AlphaDelta Growth of Dividend Income Class
Quarter 1, 2021, Commentary

Hello everyone,

This is the quarterly advisor update of the **AlphaDelta Growth of Dividend Income Class** ("GoDI" or the "Fund") from SciVest Capital Management Inc., the sub-advisor of the Fund.

Attached to this commentary is the GoDI Portfolio Disclosure as of the end of the quarter. The first page of the Portfolio Disclosure shows all of the current stock holdings of the Fund, as well as some descriptive dividend and valuation characteristics for each portfolio holding – plus overall portfolio averages. The second page of the Portfolio Disclosure shows a number of relevant pie charts depicting overall GoDI portfolio characteristics such as sector, market capitalization, dividend yield and dividend growth "bucket" exposures. We also publish and post on our website a *monthly* version of the GoDI Portfolio Disclosure document (http://scivest.com/strategies/manager-commentary).

Portfolio Income and Income Growth:

The two primary **objectives of the Fund are to provide its shareholders with: (i) a consistent, and above average, annual distribution yield; *and* (ii) growth in the absolute level of distributions per share through time (i.e., income growth)**.

We attempt to deliver on these Fund-level objectives by investing in a global portfolio of equities which, on average, pay a higher than average dividend yield and which are growing their dividends per share at a relatively high rate (in the context of their current yield). As shown in the March 31st Portfolio Disclosure, **across the Fund's current holdings, the weighted average gross dividend yield is 3.8% per annum** (versus 1.4% for the Russell 1000 Index and 1.7% for the MSCI World Index) **with impressive double-digit trailing 1, 3 and 5-year dividend growth rates of 10.2%, 11.8% and 15.6%, respectively**.

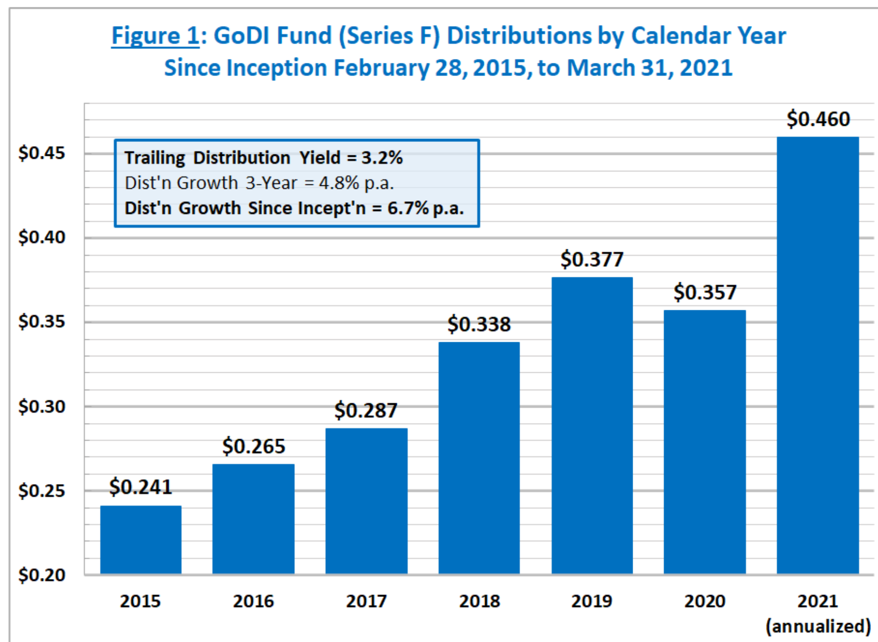
The Fund's 3.8% average portfolio dividend yield is well covered by company earnings and cash-flow. Specifically, the 3.8% average dividend yield compares to a portfolio weighted average forward earnings per share yield of 8.9% **(i.e., 233% dividend coverage by earnings)** and forward cash-flow yield of 11.8% **(i.e., 321% dividend coverage by cash-flow)**.

