same timeframe, a dividend index has also been successful in protecting capital during large pullbacks in the market.

DOWNSIDE PROTECTION OF DIVIDEND GROWERS VS. DIVIDEND YIELDERS



Source: Morningstar, Bristol Gate Jan 1, 2004 – Dec 31, 2023.

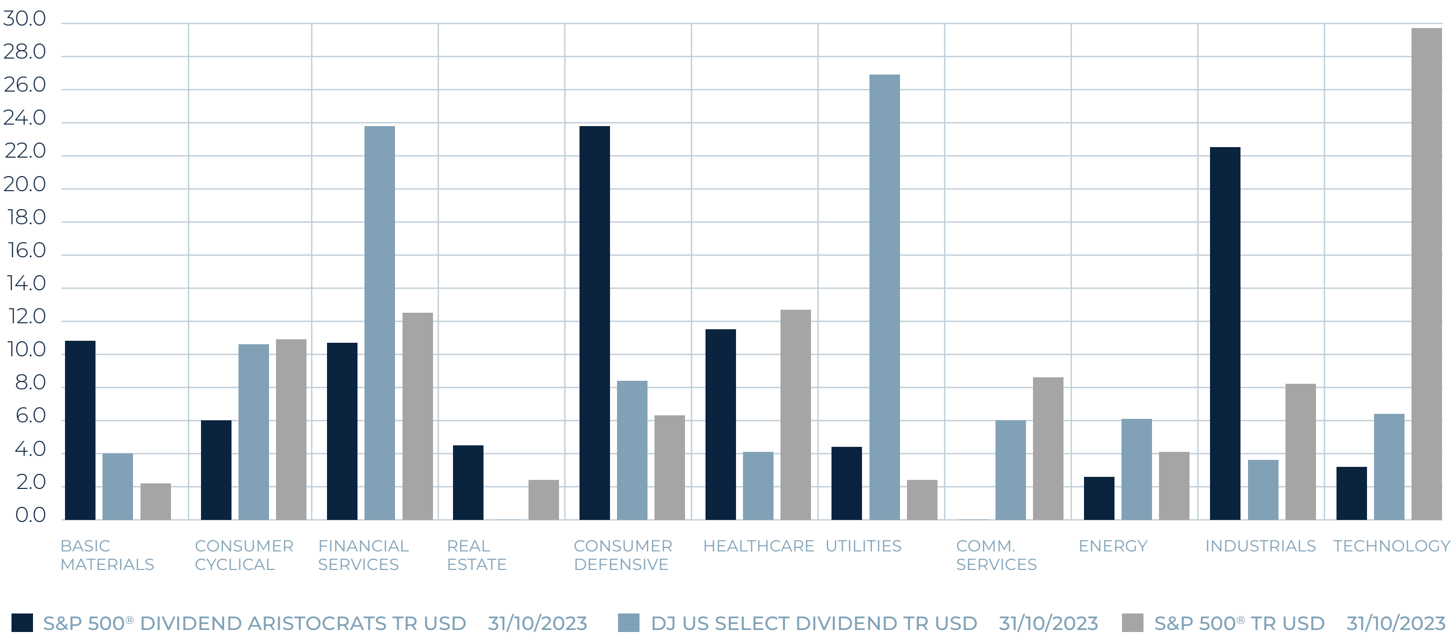
DIVIDEND EXPOSURE RETURN QUILT

As we have been exploring, it is difficult to paint dividend investing with too broad a brush. There are many strategies available within the dividend-paying universe that focus on an array of characteristics. A common distinction is between high dividend yielding companies versus high dividend growth companies. Below we have contrasted the calendar year returns of various dividend indexes.

	2023	2022	2021	2020	2019
S&P 500® Dividend Aristocrats TR USD	8.44	-6.21	25.99	8.68	27.97
DJ US Select Dividend TR USD	1.53	2.31	32.24	-4.56	23.11
S&P 500® Low Volatility High Div TR USD	1.70	0.93	25.26	-9.67	20.76
Morningstar US Dividend Growth TR USD	10.44	-7.75	26.69	9.50	30.15
MSCI USA High Dividend Yield GR USD	6.83	-3.75	21.93	1.69	22.47
NASDAQ US Dividend Achievers 50 TR USD	7.91	2.97	26.67	-3.27	25.36
Russell 1000 Dividend Growth TR USD	11.18	-5.92	27.07	12.44	28.28
Russell 1000 Value TR USD	11.46	-7.54	25.16	2.80	26.54
Russell 1000 Growth TR USD	42.68	-29.14	27.60	38.49	36.39
S&P 500® TR USD	26.29	-18.11	28.71	18.40	31.49

Source: Morningstar, Bristol Gate. As of December 31, 2023

DIVIDEND GROWTH VS. HIGH DIVIDEND YIELD SECTOR BREAKDOWN



Source: Morningstar, Bristol Gate. As of December 31, 2023

By breaking down the above indices further, we see that that are certain sectors which better facilitate a high dividend yield and those that are more conducive to high dividend growth.

