

UBS ETF *Market Matters*

Dividend Harvesting Indexed Strategy

- Dividend indices follow strict rules in order to safeguard exposure to higher-than-average yielding dividend stocks (e.g. Dow Jones Global Select Dividend).
- Such a dividend-focused strategy weights selected stocks according to their dividend yields, i.e. *higher yielders receive a higher allocation*, with the intention of harvesting dividends.
- Country/industry rebalancing demonstrates that such indexed, rules-based strategies lead to a dynamic search for dividend deliverers from around the globe, and provide a two-fold higher dividend yield than the aggregate market.

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Dividend-focused strategies attempt to buy high-quality, dividend-paying companies at competitive prices. Such a strategy can be also *indexed*, i.e. placed into a rules-based framework which creates an (investible) index holding the best stocks in view of pre-defined dividend-related eligibility criteria. The selection criteria vary across strategies but typically include some of the following: dividend yield, dividend growth, dividend-to-earnings ratio, pay-out ratio, other fundamental data, and stock liquidity needed for replicability. Price and return performance of the index can be replicated in institutional and retail portfolios with the use of investible vehicles, like Exchange Traded Funds (ETFs). This *Market Matters* discusses one of such dividend harvesting indexed strategies – the Dow Jones Global Select Dividend Index (DJGSD).

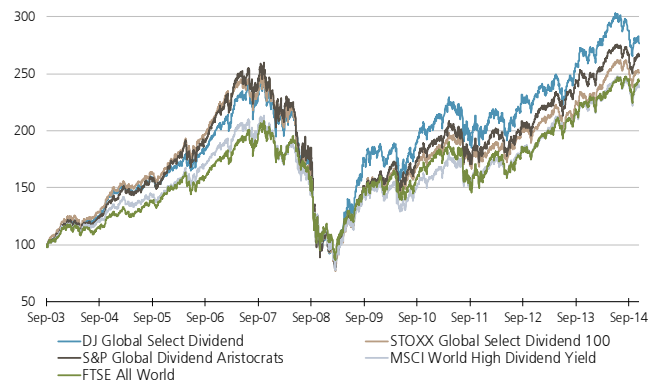
Dividend Benchmarks

Figure 1 shows historical performance of four dividend indices (data includes live and back-tested data) and the aggregate market FTSE All World dating back to 2003. All four dividend strategies have outperformed the broad market. There is substantial presence of *beta* in these dividend strategies as they highly correlate (approx. 90-98%) to the aggregate market. The presence of *beta* is not unexpected, as dividend indexed strategies usually harvest dividends from the top 100 yielding companies in the given universe. Given that total return from an equity investment combines capital appreciation with shareholder income (surplus cash paid in dividend or through stock buyback), the excess return attributes to the higher-than-market-average shareholder yield. For example, the current dividend yield of the DJGSD (5.3%) is more than two-fold higher than the FTSE All World (2.4%). And the long-run dividend yield differential of the DJGSD vs. aggregate is approx. 200bps. Given that the yield is reinvested into the strategy (total return net index after taxes), the relative historical outperformance of the DJGSD vs. the aggregate corresponds largely to the compounded yield differential as shown in **Figure 2**.

Selecting Dividend Leaders

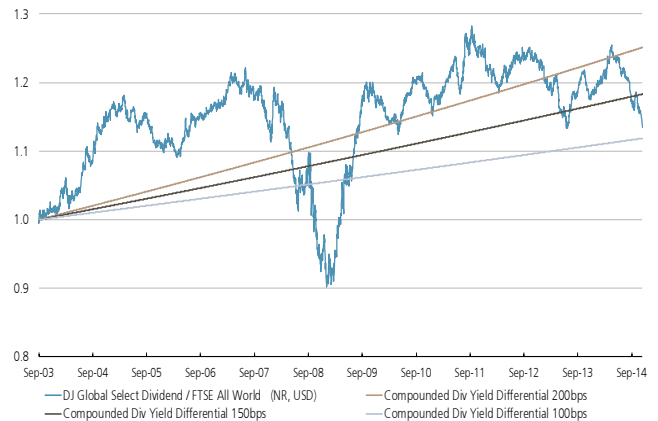
The Dow Jones Global Select Dividend Total Return Index measures the price and yield performance of global (developed markets) dividend-paying companies selected for fundamental strength relative to peers, and subject to dividend quality screens. The companies are selected from the parent aggregate universe (Dow Jones Global Index) which represents