The Fund has a distribution policy whereby it distributes to its shareholders on a month-end basis *every dollar* (and no more) of dividend income (net of any dividend withholding taxes) accrued by the Fund during the month. As a result, monthly income varies with the dividend cycle of the Fund's holdings, but the distributions perfectly reflect the true dividend income received by the Fund. Thus, the Fund does not experience the typical net asset value per share "grind" that other dividend funds experience when their distributions are set higher than the net income they actually receive. And, since the Fund distributions are a true reflection of the underlying income received by the Fund, they can be used to judge the true income generation and income growth capability of the Fund.

At the Fund-level, **the trailing 12-month distribution yield of the Fund (Series F shares) as of March 31st is a solid and above average 3.2%**. The primary reason why these Fund-level distributions are less than the average dividend yield of the Fund's holdings is that we subtract dividend withholding taxes from the Fund's distributions so that they reflect the true net of withholding tax income generation of its underlying holdings. Nevertheless, due to the Fund's corporate structure, the Fund's distribution yield is quite tax efficient in investor hands as compared to most other income alternatives.

Furthermore, the Fund's trailing 12-month 3.2% distribution income yield has been growing at a rate much faster than the inflation rate through time. Specifically, **the trailing 12-month Fund-level distribution per share has experienced 4.8% per annum growth over the past three (3) years and 6.7% per annum growth since the inception date of the Fund** (for Series F shares). We consider 6.7% per annum income growth as substantial, especially in the context of a relatively high and diversified current income yield of 3.2%, and considering it includes a period that we have coined "Dividend Armageddon". Any income growth rate higher than the inflation rate represents real growth of income purchasing power – one of our primary objectives.

To further illustrate this distribution growth effect over time, **Figure 1** below shows the total distributions for the Fund (Series F shares) for every calendar year since the inception date of the Fund. Again, note that these distributions per Fund share reflect true income and income growth resulting from the Fund's underlying portfolio of dividend-paying equities which themselves are growing their dividends per share.



Overall, the current Fund distribution yield of 3.2% compares very favourably with the March 31st yield of 1.5% per annum on the benchmark 10-year Government of Canada bond. Even with more than 2x the yield of the 10-year bond, the Fund's income has grown at a rate of 6.7% per annum since inception – whereas, of course, a 10-year bond's income does *not ever* grow.

Current Portfolio:

The **GoDI portfolio is, as always, very different from global equity benchmarks with a current Active Share of 95.3%**. This means that 95.3% of weights of our portfolio holdings do not overlap with the MSCI World

Index benchmark (alternatively, only 4.7% of the weights of the GoDI portfolio holdings do overlap with the MSCI World Index). As a result, the GoDI portfolio should **provide significant diversification and differentiation within an otherwise diversified portfolio**.

The March 31st GoDI portfolio is itself well diversified across sectors and industry groups with **the largest sector allocation (Financials) currently at 33.6%**. In order of size, we have the following sector exposures: 33.6% Financials, 17.7% Health Care, 10.7% Energy, 7.4% Industrials, 7.3% Communication Services, 5.5% Consumer Staples, 4.8% Information Technology, 2.0% Real Estate, 1.9% Materials, 1.0% Consumer Discretionary, and 1.0% Utilities. In addition, the Fund holds 5.3% in the "Other" sector category, which represents the Fund's investment in the AlphaDelta *Canadian* Growth of Dividend Income Fund.

On an individual stock holding basis, we currently hold a **diversified portfolio of 49 equity positions** (not including the Fund's holding in the AlphaDelta Canadian Growth of Dividend Fund which itself holds another 43 individual equity holdings). As of the end of the first quarter, the top 10 individual equity holdings represent 40.1% of the Fund's assets and are in descending order of size: Bristol-Myers Squibb Co (BMY, 5.3%), Abbvie Inc (ABBV, 5.1%), Lincoln National Corp (LNC, 4.3%), Broadcom Ltd (AVGO, 4.1%), Prudential Financial Inc (PRU, 4.1%), Enbridge Inc (ENB, 4.0%), Citigroup Inc (C, 3.8%), Manulife Financial Corp (MFC, 3.8%), Nexstar Media Group Inc (NXST, 3.1%), and Goldman Sachs Group Inc (GS, 2.7%). (See entire March 31st GoDI portfolio attached hereto.)