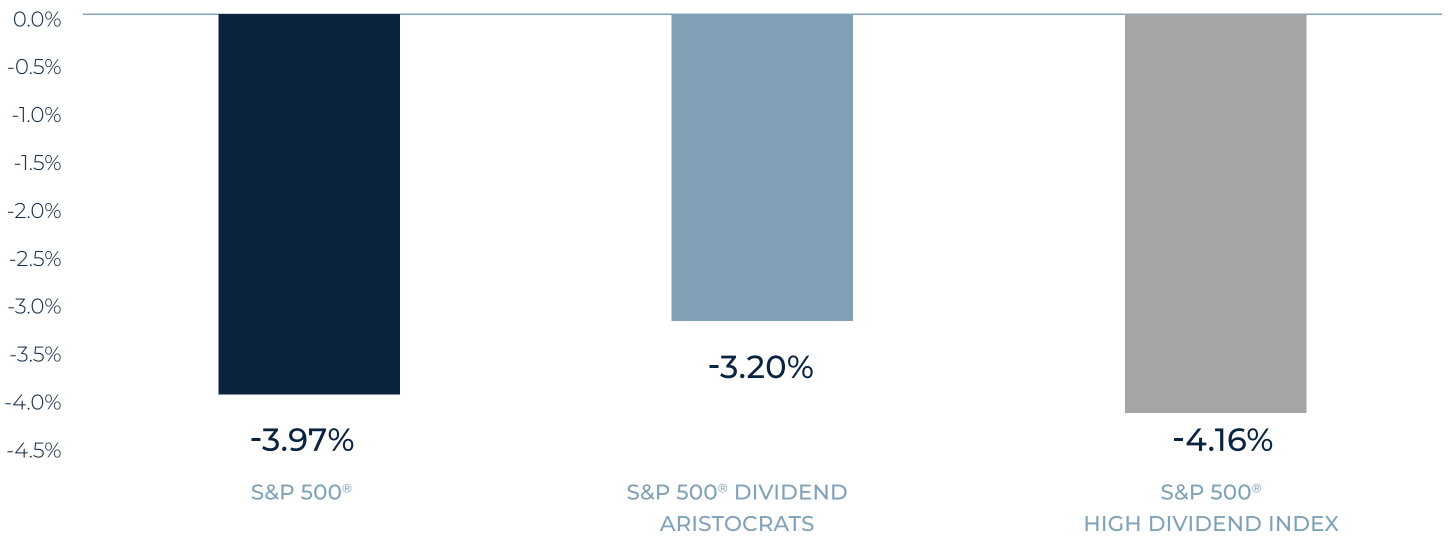
HISTORICAL DIVIDEND GROWTH OF THE S&P 500® BY GICS SECTOR

2023	DIVIDEND GROWTH	3 YEAR DIVIDEND GROWTH	DIVIDEND GROWTH	5 YEAR DIVIDEND GROWTH	DIVIDEND GROWTH
Consumer Discretionary	14.3%	Industrials	10.8%	Health Care	8.7%
Information Technology	7.6%	Consumer Discretionary	10.7%	Materials	7.6%
Industrials	7.0%	Materials	9.0%	Information Technology	6.9%
Health Care	6.6%	Health Care	8.6%	Energy	6.4%
Real Estate	5.9%	Energy	8.3%	Industrials	4.5%
Utilities	4.9%	Real Estate	8.2%	Consumer Staples	4.4%
Consumer Staples	4.5%	Information Technology	6.9%	Financials	4.3%
Communication Services	3.7%	Consumer Staples	3.5%	Real Estate	4.3%
Materials	-5.3%	Utilities	2.1%	Utilities	3.9%
Financials	-7.2%	Financials	1.8%	Consumer Discretionary	0.1%
Energy	-18.2%	Communication Services	-4.0%	Communication Services	-4.4%

Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023.

