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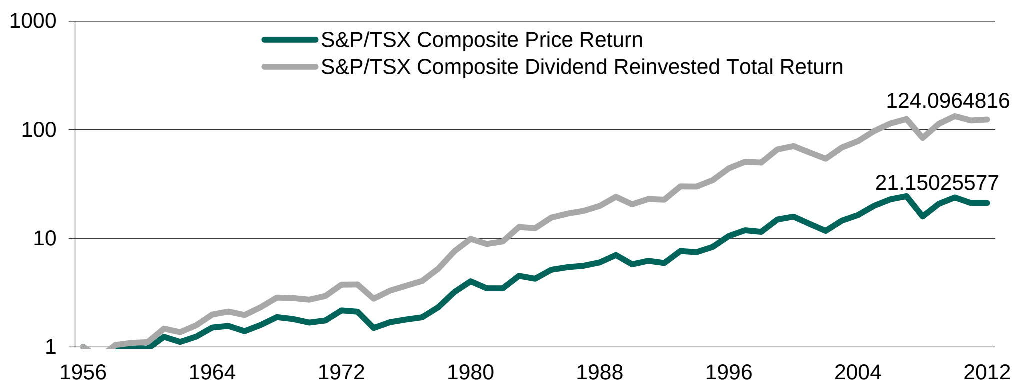
The S&P Dow Jones Indices Practice Essentials series is a curriculum-based, educational program covering selected financial markets, asset classes and indexing concepts.

THE ROLE OF DIVIDENDS IN INCOME PORTFOLIOS

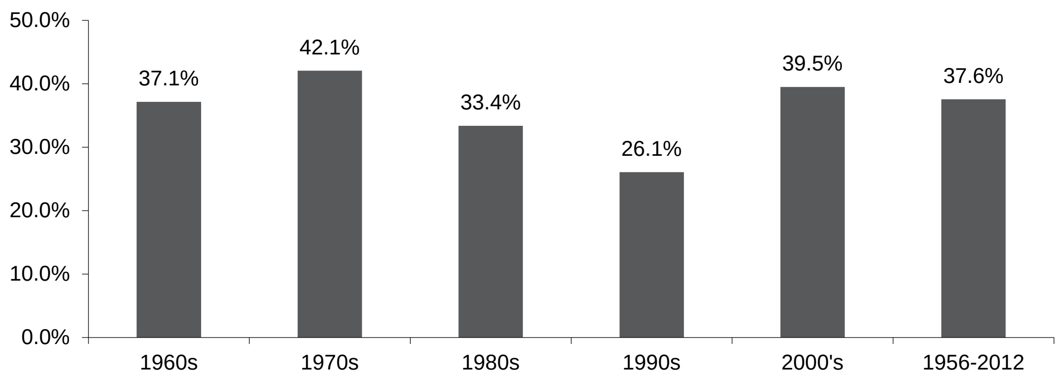
Dividends have been in existence since the 16th century, when sailing ship captains in Holland and Britain began selling the payoffs of financially motivated voyages to investors. Since 1956, dividends have contributed approximately one-third of the total equity return of the S&P/TSX Composite Index, with capital appreciation contributing two-thirds. Today, most investors are aware that sustainable dividend income and the potential for capital appreciation are both important to total return expectations. Exhibits 1 and 2 illustrate this effectively and show the historical importance of dividends.

Exhibit 1: Dividends and the Compounding Effect



Source: S&P Dow Jones Indices. Data from January 1, 1956 to August 31, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Exhibit 2: Percentage of Annualized Total Returns of the S&P/TSX Composite From Dividends



Source: S&P Dow Jones Indices. Data from January 1, 1956 to August 31, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

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The Importance of Dividends in Today's Macroeconomic Environment

With the introduction of QE3 by the Federal Reserve, investors have continued to seek yield in speculative-grade corporate bond funds. High-yield bond funds attracted inflows of USD 3.36 billion the week of September 19, 2012, swelling assets of the five largest junk-bond ETFs to USD 32 billion, a 57% increase since speculative bond ETFs were introduced five years ago.[1] The implications of this trend are two-fold.