A byproduct of our growing income investment strategy is that the GoDI portfolio typically has much better (i.e., cheaper) valuations than the overall equity markets – that is, **the GoDI portfolio has a high "value style exposure"**. In particular, the March 31st portfolio weighted average 12-month forward price-to-earnings ratio is 15.4x (versus 22.5x for the Russell 1000 Index and 20.1x for the MSCI World Index) and the average 12-month forward price-to-cash-flow ratio is 10.2x (versus 15.7x for the Russell 1000 Index and 13.3x for the MSCI World Index). In other words, **the GoDI portfolio is 25% to 35% *less expensive* than the overall global equity markets based on *forward-looking* earnings and cash-flows.**

Portfolio Changes and Movers:

During the first quarter of 2021, we **initiated new positions** in Agnico Eagle Mines Ltd (AEM), IA Financial Corp Inc (IAG), Merck & Co Inc (MRK), Nintendo Co Ltd (NTDOY), and RIO Tinto PLC (RIO). We also **increased (by at least 0.5%) our existing positions** in Bristol-Myers Squibb Co (BMY), British American Tobacco (BTI), Citigroup Inc (C), Lincoln National Corp (LNC), and Lockheed Martin Corp (LMT).

During the first quarter we **eliminated our positions** in Bayer AG (BAYRY), Brookfield Property Partners (BPY.UN), LyondellBasell Industries (LYB), Skyworks Solutions Inc (SWKS), and ViacomCBS Inc (VIAC). In addition, we **decreased (by at least 0.5%) our existing position** in Algonquin Power & Utilities (AQN) and Broadcom Inc (AVGO).

Amongst the GoDI portfolio holdings that were held through the entire quarter, the five (5) **highest returns during the first quarter** (in descending order) were: Marathon Petroleum Corp (MPC, 30.8%), Nexstar Media Group Inc (NXST, 29.3%), Valero Energy Corp (VLO, 28.5%), Caterpillar Inc (CAT, 28.1%), and Altria Group Inc (MO, 26.9%).

Amongst the GoDI holdings that were held through the entire quarter, the five (5) **lowest returns during the first quarter** were: Unilever PLC (UL, -6.6%), America Movil (AMX, -6.6%), Fiera Capital Corp (FSZ, -4.7%), Algonquin Power & Utilities (AQN, -4.0%), and Ping An Insurance (PNGAY, -1.8%).

Q1-2021 Dividend Announcements:

Since income and income growth are the Fund's primary objectives, each quarter we report those Fund holdings which declared dividend changes during the prior calendar quarter. Recall also that one of our fundamental beliefs is that, if we can select stocks which consistently increase their dividends into the future, then price appreciation *must* eventually follow – that is, **long-term price appreciation is a *consequence* of consistent earnings and dividend growth**. We believe that: **"if you get the dividends right, then you *will* get the share prices right sooner or later."**

Amongst our current 49 GoDI holdings, **during the calendar quarter ending March 31st, 2021, we received 13 declared dividend increases averaging an announced increase of 9.0% quarter-over-quarter** ("QoQ") **and 10.3% year-over-year** ("YoY"), relative to those already known at the end of the prior calendar quarter.

No.	Company Name	Ticker Symbol	Current Ind Div Yld (% p.a.)	QoQ Div Increase (%)	YoY Div Increase (%)
1	Aecon Group Inc	ARE	3.6	9.4	9.4
2	American Tower Corp	AMT	2.1	2.5	14.8
3	British American Tobacco	BTI	7.9	2.5	2.5
4	Comcast Corp	CMCSA	1.8	8.7	8.7
5	Corning Inc	GLW	2.2	9.1	9.1
6	General Dynamics Corp	GD	2.6	8.2	8.2
7	L3Harris Technologies Inc	LHX	2.0	20.0	20.0
8	Nexstar Media Group Inc	NXST	2.0	25.0	25.0
9	Ping An Insurance	PNGAY	2.8	7.3	7.3
10	Prudential Financial Inc	PRU	5.0	4.5	4.5
11	QTS Realty Trust Inc	QTS	3.2	6.4	6.4
12	Rio Tinto PLC	RIO	6.2	13.6	13.6
13	Unilever PLC	UL	3.7	0.4	3.8
	Average		**3.5**	**9.0**	**10.3**

The yield and growth combination of these 13 dividend increases is quite impressive – 3.5% average dividend yield with 10.3% average dividend growth – as good as we could hope for in a "normal" year, let alone during a global pandemic.

