Santander Asset Management

State of Play

29 April 2021

Our Investment Specialist, Simon Durling, shares his thoughts in our latest update.

Is there light at the end of the tunnel for income investors?

Over a year ago investors experienced one of the worst market shocks on record as the pandemic spread, with economies around the world closing their doors and citizens being told to stay at home. The impact on income investors was even more acute as lots of companies across nearly all sectors of the market cancelled or reduced their dividend payments as they attempted to navigate the economic shock and tried to prepare for an uncertain future. Regulators also stepped in to stop banks from paying dividends to shareholders.

Dividend payments remain, especially in the UK, a popular method of investing to create income where shares are bought in companies that historically share some of their annual profit with shareholders. As interest rates have remained at record lows, over the last decade dividend payments have grown significantly. Investors who were prepared to ride the ups and downs of the market over the longer-term, have seen the benefits: income growth and to a lesser extent capital growth, often offsetting the rise in prices, albeit inflation has been much lower over this period than in the past.

According to the latest quarterly Link Group UK Dividend Monitor Report[1] two thirds of companies made a dividend cut in the last 12 months but this varied widely depending on which sector. If we look at companies ranked purely by value, banks, miners, and oil companies made up 60% of all the dividend cuts whilst food retailers have had a bumper year with dividend pay-outs 22% higher than the previous year. This was best demonstrated by Tesco who paid

out a £6.1bn special dividend, the second biggest special dividend ever, as it shared the proceeds of the disposal of its Asian business.

The larger companies, like those who make up the FTSE 100 Index, weathered the crisis better than smaller and medium companies. This is because bigger multinationals are more financially resilient and the dividend giants in defensive sectors (like Unilever, AstraZeneca or British American Tobacco) are represented. The FTSE 100 Index pay-outs fell 39.1% compared to a decline of 60.3% in the FTSE 250 Index, but 76% of the UK's smaller firms were forced to make reductions. The final tally shows that dividends fell 41.6%, excluding special dividends, in the 12 months to the end of March 2021.

The outlook is improving slowly, helped in no small part by Regulators enabling banks to resume dividends in the second quarter of 2021, although these are likely to be much smaller than prior to the pandemic. During the remainder of 2021 special dividend payments are likely to play a more important role within many sectors impacted by the lockdowns as economies reopen and trading resumes. Special dividends are paid when companies exceed their own trading expectations and increase both revenue and profit creating larger cash balances which they choose to share with shareholders rather than simply leaving it on the balance sheet or reinvesting into the company. Housebuilders who have experienced buoyant market conditions for many years are a sector which have often used special dividend payments as additional bonuses for shareholders.

The expectations as we emerge from lockdowns are dependent on the strength and speed of the recovery, and companies will be mindful to avoid jumping to conclusions in case developments in the vaccine roll-out or new variants are identified which could hamper the return to normality. The Link Group UK Dividend Monitor Report[1] concludes that despite the small improvement in dividend payments, 2025 still looks like the most realistic point for UK dividends to finally match their 2019 high point. If the recovery is stronger than anticipated the hope is that this milestone will be reached earlier.

Market update

As I highlighted in last week's update Netflix was the first to report its earnings from the FAANG group (the five major US technology companies) with Apple, Amazon, Facebook and Alphabet (formerly known as Google) due to report this week, as well as Microsoft. Netflix subscription growth numbers were lower than in the last few years and below expectations causing the share price to fall 7% and remain flat since the earnings announcement last Tuesday. At the time of writing Alphabet, announced the technology group's revenues jumped 34% to $55.3bn in a record-breaking first quarter, lifting net profits to $17.9bn. Microsoft also released their latest earnings which beat analysts' expectations across all parts of their business as it benefited from the lockdowns with so many people having started to work from home during the last 12 months.

Tesla, the automotive technology giant, announced that it had delivered 184,800 vehicles during the first three months of the year, more than double their delivery for the same period in 2020. It pointed to strong growth in China as Tesla's revenue jumped by 74% to $10.4bn in the first quarter, propelling net income to $438m. With a market capitalisation of more than $700bn, Tesla is the world's most valuable carmaker. Rapidly growing interest in electric vehicles and solid quarterly results propelled its shares more than 700% higher than last year.

Tune in!

Listen to our UK Head of Multi-Asset Solutions, Stefano Amato, discuss whether inflation concerns are temporary and how portfolios are being positioned amidst unlocking in our latest **Market Views** here.

[1] Link Group - Link Group UK Dividend Monitor Q1 2021 Report - 30 March 2021

Note: Data as at 27 April 2021.