TD Global Investment Solutions

Spotlight 10 Minutes
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A Conversation With

Kera Van Valen, CFA
Managing Director,
Portfolio Manager and
Senior Research Analyst,
TD Epoch

Michael Jin, CFA
Managing Director,
Portfolio Manager and
Senior Research Analyst,
TD Epoch

Dividend Focused Strategies in Uncertain Times

What is driving current market uncertainty?

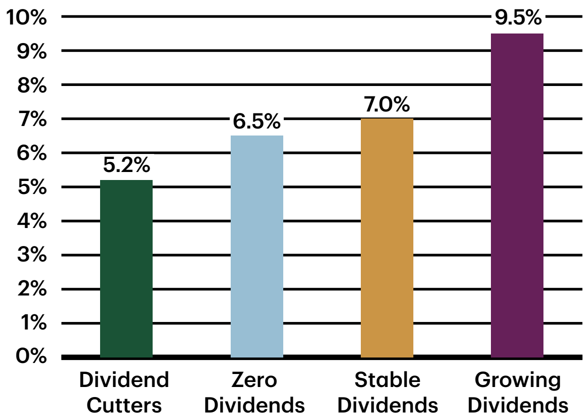
Equities have endured dynamic and often unpredictable market conditions recently, navigating a landscape defined by tariff uncertainties, volatile interest rates, inflation expectations and geopolitical shocks. Longer term structural shifts taking place, such as deglobalization and the realignment of supply chains, add further complexity to the environment. Sentiment remains fragile as investors grapple with lingering macro dislocations, and uncertainty defines the path forward. In this context, many investors are re-evaluating how best to maintain equity exposure while managing risk more deliberately.

What is the role of a dividend-focused investment strategy in the current environment?

We believe that a dividend-focused equity strategy is ideally suited to the goal of maintaining equity exposure while mitigating risk. Dividend payers tend towards steadier returns, less speculative valuations, and heightened resilience through challenging and uncertain market environments. Companies that consistently pay dividends, and especially those that grow their dividends, are empirically proven to possess lower volatility than those who do not. Representing the most historically stable and reliable component of equity returns, dividends offer a cushion to declines and add a degree of predictability to returns. Furthermore, companies that pay and grow their dividends over long periods often naturally exhibit other desirable attributes that denote durability: business maturity and strong market positions, excellent balance sheet health, and disciplined management teams. In addition, dividend payers, especially dividend growers have outperformed companies that don't pay dividends or have cut their dividends over the long term.

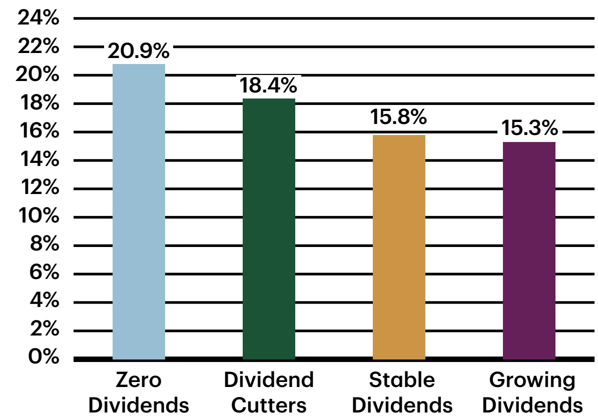
Annual Compound Returns: MSCI World

(May 1994 – March 2025)



Annual Standard Deviation: MSCI World

(May 1994 – March 2025)



Source: Ned Davis Research. Start period based on earliest available data.

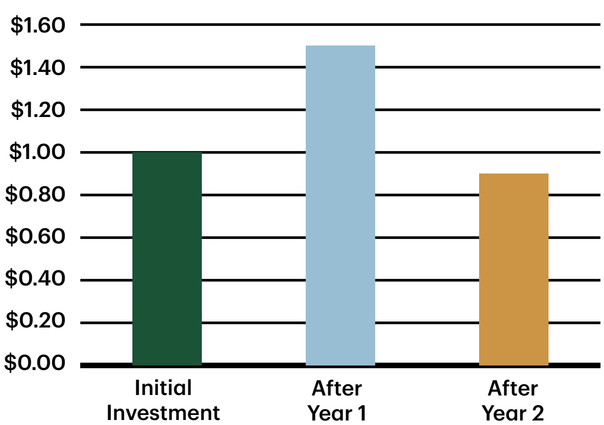
Based on equally weighted compound total returns of dividend and non-dividend paying MSCI World stocks. Each of the four portfolios were reconstituted at the beginning of each year based on the actual dividends paid over the previous year. Reporting Currency: USD

Why is lower volatility and smaller drawdowns beneficial to a portfolio?

