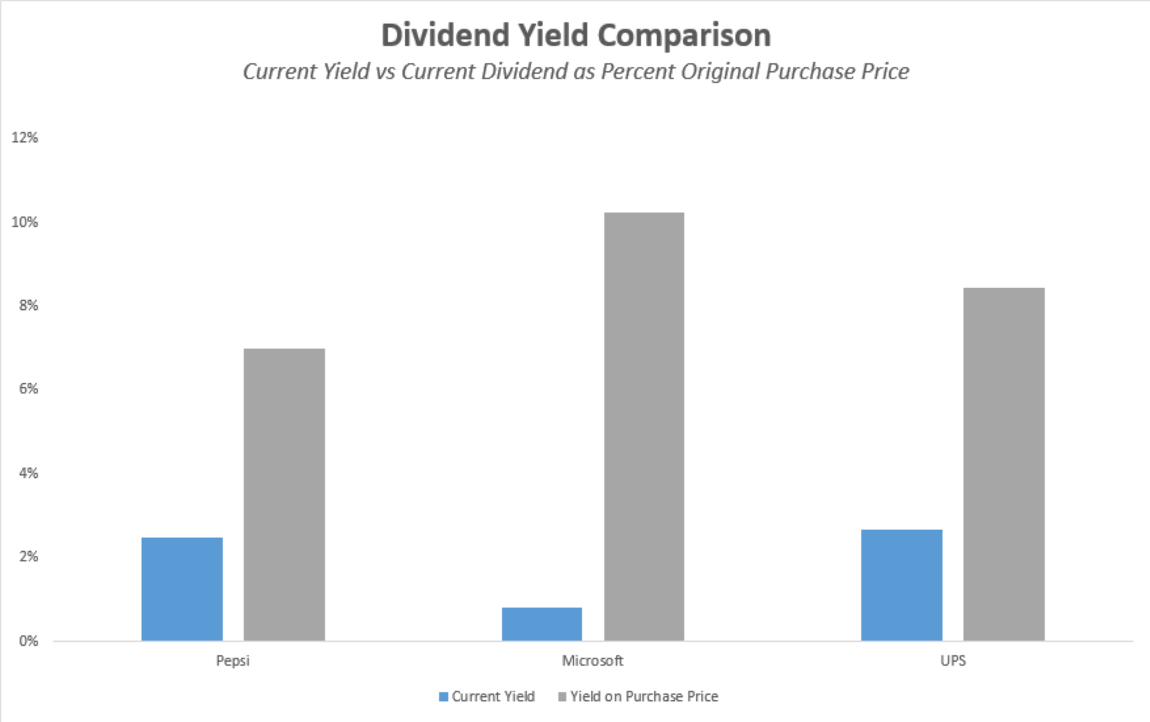
Hidden in Plain Sight

The Lead | February 2022



Source: Bloomberg, Sterling Capital. Current price as of 02.04.2022.

Our investment team is currently in the midst of earnings season as we start 2022. Reviewing and analyzing the quarterly release of financial information by companies and participating in the subsequent conference calls is an important component of our active management of client portfolios. What is occasionally more illuminating than management's response to questions on quarterly conference calls are the questions themselves. A significant challenge we face when questions are asked primarily by analysts at research brokerage firms is the short-term orientation posed to management teams. For example, at the time of this writing we are roughly halfway through the reporting season. According to a Bloomberg transcript search, the words "this quarter" have been mentioned 596 times, while the words "next decade" have been spoken only 30 times. The good news is that the conference calls that included discussion of the next decade included several of the Equity Opportunities Group's holdings, such as Merck, Ball Corporation, and General Dynamics.

We believe one of our investment advantages is taking a longer-term perspective with our investments than investors who are focused on the next quarter. While investment managers speak of taking advantage of time arbitrage, it is helpful to ask what they are looking for in the future. Perhaps it is the hope that Mr. Market will finally recognize the hidden value in their investment? When we think of the long term, our philosophy is aligned with the quote from the CFO of one of our Equity Income holdings who leases cellular towers around the country to Verizon, AT&T, and T-Mobile:

> …but what's really great about the tower business is the longevity of the growth and the returns that it generates. And as long as we stack really good years over on top of each other over and over again, that's what generate significant shareholder value creation for tower investors.
> - Daniel Schlanger, Crown Castle International Chief Financial Officer, Citi Apps Economy Conference

Rather than hoping value will be recognized, the 'stacking' of value creation is core to our quest for both growth and value. A straightforward way of assessing value for companies such as Crown Castle and other examples from our Sterling Capital Equity Income strategy is the growth of their dividends over time.

