# HAZ Quarterly Commentary

## Horizons Active Global Dividend ETF

Q1 2023

### Market Overview

In the first quarter (Q1) of 2023, there were significant shifts in volatility and sentiment in the global marketplace. January 2023 was the fifth-best start for global equities in the last 50 years[1] but was followed by declines in February, wiping out nearly half of those gains. In March, adding to volatility was a risk appetite reversed by turmoil due to events in the U.S. banking sector.

Strong employment data, rebound in some economic indicators, and China's reopening, increased investor optimism that developed economies would manage through the tightening of monetary conditions. However, continued inflation concerns in February brought shifts in markets and concerns of heading back into the cycle of U.S. Federal Reserve (Fed) driven pressure. The failure of two U.S. regional banks and Credit Suisse in Europe in March triggered a sharp reversal in investor sentiment from the optimism that had built up at the beginning of 2023.

### Quarter in Review

On a sector level, the Financials sector was the largest contributor to relative performance. Financials came under pressure near the end of the quarter with the collapse of Silicon Valley Bank, Signature Bank, and Silvergate Bank. A positive stock selection effect came from owning European insurance companies, Axa and Allianz, and RBC. In the Industrials sector, a positive stock selection effect came from positions in Wolters Kluwer and Schneider Electric. An underweight in the Utilities sector led to a positive allocation effect. A positive stock selection effect came from positions in Costco and Nestle in the Consumer Staples sector.

The Consumer Discretionary sector, which was the largest contributor to relative performance last quarter, was the largest contributor to negative performance this quarter. Heavy non-dividend-paying benchmark names, including Tesla and Amazon, which HAZ does not own, had strong rallies in Q1 2023. HAZ's underweight in this sector led to a negative allocation effect.

Positions in Home Depot and McDonald's led to a negative stock selection effect. An overweight in the Energy sector led to a negative allocation effect coupled with a negative stock selection effect coming from a position in Williams.

The negative stock selection came from the portfolio's positions in BCE and Verizon. An underweight in the sector led to a negative allocation effect as heavy benchmark non-dividend-paying stocks, including Meta, Netflix, and Alphabet, all rallied. In the Information Technology sector, a negative stock selection effect came from positions in Accenture, Mastercard and Broadcom, which lagged the sector's rally. The portfolio's position in Medical Properties Trust led to a negative stock selection effect in the REIT sector.

HAZ sold Digital Realty Trust, reducing the overweight in the REIT sector, and purchased Hartford Financial, a U.S. multiline insurance company that exhibits strong forecasted earnings and dividend growth characteristics.

Medical Properties Trust, Inc. was fully exited this quarter (position reduced previously) as the company de-rated in our model amidst issues with tenants and the probability of a dividend cut spiked. LVMH Moët Hennessy Louis Vuitton was purchased due to its strong cash flow resiliency, downside capture abilities, and secular dividend growth characteristics.

### Outlook and Positioning

The 2022 headwinds that punished equities, including inflation, rising rates, geopolitical turmoil, and recession fears, remained a force in Q1 2023. However, they continue to shift and vary in magnitude. Investors seem to have increasingly accepted a narrative of "higher-for-longer" interest rates. With likely continued volatility and uncertainty on the horizon, stocks of companies that are well-positioned to sustain profit margins and earnings growth amid a challenging economic backdrop should outperform the broad market.

[1] Source: Guardian Capital based on MSCI World Index data from Bloomberg to March 7 2023

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The current environment is viewed in the context of HOPE (Housing, Orders, Profitability and Employment) to give a sense of where we are in the market cycle. "Housing" activity, which tends to be the first area of the economy to feel rising rates, and one of the leading indicators, has not shown signs of bottoming yet. In a similar fashion, new "Orders", which tend to decline with rising interest rates, do not show signs of bottoming. In an environment with higher-for-longer interest rates, manufacturing could continue to weaken.

With respect to profitability, declining Earnings Per Share (EPS) estimates are still evident and could have more downside ahead. According to our Artificial Intelligence (AI) Model, EPS growth rates are predicted to decline, but stabilize a year from now in the U.S., while in Europe, the majority of the sectors have a negative growth forecast. Employment, which is a lagging indicator, is still strong, however, some leading indicators of employment are pointing to potential employment weakness later in the year.

It is believed that all of this points to the fact that we are in the phase when profitability, stability and safety need to be embraced, not just in the short term, but structurally for higher-for-longer rates.

HAZ continues to favour companies with solid free cash flow and earnings, and strong balance sheets, with the ability to continue to grow dividends and with a low probability of dividend cuts. Over the past 12 months, 98% of the companies in the portfolio had dividend increases. HAZ is overweight in Energy, Health Care, and Consumer Staples while being underweight in Consumer Discretionary, Materials, and Financials.

Regionally HAZ is overweight in Europe and underweight in Asia Pacific. Dividend growth predictions have come down since last year, but in the U.S., they are still expected to be stronger than in other regions, albeit, in the low single digits. In Europe, while EPS growth is expected to decline overall, dividend-paying companies in certain sectors such as Consumer Staples, Oil, Health Care, Insurance, and Industrials are expected to still have attractive dividend growth. This offers an opportunity to harvest payouts coming out of Europe, with careful stock selection based on the AI model predictions. In Europe, higher-yielding companies with a low probability of dividend cuts are favoured, while in the U.S., dividend growth is favoured.

In the current environment, dividend yields and growth are anticipated to moderate, and as always, HAZ will aim to hold companies with attractive dividend yields and growth, rather than chasing the highest-yielding companies that may expose the strategy to unwanted credit risk and potential dividend cuts.

After years of muted performance versus other equity styles, it is potentially time to consider the duration and credit cycles within the dividend asset class. It is the sub-advisor's view that dividends could offer the best of many options by owning companies that can continue to reward shareholders through dividends, buybacks and debt reduction, combined with careful consideration of stock and sector allocations.

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