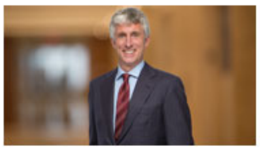
AGF FUND INSIGHT

AGF | Investments

March 2024

Dividends, Growth stocks, Japan and the ECB



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Dividends offer a compelling investment opportunity in 2024

We believe dividends may provide a compelling investment opportunity for investors this year for several key factors that underscore their appeal.

- High dividend yields typically lead during periods of economic recovery and global upturns. Whether we experience a soft landing or a mild recession, we believe a robust expansion in economic activity could follow and higher dividends ahead.
- If inflation is stickier than the market expects, which is our base case scenario, the U.S. Federal Reserve Board (Fed) will likely need to maintain higher policy rates to stem persistent inflation. It's important to recall the resilience of dividends, which has provided solid downside protection against inflation and mitigated the significant equity losses during the rate hike cycle in 2022.
- There are trillions of dollars sitting in cash within retiree accounts, and a shift toward equity income becomes increasingly likely, especially if short-term interest rates decline.
- A substantial portion of S&P 500 stocks are projected to offer higher dividend yields than cash, making them attractive for income-seeking investors. This scenario highlights the immediate income generation potential of dividends and their role in capital appreciation over time.

While the above highlights our positive view on dividend payers this year, our investment process focuses equally on dividend growth. We want to own companies with strong management teams that have a history of solid capital allocation decisions. For example, we focus extensively on companies that reinvest in their business and return capital to their shareholders, preferably through a consistent and growing dividend.

History suggests that Growth stocks may be challenged this year

Last year, Growth stocks significantly outperformed Value stocks by a wide margin. The Russell 1000 Growth Index returned 42.7%, leaving the Russell 1000 Value Index's 11.4% return in the dust—an enormous difference of 31.3%. This surge was powered by the stellar performance of the "Magnificent 7" — Apple, Alphabet, Tesla, Microsoft, NVIDIA, Amazon, and Meta Platforms — who together drove nearly two-thirds of last year's performance, in the S&P 500 Index, which returned 26.3%.

This year, however, there is a solid case for a shift away from Growth stocks. History has shown that after standout years where Growth stocks have outperformed Value stocks by 25% or more (last year was 31.3% as discussed above), Value stocks tend to outperform Growth stocks in the subsequent 3-, 6-, and 12-month periods. If this scenario unfolds, we believe this sets the stage for AGF Global Dividend Fund and AGF Global Equity Class to potentially outperform their benchmark, the MSCI All Country World Index. Remember, our investment style is not

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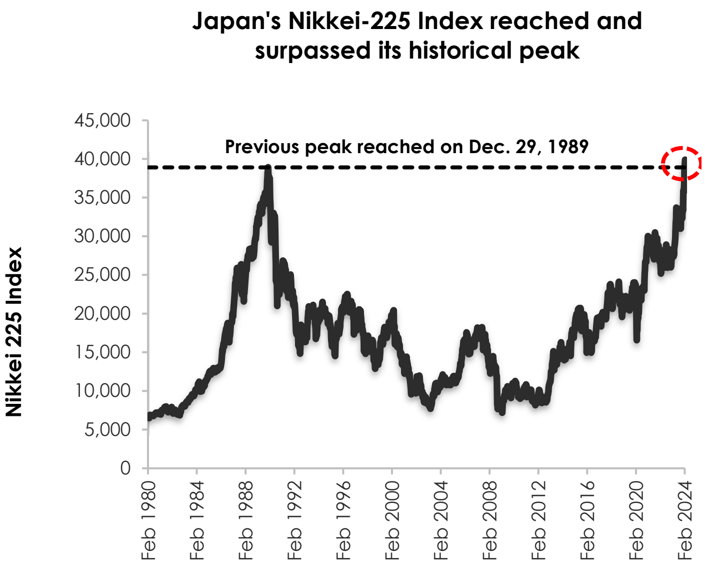
Value– it is Core, having exposure to both Value and Growth stocks. However, our Value *bias* relative to our benchmark could provide a tailwind should Value stocks outperform Growth stocks.