We did, nevertheless, experience one dividend decrease during the Q1. Bayer AG, the large German healthcare and agricultural company, pays an annual dividend and it declared a lower annual dividend of €2.00 in late February versus €2.80 last year. This is Bayer's first dividend declared since the Pandemic began and represents their first dividend decrease since 2004. As per our policy regarding dividend cuts, we liquidated our position in Bayer shortly thereafter.

Notwithstanding Bayer, we do continue to observe an expanding number of dividend increases within North America. Last quarter's 13 announced dividend increases for the Fund's holdings highlights this observation

(26.5% of the names in the GoDI portfolio). These dividend increase announcements will translate into actual dividend payment increases this coming quarter, and in the quarters after that, which in-turn should result in Fund-level distribution increases.

Interestingly, most US and Canadian financial companies have not increased their dividends since the beginning of the Pandemic (nor initiated new share buybacks) because the banking and financial service regulators have not allowed these companies to do so until they deem that the Pandemic risk has passed. We expect that the US regulators will begin to allow banks and other financial services companies to once again increase dividends and initiate share buybacks early this summer with Canadian regulators following shortly afterwards. We also expect that US financials will *immediately thereafter* announce material dividend increases as well as large new share buybacks, because many of these financial firms have remained highly profitable throughout the Pandemic and have built up large excesses in capital that they wish to return to shareholders. We look forward to these up-coming announcements, given our substantial exposure to financials.

Market Commentary:

With continued fiscal support from the governments of the developed world and monetary support from the central banks of the developed world, and with large-scale COVID-19 vaccine rollouts around the world, we believe that the developed economies of the world are set for a historically significant rebound in growth and employment beginning in the late spring or early summer of 2021. Numerous analysts expect US growth in the second half of 2021 to be the strongest in many decades. The timing of these re-opening re-bounds in economic growth will vary country-by-country depending upon the timing and success of their respective vaccine rollouts (e.g., US versus Canada, or UK versus continental Europe); however, virtually all developed country economies should be booming by Q3-2021.

With this macroeconomic backdrop, we remain quite bullish on global equities in general, and especially dividend-paying value-based equities in particular. We do need, however, several pre-conditions to remain in place to preserve our overall bullishness: (i) short-term interest rates in North America to remain pegged near 0% for the foreseeable future (as promised by the US Federal Reserve and the Bank of Canada), (ii) long-term interest rates in North America continue to drift higher with enhanced growth expectations but remain contained (as is likely given quantitative easing programs in most developed countries), (iii) long-term inflation expectations remain anchored around 2% per annum (although we do expect a sharp, transitory, spike in near-term inflation as a result of the re-opening rebound and base effects from last year), and (iv) no new variant of COVID-19 emerges that is vaccine resistant, far more transmissible and/or far more deadly than the existing known strains of the virus. *Within* global equity markets, however, we do expect significant rotations between countries and investment styles with money flowing to previously underperforming countries and investment styles.

