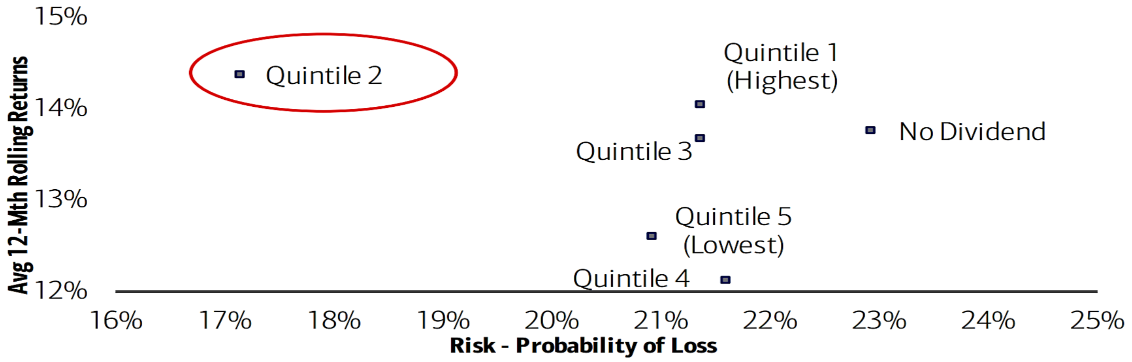
Optimal Yield

The Lead | July 2022

Average Annual Returns versus Downside Risk of Russell 1000® Index Quintiles by Dividend Yield

1/31/84-05/31/22. Quintile 2 had significantly lower risk than the other quintiles, and the highest return



Source: BofA US Equity & US Quant Strategy, Russell

Note: Average 12-month performance in the above exhibit is based on backtested results from 1/31/84 through 9/28/10 and actual performance from 9/28/10 to present. And does not represent the actual performance of any account or fund. Backtested performance depicts the theoretical (not actual) performance of a particular strategy over the time period indicated. No representation is being made that any actual portfolio is likely to have achieved returns similar to those shown herein. Disclaimer: The screen identified as Quintile 2 is intended to be an indicative metric only and may not be used for reference purposes or as a measure of performance for any financial instrument or contract, or otherwise relied upon by third parties for any other purpose, without the prior written consent of BofA Global Research. This screen was not created to act as a benchmark.

Source: BofA Global Research.

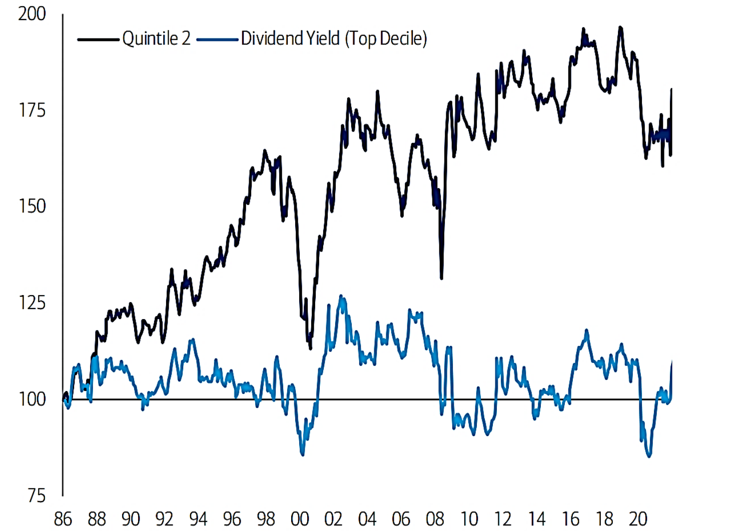
Over the last several months during prospective client meetings, we were asked the same question. Manager research teams wanted to know why, within our Sterling Capital Equity Income strategy, we don't own the highest-yielding dividend-paying stocks. Instead, we seek companies that not only have a dividend yield above 'the market', but are also growing. We don't disagree that maintaining an attractive dividend yield in the strategy can contribute to the total return equation for clients, but how much is the right amount?

Last May, we highlighted how owning the second quartile (25% increments) of dividend growth generated the strongest relative performance versus the Russell 1000® Value Index by using decades-long Ned Davis Research data. This month, Bank of America's (BofA's) Global Research team provided long-term data on the relative outperformance of Quintile 2 (20% increments) dividend yielding stocks within the Russell 1000. Not only were their annualized returns the best over time relative to other levels of dividend yielders, but they also exhibited the best downside capture characteristics. We provided a chart of their analysis above.

BofA Global Research also looked at the long-term performance of stocks that pay the slightly lower dividend yield (Quintile 2) relative to the top dividend yielding stocks. Over time, 'the market' appears to reward companies that pay above market and secure dividends, but not stretched dividend yields. We provided a chart of these dynamics below, with the dark blue line representing the above market and secure dividend payers.