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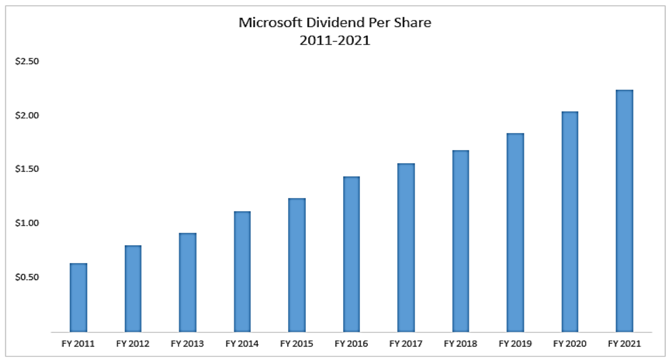
Dividend Contribution to Total Return

Decade	Price Pct. Change	Dividend Contribution	Total Return	Dividends Pct of TR	Avg Payout Ratio
1930s	-41.9%	56.0%	14.1%	100.0	90.1
1940s	34.5%	100.1%	134.6%	74.4	59.4
1950s	257.3%	180.3%	437.7%	41.2	54.6
1960s	53.7%	54.2%	107.9%	50.2	56.0
1970s	17.2%	59.1%	76.4%	77.4	45.5
1980s	227.4%	143.1%	370.5%	38.6	48.6
1990s	315.7%	115.7%	431.5%	26.8	47.6
2000s	-24.1%	15.0%	-9.1%	100.0	35.3
2010s	189.7%	66.9%	256.7%	26.1	35.2
2020s	45.4%	4.8%	50.2%	9.6	39.5
Average	**114.4%**	**87.8%**	**202.2%**	**59.4**	**52.5**

Source: Strategas

While perhaps not evident during a given year, the impact of compounding value can become evident. On the first page, we highlight three actual Equity Income holdings and take the dividend they pay today and divide it by the share price this month and by the share price when it was initially purchased in the strategy. How can a stock such as Microsoft have a dividend yield of roughly 10% on our original purchase price ten years ago? As the chart to the right shows, this was done by ‘stacking’ their quarterly dividend by 250% over that time period. A similar observation can be made with holdings Pepsi and UPS.

Indeed, collecting these dividends over time is an important part of the overall total return profile for stocks that pay investors an attractive dividend yield. Since the 1930s, dividends provided the majority of the total return provided to shareholders, as shown in the Strategas chart above.



Source: Bloomberg

To paraphrase Crown Castle, stacking growing dividends over and over appears to be a great value creator hidden in plain sight.

As always, thank you for your interest and trust in managing your investments.

Charles J. Wittmann, CFA®, Executive Director, joined Sterling Capital Management in 2014 and has investment experience since 1995. Chip is co-portfolio manager of the Global Leaders strategy and associate portfolio manager of the Equity Income strategy. Prior to joining Sterling, he worked for Thompson Siegel & Walmsley as a portfolio manager and (generalist) analyst. Prior to TS&W, he was a founding portfolio manager and analyst with Shockoe Capital, an equity long/short hedge fund. Chip received his B.A. in Economics from Davidson College and his M.B.A. from Duke University's Fuqua School of Business. Chip earned the Certificate in ESG Investing, which is developed, administered and awarded by the CFA Society of the United Kingdom. He holds the Chartered Financial Analyst® designation.

Important Information

Disclosures

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Dividend Policies: Dividend Paying vs. Non-Paying: Each stock's dividend policy is determined by its indicated annual dividend. We classify a stock as a dividend-paying stock if the company indicates that it is going to be paying a dividend within the year. A stock is classified as a non-payer if the stock's indicated annual dividend is zero. Prior to July 2000, the indicated annual dividends were updated on a quarterly basis. Since July 2000, the indicated annual dividends are updated on a daily basis, so the most up-to-date information is used. The index returns are calculated using monthly equal-weighted averages of the total returns of all dividend-paying (or non-paying) stocks. A stock's return is only included during the period it is a component of the underlying index. The dividend figure used to categorize the stock is the company's indicated annual dividend, which may be different from the actual dividends paid in a particular month. **Dividend Growing, No-Change-in-Dividend, and Dividend Cutting:** Each dividend-paying stock is further classified into one of the three categories based on changes to their dividend policy over the previous 12 months. Dividend Growers and Initiators include stocks that increased their dividend anytime in the last 12 months. Once an increase occurs, it remains classified as a grower for 12 months or until another change in dividend policy. No-Change stocks are those that maintained their existing indicated annual dividend for the last 12 months (i.e., companies that have a static, non-zero dividend). Dividend Cutters and Eliminators are companies that have lowered or eliminated their dividend anytime in the last 12 months. Once a decrease occurs, it remains classified as a cutter for 12 months or until another change in dividend policy. (Source: Ned Davis Research).

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