First, high demand has resulted in a shortage of speculative-grade bonds in the market. As a result, institutional investors seeking high-yield corporate bonds have turned to ETFs to help fill their mandates.[2]

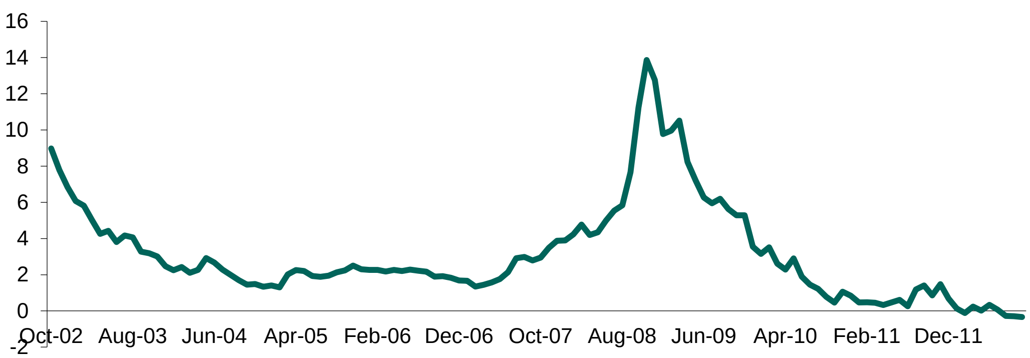
Equity-based income is an important area for investors to look at in the current macroeconomic environment.

Higher demand has also pushed down the effective yields on junk bonds in the U.S. from an average of 9.97% in 1997 to 6.48% on October 10, 2012.[3] This may cause some investors to wonder if they are being adequately compensated for the risk they are taking.

One asset class currently trading inexpensively compared to high-yield bonds is stocks. A standard measure typically used to compare equity returns to other asset classes is earnings yield. Looking at earnings yield may help determine whether or not the return is commensurate with the additional risk borne by equities versus another asset class. In the case of U.S. equities, earnings yield is often measured by the trailing twelve-month earnings of the S&P 500® divided by its index level.

Exhibit 3 illustrates the difference in earning yields (since 2002) between the Barclays Corporate High Yield Bond Index and the S&P 500. Currently, the earnings yield on the S&P 500 (6.8%) is only slightly greater than the high-yield bond index (6.5%)[4]; making high-yield bonds the most expensive they have ever been relative to equities over the past 10 years.

Exhibit 3: Difference in Yield between the Barclays Corporate High Yield Bond Index and the Earnings Yield of the S&P 500



Sources: Bloomberg, Barclays, SeekingAlpha. Data from October 31, 2002 to September 28, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results.

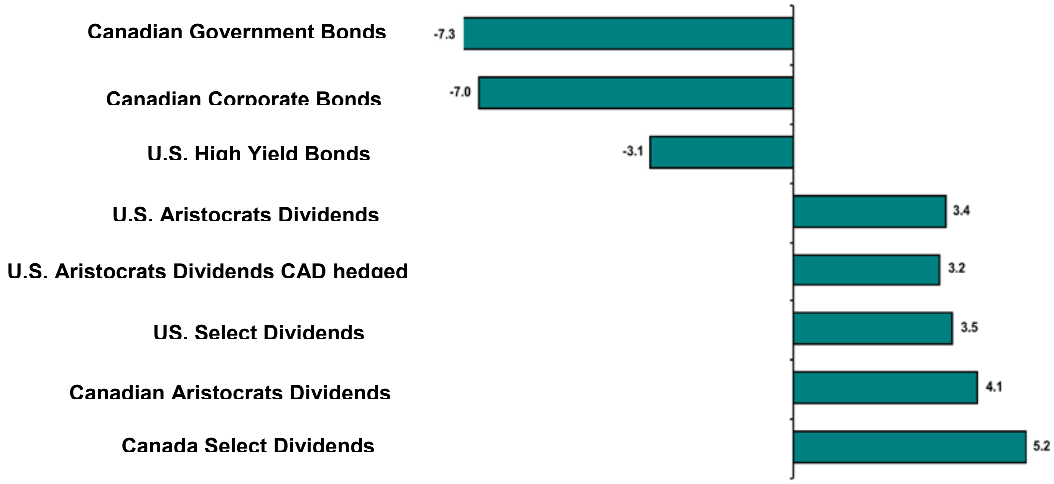
Second, although the appetite for high-yield corporate bonds remains strong, allocations away from this asset class are starting to occur. According to data compiled by JPMorgan Chase & Co., speculative-grade funds suffered two straight weeks of significant outflows of USD 309 million and USD 892 million respectively ending the week of October 1, 2012.[5] This may indicate a concern about inflation risk. One way to reduce this risk is by shifting into assets whose values tend to rise along with improving economic conditions. Exhibit 4 below illustrates the sensitivity in market values of varying income-producing assets to interest rate movements as measured by the Canadian 10-