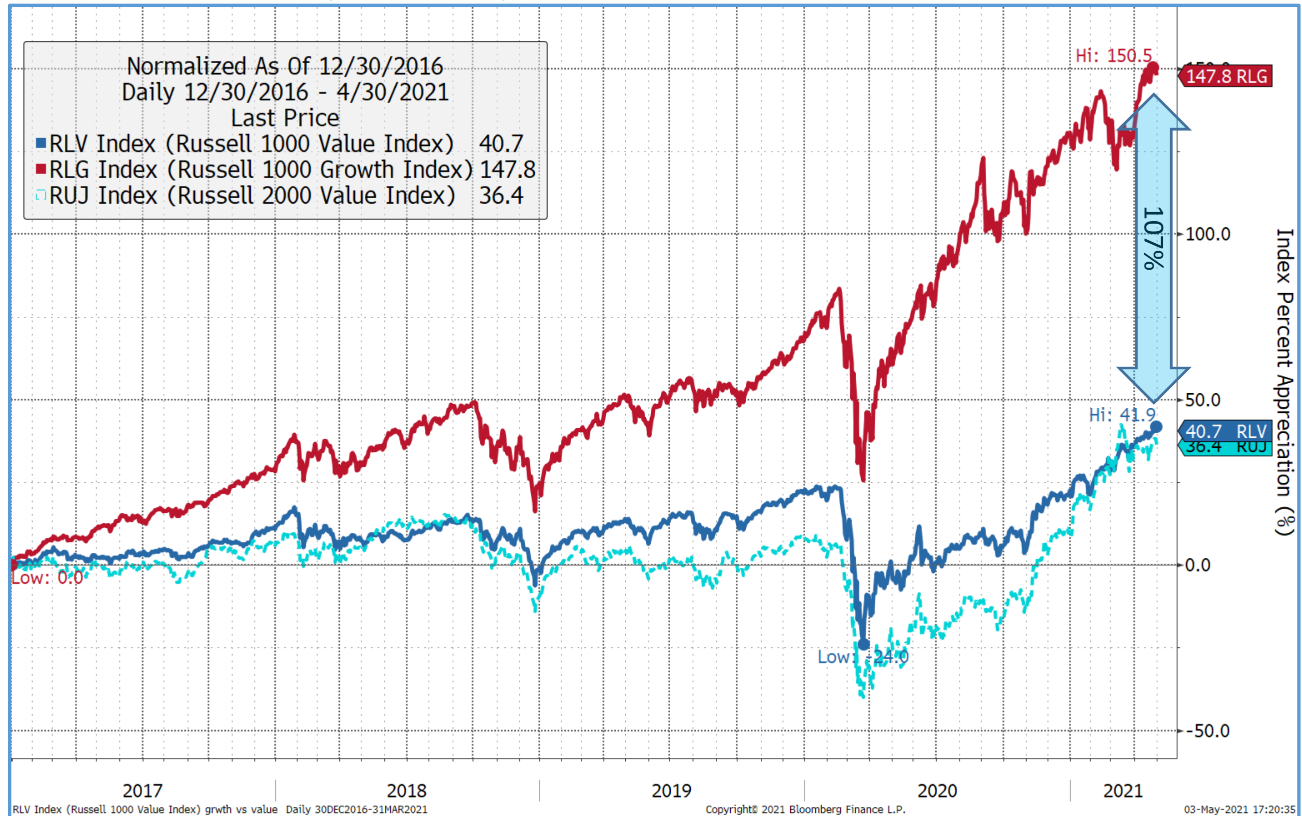
In prior commentaries over the past year, we have written extensively about the growth-versus-value bubble that has been rapidly inflating over the prior four (4) years but was turbo-charged by the COVID-19 Pandemic. We believe that markets are in a similar position as to where they were in mid-2000, except this time the bubble is more pervasive in nature encompassing most growth stocks – as opposed to simply internet-based technology and communication stocks during the technology stock bubble.

Nevertheless, a significant difference between now and 2000 is that the current macroeconomic backdrop is very different – we are now coming out of a very deep recession with interest rates historically low at both the short and long ends of the curve and with incredibly large and on-going fiscal support from the developed

country governments of the world. While US growth stocks are in general more expensive now than in early 2000 on virtually every valuation measure, US growth stocks are *not* more expensive than they were in early 2000 *relative to* current bond yields. Equity, in general, appears more reasonable on a relative basis to fixed income yields (i.e., bond markets are substantially more overvalued than equity markets, even the US equity market).

