Third Quarter 2018

The Copeland Review

"We believe that stocks with sustainable dividend growth consistently outperform the market with less risk."

Ten Years Gone

Then as it was, then again it will be
And though the course may change sometimes
Rivers always reach the sea

"Ten Years Gone," Led Zeppelin 1975

At some point in their lives, most have likely had the frustrating experience of trying to encourage a friend or family member to make a positive life change, only to be met with a half-hearted commitment that both parties know is unlikely to go anywhere. Indeed, if everyone actually heeded such advice, America would soon be a nation full of exercise fanatics who enjoyed eight hours sleep and flossed their teeth daily. Instead, we're constantly tired, only 30% of us acknowledge daily flossing, and even fewer get the recommended amount of exercise.[1]

Of course, we use many explanations (some might say excuses) to justify our unwillingness or inability to change. One common reason is an "If it ain't broke, don't fix it," attitude. After all, if a close friend is currently enjoying good health, despite the sedentary lifestyle of the average American office worker, it's sure to be hard to convince him that he should train for an upcoming 5-K race – even if, in the long-term, you both know the benefits of doing so.

Most investors would likely benefit from making some changes as well, but for the same reasons, they are often slow to do so. For example, one year ago, in "The Winding Road," we explored the potential virtues of expanding one's investing horizon to include international markets, noting that investing globally, as opposed to just domestically, provided investors with diversification benefits through:

- Expanding their universe of opportunities
- Providing exposure to varied capital market conditions; and
- Correlations across countries and regions < 1

It is with these attributes in mind that we launched our international all cap, small cap and global Dividend Growth portfolios in recent years. We believe the successful the performance track-records of these strategies, as well as those of our domestic offerings, have been substantially aided by our dividend growth discipline, as shown on page 3.

Still, according to Forbes, US investors hold only 15% of their stock portfolios in foreign companies. This level is well short of even the generalized 20% foreign stock allocation commonly recommended by large mutual fund companies. To put these percentages in even more stark perspective though, consider that the collective market cap of non-US equities is currently 60% of the global total, while foreign countries generate approximately 75% of global GDP.[2,3,4,5]

Though there may be legitimate justification for keeping one's foreign stock allocation below those higher levels, such as structural difficulties in participating in certain markets, the statistics nevertheless highlight the significant investment opportunities outside of the US, to which many investors are not commensurately exposed. Still, since the end of the financial crisis, the "If it ain't broke, don't fix it" justification has been especially in vogue among domestically biased investors as they have enjoyed substantially better returns from such positioning than they would have seen if their international allocations had been higher.

We highlighted this advantage in "The Winding Road," noting that while the S&P 500 Index had broken well above its pre-crisis highs, ten years later the MSCI EAFE Index remained modestly, albeit stubbornly, below those levels. For investors with significant allocations to the EAFE markets (Europe, Australasia and Far East), ten years gone, indeed…

This year is no exception to that recent experience. With a global trade war in full swing, investors who were previously cautious about international markets appear to be even more skittish now. No doubt there are some legitimate question marks arising from this activity, whether they stem from our relations with China or fall closer to home where the Administration has been trying to rework NAFTA. As a result, it is probably not surprising that the performance gap between the domestic and international stock indices has only widened. The S&P 500 Index cruised to new highs as of quarter end, while the MSCI EAFE Index failed to crack pre-crisis levels yet again (Chart 1).[6] This on-going advantage in favor of US stocks has likely done little to dissuade many investors from their apparent view that modest, if any, exposure to international equities is the best policy.

By our reckoning, this view is too broad in scope however. If we divide domestic and international stocks into buckets according to their respective dividend policies, and look back over the last ten years, we see that the total return results over that period are quite different (Chart 2 on next page).