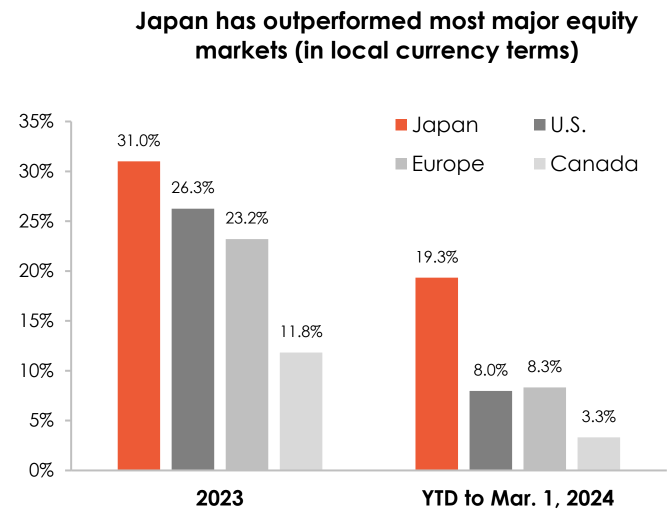
Subsequent outperformance of Russell Value vs Russell Growth following 25%+ Growth vs Value outperformance	Next 3 months	Next 6 months	Next 12 months
Russell 1000 Value Index – Russell 1000 Growth Index	3.9%	10.4%	16.5%
Hit rate (% of time Value outperformed Growth)	63%	79%	74%

Source: BofA U.S. Equity & Quant Strategy, Bloomberg, February 16, 2024. Data from December 29, 1978 to February 16, 2024. One cannot invest directly in an index. **Past performance is not indicative of future results.**

We continue to favour Japan

On February 22, 2024, Japan's Nikkei-225 Index reached and surpassed a historical peak, marking its highest point since December 29, 1989. This significant achievement reflects Japan's growing attractiveness to global investors, seeking opportunities for diversification, capital growth, and increasingly competitive dividend yields. Japanese equities have demonstrated remarkable resilience in achieving this milestone even as the nation grapples with a technical recession characterized by two consecutive quarters of negative GDP growth. Despite the significant differential between economic growth in Japan and the U.S. and the solid absolute performance of U.S. equities last year, Japanese equities outperformed U.S. equities (in local currency terms). Japan has continued outperforming most major global equity markets this year, prompting some investors to ponder the sustainability of such outperformance.





Sources for both charts: Bloomberg, March 1, 2024. Right chart shows total returns. Japan is represented by the Nikkei 225 Index, U.S. is represented by the S&P 500 Index, Europe is represented by the Euro Stoxx 50 Index, and Canada is represented by the S&P/TSX Composite Index. One cannot invest directly into an index. **Past performance is not indicative of future returns.**

We believe Japan's recent outperformance will continue as it reflects deep-rooted, structural transformations within the market. These changes are propelled by a combination of strategic initiatives to overcome decades-long deflation through increased corporate capital spending and comprehensive reforms in corporate governance. These foundational shifts are redefining Japan's investment landscape, enhancing its appeal to global investors.

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A pivotal element in this transformation has been the Tokyo Stock Exchange's (TSE) reform initiative, launched in March 2023. This reform has catalyzed the stock market rally throughout 2023, underscoring a strategic realignment towards management practices that prioritize the cost of capital and stock valuation. The widespread market outperformance can be attributed to a market-wide endorsement of these reforms, which are seen as integral to Japan's departure from deflation and the normalization of interest rates by the Bank of Japan. Despite potential shifts from NIRP (negative interest rate policy) to ZIRP (zero interest rate policy), the expectation of persistently real negative interest rates provides a supportive environment for Japan's continued economic expansion.

Since 2014, corporate governance reforms under the banner of Abenomics have laid the groundwork for the TSE's efforts, ushering in significant enhancements in corporate governance and return on equity (RoE). Notable milestones include the introduction of Japan's Stewardship Code, a corporate governance code, and the publication of the Ito Review. These reforms have led to a marked decrease in banks' cross-shareholdings, a significant rise in the proportion of external board directors, and an increase in female board representation, driven by the Abe administration's Womenomics policies.

Building on these achievements, the TSE's "second chapter" of reforms introduced novel price-to-book (P/B) value reforms and a framework for companies to disclose actions relating to the cost of capital and share price. The TSE's commitment to regularly update these disclosures and best practices demonstrates a continuous drive towards enhancing corporate transparency and accountability.

