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Dividend Barometer

Q1 2023

What is the Dividend Barometer?

Much of the UK equity income conversation is focused on a narrow set of large companies. This overlooks businesses outside the FTSE 100 with strong dividend cover and a track record of growing dividend distributions. The barometer is a report, compiled by the Quoted Funds team at Octopus Investments, which champions the lesser-known dividend credentials of small and mid-cap income stocks.

> ***Barometer (n.)*** *something that can show how a particular situation is developing, or how people's opinions on a particular matter are changing.*

Headlines

Investors can achieve a solid dividend yield looking away from the FTSE 100.

Just ten stocks are expected to generate 55% of total payouts in the FTSE 100.

With Rio Tinto recently cutting its dividend, the cover offered by many small and mid-cap stocks is attractive.

FTSE AIM is the only index where payouts are expected to recover to pre-Covid levels in 2023.

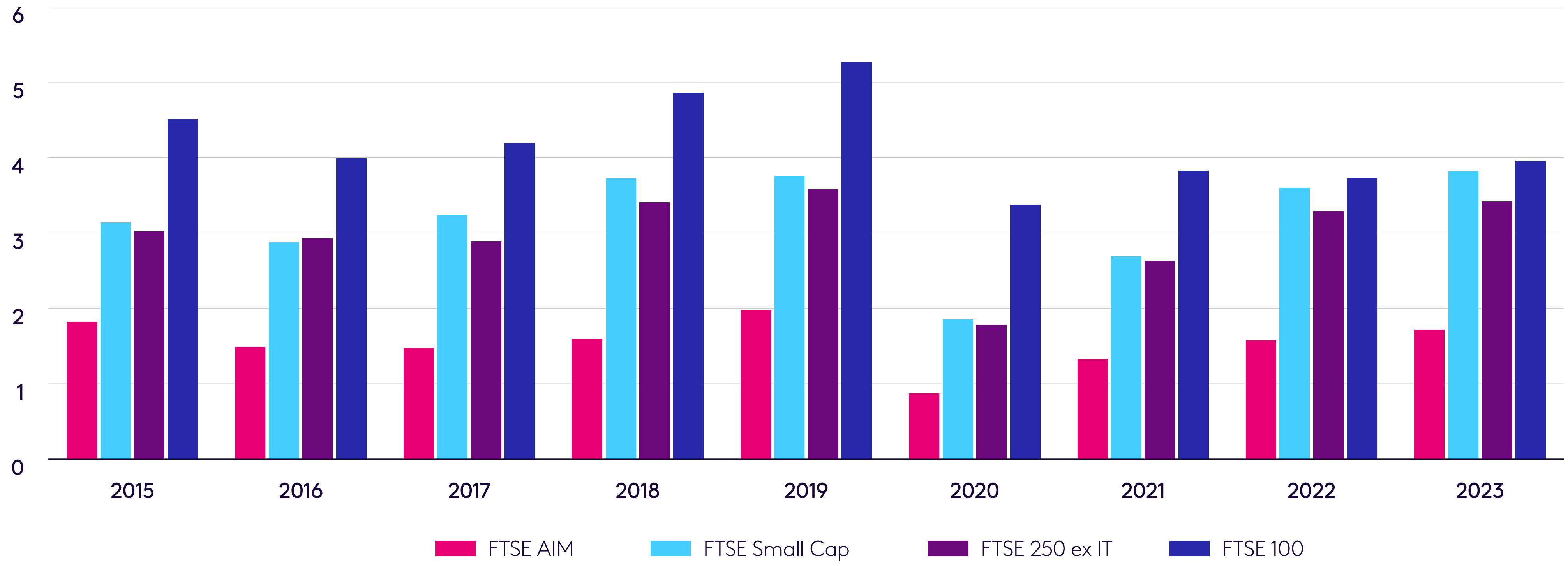
Attractive dividend yields available outside of the FTSE 100

While many of the better known 'traditional' equity income stocks focus on the FTSE 100, there are over 550 dividend paying companies across the entire UK equity market.

Many of these outside the FTSE 100 have attractive levels of earnings growth, that can underpin sustainable and growing dividends.