Despite the performance results of the domestic benchmark far exceeding those of its international counterpart, the performance of Dividend Growth stocks has been comparable regardless of geography. Domestic Dividend Growers have posted a 12.8% annualized re-

Chart 1—U.S. vs. International Equity Returns (Indexed)

turn and international Dividend Growers have posted a 12.0% annualized return over the ten years ended September 30, 2018. In fact, as recently as February 2018, international Dividend Growth stocks had outperformed domestic Dividend Growth stocks since the beginning of that period. [7]

Even more striking, consider an investor who had constructed a global Dividend Growth portfolio 75% invested in domestic Dividend Growers and 25% invested in international Dividend Growers on September 30, 2008. By executing a consistent rebalancing strategy whenever the portfolio's domestic/international balance moved more than two percent out of line with its original 75/25 positioning, this investor would have posted a 12.7% annualized return – nearly identical to the 12.8% return experienced by an investor who had allocated 100% to domestic Dividend Growers. However, the globally diversified investor would have achieved that result with less risk as measured by comparing the standard deviation statistics for the two hypothetical portfolios – 15.9% for the global portfolio v. 16.0% for the domestic only portfolio.[8] Further, the annualized performance of the 75/25 Dividend Growth portfolio would have bested a comparable blended benchmark by more than 230 basis points.[9]

In our view, these observations offer critical answers to a common pair of questions that we hear from investment advisors (and their clients) and institutional investors, respectively. From investment advisors, the common refrain is that they are looking for the right time to allocate internationally. For institutional investors, who typically have a targeted long-term allocation to international equities, how do they remain committed to that target (or even increase their allocations) when the US market has been outperforming for so long? We would argue that the results noted above demonstrate that for investors who exclusively pursue a Dividend Growth approach to international investing, the right time is, "always" and the right amount is likely far higher than they believe.

For investors who still aren't convinced of the potential opportunities in global markets however, we would also point out the favorable valuation gap between international and domestic stocks. One year ago, we noted that the trailing 12-month price to earnings ratio of the MSCI EAFE Index was 18.8x versus 20.1x for the S&P 500 Index, a -7% discount – relatively consistent with historical levels. Since then, US companies have posted very strong earnings, supported by tax reform and continued economic growth. Although this has put downward pressure on domestic valuations, the international valuations have fallen further, and the discount has ballooned to -21%. [10]

We understand that even after considering the preceding commentary, investors who have been reticent to increase their exposure to global markets might still have trepidation. Company names and tickers are often not as well-known as their domestic peers, financial reports are not necessarily consistent with those in the US and, of course, there is no shortage of headlines to fuel concern – whether one reads about Britain's difficulty in executing Brexit, Italy's recent political turmoil or the economic slowdown in China.

Nevertheless, we believe that global diversification is an important part of most properly constructed portfolios. Though predicting the precise end of the "lost decade" for international markets is difficult, just as "rivers always reach the sea," eventually they are likely to have their day in the sun, outperforming the US indices and recovering some or all of their current valuation discount. With those expectations in mind, we believe that marrying Copeland's domestic and international dividend growth strategies significantly enhances one's odds of generating risk-adjusted returns above those of a blended benchmark, whether current global performance trends persist or reverse.

October 2018

[1] *https://www.usnews.com/news/articles/2016-05-02/how-many-americans-floss-their-teeth, https://www.cbsnews.com/news/cdc-80-percent-of-american-adults-dont-get-recommended-exercise/*

[2] *https://news.gallup.com/poll/166553/less-recommended-amount-sleep.aspx*

[3] *https://www.forbes.com/sites/simonmoore/2018/08/05/how-most-investors-get-their-international-stock-exposure-wrong/#7b5dac6a6aac*

[4] *https://www.vanguard.com/pdf/flgiecr.pdf*

[5] *https://seekingalpha.com/article/4202768-u-s-percent-world-stock-market-cap-tops-40-percent*

[5] *https://en.wikipedia.org/wiki/List_of_countries_by_GDP_%28nominal%29#cite_note-0*