[1] Abramowicz, Lisa, "Junk-Bond Fund Deposits Soar to Highest This Year as ETFs Lead," Bloomberg, September 21, 2012.
[2] Abramowicz, Lisa, "Junk-Bond Fund Deposits Soar to Highest This Year as ETFs Lead," Bloomberg, September 21, 2012.
[3] Federal Reserve Economic Data, "Bank of America Merrill Lynch U.S. High Yield Master II Effective Yield," October 9, 2012.
[4] SeekingAlpha.com, "The High-Yield Corporate Bond Conundrum," October 2, 2012.
[5] Federal Reserve Economic Data, "Bank of America Merrill Lynch U.S. High Yield Master II Effective Yield," October 9, 2012.

Year Bond rate. For example, for every 1% increase in the Canadian 10-year bond rate, U.S. high-yield bonds values would have fallen by 3.1% over the time period studied. In contrast, Canadian dividends would have gained between 4.1% and 5.2%.

Reinvested dividends and dividend income have both provided not only protection but critical, steady cash flow during down markets.

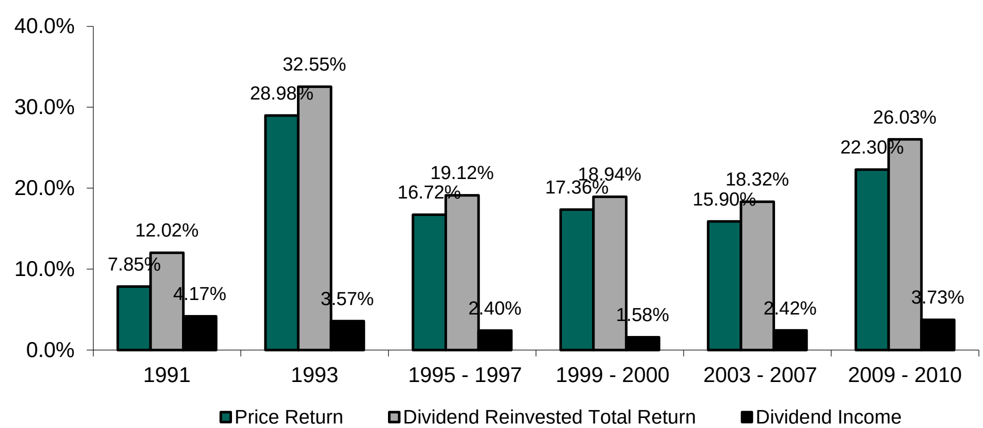
Exhibit 4: Betas of Various Asset Classes Computed with Respect to the Canadian 10-Year Government Bond



Source: S&P Dow Jones Indices and PC-Bond, a business unit of TMX Group Inc. Total return (TR) data for Equity and Dividend indices is from January 30, 2004 to September 28, 2012 and compared to CAD 10 year Government Rates. Bond duration is as of September 28, 2012. Canadian Government Bond 10 year rates with changes in returns of Canada Select Dividends, Canadian Dividend Aristocrats, U.S. Select Dividends, and U.S. Dividend Aristocrats from January 30, 2004 to September 28 2012. Charts are provided for illustrative purposes. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance. Representative indices used for equity and preferred asset classes are as follows: Canadian Aristocrats Dividends are represented by S&P/TSX Canadian Dividend Aristocrats Index (TR), Canada Select Dividends are represented by the Dow Jones Canada Select Dividend Index (TR), U.S. Dividend Aristocrats cad-hedged are represented by S&P High Yield Dividend Aristocrats Index CAD-Hedged (TR) , U.S. Dividend Aristocrats are represented by S&P High Yield Dividend Aristocrats Index (TR), and the U.S Dividend Select is represented by the Dow Jones U.S. Select Dividend Index (TR). Modified bond durations are represented as follows: Canadian Government Bonds is represented by DEX Universe All Government Bond Index, Canadian Corporate Bonds is represented by DEX Universe All Corporate Bond Index and U.S. High Yield Bonds is represented by Barclays Capital U.S. High-Yield Very Liquid Index (CAD-hedged).