While many "believe" that value has been significantly outperforming growth recently, **Figure 2** below demonstrates that this "belief" is, so far, incorrect – value has recently been attempting to keep-up with growth in a strongly advancing market, but no more. In fact, Figure 2 shows that the four (4) year large-cap value-to-growth spread is actually just as wide now at 107% as it has been for the last 6 to 10 months. Both the value and growth indexes have advanced nicely over the past several quarters; but, despite a couple of instances where value did appear to be breaking out relative to growth, value has through April 30th just kept up with growth the past several quarters. Nevertheless, relative to the past four (4) years, value "just keeping up" with growth is a significant accomplishment and, as shown below, may indicate that a significant bottom may have been put in place with respect to the value-versus-growth spread.

Figure 2: Relative Performance of the Russell 1000 Growth Index, Russell 1000 Value Index and Russell 2000 Value Index – January 1, 2017, to April 30, 2021.



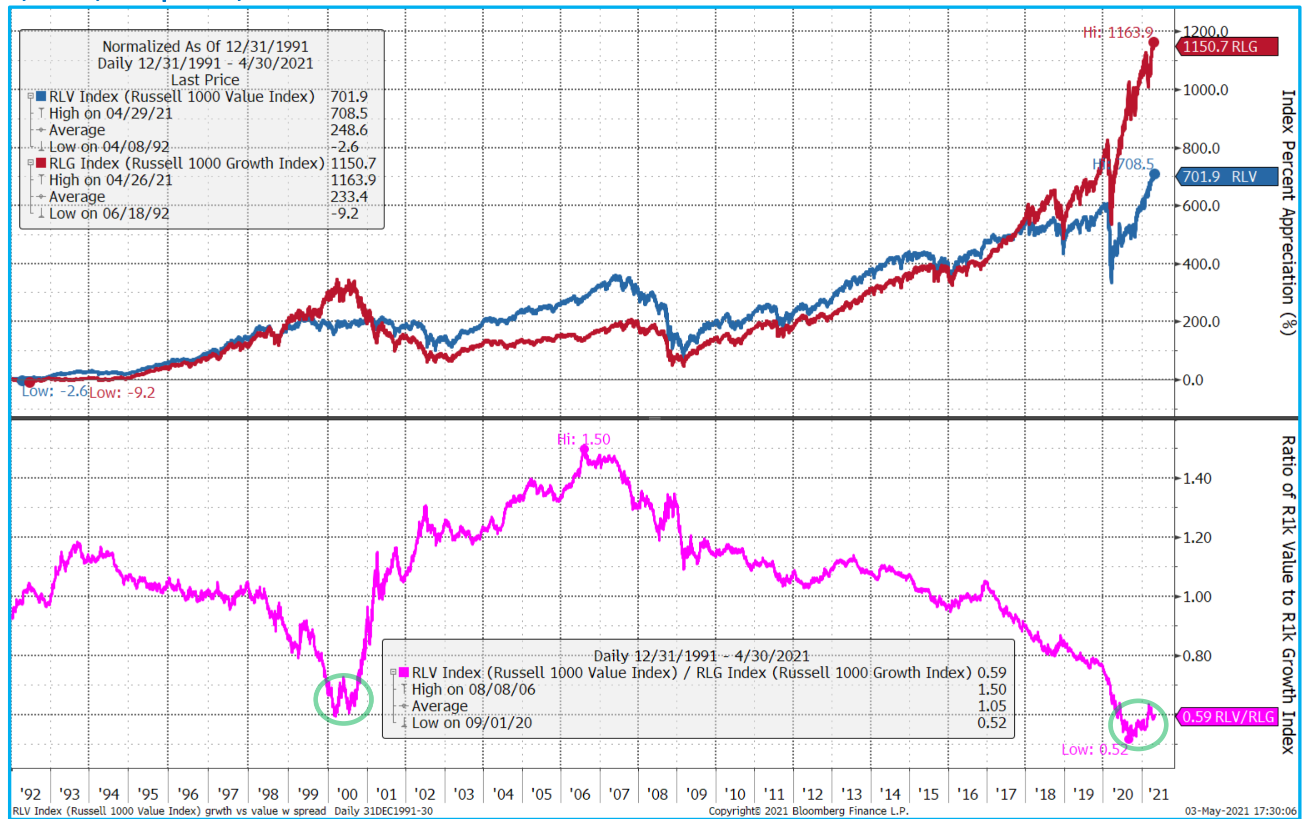
For longer-term context, **Figure 3** plots the Russell 1000 Value Index relative to the Russell 1000 Growth Index from January 31, 1990, through April 30, 2021, to intentionally include the technology stock bubble of the late-1990's. The bottom half of Figure 3 shows the *ratio* of the Russell 1000 Value Index price level to the Russell 1000 Growth Index price level (the purple line). The average of the value-to-growth price index ratio over the entire 31-year period of time is 1.06 (i.e., the Value Index was on average slightly higher than Growth Index), with the value-to-growth index ratio drifting around this average level for the majority of the past 31-

