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EXECUTIVE SUMMARY

Equity markets have suffered significant turbulence in recent years. In the aftermath of the Eurozone crisis, Europe remains fragmented as economic growth languished. 2014 has seen the glimmer of reversal of these trends as the UK economy returned to growth and M&A markets heated up. Throughout this period of volatile earnings, dividends have remained a key channel of shareholder remuneration and emerged as one of the major investment themes. Bloomberg’s dedicated Dividend Forecasting Team leverages the full power of the Bloomberg Terminal to accurately forecast dividend schedules and amounts for up to four years.

In the following report, we use our dividend forecasts as well as Bloomberg’s comprehensive data and analytical tools to examine the latest developments and trends.

– Bloomberg Dividend Forecasting Team, September 2014

DIVIDEND YIELDS BY SECTOR

The analysis of 2014 dividend yields by sector reveals that Telecoms, at 4.74%, followed closely by Insurance and Utilities at 4.57% and 4.37% respectively, has the highest projected 12 month dividend yield among STOXX600 industries. The lowest yielding industries are projected to be Healthcare, Technology and Food and Beverage, at 2.10%, 2.27% and 2.36%, respectively.

The comparison of the trailing 12 month dividend yield to 12 month BDVD projected dividend yield indicates that 12 out of 19 sectors are forecasted to increase their dividends during next year. Noticeably, the projected dividend yield for Banks may increase from 3.11% to 3.55%; Automobiles from 2.44% to 2.89%; and Constructions and Materials from 2.94% to 3.43%. Seven industries are projected to lower their dividend payments. Among them, Telecoms may decrease from 5.07% to 4.74% and Utilities from 4.62% to 4.37%.

DIVIDEND PAYOUT RATIO

Dividend payout ratio is one of the key indicators of a company’s ability to maintain its dividend as it represents the amount of earnings paid back through dividends. A continuously rising payout ratio cannot be sustained in the long term unless the company is able to boost earnings. If this is not the case, the dividends may eventually be cut. Recent trends in Europe showed a spike in the ratio. Taking the Euro STOXX 50 Index of the 50 largest and most liquid European stocks as a proxy of the overall European market, a hike in the payout ratio from 51% to 54% can be observed for the most recent financial year. As seen in Chart 2, the projected payout ratio (using BDVD forecasted dividends for the next three years over consensus earnings estimates) is expected to return to the previous levels of around 50% by 2016.
DIVIDENDS VS SHARE BUYBACKS

Modest economic growth has contributed to a decline in dividend growth in Europe. The total cash amount returned to shareholders increased by just over 6% to EUR362.8bn last year, compared to 18% increase the previous year. Even though dividend payments were still the preferred way of shareholder remuneration within the STOXX Europe 600 Index (Chart 3), the year-on-year increase in share buybacks was notable.

The cash amount spent on share repurchases increased by 12.7% since last year, with the Oil & Gas, Insurance and Real Estate sectors showing the highest increases. The significant rise in share buybacks versus the increase spent on dividends could be explained by the fact that companies stick to rather conservative dividend policies and are reluctant to change payouts. Stock buybacks tend to be a more flexible option for companies to return cash to shareholders. Budget constraints and lower CAPEX could suggest more buyback programmes to come.

SECTOR ANALYSIS

Banks

The analysis of dividends in the European Banking sector present a mixed picture, which reflects the significant disparity between the economic conditions of different countries following the most recent Eurozone crisis. Chart 4 shows a breakdown of trailing 12m and projected dividend yields as well as Core Tier 1 capital ratios by country of domicile.

Scandinavian banks forge ahead in terms of trailing 12m dividend yield, with Swedbank leading at 6.4%. This trend looks to continue as capital buffers for Scandinavian banks swell amidst rising profits and cost cutting. In terms of projected dividend yield, Santander leads at 8.3% though it is worth noting that these dividends are scrip. Italian banks rank amongst the lowest in yields at an average of 1.42% and this is not expected to rise significantly due to the local concentration of their loans base and the sluggish recovery of the Italian economy. Banks in Portugal, Italy and Greece (PIG) remain constrained by debt covenants and as a result have not paid out dividends in recent years. BDVD does not expect them to resume payments in the next 12 months. Across the board, regulatory requirements have ensured that banks have concentrated on building up their capital buffers. Chart 4 indicates the positive correlation between capital ratios and the dividend yield. Sweden ranks top at an average of 17.93%, while Italy and Austria are ranked bottom. Italy’s Banco Popolare SC has the highest capital ratio (21.20%), but has not paid dividends since 2011 as loan loss provisions climbed and earnings declined.

Several factors present challenges to sustained dividend growth in coming years. The results of the ECB stress tests are expected in the latter half of this year and may impose additional capital requirements on banks. The settlement of high profile litigation cases such as the $2.6bn and $8.9 billion settlements for Credit Suisse and BNP Paribas respectively, indicate significant headwinds for profitability for the industry. Finally, low European GDP growth expectations (1.63% for 2014, as surveyed by Bloomberg) may contribute to stagnant loan growth and the risk of deflation, potentially putting further restraints on dividend capacities.