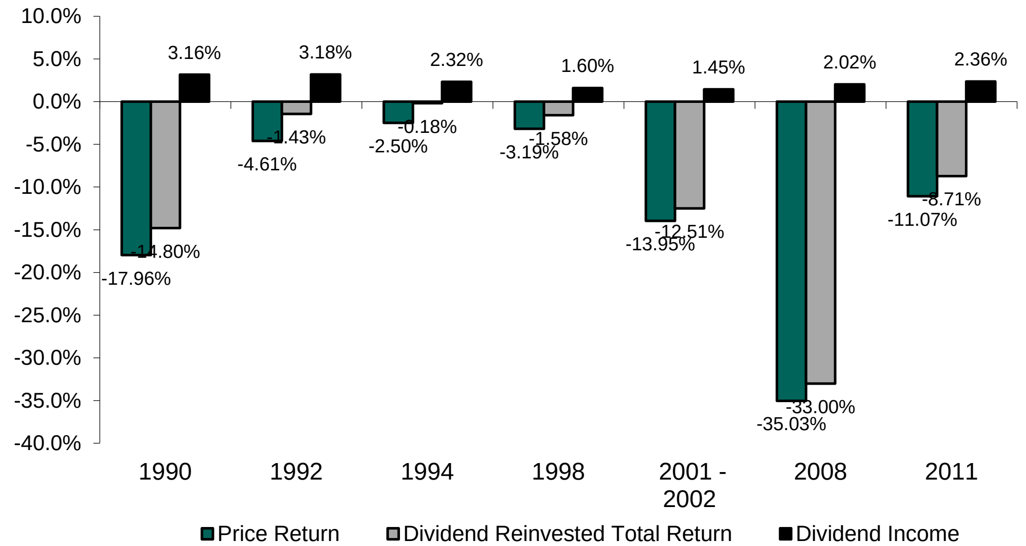
This leads to a third point to consider: the upside participation and downside protection dividends have historically provided. As illustrated in Exhibit 5, reinvested dividends and dividend income have both provided not only protection but critical, steady cash flow during down markets. Conversely, they have also allowed for participation in rising markets without sacrificing yields or returns.

Exhibit 5: Price and Total Returns and Dividend Income in Up Market Years



Source: S&P Dow Jones Indices, Data from December 1991 to September 2012. Up market years are those years where the S&P/TSX Composite ("the market") had a positive annual return on a price return basis. Charts are provided for illustrative purposes. Past performance is no guarantee of future results.

Exhibit 6: Price and Total Returns and Dividend Income in Down Market Years



Source: S&P Dow Jones Indices. Data from January 1991 to September 2012. Down market years are those years where the S&P/TSX Composite ("the market") had a positive annual return on a price return basis. Charts are provided for illustrative purposes. Past performance is no guarantee of future results.

Due to its sector stability, the Dow Jones Canada Select Dividend Index may be an appropriate alternative to an active manager strategy with a similar investment approach.

Two Dividend Exposures Compared

The S&P/TSX Canadian Dividend Aristocrats and Dow Jones Canada Select Dividend indices are designed to measure the performance of dividend-paying companies traded in Canada. Due to their unique construction, their performance, risk/return and sector characteristics can differ.