Performance in the FTSE 100 may have improved recently and is expected to deliver a dividend yield for the current year of just over 3.9%, but other indices are increasingly on its tail. The FTSE 250 (ex-Investment Trusts) is expected to pay out a healthy 3.4%, and the FTSE Small Cap (ex-Investment Trusts) is positioned to do even better with an attractive 3.8% expected.

Dividend Yield By Index (%)



Past performance is not a reliable indicator of future results. Source: Octopus Investments/Factset to 25/01/2023.

Eggs and baskets

There's significant dividend concentration in the FTSE 100, where the bulk of dividend yields come from a small number of big names. These companies form the cornerstone of most traditional equity income funds and investors should consider how exposed they are to stock-specific risk.

In the FTSE 100, the largest ten dividend payers are expected to generate 55% of total cash payouts for the year to December 2023. It is also a relatively narrow range of sectors that feature here too. Banks, resources, tobacco and healthcare stocks feature heavily amongst the largest payers including regular dividend stalwarts such as HSBC, Shell, BAT, Glencore, Rio Tinto, BP, AstraZeneca and GSK.

It's worth noting the recent dividend cut by Rio Tinto following a fall in annual profits, due in part to lower commodity prices. Other mining industry peers have also recently cut dividends for similar reasons. So macroeconomic risks need to be factored in when deciding the sustainability of dividend streams for some FTSE 100 dividends stalwarts.

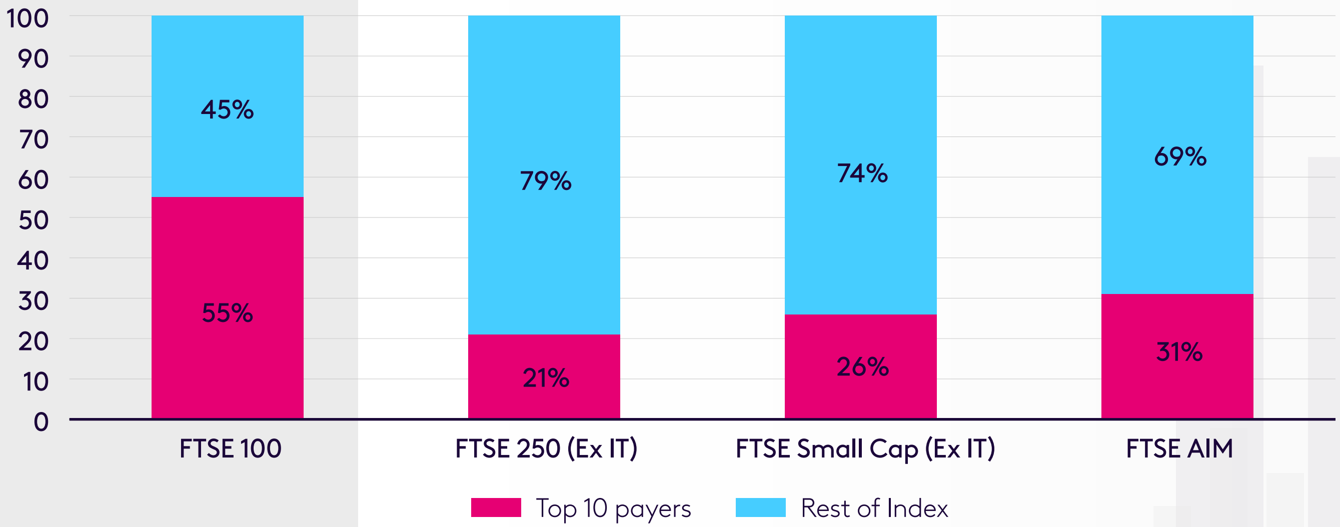
Other indices benefit from a wider base of dividend yielding stocks.

Within the FTSE 250 ex-Investment Trusts, the largest ten dividend payers account for 21% of total payouts. Stocks which are expected to generate the largest payouts for the year to December 2023 are also across a wider variety of sectors and include names such as insurer Direct Line, housebuilder Vistry, media company ITV, financial services companies Intermediate Capital, Investec, Man Group, IG Group, OSB and oil sector names including Israeli producer Energean and Scottish-based Harbour Energy.