Figure 1: Dividend Benchmarks (Net Returns, USD)



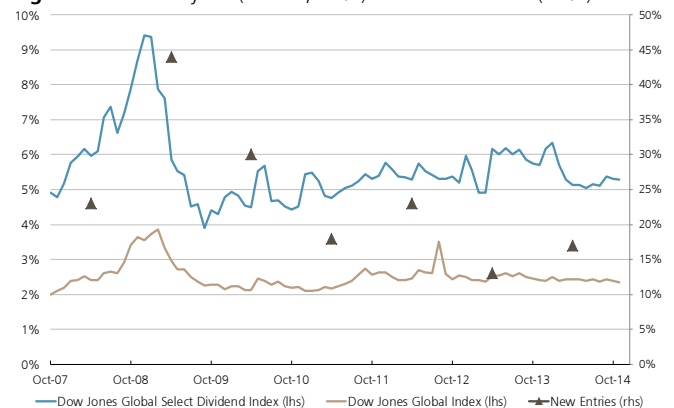
Source: Morningstar, UBS Global AM, as of 28 November 2014

Figure 2: Relative Performance and Compounded Dividend Yield Differential



Source: Morningstar, UBS Global AM, as of 28 November 2014. For illustrative purposes only.

Figure 3: Dividend yield (in USD, in %) and new entries* (in %)



Source: S&P Dow Jones, UBS Global AM, as of 28 November 2014.

*New entries statistic measures proportion of newly added stocks compared to the previous year DJGSD index revision. For illustrative purposes only.

For all charts/tables: Past performance is not a reliable indicator for the future.

approx. 95% of the global developed market and holds currently approx. 7200 securities. This *indexed* strategy defines rules for the portfolio construction, which is subject to annual revisions. In particular, a selected company must:

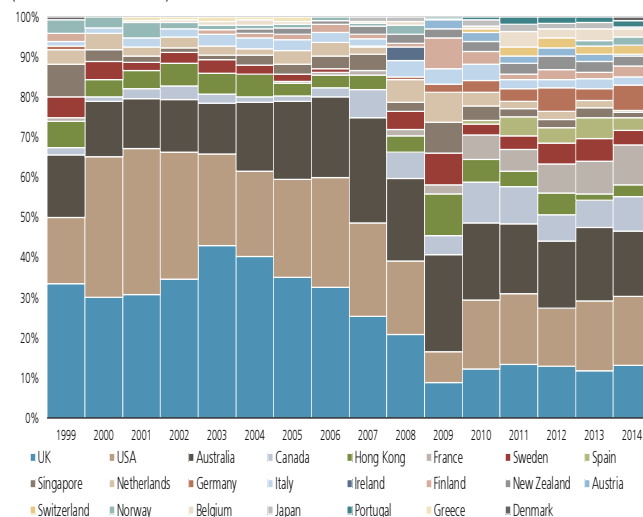
- be a dividend yielder
- be a dividend grower (last dividend-per-share ratio higher than the 5 year average)
- retain portion of earnings (dividend pay-out ratio capped to 80%, or 60% for US stocks) to ensure future business growth
- be profitable (non-negative 12month earnings-per-share)
- be liquid (for replicability)

The top 100 stocks which pass the dividend quality screens are weighted by indicated dividend yield, i.e. higher yielders receive a higher allocation (Source: *Dow Jones Dividend Indices Methodology*, November 2014). This approach intends to safeguard exposure to global, high quality, sustainable, higher-than-average yielding dividend stocks. **Figure 3** presents the monthly dividend yield (since the index was launched live in October 2007) against the Dow Jones Global aggregate, showing a realised yield differential of approx. 200-300bps in normal market conditions. **Figure 3** shows also (right-hand scale) the year-on-year proportion of newly selected companies, highlighting a higher turnover following more volatile periods, 2008-2009 or 2011.