years. However, it is easy to observe the two (2) extreme Growth Index outperformance periods (and one (1) extreme Value Index outperformance period).

The first extreme Growth Index outperformance period was the technology stock bubble of the late-1990's whereby the Growth Index massively outperformed the Value Index from early 1998 through March of 2000. During this period, we saw the value-to-growth index ratio compress from roughly average at the beginning of 1998 to a low of 0.594 in the middle of March 2000. That is, the price of the Value Index was trading at only 59.4% of the price of the Growth Index. Amazingly, over the next 12-months almost all of the Growth Index outperformance resulting from the late-1990's technology stock bubble was unwound with the value-to-growth index ratio returning to its long-term average by mid-March of 2001.

The second, and most extreme, Growth Index outperformance period is the current growth stock bubble. From January 2017, the value-to-growth index ratio went from approximately its long-term average to a new all-time low of 0.517 on September 1st, 2020 – well below its prior all-time low of 0.594 at the peak of the late-1990's technology stock bubble. This current period of value underperformance, using almost all definitions, is now the largest and the longest in recorded US stock market history (~150 years).

Figure 3: Relative Index Level of the Russell 1000 Value Index Versus Russell 1000 Growth Index – January 1, 1991, to April 30, 2021.



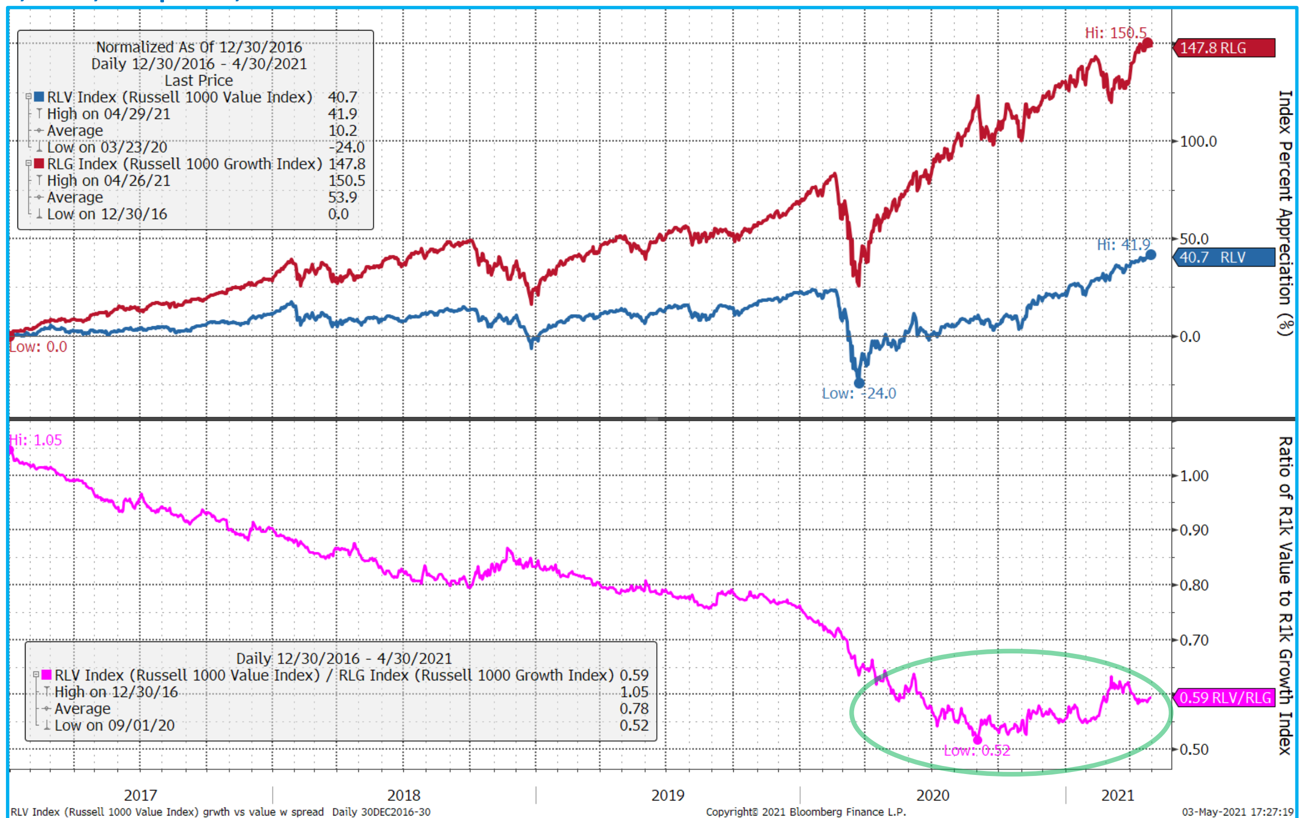
The bottom half of Figure 3 also shows that the value-to-growth index ratio may have finally bottomed, beginning with its low on September 1st, 2020. Indeed, the last eight (8) months of the value-to-growth index ratio graph (bottom half of figure 3) is looking similar to the bottoming process in the value-to-growth index ratio that took place in mid-2000. As in 2000, it may take six (6) to nine (9) months for a true bottom