Looking beyond present uncertainty, maintaining lower volatility in an equity allocation can lead to a smoother return profile and enhance wealth creation in the long term. Market losses are asymmetric in nature and compound exponentially; the larger the loss, the more gain is needed to break even. For example, a portfolio with a 10% drawdown would need an 11% return to get back to even, while one with a 50% drawdown would require a 100% return. Over multiple time periods, consistently higher volatility can have a destructive impact on value, even if the portfolio has higher returns in up periods. To illustrate, a portfolio with a 50% return in one year would actually lose 10% of its value if its year 2 return was -40%, while a portfolio with a much more modest 20% return in year 1 would have a gain of 8% if its year 2 return was -10%. If two portfolios have the same average annual return, the one with lower volatility will always annualize at a higher rate.

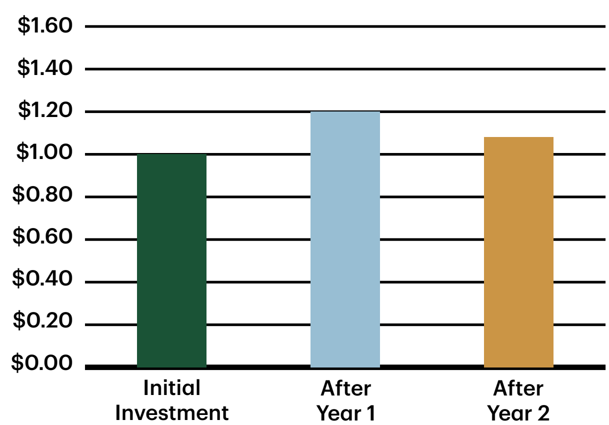
Strategy A

Year 1: 50% Return
Year 2: -40% Return



Strategy B

Year 1: 20% Return
Year 2: -10% Return



Both investments have the same average annual return of 5%

How do interest rates impact a dividend-focused investment strategy?

The Federal Reserve began cutting interest rates in 2024, going from 5.5% in August to 4.5% in December. Since December, however, interest rates have held steady. That said, more cuts are likely on the horizon. As of June 18, 2025, the Fed is projected to cut rates to between 3.5% and 3.75% by the end of 2026. Fixed income yields tend to move in conjunction with interest rates, so their yields fall as interest rates fall. Dividend strategies can be attractive in a falling rate environment as investors look to replace the income they may be losing in their fixed income allocations. This is particularly true of those strategies that have offered a consistent level of dividend yield such as our Shareholder Yield strategies. In addition, falling rates could positively impact price appreciation on dividend paying stocks as they become more popular. That is not to say the dividend strategies are unattractive in rising rate environments. Often, when interest rates are rising, it is because there is sustainable growth in the economy which is a favorable macroeconomic environment for companies. It should imply rising revenues, rising earnings and rising cash flows. This is particularly important to our Shareholder Yield strategies which are focused on identifying companies that have the ability to generate growing cash flow.

How does inflation affect dividend paying companies?

While inflation has been trending downward so far this year, based on the U.S. CPI and CPI ex-food & energy, there are some concerns that it could begin to trend up again, particularly in the face of new tariffs when they are implemented and not absorbed by the exporting countries and/or importing entities. Dividend paying companies can often be a hedge to inflation, as long as their dividends are growing at a rate higher than the rate of inflation. Strategies that focus on companies that grow their dividends, like our Shareholder Yield strategies, are typically in a better position because the dividend can grow while inflation is growing as well. The market has also proven that inflationary periods favor companies that pay a consistent dividend or grow their dividends. In three distinct periods where inflation was meaningfully higher than historical averages (1973-1981, 1987-1990 and 2007), dividend payers and dividend growers in the S&P 500 outperformed those that didn't pay or cut their dividends and the index as a whole. In the fourth period (2021-2022) dividend payers and dividend growers outperformed those that did not pay a dividend and the index as a whole (strangely enough, dividend cutters outperformed all other categories and the index in that period).[1]

How might tariffs impact dividend strategies?

The largest impact of tariffs might be the uncertainty it causes since, in many instances, it is not entirely clear what the final tariffs will be. As already mentioned, dividend stocks can be an ideal portfolio fit in times of uncertainty. There are some concerns that companies could cut dividends to make up for revenue lost to tariffs. While that may be the case for some dividend paying companies, we generally focus on quality companies with strong market positions, pricing power, and experienced management teams that are good stewards of capital allocation. These companies tend to have strong free cash flow coverage of their dividends and are less likely to put their dividends at risk. In addition, some of these companies are global champions with geographic diversity in their sources of revenue, so they are better positioned to ameliorate or offset the negatives from tariff. Finally, some of the domestically focused sectors that traditionally consist of more dividend paying companies, like Utilities, Telecommunications and Health Care are predicted to be less impacted by tariffs.

What is your approach to managing your portfolios in light of the uncertainty?

Our approach to building and managing the portfolios has not changed. We seek to build diversified portfolios of companies that generate free cash flow and allocate that capital to the three components of Shareholder Yield – cash dividends, share buybacks and debt reduction. We are looking for quality companies with strong management teams that are good capital allocators. We have risk management integrated within the investment process, with a portfolio construction framework designed to help diversify the sources of shareholder yield and minimize volatility. We believe our portfolios are poised to capture the productivity of a growing economy while remaining defensively positioned for resiliency should growth begin to falter.

[1] Source: TD Epoch, Ned Davis Research

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