Across the FTSE Small Cap (ex- Investment Trusts), the largest ten cash payers account for 26% of payouts. Names featured include prepared food specialist Bakkavor, Irish headquartered miner Kenmare Resources, payments processor Paypoint, and window and door manufacturer Tyman.

[1]For the year to December 2023, the FTSE 100 is expected to deliver a dividend yield of 3.96%, whereas the FTSE Small Cap index is expected to deliver a yield of 3.8%, and the FTSE 250 at 3.4%.

Dividend Concentration By Index to December 2023 e



Source: Octopus Investments/Factset to 25/01/2023.

Within AIM, the concentration increases slightly against other small and mid-cap indices. But it still fares much better than the FTSE 100. Within FTSE AIM, the top ten cash payouts account for 31% of total dividends. This concentration increase is likely a result of the size skew within AIM, with many of the largest stocks within the index being large cash payers. Names include international translation services specialists RWS Holdings, business information provider GlobalData, and UK and Irish aggregates specialist Breedon, as well as Impax Asset Management, and iEnergizer, all with a market capitalisation in excess of £1 billion.

Largest 10 Payers By Index

FTSE AIM	FTSE Small Cap (Ex IT)	FTSE 250 (Ex IT)
iEnergizer Limited	Provident Financial	Intermediate Capital Group
RWS Holdings	Bakkavor Group	Investec
Polar Capital Holdings	Kenmare Resources	Harbour Energy
Serica Energy	Chesnara	ITV
Smart Metering Systems	Regional REIT Ltd	IG Group Holdings
Impax Asset Management Group	Civitas Social Housing	Direct Line Insurance Group
Breedon Group	PayPoint	Energean
GlobalData	Impact Healthcare REIT	Man Group
James Halstead	Tyman	Vistry Group
Central Asia Metals	Foresight Group Holdings Ltd	OSB Group

Past performance is not a reliable indicator of future results. Source: Octopus Investments/Factset as at 25/02/2023 forecast for the year to December 2023.

Yields and cover

Dividend cover is an important consideration for income investors. It's a simple measure that shows the amount of profit a company has available to meet its obligations to pay shareholders a dividend.

Cover below 1.5x can put a stock at risk of reducing or postponing a dividend, since it has less flexibility to continue paying a dividend should its profits fall.

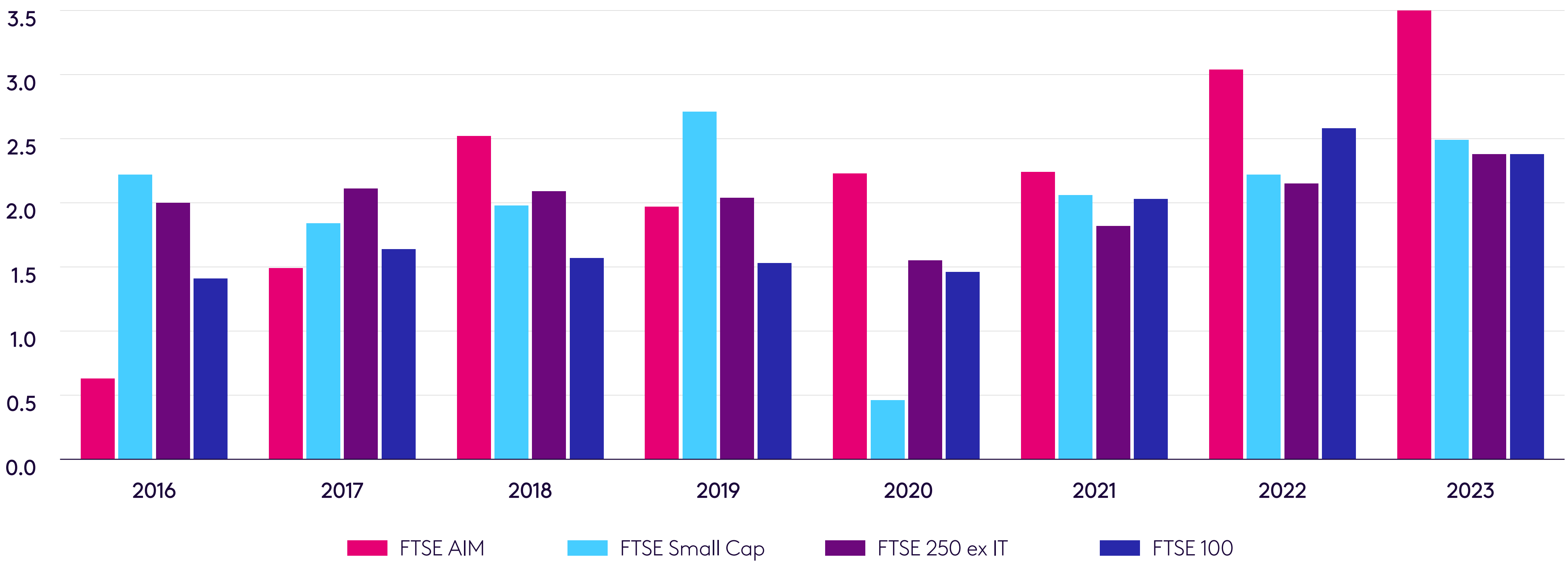
If we look back to the middle of the last decade, FTSE 100 cover had declined to less than 1.5x, well below its 20-year average of 2.0x. This level was maintained, arguably unsustainably, until Covid-19 forced many companies to cut dividends in the uncertain conditions.

