

## Flash Report

# Emerging Market Dividend Investing

– April 2021

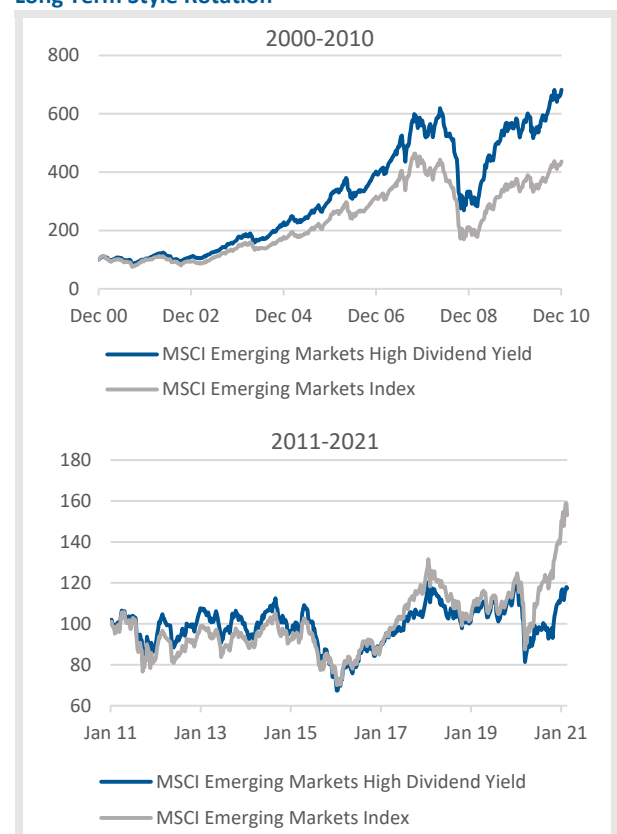
Coming off the back of a notable long period of very low interest rates globally, this report examines the past evolution of this style of investing (emerging market dividend investing), and examines whether there is a renewed opportunity and demand to allocate to emerging markets equity high yielding strategies.

At Fiera Capital, our highly experienced emerging markets equity Portfolio Managers established the Fiera Capital Emerging Markets Income and Growth Strategy (Strategy) over 11 years ago, as a sub set of traditional active management focused on global emerging market equities. In the first quarter of 2021, the Strategy has appreciated by +7.6% versus a +6.5% increase for the MSCI Emerging Markets Index. This brings the outperformance over the last 12 months to +5.2% (all data in gross euros). The approach to dividend investing in emerging markets employed by the Strategy is not simply to buy a basket of the highest yielding stocks, but to find stocks not only yielding above average dividends, but for those dividends to rise over time. This requirement for compounding dividends leads us to higher quality companies with growth which is attractive and predictable.

**A more detailed look at performance, can be seen from the following 20-year charts. There have been strong periods of outperformance of this style, almost entirely negated by the events of the last 12 months.** The COVID-19 pandemic saw hypergrowth digital assets, nearly all of which pay zero or minimal dividends, vastly outperform as investors sought safety in online businesses perceived to benefit from lockdowns and the work from home trend. At the other end of the scale many more traditional businesses, with

operations grounded in the offline world, saw severe disruption which temporarily disrupted their earnings power.

### Long Term Style Rotation



Source: Bloomberg, as at 24 Feb 2021

The Strategy paid dividends over the last 12 months which were down just 9% in GBP terms, reflecting a flat dividend profile in local emerging currency terms. **Such an outcome reflects well on the resilience of the portfolio companies and their dividend paying capabilities** meaning that in many cases, the dramatic share price falls this time last year were overdone relative to the long term earnings power and dividend potential of the underlying operations.

Looking at the key valuation metrics below between the MSCI Emerging Market High Yield Index and the MSCI Emerging Markets Index, it becomes very clear that a severe valuation discrepancy has emerged.

#### Index Valuation Dislocation

	MSCI Emerging Market High Yield	MSCI Emerging Markets Index
PE 2021	9.1	15.3
ROE 2021	11.7%	11.2%
ND/EBITDA	0.1x	1.3x
2022/2020 Earnings expansion	45%	52%
Dividend Yield 2021	5.3%	2.4%

Source: Fiera Capital, MSCI, as at 31 Mar 2021

Whilst the Strategy is orientated much more towards growing rather than absolute dividend yields than the High Yield Index, **the valuation discrepancy still remains substantial with a higher dividend yield, stronger forecast earnings growth and return on equity, and still a valuation discount on a P/E basis.**

#### Strategy Portfolio Characteristics

	Emerging Markets Income and Growth Strategy	MSCI Emerging Market Index
Forecast 3 year EPS (%)	15.3	11.4
Forecast 3 year DPS (%)	14.7	4.0
2020 Dividend Yield (%)	3.4	2.2
Net Debt/EBITDA*	0.2x	0.2x
Earnings Revision (%)**	-18	-29
PE ***	15.2x	16.1x
ROE (%)***	20.1	11.8

Emerging Markets Income and Growth Strategy. All figures based on current weighted averages. \* Excluding Financials, \*\* Previous 12 months, \*\*\* Next 12 months. Source: Fiera Capital, MSCI as at 31 Mar 2021. Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

This leads us to then examine where relative performance has been lost in recent times. Below are the number of basis points lost on an annualised basis through not owning the main index constituents in the Chinese internet sector, none of which meet our yield requirements. **The MSCI Emerging Markets Growth Index, dominated by these Chinese internet and tech companies, outperformed the MSCI High Dividend Yield Index by 36% in 2020, the widest dispersion since inception of the indices.** After a dizzying upward revaluation of the highest growth segment of the market through 2020 we are seeing some signs of caution (or just a reminder that valuation does matter?) evidenced by the 30% correction amongst some of these stocks.

#### Underperformance of Higher Dividend Yielding Stocks

Stock Name	1 Year	3 Year	5 Year
Tencent/ Alibaba	-109 bps	-75 bps	-95 bps
Tencent/Alibaba/Meituan/JD/ Pinduoduo/Baidu/Nio	-433 bps	-153 bps	-126 bps

Source: Fiera Capital, data above shows active relative return as at 26 Feb 2021

Whilst as highlighted above, there has been a recent substantial underperformance of higher dividend yielding stocks, **within this universe the Strategy performance has been very strong and bodes well if the extreme style dispersion witnessed in 2020 begins to mean revert.**

**The Strategy has Consistently Outperformed the MSCI Emerging Markets High Dividend Yield Index**

	Emerging Markets Income and Growth Strategy	MSCI EM High Dividend Yield Index	Strategy Outperformance vs. MSCI EM High Dividend Yield
1 Year	52.7%	30.5%	+22.2%
3 Years	7.1%	3.2%	+3.9%
5 Years	10.1%	7.5%	+2.6%
7 Years	8.1%	5.3%	+2.8%
10 Years	7.9%	3.5%	+4.4%

Source: Fiera Capital, Morningstar Direct, MSCI. All data displayed above is in euros for the period to 31 Mar 2021. Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

In the current uncharted global environment with politicians making huge decisions with very little historical perspective to fall back on, it is difficult to confidently predict the style winners over the near term. Inflation remains the biggest area of macro debate with the short-term economic dislocation effect versus the long-term impact of huge amounts of monetary and fiscal stimulus forming the two sides of the argument. The risks to equity performance are obviously much greater for long duration assets in a rising yield environment (with many now trading at record valuation premium to the broader universe) but have to be weighed against not having exposure to probably the highest growth regions of the world over the next few years. **We believe that dividend investing style offers a way to balance these risks whilst maintaining exposure to the growth aspects of the asset class.**

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