[6] *FactSet*

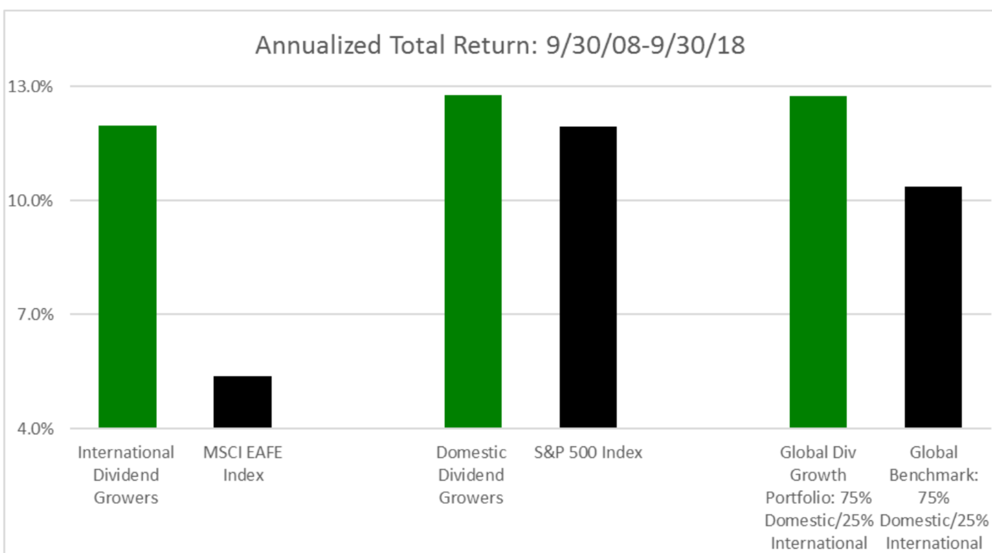
[7] *Ned Davis Research*

[8] *Ned Davis Research, CCM*

[9] *MSCI, S&P*

[10] *FactSet*

Chart 2—Returns of Domestic, international & Global Dividend Growers vs. Benchmarked



Source: NDR, MSCI and Standards & Poors
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Discipline Has Paid Dividends

Returns of Copeland Strategies as of September 30, 2018

	YTD % Return (Gross)	One Year % Return (Gross)	Three Years Annualized % Return (Gross)	Five Years Annualized % Return (Gross)	Since Inception Annualized % Return (Gross)	Inception Date
Copeland Large Cap Dividend Growth	13.07	21.49	15.98	11.98	**9.22**	1/1/2006
S&P 500 TR USD	10.56	17.91	17.31	13.95	9.15	
Copeland Mid Cap Dividend Growth	11.24	19.70	17.00	10.52	**13.07**	1/1/2011
Russell Mid Cap TR USD	7.46	13.98	14.52	11.65	12.50	
Copeland Smid Cap Dividend Growth	10.71	16.77	17.41	12.62	**12.62**	10/1/2013
Russell 2500 TR USD	10.41	16.19	16.13	11.37	11.37	
Copeland Small Cap Dividend Growth	11.81	16.83	18.12	14.92	**16.41**	10/1/2009
Russell 2000 TR USD	11.51	15.24	17.12	11.07	13.68	
Copeland Micro Cap Dividend Growth	12.72	13.71	17.55		**14.42**	2/1/2015
Russell Micro Cap TR USD	11.64	13.65	16.41		11.79	
Copeland Global All Cap Dividend Growth	9.26				**9.26**	12/31/2017
MSCI World NR USD	5.43				5.43	
Copeland Global Small Cap Dividend Growth	8.34	13.48			**18.50**	2/1/2017
MSCI World Small Cap NR USD	4.71	10.18			14.63	
Copeland International All Cap Dividend Growth	3.08	7.24	6.96		**6.34**	1/1/2014
MSCI World ex USA NR USD	-1.50	2.67	9.32		3.29	
Copeland International Small Cap Diversified Dividend Growth	2.95	9.46			**20.09**	1/1/2017
MSCI World Ex USA Small Cap NR USD	-2.28	3.42			15.18	

Currency: US Dollar

The data presented herein represents past performance. Past performance is no guarantee of future results. Please see the Disclosures section for additional information.

