Investing in Asia's Dividend Achievers:

What Do Stronger Dividends Get You over the Long Run?

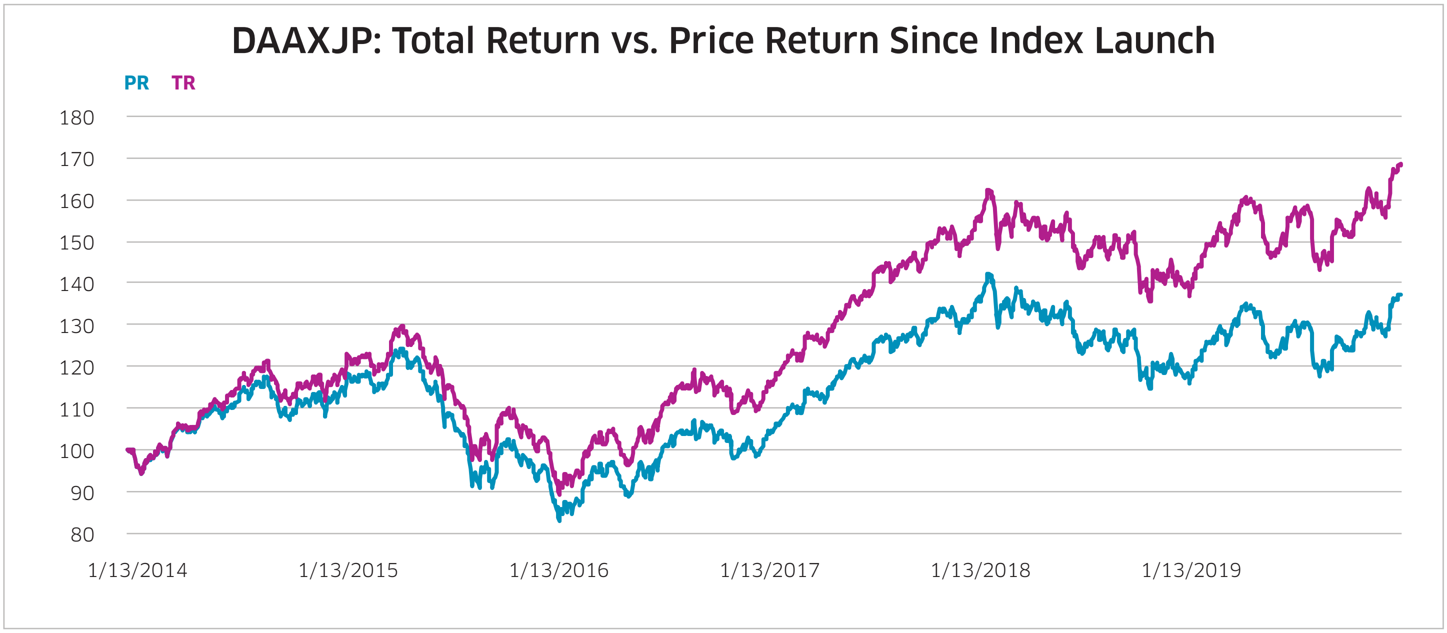
Mark Marex, Product Development Specialist, Global Information Services

For as long as most professional investors can remember, Emerging Markets have on average offered higher-yielding assets – especially within Fixed Income – than their Developed Market counterparts. At the most basic level, higher interest rates are a function of higher inflation, which can persist as a result of elevated economic growth rates, suboptimal monetary and fiscal policy, or in many cases, some combination of these factors. Stronger demographic trends and upward commodity price pressures are often corollaries to this phenomenon, and largely defined the pre-2008 era for EM.