Index Construction and its Impact on Sector Exposure Over Time

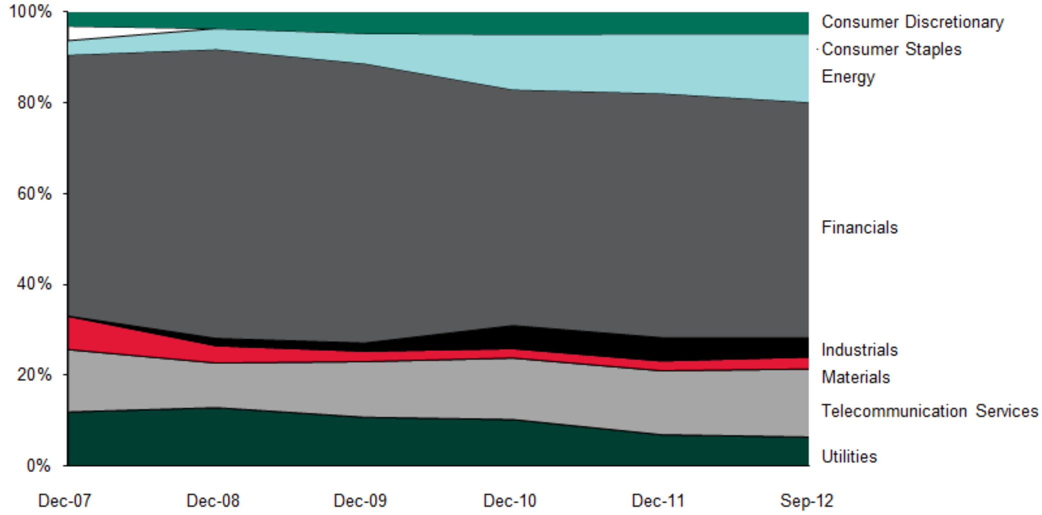
Since its inception on December 5, 2005, sector exposures for the Dow Jones Canada Select Dividend Index have remained relatively stable over time and through various economic cycles (see Exhibit 7). The index has consistently had large concentrations in financials, energy and telecommunications, a representation similar to that of the Canadian market place, which tends to be heavily concentrated in financials, energy and materials. Smaller sectors such as consumer staples, healthcare and information technology have historically had little to no representation. A focus on a relatively small number of 30 high-paying dividend stocks, an individual security cap weighting of 10% and annual re-weightings have all contributed to a steady sector representation over time.

This is in contrast with the S&P/TSX Canadian Dividend Aristocrats Index, whose sector exposures have moved more dynamically. Launched on October 16, 2007, the S&P/TSX Canadian Dividend Aristocrats Index reweights its constituents quarterly, has only a minimum requirement of 40 constituents rather than a target maximum and has an 8% constituent weighting for individual securities. Until January 2012, the S&P/TSX Canadian Dividend Aristocrats constituents were also required to follow a managed dividend policy of increasing dividends each year for each of the prior five years.

As a result, during the financial crisis, the index quickly shed many stocks such as financials, which held their dividend rates rather than increased them, a departure from the historical trend. As can be seen in the following exhibits, this resulted in sharp reduction in allocation to financials throughout 2010. The index methodology was recently amended to include securities that have maintained the same dividend for a maximum of two consecutive years within a five-year period of increasing dividends, which may change the index's response to a similar economic downturn going forward.

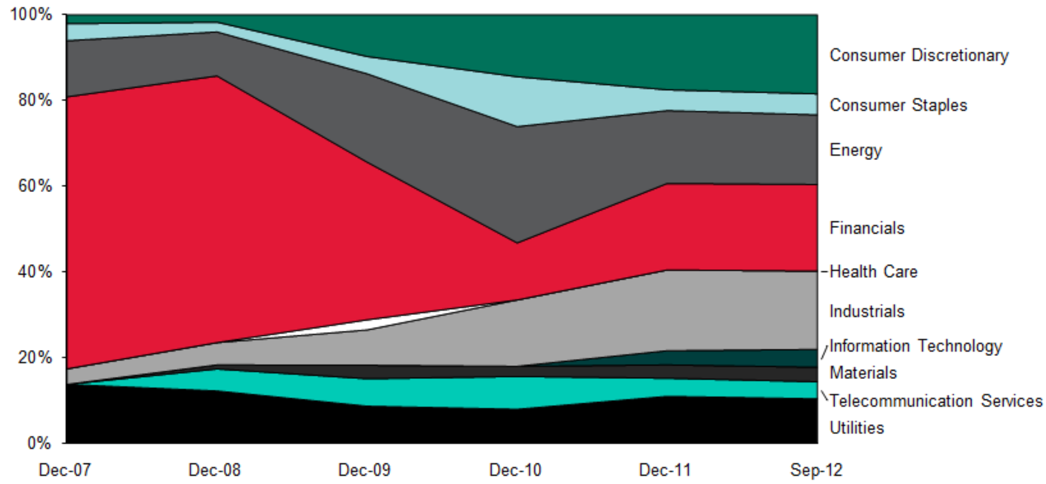
This change reflects S&P Dow Jones Indices' ongoing effort to ensure that investable indices remain liquid and tradable for those products based on indices such as the S&P/TSX Canadian Dividend Aristocrats Index.

Exhibit 7: Sector History for the Dow Jones Canada Select Dividend Index (December 2007 - September 2012)



Source: S&P Dow Jones Indices. Data from December 2007 to September 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results.