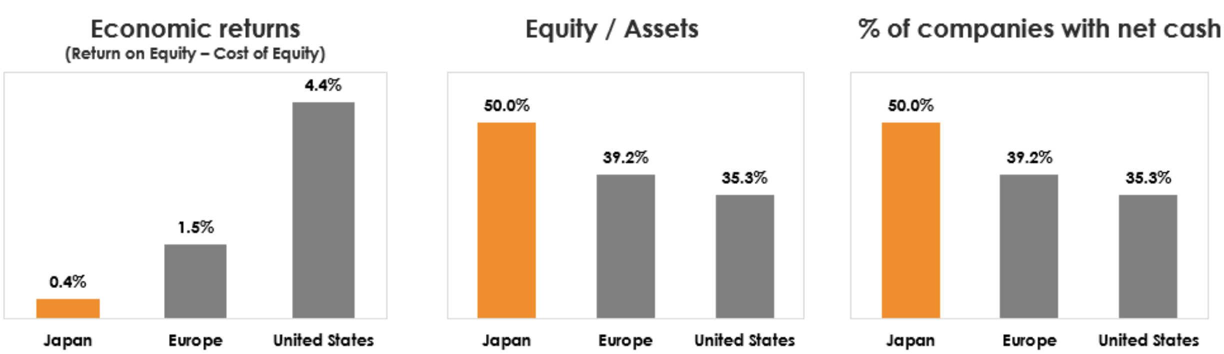
The aftermath of these reforms has witnessed a surge in corporate activities, including record-high share buybacks and dividends, alongside increased investments in growth and mergers and acquisitions (M&A). This uptick in corporate initiatives underscores the growing significance of corporate governance in the eyes of companies and market participants alike, contributing to the market's revitalization and a more vibrant corporate ecosystem.

Interestingly, the effectiveness of TSE reforms has been achieved without mandatory compliance requirements for companies. Instead, a combination of peer pressure, decisive corporate actions once a direction is established, enhanced market engagement capabilities since the introduction of Abenomics, and the growing influence of activist investors have driven reform adoption. The record number of shareholder proposals by activist investors in 2023 further highlights the evolving dynamics within Japan's corporate governance landscape.

These reforms signify a strategic pivot towards more transparent, accountable, and growth-focused corporate management practices, laying what we believe to be a solid foundation for sustained market growth and bolstering investor confidence in the Japanese equity market.

Additionally, the Japanese government's introduction of the tax-exempt Nippon Individual Savings Account (NISA) program in January 2024 has catalyzed record equity inflows from domestic investors, serving as another catalyst for the potential long-term appreciation of Japanese equities.

Significant long-term potential for Japanese equity performance



Source: J.P.Morgan, Bloomberg. Left and centre charts: The median is calculated based on the latest actual Return on Equity (ROE), Bloomberg estimated Cost of Equity (COE), total equity and total assets of the constituents TOPIX 500 Index, S&P 500 Index, and EURO STOXX 600 Index as of January 15, 2024. Right chart: Calculated based on the net cash status of the constituents TOPIX 500 Index, S&P 500 Index, and EURO STOXX 600 Index as of January 15, 2024. One cannot invest directly in an index. **Past performance is not indicative of future results.**

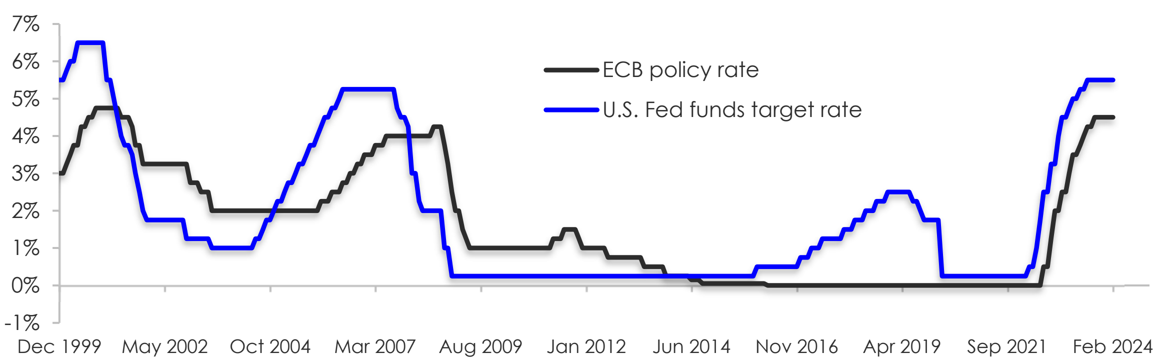
Over the next decade, improvements in operational efficiency, scale, financial stability, competitiveness, growth, balance sheet optimization and shareholder returns are expected. The comprehensive suite of reforms and initiatives underscores a compelling narrative for investment in Japan, potentially offering global investors sustainable long-term growth and diversification benefits. Potential risks to the outlook include Japan failing to exit deflation or companies largely fail to improve their efficiency and competitiveness and balance sheets remain flush with cash.