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The S&P 500® Index consists of 500 stocks chosen for market size, liquidity and industry group representation. It is a market value weighted index with each stock's weight in the Index proportionate to its market value.

The Russell Mid Cap® Index is comprised of the 800 smallest companies in the Russell 1000® Index.

The Russell 1000® Index measures the performance of the 1000 large cap U.S. companies based on total market capitalization, which represents approximately 90% of the investable U.S. equity market.

The Russell 2500® Index is comprised of the bottom 2500 companies in the Russell 3000® Index.

The Russell 2000® Index is comprised of the smallest 2000 companies in the Russell 3000® Index.

The Russell 3000® Index measures the performance of the 3000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market. The Russell 3000® Index measures the performance of the 3000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

The Russell Microcap® Index measures the performance of the microcap segment of the U.S. equity market. It makes up less than 3% of the U.S. equity market. It includes 1,000 of the smallest securities in the Russell 2000® Index based on a combination of their market cap and current index membership and it includes the next 1,000 stocks.

The MSCI World® Index is a market cap weighted stock market index of 1,653 stocks from companies throughout the world.

The MSCI World Small Cap® Index captures small cap representation across 23 Developed Markets (DM) countries. With 4,320 constituents, the index covers approximately 14% of the free float-adjusted market capitalization in each country.

The MSCI World Ex-US® Index is a market capitalization-weighted index designed to provide a broad measure of stock performance throughout the developed world, excluding U.S. stocks.

The MSCI World Ex-US Small Cap® Index captures small cap representation across 22 of 23 Developed Markets (DM) countries (excluding the United States). With 2,437 constituents, the index covers approximately 14% of the free float-adjusted market capitalization in each country.

About Copeland Capital Management — Copeland Capital Management is an employee owned, registered investment adviser with offices in Conshohocken PA, Wellesley MA and Atlanta GA. The firm specializes in managing Dividend Growth strategies for both institutions and high net worth individuals. For more information, please contact Chuck Barrett, Senior Vice President - Director of Sales and Marketing at (484) 351-3665, cbarrett@copelandcapital.com or Robin Lane, Marketing Manager at (484) 351-3624, rlane@copelandcapital.com.

Disclosure Section:

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Currency -Unless otherwise specified or disclosed, the currency used for data in the report is US Dollar (USD).

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Chart 2: *© 2018 Ned Davis Research, Inc (NDR). Further distribution prohibited without prior permission. All Rights Reserved. See NDR Disclaimer at www.ndr.com/copyright.html. For data vendor disclaimers refer to www.ndr.com/vendorinfo/.* Ned Davis Research adjusted the universe used for the domestic study as of December 31, 2017, from the Ned Davis Investable Universe to a universe based on the applicable Russell benchmarks. As a result, historical performance information may differ from previously disseminated performance information for stocks according to their dividend policy. This is not the performance of the firm and there is no guarantee that investors will experience the same type of performance. **Dividend Growers** included stocks that raised their existing dividend or initiated a new dividend during the previous 12 months. **Flat Dividend Payers** included stocks that pay a dividend but have not raised or lowered their existing dividend during the previous 12 months. **Non-Dividend Payers** included stocks that have not paid a dividend during the previous 12 months. **Dividend Cutters** included stocks that lowered their existing dividend or eliminated their dividend during the previous 12 months.

The Indexes mentioned are unmanaged, are not available for investment and do not incur expenses. The **S&P 500® Index** is a market-capitalization-weighted index of the stocks of 500 leading companies in major industries of the U.S. economy. The **MSCI EAFE® Index** (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Index consists of the following 22 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

Definitions

Dividend Growth Rate - The annualized percentage rate of growth that a particular stock's dividend undergoes over a period of time.

Standard deviation is a measure of the variability of returns-the higher the standard deviation, the greater the range of performance (i.e., volatility).

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