

## In Defence of the Dinosaurs

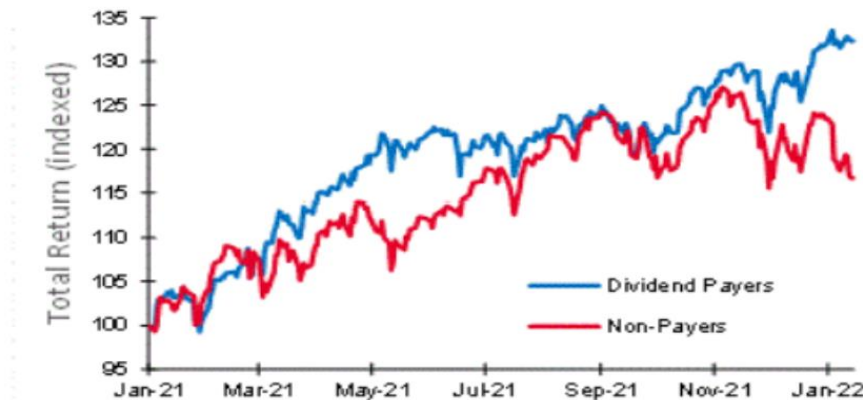
A couple of months ago an article appeared in the Financial Times, written by a well-known City investor, bemoaning the state and performance of the UK stock market\*. References were made to London becoming the ‘Jurassic Park’ of stock exchanges through lack of leadership in so many new, exciting industries. Equity Income funds came in for particular criticism as, it was claimed, their demands for significant dividend payments were starving companies of their ability to invest in growth and productivity – financial decadence allegedly.

A week is a long time in politics, as Boris Johnson can surely attest, but a couple of months can feel like an eternity in stock markets, such has been the upheaval witnessed recently. Underlying changes in drivers of returns have been significant and, we think, relevant in our defence of the dinosaurs. This first chart shows the best performing factors, as covered by Bloomberg, in global equities over the last 12 months. Whilst the resurgence in performance of ‘value’ will not surprise many, the fact that ‘dividend yield’ is the second-best performer possibly will.



Analysis from the quantitative team at Société Générale delves into this further and the following 2 charts confirm this development.

### In the S&P 500 investors are strongly favouring those stocks that pay dividends (20% of the S&P 500 do not pay a dividend)



The chart above shows the relative performance of the c.400 dividend paying companies in the S&P 500 to the c.100 companies that do not pay a dividend, over the last 12 months. Meanwhile, the chart below compares the performance of the top 20% to the bottom 20% of European stocks, when ranked by dividend yield, since last summer.

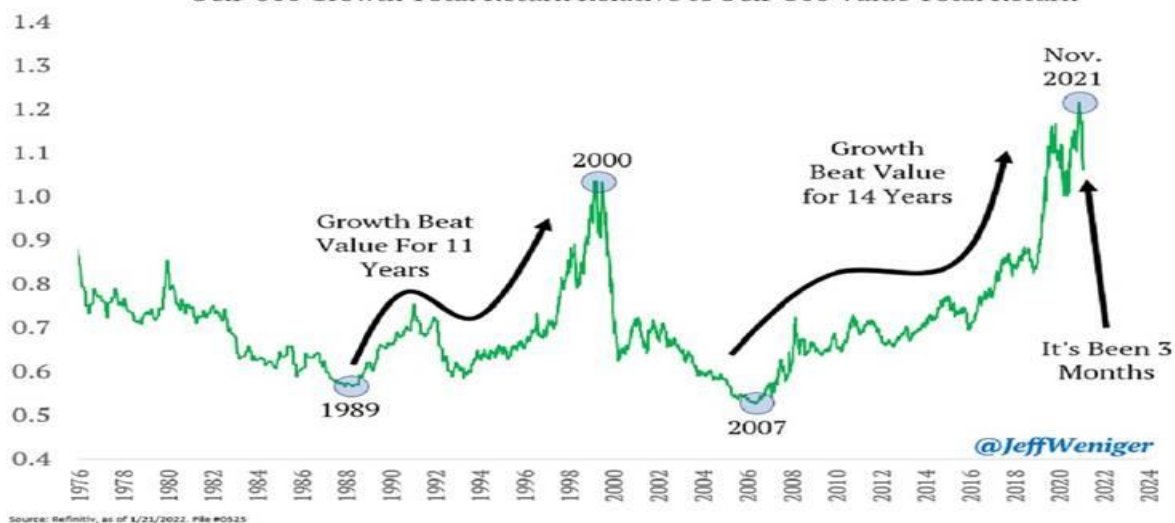
**Highest versus lowest dividend yielding quintile performance in Europe (based on forward consensus dividend yield)**



Source: SG Cross Asset Research/Equity Quant, Factset

Of course, these are relatively short periods of time, and factor performance can be notoriously volatile. However, as we all know, ‘growth’ investing has been in fashion for a significant period, as can be seen in the chart below.

