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Cardinal Update

Dividends Shine A Light In Canada

Canadian investors who aren't putting their money in dividend-paying companies on the S&P/TSX are missing out on 30 per cent to 40 per cent of their total return, according to new research from CIBC World Markets.

The report, entitled "It's Raining Dividends in Canada," found that dividends from Canadian public companies have increased by one-third since 2019 with most of that coming from sectors with "excellent track records of stable dividend contributions."

Four industries do the bulk of the heavy lifting when it comes to dividend payments on the TSX – financials, pipelines, communications and utilities. Combined, this quartet accounts for more than two-thirds of all dividends.

"We believe Canadian equities remain attractive – yields are compelling, stable businesses underly most of our dividends and our banking system continues to exhibit tremendous stability," the report says.

It also notes that dividend yields north of the 49th parallel are double what U.S. counterparts are paying. "A record level of relative yield," the report says.

If investors were wondering if they were getting their money's worth with Canadian dividend-paying stocks, wonder no more. Emily Burt, executive vice-president at Cardinal, says that many Canadian investors have a bias towards Canada in their portfolios.

"With the preferential tax treatment on Canadian-based dividends, the strong yields, great growth track records and high-quality companies behind them, it's hard not to want to fill a portfolio with them," she says.

The report also notes that Canadian public companies have become even more focused on dividends than their U.S. peers. Prior to the financial crisis 50 years ago, yields in Canada lagged behind those in the U.S.

"But since, Canadian companies have become dividend converts and today, Canadian yields are a multiple of the yield on the S&P 500," the report says.

Companies that increase their dividends have boards of directors that are confident and optimistic about the future. According to the report's research dating back to 2000, banks – and to a lesser extent, insurance companies – have consistently been the largest contributor to overall dividends along with a track record of managing dividend pay-outs. This typically enables them to handle the cyclicality of their sectors or businesses "without a high likelihood of dividend cuts."

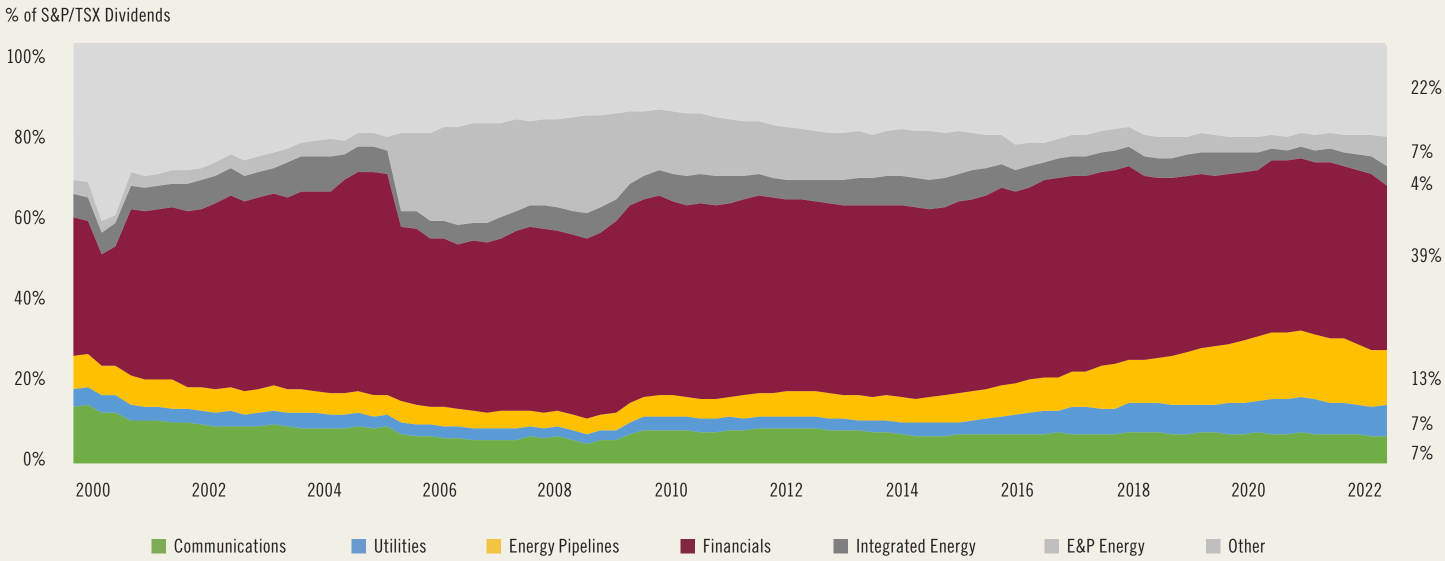
Other sectors that punch above their weight include communications, utilities and pipelines. Along with financials, these sectors make up about two-thirds of all dividends on the TSX.

