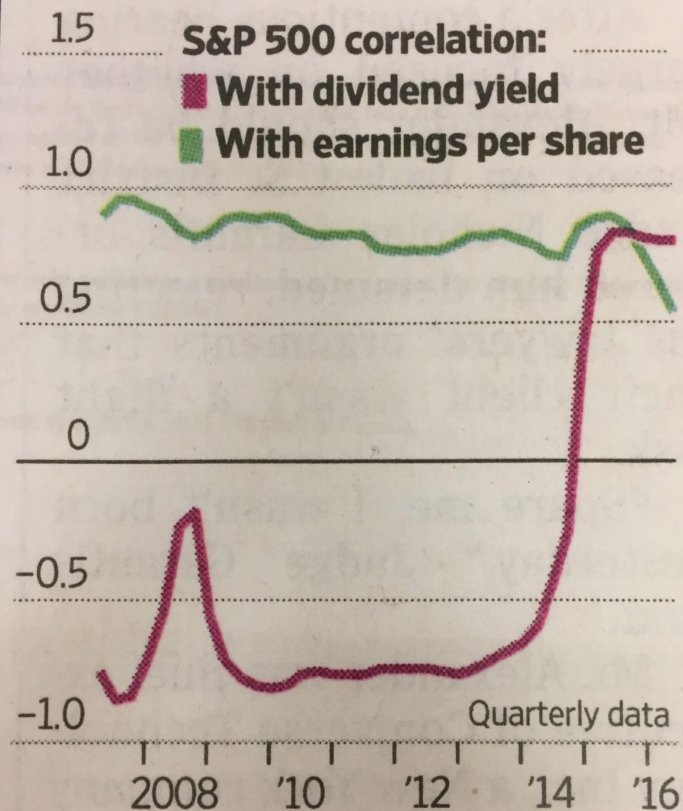


QF-101B Project #2

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Derek Ma



Note: Data are five-year rolling correlations.
EPS and dividends are measured for the 12
months through each quarter.

Source: S&P Global Market Intelligence

Dividend Yield

- Ratio that indicates how much a company pays out in dividends each year relative to its share price
- $$\text{Dividend Yield} = \frac{\text{Dividends per Share}}{\text{Price per Share}}$$
- Way to measure how much cash flow you are getting for each dollar invested in an equity position
- High yield could be risky



Earnings per Share

- The portion of a company's profit allocated to each outstanding share of stock
- Serves as an indicator of a company's profitability
- $$\text{Earnings per Share} = \frac{\text{Net Income} - \text{Dividends on Preferred Stock}}{\text{Shares Outstanding}}$$



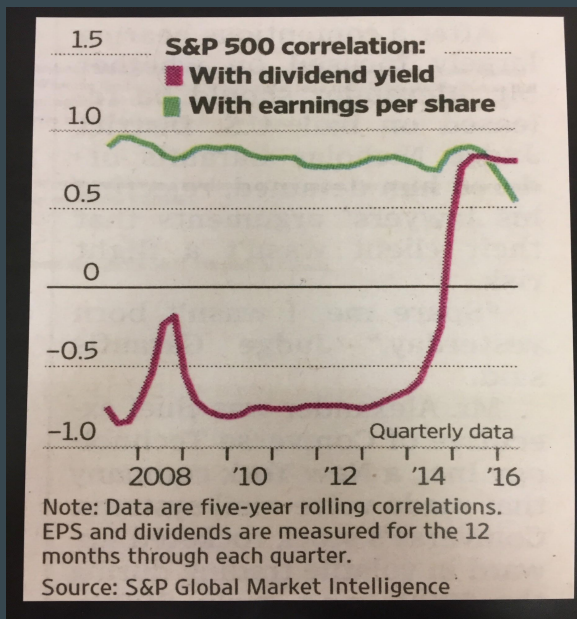
Correlation

- Tracks the relationship between two variables
- Correlation of 1: They move together
- Correlation of -1: They move exactly opposite each other
- Correlation of 0: Only a random connection