But since shortly after the 2008 Financial Crisis, China – by far the biggest still-emerging economy – has certainly slowed down, and along with it many of its trading partners in Asia and the broader EM space; its benchmark rate is now approaching 4%, which is far below where many slower-growing, Developed Markets had their benchmarks set by central banks in the mid-to-late 2000s. Indeed, 2019 was a record-setting year in terms of central banks cutting rates globally. By one measure it was the longest easing cycle for emerging market central banks since 2013, with 10 straight months of net cuts across 37 developing economies.[1] By another measure, there was more widespread rate-cutting than at any time since the 2008 Financial Crisis.[2]

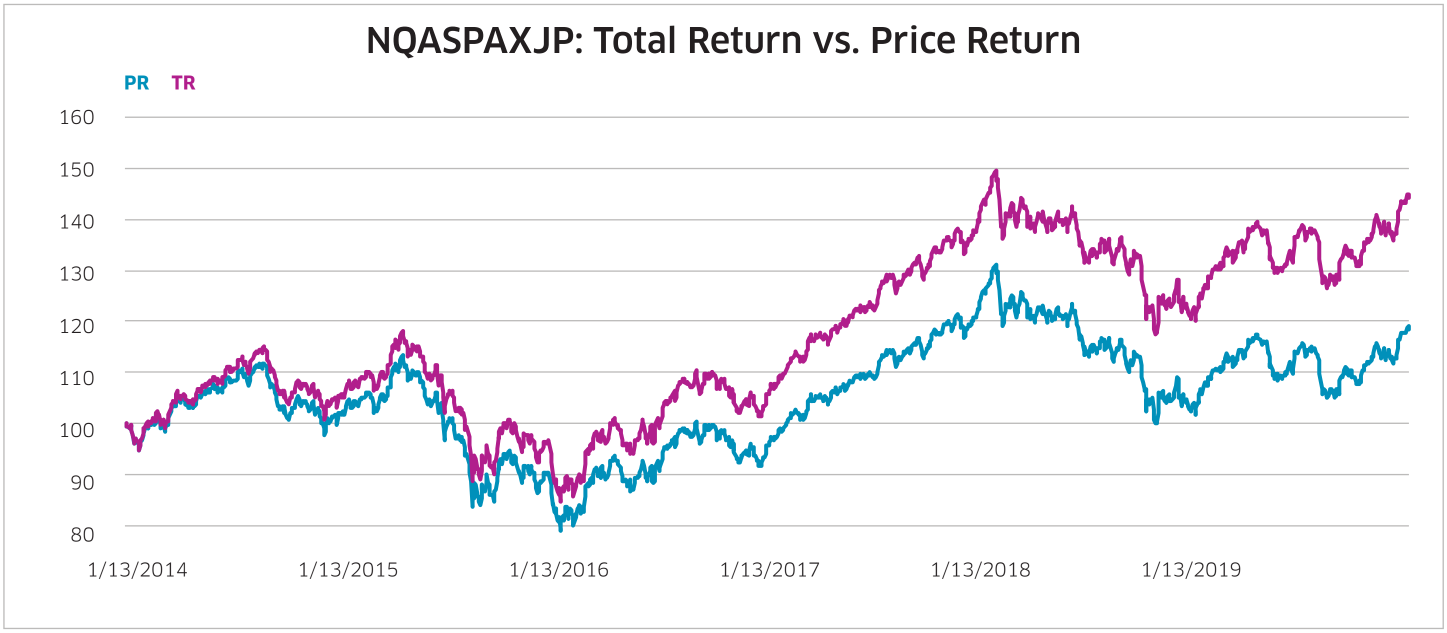
With lower interest rates, fixed income investments become less and less appealing. For investors looking to maintain exposure to Asia's economic potential, equities represent the natural option to rotate their allocations. But there are many reasons why a standard market capitalization-weighted index might not qualify as the best portfolio opportunity, especially for those seeking higher yields. Instead, an investor may consider an index specifically constructed to target higher-yielding equities, such as the Nasdaq Asia ex Japan Dividend Achievers Index (DAAXJP).