Exhibit 8: Sector History for the S&P/TSX Canadian Dividend Aristocrats Index (December 2007 - September 2012)



Source: S&P Dow Jones Indices. Data from December 2007 to September 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results.

Another unique characteristic of the S&P/TSX Canadian Dividend Aristocrats Index construction is its minimum constituent requirement. Since there is no ceiling on the number of securities in the index, there is broader sector representation across Canada[6] including the information technology and consumer staples sectors.

[6] As defined by The Global Industry Classification Standard or GICs, which was developed by, and is the exclusive property of, Standard & Poor's and MSCI. GICS is the trademark of Standard & Poor's and MSCI. Global Industry Classification Standard (GICS) and GICS Direct are service marks of Standard & Poor's and MSCI.

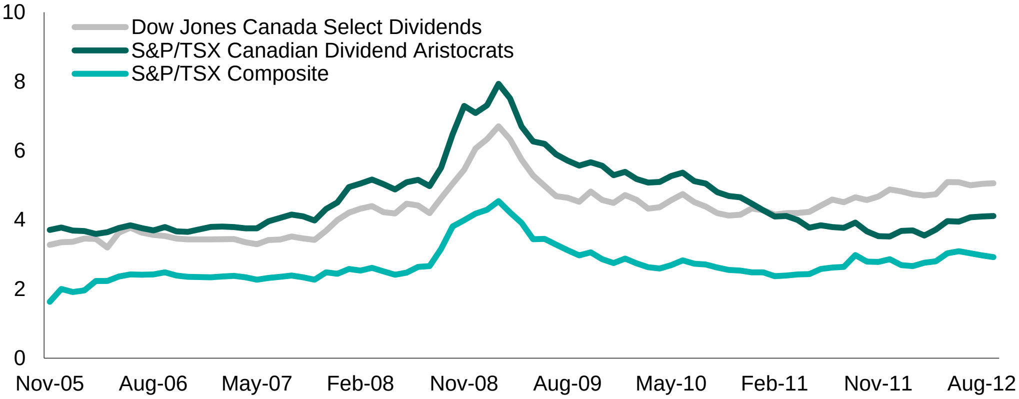
Index Construction and its Impact on Yield

Yield is a distinguishing feature between these two indices. The S&P/TSX Canadian Dividend Aristocrats Index has delivered 4.63% on average since 2005, which is slightly higher than the Dow Jones Canada Select Dividend Index at 4.34%. However, due to differences in index methodology, these two indices have produced dissimilar income streams during the last two years, with the S&P/TSX Canadian Dividend Aristocrats Index generating a 3.8% yield versus 4.6% for the Dow Jones Canada Select Dividend Index. The Dow Jones Canada Select Dividend Index, with its continued focus on financials, has produced higher yields post-crisis

The less dynamic nature of the Dow Jones Canada Select Dividend Index, with its continued focus on financials, has produced higher yields post-crisis, which may be a consideration for those investors who are most concerned with income.

Exhibit 9: Dividend Yields Over Time

(Both indices have delivered consistently higher yields than the benchmark over the last few years.)

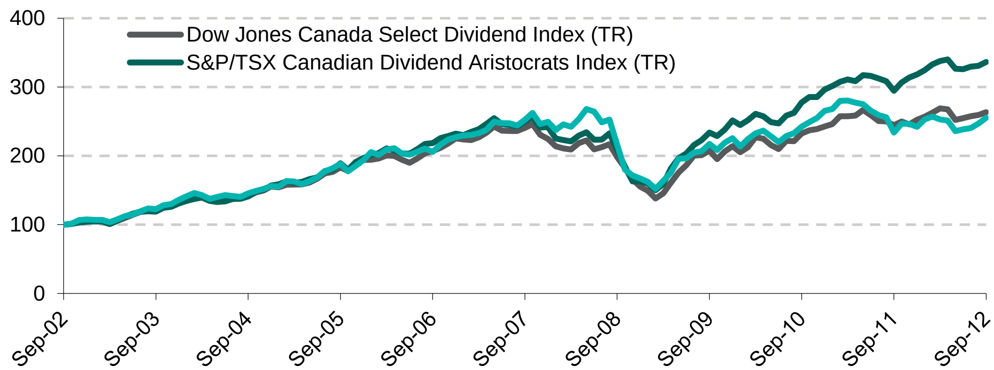


Source: S&P Dow Jones Indices. Monthly dividend yield data from November 30, 2005 to September 28, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Performance and Risk Return Characteristics

Yield comes with a price. A comparison of these two indices over time illustrates that in the long run, the S&P/TSX Canadian Dividend Aristocrats Index outperforms on both an annualized and risk-adjusted return basis. Its focus is on stocks with a managed dividend policy versus a high dividend paying strategy, which may indicate a bias to companies that have both growth and value characteristics. This means that these companies reward shareholders with both dividends and capital gains by reinvesting more company earnings than high dividend paying stocks.