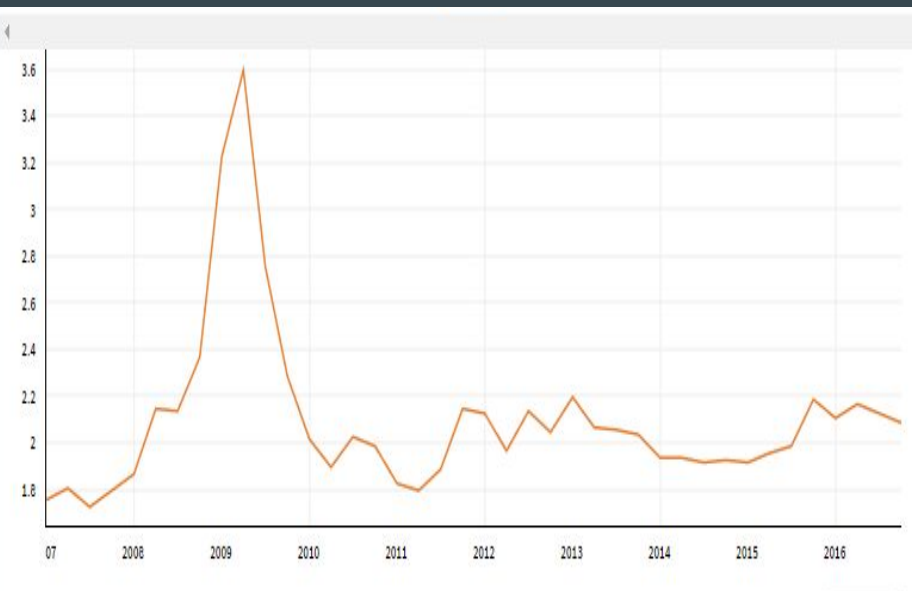
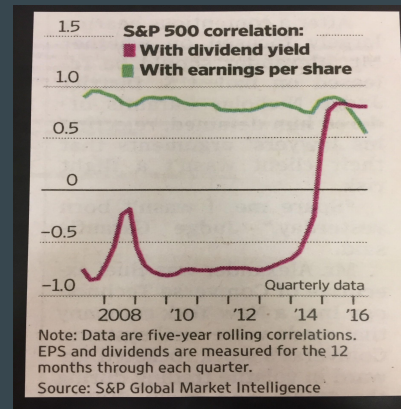
Correlation with Earnings per Share

- Orange - Earnings per Share
- Blue - S&P 500



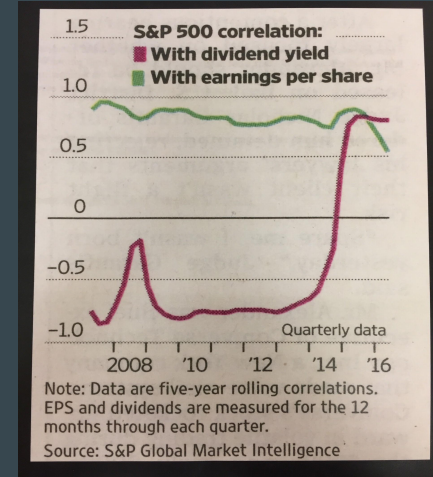
Correlation with Dividend Yield

- Orange - Dividend Yield
- Blue - S&P 500



What the Graph Shows

- Tracks correlation of S&P 500 price versus:
 - Dividend yield
 - Earnings per share
- A traditionally strong EPS correlation has declined
- A traditionally very weak dividend yield correlation has spiked dramatically
- Dividend yield now more strongly correlated with stock price
- Stock returns being driven by dividend yield, instead of earnings



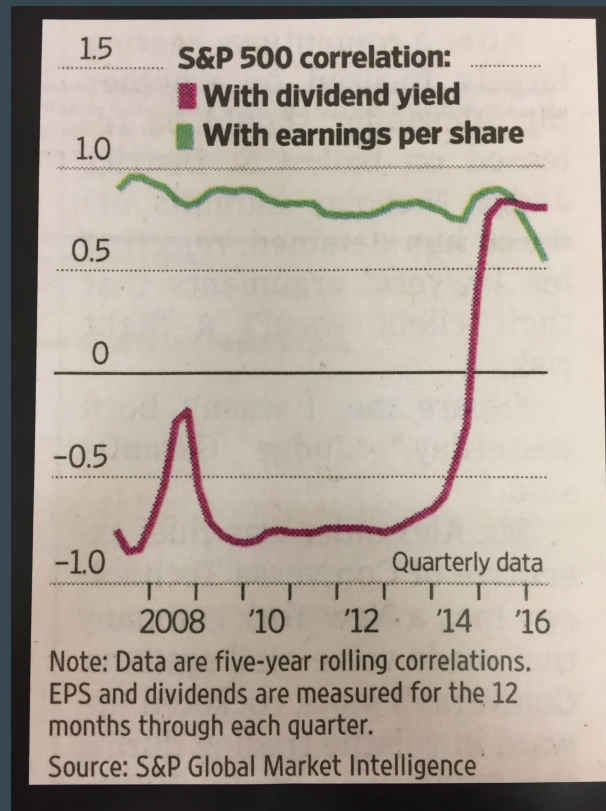
Exxon Mobil Corp. Example

- Strong example of the shifting trend
- Over last year, per share
 - Earnings fell to \$2.52 from \$5.62
 - Dividend payouts rose to \$2.94 from \$2.80
 - Price has gained 13%
- Is this sustainable?



Why? And Problems...

- Possible response to low interest rates
 - Dividends being used to hedge slumping fixed income payouts
- Less confidence in stock prices
- Catch-22
 - Stock can't perform well without strong dividends
 - Earnings have become increasingly hard to improve
 - Dividends increasing while earnings decline
 - Sustainability
- What will happen with the looming interest rate hike?
 - Will the trend reverse itself?



Thank you.