Since dividends were reinstated after the pandemic, cover has increased for the FTSE 100 back to 2.0x for 2021 and is estimated to be 2.4x for 2023. But we should bear in mind that this level of attractive cover can also be found by seeking out growth-focused stocks. The FTSE 100 is dominated by established companies that have limited growth opportunities and pay out the majority of profits as dividends, as opposed to reinvesting them. This can lead to poorer levels of sustainable growth.

Looking outside of the main list, for example, FTSE AIM is expected to deliver a yield of 1.7% - lower than other indices - but the growth focus of many of the stocks listed on AIM means dividend cover is an attractive 3.5x. This is versus 2.5x for the FTSE Small Cap (ex IT) and 2.4x for the FTSE 250.

Dividend Cover By Index (x)

Past performance is not a reliable indicator of future results. Source: Octopus Investments/Factset to 25/01/2023.



FTSE AIM - Growing and resilient dividends?

Across indices, cash payouts this year are not yet expected to fully recover back to pre-Covid levels, with one exception being FTSE AIM.

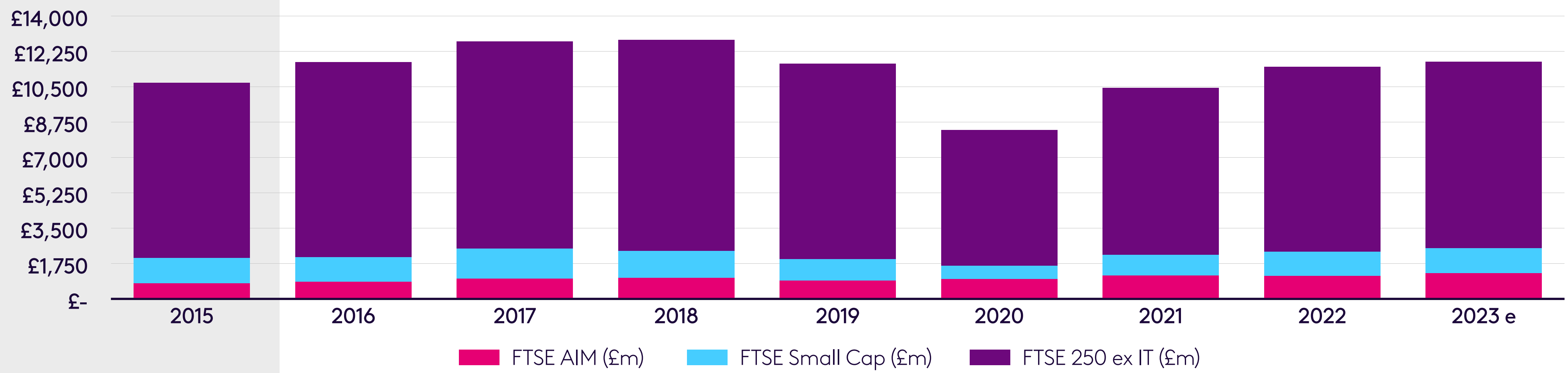
Since 2015, FTSE AIM total dividend payouts have increased by an impressive 64%, from around £770 million to almost £1.3 billion expected for 2023. This compares to FTSE 100 total dividend payouts increasing by only 17.3%. This increased AIM payout has largely been driven by an increased payout per company, rather than a significantly larger number of companies within AIM issuing a dividend.