Weaker growth and inflation in Europe than in the U.S. – Will the ECB cut policy rates before the Fed?

A thought-provoking narrative has emerged, centred around the European Central Bank (ECB) and its potential move to preempt the Federal Reserve in cutting policy rates. As the U.S. economy continues to pleasantly surprise to the upside, Europe is beating to a different rhythm, characterized by stagnation and disinflationary pressures. This contrasting scenario has sparked a narrative among investors of the possibility of the ECB cutting policy rates before the U.S. Fed.

However, from a historical standpoint, the ECB and the Fed have followed a choreographed sequence, with the ECB never stepping ahead in the easing cycle since its inception a quarter-century ago. The ECB has consistently trailed behind the Fed from the early 2000s through the crescendo of the global financial crisis and into the recent rate hiking cycle. Yet, the current economic environment paints a scenario where the ECB could, theoretically, break from tradition and pioneer the path forward in rate adjustments.

The Fed has always cut policy rates before the ECB



Source: Bloomberg, February 29, 2024.

The intrigue lies in historical patterns and the practical repercussions of such a strategic divergence. Should the ECB initiate a rate cut before the Fed, we could witness the euro's (€) depreciation, fostering an inflationary uptick through more costly imports. However, a weaker euro would likely increase competitive advantages for European exporters. This scenario, with its complex interplay of disinflation and industrial challenges, seems like a potential path that the eurozone might well navigate.

Another layer of complexity arguing against the ECB moving before the Fed is in the context of the ECB's commitment to its price stability mandate. Despite the allure of stimulating economic activity through a weaker euro, particularly to bolster economies like Germany facing industrial and growth headwinds, the ECB remains squarely focused on its inflation mandate. This prudence is echoed in the hawkish tones of ECB policymakers, underscoring a resolve to tread the battle against inflation.

As the narrative unfolds, the ECB's decision-making will pivot on a delicate balance of risks—weighing inflationary concerns against deflation risks. Emerging signs suggest a potential shift in the ECB's stance, with some council members advocating for timely action against the risk of delayed rate cuts. This evolving perspective and forthcoming adjustments to inflation forecasts and labour cost dynamics could pave the way for an unprecedented ECB move ahead of the Fed, potentially by mid-year.

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AGF Global Dividend Fund – annualized returns as of February 29, 2024

CAD, net of fee returns, %	3 mths	YTD	1 Yr	3 Yrs	5 Yrs	10 Yrs	15 Yrs	PSD*
AGF Global Dividend Fund – Series F	8.6	6.3	15.8	9.9	8.9	8.8	10.8	8.0
AGF Global Dividend Fund – Series MF	8.3	6.1	14.5	8.6	7.6	7.5	9.6	6.7
Morningstar Global Equity Category	9.8	7.0	19.0	7.0	9.1	8.2	10.4	
Quartile Ranking – Series F	3	3	3	1	3	2	2	-
Quartile Ranking – Series MF	3	3	3	2	3	3	3	-
Total number of funds in the Global Equity Category	2,030	2,030	1,903	1,602	1,436	708	373	-

Source: AGF Investments Inc. as of February 29, 2024. **Performance Start Date: August 22, 2007. "Global Equity Category" as per Morningstar. Morningstar Quartile Rankings are calculated as of February 29, 2024, and subject to change monthly. The rankings are calculated from a fund's total return percentile rank against others in its applicable Morningstar category for the 1-month, 3-month, 1-, 3-, 5-, 10-, and 15-year periods. Percentile ranks always range from 1 (best) to 100 (worst), with all intermediate values spread evenly over that range. For greater detail see http://www.morningstar.ca. One cannot invest directly in an index. **Past performance is not indicative of future results.** MERs: Series MF: 2.38%, Series F: 1.21%, as of September 30, 2023.

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