S&P 500 AND S&P/TSX COMP. – DIVIDEND RETURN AS PERCENT OF TOTAL RETURN, VARYING TIME PERIODS

	S&P 500 Total Return Breakdown					S&P/TSX Comp. Total Return Breakdown			
CAGRS	Price Return	Dividend Return	Total Return	%Dividend Return	CAGRS	Price Return	Dividend Return	Total Return	%Dividend Return
30 Year	7.8%	2.1%	9.9%	21.3%	30 Year	5.8%	2.6%	8.4%	31.0%
20 Year	7.9%	2.1%	10.0%	21.4%	20 Year	5.9%	3.0%	8.9%	33.6%
10 Year	10.1%	2.1%	12.2%	17.4%	10 Year	5.2%	3.2%	8.4%	38.5%
5 Year	9.5%	1.9%	11.4%	16.8%	5 Year	5.7%	3.3%	9.1%	36.7%
2 Year	-0.1%	1.5%	1.4%	109.9%	2 Year	3.9%	3.2%	7.1%	44.8%
1 Year	0.9%	1.7%	2.6%	65.5%	1 Year	-0.6%	3.4%	2.8%	121.9%

Source: TSE, Bloomberg and CIBC World Markets Inc.

S&P/TSX COMP. – TOTAL TRAILING DIVIDENDS PAID BY SECTOR, SINCE 2000



Note: Values to the far right represent proportions based on most recent trailing dividend data. Source: Compustat and CIBC World Markets Inc.

More than 60 per cent of companies on the TSX increased their dividends in 2022, which is up significantly from 2020 at the height of the pandemic lockdowns. A better indication of the dividend picture, however, is Canadian companies are currently paying out more than $100 billion annually in dividends, up more than 30 per cent from the $76 billion paid out prior to COVID.

Spiking interest rates over the past 12 months haven't dampened the attractiveness of dividend-paying companies, either.

"The after-tax yield on the S&P/TSX is still 50 per cent better than a 10-year Canadian bond. In our opinion, this more than justifies the higher risk associated with dividends," the report says.

During the high inflation we've all experienced since early 2022, many investors have wondered what they should do with their portfolios in order to maintain their purchasing power. Burt says that dividend-paying stocks continue to play an important role here, one that's been tried and tested for decades.

"The dividend growth rate Cardinal has seen on its Canadian portfolios in the last 30 years has consistently outperformed the benchmark. If you can get that with a high-quality investment, it makes an income investor think twice about a bond portfolio being their answer," she says.

COMPANY FOCUS: SAP

SAP is a global software leader known best for their enterprise resource planning ("ERP") systems and similar "run-the-company" software solutions. This includes everything from management of accounting, inventory, customer relationships, human resources, along with added benefits of data and insights powered by growing AI capabilities.

The German-based company has been a strong performer for the Foreign portfolio of late. One of its key drivers has been the solid execution of its 2020 strategic roadmap that laid out a path to emphasizing growth in cloud-based solutions and de-emphasizing license-based sales. This has driven greater recurring revenues with the added bonus of higher margins over time following an initial investment period. Combined with the already core and integrated nature of SAP's software offerings to a customer's operations, this will result in a highly predictable stream of revenues and profits.

An improving revenue growth and margin profile, a pristine balance sheet with cash exceeding debt and pending proceeds from the sale of Qualtrics at an implied US$12 billion price have made SAP an attractive investment for the firm.

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