Looking to more recent history, and comparing current payouts to pre Covid, within the FTSE AIM index, the total cash payout to December 2023 is expected to be 22.4% above that delivered for the year to December 2018. This dividend recovery and growth is well ahead of all other indices.

Looking across the other SMID indices over the same period, the total cash payout for December 2023 is expected to be down c8.4% with the FTSE Small Cap (ex IT), with payouts still 7.1% below 2018, and the FTSE 250 (ex IT) down c11.7% against 2018.

That being said, all small and mid-cap indices compare favourably against the FTSE 100, which for year to December 2023, is still expected to be down -14.7% against 2018.

Overall Cash Payments By Index (£m) **Past performance is not a reliable indicator of future results.** Source: Octopus Investments/Factset to 25/01/2023.



This quarter's dividend diamonds

This Dividend Barometer has shown that looking at the lesser-known dividend credentials of small and mid-cap income stocks should be worth considering as part of a UK equity income strategy. If you would like to discuss any elements of the Barometer in more detail, do get in touch with the Quoted Team at Octopus Investments. In the meantime, the below are two current, portfolio stocks that the team think have shone over Q1:

Intermediate Capital
Global alternative asset manager

Sector: Financial services

Index: FTSE 250

Intermediate Capital is a global alternative asset manager operating across four asset classes including structured and private equity, real assets and credit. The business was established in 1988 and benefits from the continued growth in alternative asset investments. The group has seen growth in its ordinary dividend for 12 consecutive years, with FY 22 reporting a 36% increase compared to FY21. For this financial year, the business is expected to generate a 5-year dividend compound annual growth rate of almost 22%, and an expected dividend yield of 5.8% for the fiscal year to March 2023.

RWS
International translation services specialist

Sector: Industrial services

Index: FTSE AIM

RWS is a provider of technology enabled language translation and content services. The business was established in the UK in 1998 and has grown to be the number two in the market globally. Following the record £41.9 million paid out in 2022, for the year to December 2023, the business is expected to be one of the largest cash dividend payers on AIM. This will mark 17 years of unbroken dividend progression, a 5-year dividend compound annual growth rate of 10.8%, and an expected dividend yield for the year to September 2023 of 3.5%.

These companies are for illustrative purposes only and are not an investment recommendation.

Discrete 1-year performance
% return to February 2023

	2023	2022	2021	2020	2019
FTSE 100 TR	9.6	19.2	1.4	-2.7	2.2
FTSE 250 (ex Investment Trust TR)	-2.3	2.8	7.7	4.0	-0.9
FTSE AIM TR	-16.1	-11.3	39.3	-4.4	-11.3
FTSE Small Cap TR	-2.9	8.9	23.3	2.7	-1.7
Intermediate Capital Group	-18.2	-1.0	8.7	51.9	-1.0
RWS	-22.6	-24.0	15.2	11.2	6.1

Past performance is not a reliable indicator of future results. Source: Lipper to 28/02/2023.
Returns are based on published dealing prices, single price mid to mid with net income reinvested, net of fees, in sterling.

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Risks to bear in mind

The value of an investment can fall or rise and you may not get back the full amount you invest. Smaller company shares are also likely to fall and rise in value more than shares in larger, more established companies listed on the main market of the London Stock Exchange. They may also be harder to sell.

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