1. https://www.cnbc.com/2019/12/03/reuters-america-graphic-down-down-they-go-emerging-central-banks-deliver-more-rate-cuts.html
2. https://www.reuters.com/article/us-emerging-rates/down-down-they-go-emerging-central-banks-deliver-most-rate-cuts-in-a-decade-idUSKCN1VN1J2

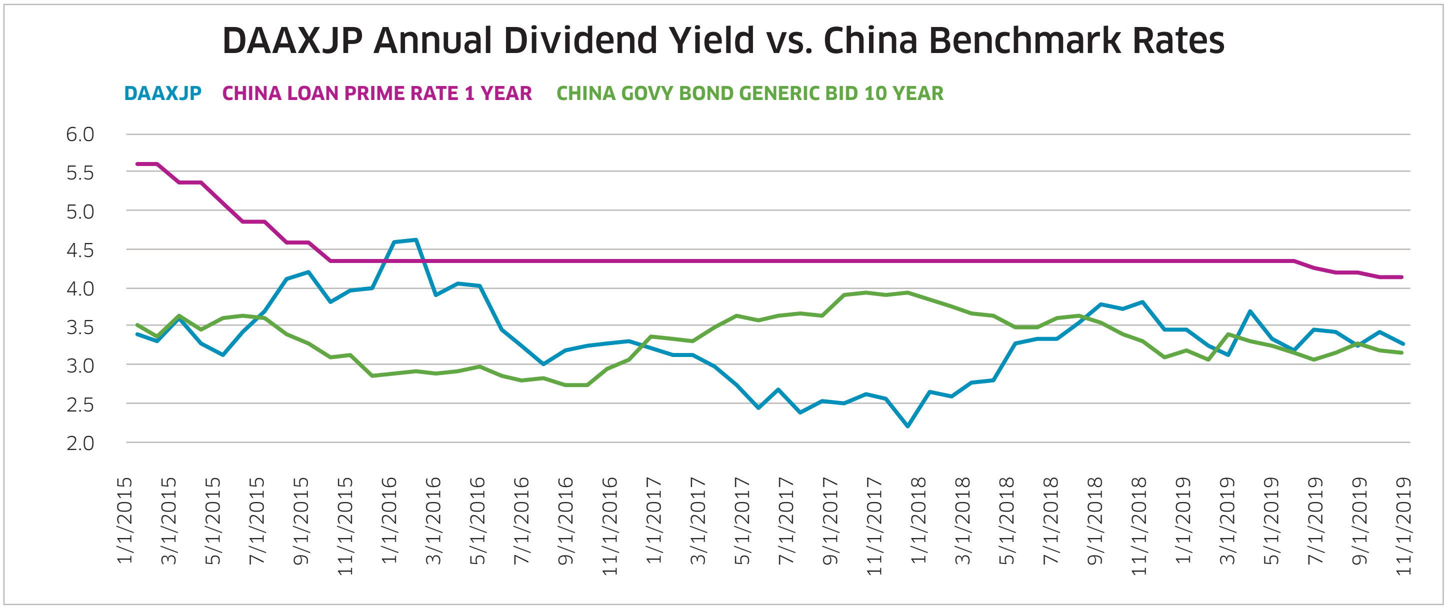


Since the launch of the index on Jan 13, 2014, it has appreciated by 68.1% on a total return basis. Impressive on its own, but even more so when contrasted with its price return of 37.1%, which strips out the contribution of dividends. Of course this is by design, since the index seeks out companies with at least three consecutive years of increasing annual regular dividend payments. As of year-end 2019, this meant 168 constituents qualified for index inclusion with an (unweighted) average dividend yield of 4.43%, vs. only 3.21% for its parent index, the Nasdaq Asia Pacific Ex Japan Index (NQASPAXJP) which consists of 2,268 companies in the region.