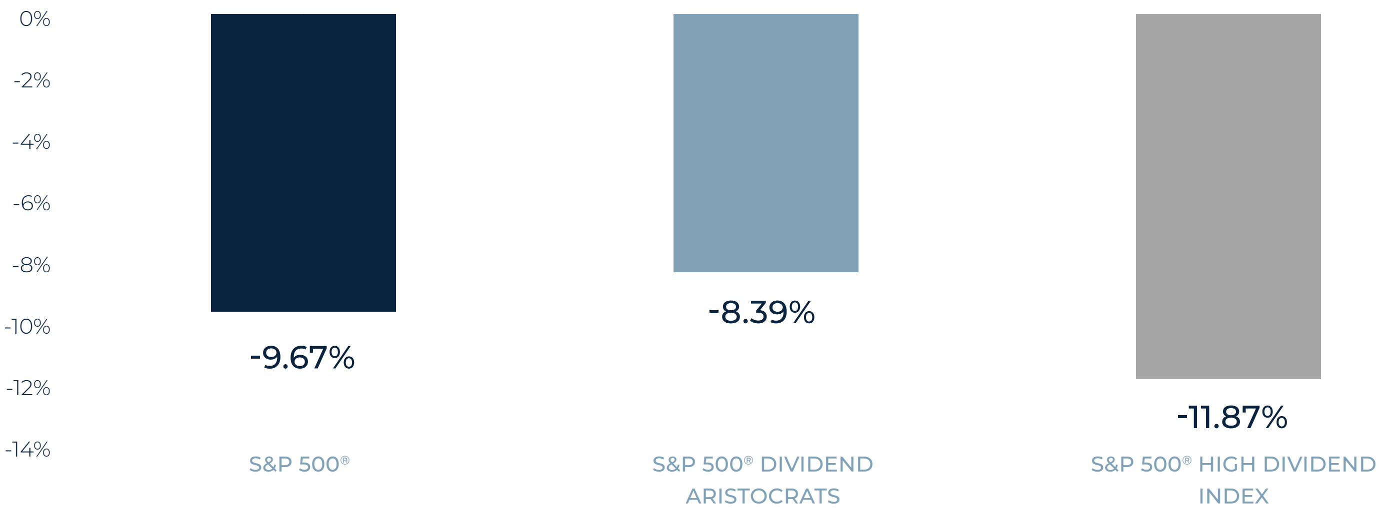
DIVIDEND GROWERS VS HIGH DIVIDEND PAYERS IN DOWN MONTHS

AVERAGE RETURN DURING S&P 500® DOWN MONTHS



Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023.

AVERAGE RETURN DURING S&P 500® WORST 15 MONTHS



Source: Bristol Gate Capital Partners, Bloomberg. Data from Jan 1, 2000 - December 31, 2023.

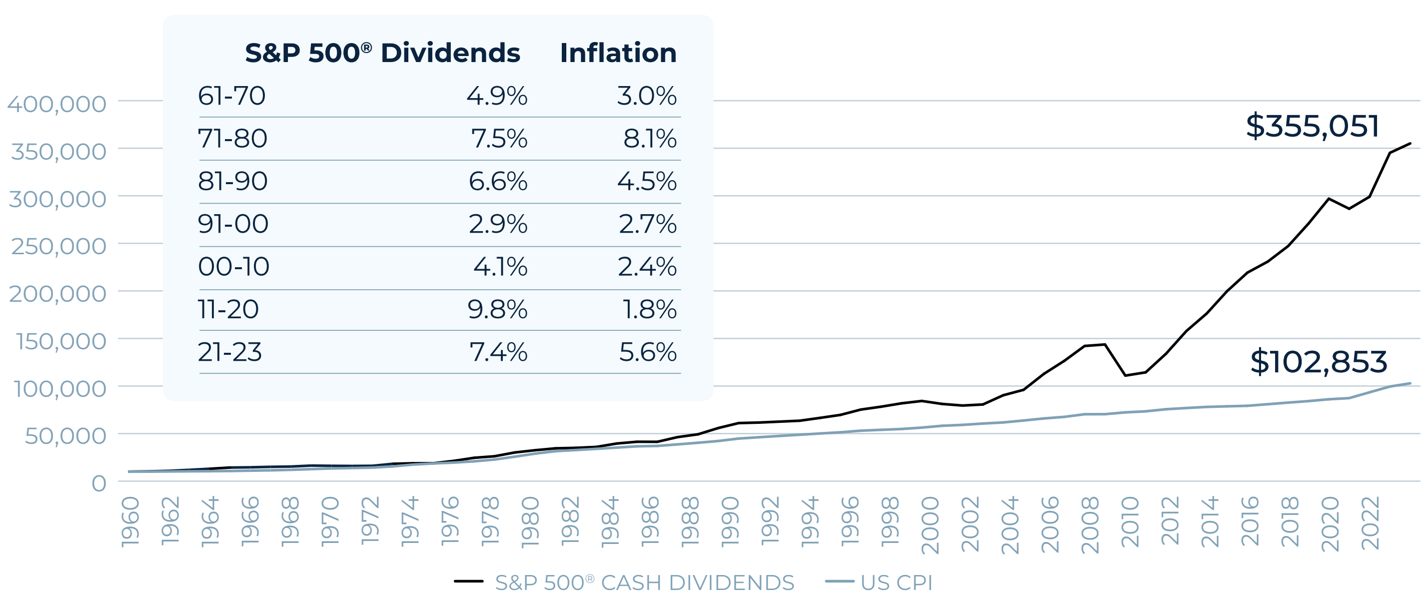
As we had noted above, overtime dividend growth companies (using the Dividend Aristocrats as a proxy) can provide better protection during periods of downside volatility. During both down months in general and the 15 most severe down months, the dividend growth index provided a better buffer than the yield focused index (High Dividend Index).