Telecoms

Telecommunication sector has been constrained by regulations as the need for more consolidation has been seen throughout the year. Hutchinson’s Three has acquired Orange Austria, Numericable is merging with SFR, Telefonica is set to buy KPN’s German unit, and Hutchison 3G was cleared by EU Commission to acquire Telefonica Ireland. This situation appears to have impacted dividend payments as some of the biggest firms, like Orange and Belgacom, cut their dividends. Even though Telecoms is the highest dividend paying sector with a 12 month trailing yield of 5.07%, the spread between estimated dividend yields and Stoxx 600 companies has narrowed to 1.4% in May 2014; whereas this reached 4.5% in June 2012.

DIVIDEND FORECASTS
Companies are counting on the development of high speed 4G and fibre networks as the European market recovers. Chart 5 shows that capital expenditures in the sector have been increasing continuously since 2009. Simultaneously, dividend payments, as indicated by dividend index points, have gone up in a similar fashion to CAPEX until 2011. The following years, 2012 and 2013, were marked by a sudden drop in dividend return. The companies appear to have been saving on current shareholders return (dividends) and investing in future growth (capital expenditures) instead.

Retail
As European markets attempted to recover from the crisis, severe market conditions resulted in the implementation of austerity measures and subsequent slow wage growth. This situation made consumers actively seek lower prices and therefore price cutting became the main strategy among retailers. Online shopping remains a key theme as retailers look for growth in Internet sales and simultaneously enticing customers with venues that can provide a complete shopping experience.

Retail companies’ sales depend on GDP growth and the real income of consumers. Chart 6 reveals that retailers have not cut dividend payments in recent years despite falling real GDP growth. Economic forecasts show that European GDP growth may rebound from the crisis in upcoming years, which may have a positive impact on companies’ willingness to share their profits with shareholders.

Large Pharmaceuticals
2013 was a challenging year for Large Pharma. The infamous “Patent Cliff” meant the expiration of key patents, leading to the erosion of net profits by generic competitors. Austerity measures in Europe and slowing growth in the Emerging Markets pharma also contributed to strong headwinds for the industry. Nevertheless, dividends remain a strong channel for returning cash. Chart 7 shows the breakdown in trailing and projected dividend yields for the Stoxx 600 Healthcare Index. While average yields across the other subsectors lie below 2%, large pharmaceuticals continue to lead with average trailing yield of 2.62%. Our forecasts expect the average yield in this sub-sector to rise to 2.76% in the next 12 months.

For 2014, the rebound in economic growth and emergence from the patent cliff has proven to be a turning point, as evidenced by a rapid recovery in earnings and a resurgence of positive investor sentiment. PE ratios recovered from a low point of 12x in June 2010 to 24x in June 2014. The return to growth has led to a period of strategic review and an unprecedented level of M&A in the sector, with 3 of the top 5 deals in the Pharmaceutical Industry to date involving Large Pharma companies in the EU, according to data collected by Bloomberg. The most notable of these was the proposed acquisition of UK-based Astrazeneca by U.S.-based Pfizer, which would have created the world’s largest pharmaceutical company. Chart 8 shows that the total deal volume in 2014Q2 rose to 223.42bn with an average premium of 25.62%.

While the spike in cash being diverted into M&A activity may act as temporary limitation on dividend growth, the strategic realignment of product portfolios is expected to yield significant synergies. We expect to see the industry to continue to provide shareholders with returns via dividends and expect further upward pressure on dividend yields in coming years.
In order for you to maximize the uses and benefits of Bloomberg Dividend Forecasts, Bloomberg has created the BDVS <GO> function for the specific purpose of providing help and transparency on our BDVD <GO> dividend forecasts. In addition, BDVS <GO> provides additional resources to assist in your dividend-related investment decisions.

BLOOMBERG FORECAST ACCURACY
» View our historical accuracy to see how we have been consistently more accurate than street analysts at forecasting dividends.

FORECASTING METHODOLOGY
» Learn more about the BDVD methodology and factors that Bloomberg analysts use to forecast dividends.

ANALYSTS & COVERAGE
» See each Bloomberg analyst’s market sector and regional coverage.

OPTIONS VALUATION & IMPLIED RANGE
» Find out more about our Options Implied Dividend Range model which displays on the BDVD <GO> function for individual equities and ETF’s.

MERGER ARBITRAGE
» Because future dividends affect merger arbitrage pricing, we provide a risk-arbitrage spread calculator, enabling you to more accurately determine transaction prices.

DIVIDEND PORTFOLIO MAP
» Download this excel-based tool to visualize your portfolio’s estimated future dividends and see in which months and from which companies you might see dividend income.

FREQUENTLY ASKED QUESTIONS
» Others may have the same questions as you. Find answers to your questions here to help clear any misconceptions or concerns you may have.

EQUITY INDICES & ETFS
» Learn more about how forecasts are made for Indices and ETF’s and how to understand and use the functions most efficiently.

DIVIDEND REPORTS
» We provide dividend forecast reports on a regular basis. To subscribe, visit this page. In addition, you can read BDVD-related articles recently published in Bloomberg Markets magazine.

BDVD IN EXCEL
» Each BDVD data field can be downloaded easily into Excel. Learn more about how this is done, and download a template for single-data point and bulk data downloads.
Bloomberg analysts forecast dividends for over 7500 securities globally, including equities and ETFs, as well as dividends for indices. Seven factors are used, which incorporate all pertinent information about a company and its dividend. This enables analysts to reach a subjective decision about the dividend amounts and direction for the next three years. BDVS promotes transparency across the product, allowing Bloomberg users to better understand our accuracy and forecasting methodology.
To find out more about Bloomberg Dividend Forecasting, email bdvd@bloomberg.net or call your regional representative.