to be formed before a potentially substantial and sustained move upwards in the value-to-growth index ratio. We do believe that we could be at that point – potentially beginning the "the great rotation."

It is important to note, however, that the value-to-growth index ratio could normalized with the Value Index being relatively flat while the Growth Index falls – similar to what happened following the technology stock bubble – or normalize with the Value Index going up substantially while the Growth Index remains flat or only moderately up. To unwind the growth-versus-value stock bubble only requires that the Value Index significantly outperforms the Growth Index going forward, regardless of the direction of the overall market (note, however, that the US stock indexes are now dominated by super-mega-cap growth stocks).

Figure 4 zooms back in again at the prior four (4) years. Here we see again what appears to be a bottoming process – however, the past couple of months has seen a sharp rebound in growth relative to value stocks emanating from the FANMAG stocks (Facebook, Amazon, Netflix, Microsoft, Apple and Google). **While bottoming may be evident, the beginning of a significant reversal is not yet clear.**

Figure 4: Relative Index Level of the Russell 1000 Value Index Versus Russell 1000 Growth Index – January 1, 2017, to April 30, 2021.



As a reminder, the above is all highly relevant to the *relative performance* of the GoDI Fund because, as a consequence of our process to simultaneously *maximize* dividend yield, dividend growth and dividend safety, the GoDI portfolio generally has a significant value style bias – as well as, of course, a significant dividend yield exposure. For example, we have shown in prior commentaries that the GoDI Fund possesses approximately 3x more Dividend Yield style exposure *and* 3x more Value style exposure of the Russell 1000 *Value* Index. **The GoDI Fund may therefore be one of the few high Active Share investment products available in Canada that is well positioned to capitalize on any such global growth-to-value rotation**.

Nevertheless, always remember our primary message: **"Growing income", as opposed to "fixed income", is the only means of maintaining the purchasing power of your (or your client's) income stream over the years and decades to come**.

If you would like more information regarding the **AlphaDelta Growth of Dividend Income Class** and its current portfolio (including the up-to-date presentation piece), please feel free to contact me directly or alternatively contact AlphaDelta Management Corp. (www.AlphaDelta.com).

Thank you for your continued interest in the Fund,

John J. Schmitz

John J. Schmitz, Ph.D., CFA