**S&P 500 Growth Total Return Relative to S&P 500 Value Total Return**



Source: Refinitiv, as of 1/21/2022. File #0525

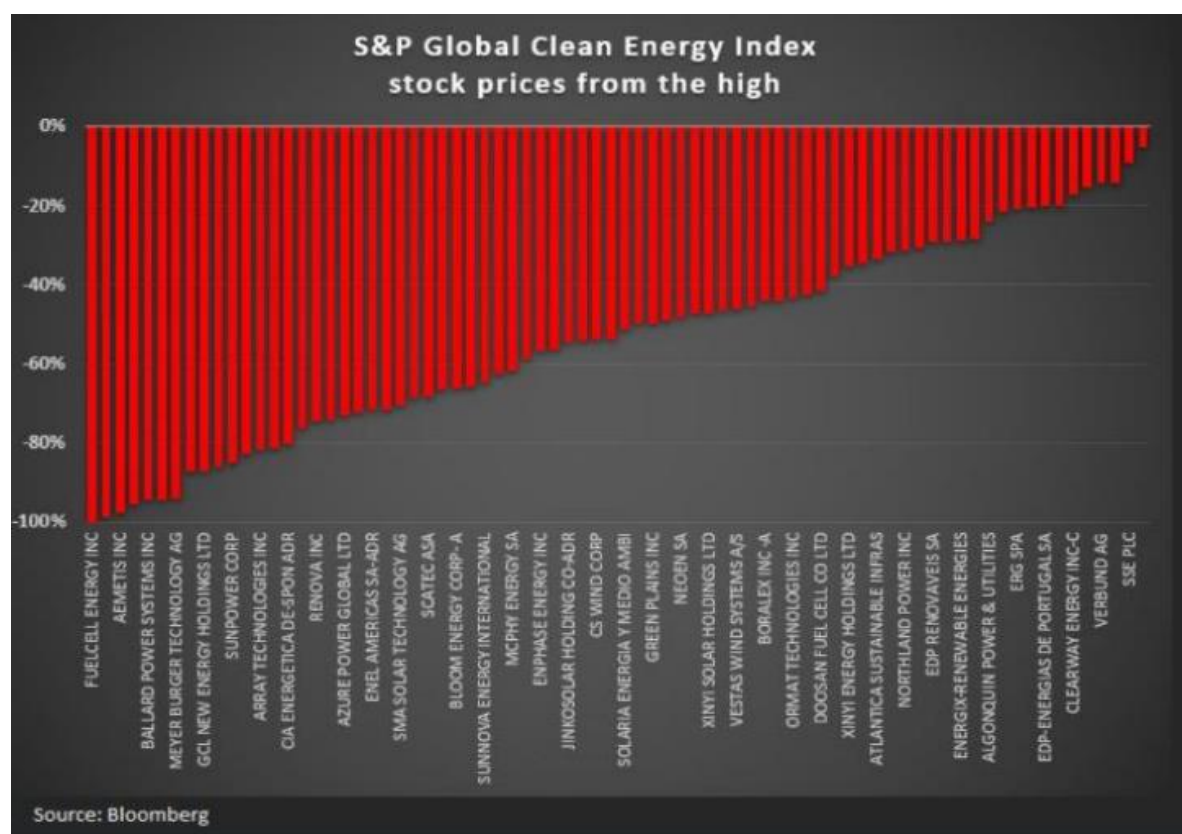
Only time will tell whether or not we are at the start of a sustained reversal in performance for ‘value’ but we strongly suspect we are, and with that will almost certainly come better long-term performance from ‘dividend yielding’ shares.

Should that prove to be the case, we have a high degree of conviction that the UK stock market’s relative performance will significantly improve and, just maybe, the dinosaurs will avoid extinction this time around. Indeed, whilst very, very early days, the UK has been the best performing stock market in the G7 so far this year.

Given the widely publicised issues the UK market has endured recently, it has been a long time since the UK has been the best performing market in the G7 for a sustained period. It is, perhaps, notable though, that following the collapse of the last big growth bubble that peaked in 1999/2000, the UK market enjoyed a substantial period of outperformance thereafter.

With regards to our role in the allocation of company capital, the article mentioned above made specific reference to the ‘thumbs down’ given by the UK market to results from Scottish & Southern Energy (now SSE plc). Apparently, we should have ‘cheered’ when they announced a 2.5-fold increase in their renewable energy investment plans instead of ‘booing’ a reduction in the dividend.

We have no detailed knowledge of their specific investment plans and we are not currently shareholders in SSE plc. However, we do wonder, when looking at the chart below, how many current shareholders will be somewhat relieved that they aren’t being even more aggressive in their investments in these, undoubtedly exciting areas, but where future returns are highly uncertain. The chart highlights the percentage decline in stock price, from the highest point, for members of the S&P Global Clean Energy Index and, in case you can’t read it clearly, SSE are the very far right.



Our point here is not to berate investment in new, world improving industries and technologies but simply to offer a note of caution. The future frequently looks infinitely more exciting than the past and it is absolutely right that investment is made to fulfil that potential. However, all too often stock market investors overestimate the speed with which changes will occur, underestimate the costs associated with such changes and have difficulty, in advance, knowing which technologies and business models will ultimately prove successful. In our experience, people tend to forget just how much capital gets destroyed on the journey to finding the few that truly succeed.

For what it’s worth, we have absolutely no problem in our portfolio holdings reinvesting, often aggressively, in profitable growth opportunities within their businesses. However, we firmly believe that a balanced approach to capital allocation, one that rewards patient investors with cash flows



today, whilst providing sufficient resources to fund profitable reinvestment opportunities for tomorrow, is the right course of action through any investment/innovation cycle. If that makes us dinosaurs, we can live with that.

**Simon Murphy, Fund Manager, VT Tyndall Real Income Fund, 4<sup>th</sup> February 2022**

Data source (unless otherwise stated): Bloomberg.

\*'London is becoming the Jurassic Park of stock exchanges', Paul Marshall, Financial Times, 1<sup>st</sup> December 2021

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