Exhibit 195: High dividend yield strategies underperformed during market downturns; secure yield outperformed over the long run

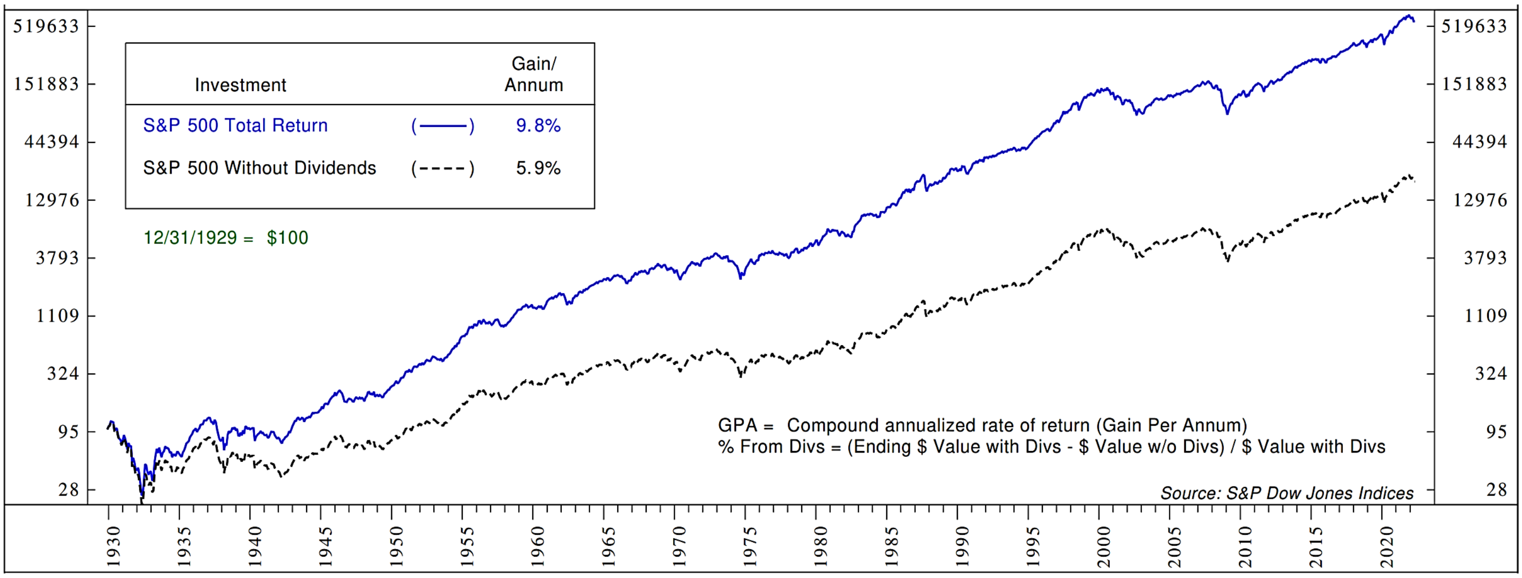
Relative performance of Quintile 2 vs. the equal-weighted Russell 1000 Index and the Dividend Yield* factor vs. the equal-weighted S&P 500 Index (1/1986-3/2022)



Source: Ned Davis Research.

Note: *See our Quantitative Profiles Report for details about the Dividend Yield (QP) factor. Quintile 2 performance in the above chart is based on backtested results from 1/31/84 through 9/28/10. Actual performance is from 9/28/10-present. This performance is backtested and does not represent the actual performance of any account or fund. Backtested performance depicts the theoretical (not actual) performance of a particular strategy over the time period indicated. No representation is being made that in any actual portfolio is likely to have achieved returns similar to those down herein. Disclaimer: The screen identified as Quintile 2 is intended to be an indicative metric only and may not be used for reference purposes or as a measure of performance for any financial instrument or contract, or otherwise relied upon by third parties for any other purpose, without the prior written consent of BofA Global Research. This screen was not created to act as a benchmark.

S&P 500® Index Returns With and Without Dividends (Monthly log scale from 12.31.1929 - 05.31.2022)



Source: Ned Davis Research.

We recognize that dividend yield is an important component to the mission of delivering attractive client returns. We wrote about this dynamic in the winter of 2004, stating "dividends (reinvested) contributed over 40% of the total return from equities over the 77 years ended December 2002, according to Ibbotson Associates, and the majority of total return in three of seven full decades." Seventeen and a half years later, we provided an update on the percentage of long-term total returns derived from dividends using the most recent Ned Davis Research data, and the ratio is similar. Clients may be interested to know that the most recent Sterling Capital Equity Income portfolio yield is positioned firmly within BofA's Quintile 2, providing another positive data point that, in our view, the strategy is well positioned to deliver attractive total returns for our clients over time.

As always, thank you for your interest and trust 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 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

The securities described are neither a recommendation nor a solicitation. Security information is being obtained from resources the firm believes to be accurate, but no warrant is made as to the accuracy or completeness of the information.

The volatility of an index varies greatly. All indices are unmanaged and investments cannot be made directly in an index.

The Russell 1000® Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000® Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000® represents approximately 92% of the U.S. market. The Russell 1000® Index is constructed to provide a comprehensive and unbiased barometer for the large-cap segment and is completely reconstituted annually to ensure new and growing equities are included.

The Russell 1000® Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000® companies with lower price-to-book ratios and lower expected growth values. The Russell 1000® Value Index is constructed to provide a comprehensive and unbiased barometer for the large-cap value segment. The index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect value characteristics.

The S&P 500® Index is a readily available, carefully constructed, market-value-weighted benchmark of common stock performance. Currently, the S&P 500 Composite includes 500 of the largest stocks (in terms of stock market value) in the United States and covers approximately 80% of available market capitalization.

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).

Technical Terms: **Dividend Yield**: a financial ratio that measures the annual value of dividends received relative to the market value per share of a security. In other words, the dividend yield formula calculates the percentage of a company's market price of a share that is paid to shareholders in the form of dividends. (Technical definitions are sourced from Corporate Finance Institute and Investopedia.)

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Past performance is not indicative of future results. Any type of investing involves risk and there are no guarantees that these methods will be successful.

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