DIVIDENDS IN DIFFERENT INFLATIONARY ENVIRONMENTS

Having a dividend growth component within a well diversified portfolio has proved to provide attractive risk-adjusted returns. Having exposure to the growth of dividends has also been an effective way to preserve purchasing powering among the steady march upwards of the cost of living.

DIVIDENDS VS. INFLATION

	S&P 500® Dividends	Inflation
61-70	4.9%	3.0%
71-80	7.5%	8.1%
81-90	6.6%	4.5%
91-00	2.9%	2.7%
00-10	4.1%	2.4%
11-20	9.8%	1.8%
21-23	7.4%	5.6%

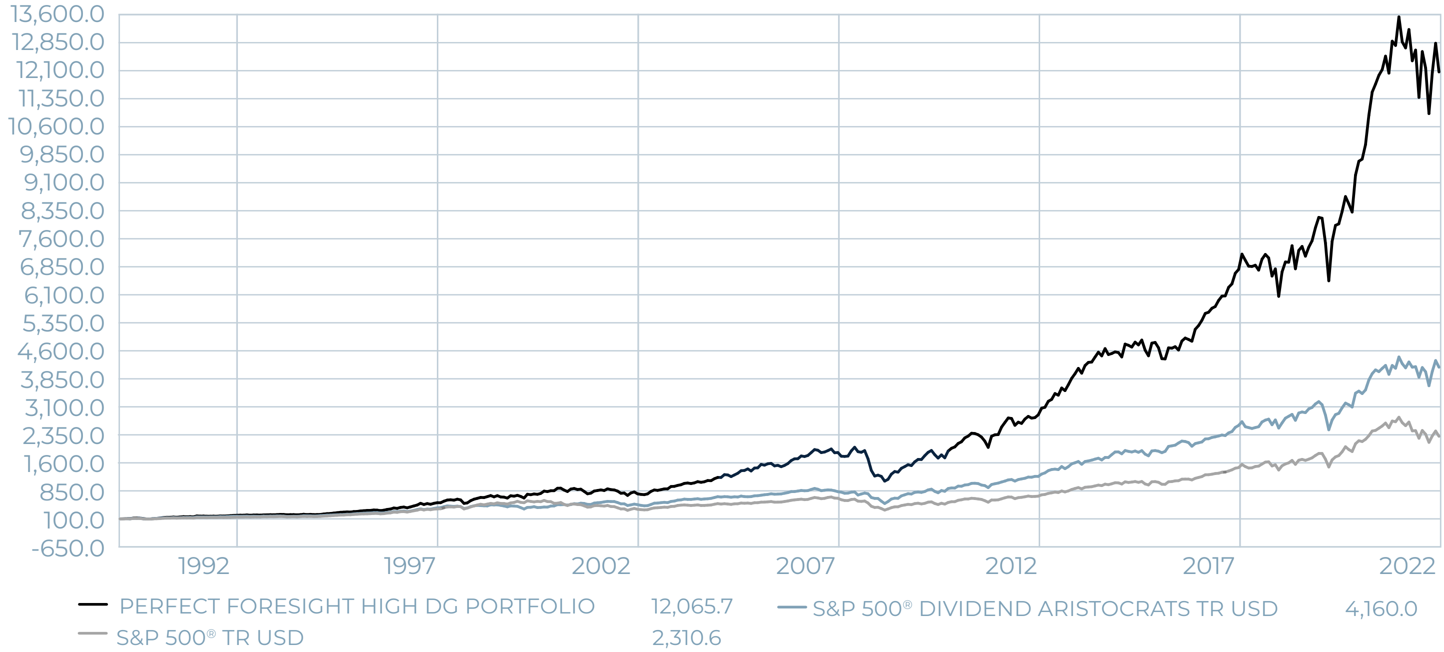


Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023.