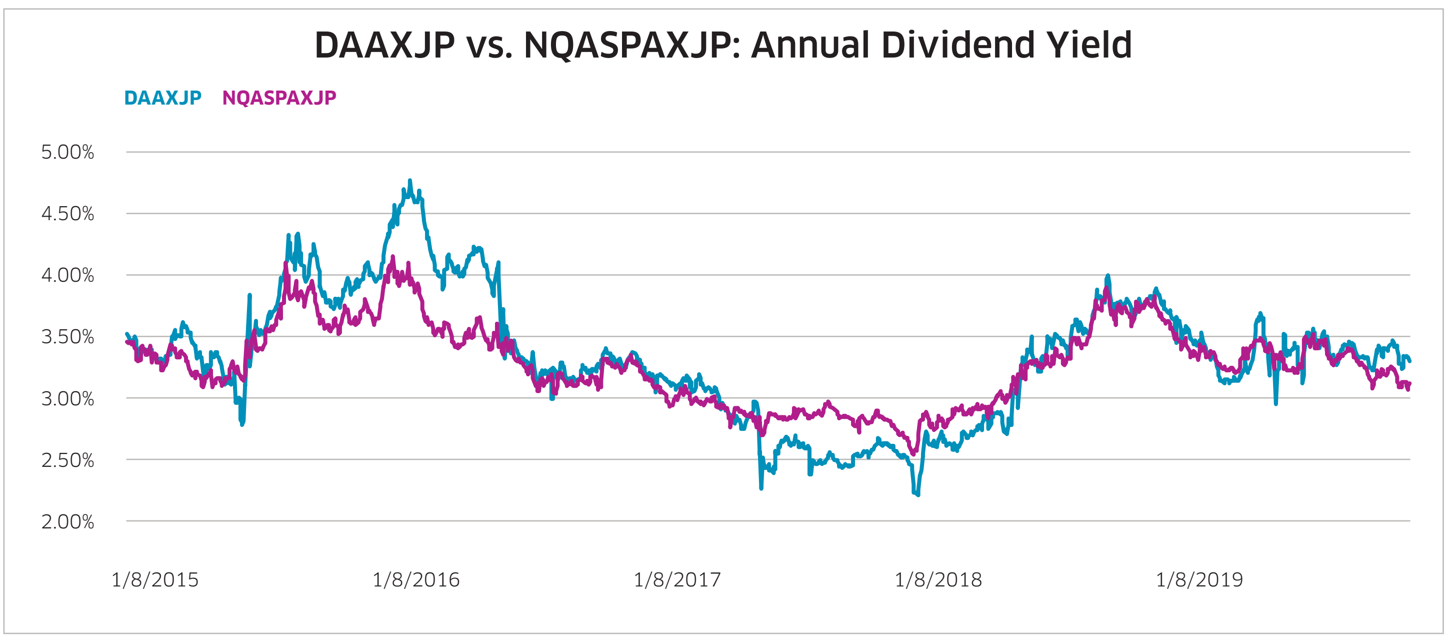
We can further observe that on a comparative performance basis, selecting DAAXJP instead of the broader NQASPAXJP resulted in a higher-quality portfolio. On a price return basis, NQASPAXJP appreciated only 18.4% over the same time period – about half that of DAAXJP. On a total return basis it fared much better, generating 44.2%, but still only about two-thirds of DAAXJP. These performance gaps are meaningful and material, especially over a longer time horizon during which the impact of dividends only grows exponentially due to the power of compounding.



As a final point of analysis, let's consider the pure, point-in-time annualized dividend yield of DAAXJP and observe how it has evolved over time in comparison with the benchmark interest rates in China.



As can be seen, China's benchmark lending rate (the 1-Year Prime) has fallen from 5.6% at year-end 2014 to 4.15% at year-end 2019, while China's 10-year government bond yields only 3.15%. Despite already offering the potential for considerable price appreciation, DAAXJP in addition offers a healthy 3.30% annualized dividend yield as of year-end 2019, which is little changed from where it was 5 years ago.



Products currently tracking this index include the BMO Asia High Dividend ETF (Ticker: 3145).

Sources: FactSet, Bloomberg, Nasdaq Global Indexes.

0295-Q20