Exhibit 10: Performance of the S&P/TSX Canadian Dividend Aristocrats and Dow Jones Canada Select Dividend Indices



Source: S&P Dow Jones Indices. Data from September 30, 2002 to September 28, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Exhibit 11: Performance Characteristics of the S&P/TSX Canadian Dividend Aristocrats Index, Dow Jones Canada Select Dividend Index and the S&P/TSX Capped Composite Index

Year	Dow Jones Canada Select Dividend Index (TR)	S&P/TSX Canadian Dividend Aristocrats Index (TR)	S&P/TSX Capped Composite Index (TR)
Annualized Return			
1	7.66%	14.18%	9.17%
3	8.24%	12.89%	5.52%
5	1.81%	6.14%	0.22%
10	8.40%	10.64%	8.12%
Annualized Volatility			
1	8.26%	6.76%	10.97%
3	11.00%	8.95%	12.26%
5	15.44%	15.66%	17.39%
10	12.34%	12.59%	14.12%
Sharpe Ratios			
1	0.93	2.10	0.84
3	0.75	1.44	0.45
5	0.12	0.39	0.01
10	0.68	0.85	0.58

Source: S&P Dow Jones Indices. Data from November 30, 2005 to September 28, 2012. Charts are provided for illustrative purposes. Past performance is no guarantee of future results. This chart may reflect hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Conclusions

In summary, dividends have historically provided portfolios with attractive yields and total returns, allowing investors to participate in growth markets while achieving protection in down markets. Dividend-paying stocks uniquely provide both capital gains and income, which for investors with long-term horizons, may be critical to achieving their portfolio objectives. In the current low interest rate environment, stock valuations are generally seen as inexpensive when compared to speculative-grade corporate bonds. Given their historical tendency to increase in value during economic growth periods, dividends may continue to play an important role.

Performance Disclosure

The inception date of the S&P/TSX Composite (the “Index”) was January 3, 1977, at the market close. All information presented prior to the index inception date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. Complete index methodology details are available at www.spindices.com.

The inception date of the S&P/TSX Canadian Dividend Aristocrats Index (the “Index”) was October 16, 2007, at the market close. All information presented prior to the index inception date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. Complete index methodology details are available at www.spindices.com.

The inception date of the Dow Jones Canada Select Dividend Index (the “Index”) was December 5, 2005, at the market close. All information presented prior to the index inception date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. Complete index methodology details are available at www.spindices.com.

The inception date of the S&P High Yield Dividend Aristocrats Index (the “Index”) was November 9, 2005, at the market close. All information presented prior to the index inception date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. Complete index methodology details are available at www.spindices.com.

The inception date of the S&P High Yield Dividend Aristocrats Index CAD Hedged (the “Index”) was November 9, 2005, at the market close. All information presented prior to the index inception date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect when the index was officially launched. Complete index methodology details are available at www.spindices.com.

Past performance of the Index is not an indication of future results. Prospective application of the methodology used to construct the Index may not result in performance commensurate with the back-test returns shown. The back-test period does not necessarily correspond to the entire available history of the Index. Please refer to the methodology paper for the Index, available at www.spdji.com or www.spindices.com for more details about the index, including the manner in which it is rebalanced, the timing of such rebalancing, criteria for additions and deletions, as well as all index calculations. It is not possible to invest directly in an Index.

Another limitation of back-tested hypothetical information is that generally the back-tested calculation is prepared with the benefit of hindsight. Back-tested data reflect the application of the index methodology and selection of index constituents in hindsight. No hypothetical record can completely account for the impact of financial risk in actual trading. For example, there are numerous factors related to the equities (or fixed income, or commodities) markets in general which cannot be, and have not been accounted for in the preparation of the index information set forth, all of which can affect actual performance.

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