HIGH DIVIDEND GROWTH WITH PERFECT FORESIGHT – THE BRISTOL GATE METHODOLOGY

Bristol Gate uses a proprietary Machine Learning model to identify the best dividend growers of tomorrow, today. While unable to be perfect, it is important to understand the opportunity of the universe. We have analyzed how the top quintile (top 20%) of dividend growers annually, as a portfolio, would have returned over the last twenty years and since 1990. Below is a clear example of why we focus on high dividend growth.

PERFORMANCE OF THE PERFECT DIVIDEND GROWTH PORTFOLIO



Source: Bristol Gate, Bloomberg, Jan 31, 1990-Dec 31, 2023, in USD.

It is clear through the above that owning the fastest dividend growers each year can amount to very attractive returns over time.

If you had perfect foresight and invested in the top 20% (Top Quintile Dividend) of the highest dividend growth companies for the next twelve months at the beginning of each year, you would outperform the market over the past 20 years, resulting in very attractive risk-adjusted returns over time. Each theoretical portfolio presented for the stated category was constructed from an equal weight basket of stocks selected from the S&P 500® universe and reconstituted annually. In the world of dividends, we think an emphasis on dividend growth is a valuable addition to a portfolio.

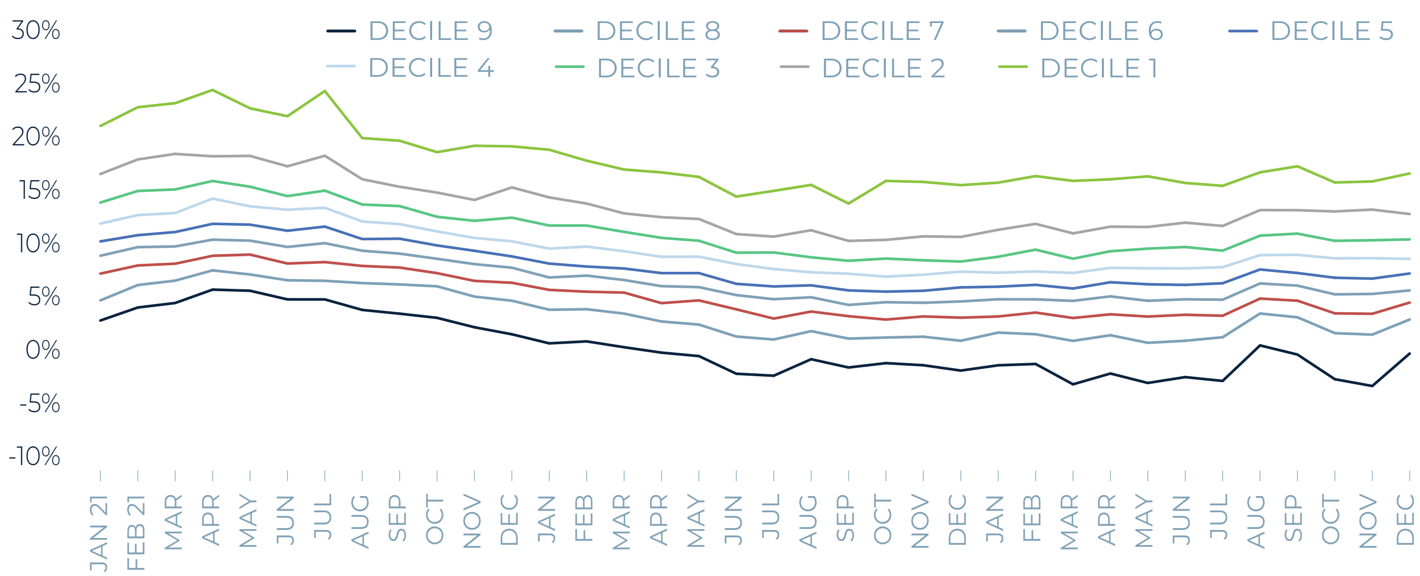
This strong performance can also be attributed to the capital preservation potential of companies growing their dividends at high rates. Over time, we see the fastest dividend growers drawing down less than the market (S&P 500®) during periods of increased volatility.

Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023.

DIVIDEND GROWTH TRENDS – LOOKING FORWARD TWELVE MONTHS

Continuing off our previous Dividend Report editions, we are happy to provide our updated proprietary predictions of dividend growth. Below you will find our median prediction for dividend growth looking forward over the next 12 months, broken into 9 deciles of dividend payers. Decile 1 are the fastest dividend growers, with Decile 9 representing the slowest.

12 MONTH FORWARD DIVIDEND GROWTH PREDICTION BY DECILE



Source: Bristol Gate Capital Partners, FactSet. Data represents the Next Twelve-Month prediction of Dividend Growth. As an example, the 01/01/23 represents the prediction for 01/01/2024

As of December 2023, we are beginning to see an increase in dividend growth predictions after a steady decline in 12 month-forward predicted dividend growth throughout 2021 and 2022. While the 9th decile is still predicting to produce negative dividend growth over the next 12 month, the majority of the dividend universe in is positive territory.

As stated in the past, not all dividend growth is made equal. There is a predicted dividend growth spread of nearly 17% between the top and bottom decile. We believe there is an opportunity to earn above average rates of dividend growth by focussing consistently on the first and second decile of dividend growers.

If you would like to learn more about dividend payers, please reach out to anyone on our Relationship Management Team who will be happy to share information on the constituents in these deciles.

TOP 15 DIVIDEND PAYERS HISTORICALLY BY DOLLAR AMOUNT

2023	DIVIDENDS PAID ($B)	2022	DIVIDENDS PAID ($B)	2021	DIVIDENDS PAID ($B)	2020	DIVIDENDS PAID ($B)	2019	DIVIDENDS PAID ($B)
Microsoft Corp	20.2	Microsoft Corp	18.6	Microsoft Corp	16.9	Microsoft Corp	15.5	At&T Inc	14.8
Apple Inc	15.0	Exxon Mobil Corp	14.9	At&T Inc	15.1	At&T Inc	14.9	Exxon Mobil Corp	14.44
Exxon Mobil Corp	14.9	Apple Inc	14.8	Exxon Mobil Corp	14.9	Exxon Mobil Corp	14.9	Apple Inc	14.12
JP Morgan Chase	13.4	JP Morgan Chase	13.6	Apple Inc	14.5	Apple Inc	14.1	Microsoft Corp	14.1
Johnson & Johnson	11.9	At&T Inc	11.6	JP Morgan Chase	12.6	JP Morgan Chase	12.8	JP Morgan Chase	12.2
Chevron Corp	11.2	Johnson & Johnson	11.5	Johnson & Johnson	10.9	Johnson & Johnson	10.3	Verizon Communic	9.96
Verizon Communic	11.0	Chevron Corp	10.8	Verizon Communic	10.4	Verizon Communic	10.2	Johnson&Johnson	9.83
Abbvie Inc	10.4	Verizon Communic	10.7	Chevron Corp	10.1	Chevron Corp	9.4	Wells Fargo & Co	9.5
Pfizer Inc	9.2	Abbvie Inc	9.9	Abbvie Inc	9.1	Pfizer Inc	8.3	Chevron Corp	8.85
Procter & Gamble	9.0	Pfizer Inc	8.9	Coca-Cola Co/The	9.0	Procter & Gamble	7.9	Pfizer Inc	8.01
Bank Of America	9.0	Procter & Gamble	8.8	Pfizer Inc	8.7	Wells Fargo & Co	7.8	Fox Corp - A	7.92
Home Depot Inc	8.2	Bank Of America	8.4	Procter & Gamble	8.4	Bank Of America	7.8	Fox Corp - B	7.92
At&T Inc	8.1	Philip Morris In	7.8	Bank Of America	7.9	Gen Digital Inc	7.6	Bank Of America	7.76
Philip Morris In	7.9	Home Depot Inc	7.6	Philip Morris In	7.5	Philip Morris In	7.3	Procter & Gamble	7.58
Coca-Cola Co/The	7.8	Broadcom Inc	7.0	Home Depot Inc	6.9	Abbvie Inc	7.2	Philip Morris In	7.11

Source: Bristol Gate Capital Partners, Bloomberg. Data as of December 31, 2023. Constituents selected from the S&P 500®

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