Hunting for Yield

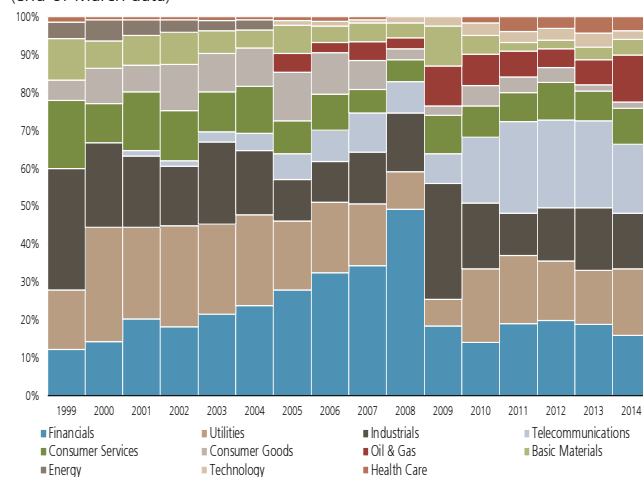
The allocation to stocks behind the DJGSD strategy is reviewed annually (every March), implying that exposure shifts are likely, reliant on year-on-year global dividend discrepancies. The re-allocations occur among countries and industries. **Figure 4** shows a country breakdown and **Figure 5** shows an industry breakdown, respectively (incl. all back-tested data available). Prior to the financial crisis, there was a substantial dominance of the UK, USA and Australia, with their share reaching 70-80%. In contrast, the country allocation - post the financial crisis - appears more diverse and balanced. In the same way, there was a weighty and increasing allocation to the financial industry, reaching approx. 50% just prior to the financial crisis in 2008. In more recent years, an increased presence of more defensive stocks (telecommunication services or utilities) is apparent, also confirmed in the top ten holdings (**Table 1**). The country/industry rebalancing demonstrates that this indexed, rules-based strategy leads to a dynamic search for dividend opportunities from around the globe. **Table 2** shows the details of the UBS ETF physically replicating the DJGSD dividend benchmark.

Figure 4: DJGSD: country allocation
(end-of-March data)



Source: S&P Dow Jones, UBS Global AM, as of November 2014

Figure 5: DJGSD: industry allocation
(end-of-March data)



Source: S&P Dow Jones, UBS Global AM, as of November 2014

For all charts/tables: Past performance is not a reliable indicator for the future.

Table 1: Dow Jones Global Select Dividend Index – Top Ten Components

Company	Country	ISIN/Ticker	Industry	Weight	Dividend Yield 12-month
ProSiebenSat.1 Media AG	Germany	DE000PSM7770	Consumer Services	2.6%	4.3%
Belgacom SA	Belgium	BE0003810273	Telecommunications	2.4%	6.8%
Orange	France	FR0000133308	Telecommunications	2.0%	4.8%
Spark New Zealand Ltd	New Zealand	NZTELE000154	Telecommunications	2.0%	7.9%
PCCW Ltd.	Hong Kong	HK0008011667	Telecommunications	1.6%	3.7%
GDF Suez	France	FR0010208488	Utilities	1.6%	5.8%
CenturyLink Inc	United States	US1567001060	Telecommunications	1.5%	5.0%
Pepco Holdings Inc	United States	US7132911022	Utilities	1.5%	3.7%
K&S AG	Germany	DE000KSAG888	Basic Materials	1.4%	1.0%
Zurich Financial Services AG	Switzerland	CH0011075394	Financials	1.4%	5.5%

Source: S&P Dow Jones, Bloomberg, UBS Global AM, as of 5 December 2014

Table 2: UBS ETF Dow Jones Global Select Dividend – UBUM GY

Fund Name (Benchmark)	Base					Incept. date	Exchange					
	TER	AuM	Ccy.	Replication	Domicile		ISIN	Bloomberg	SIX	Xetra	Borsa Italiana	LSE
UBS ETF (IE) DJ Global Select Dividend UCITS ETF (Dow Jones Global Select Dividend Total Return Index)	0.30%	13	USD	Physical	Ireland	04.09.2014	IE00BMP3HG27	UBUM GY	CHFUSD	EUR	EUR	GBP

AuM in USDmn, as of November 2014

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