EAGLE GLOBAL ADVISORS

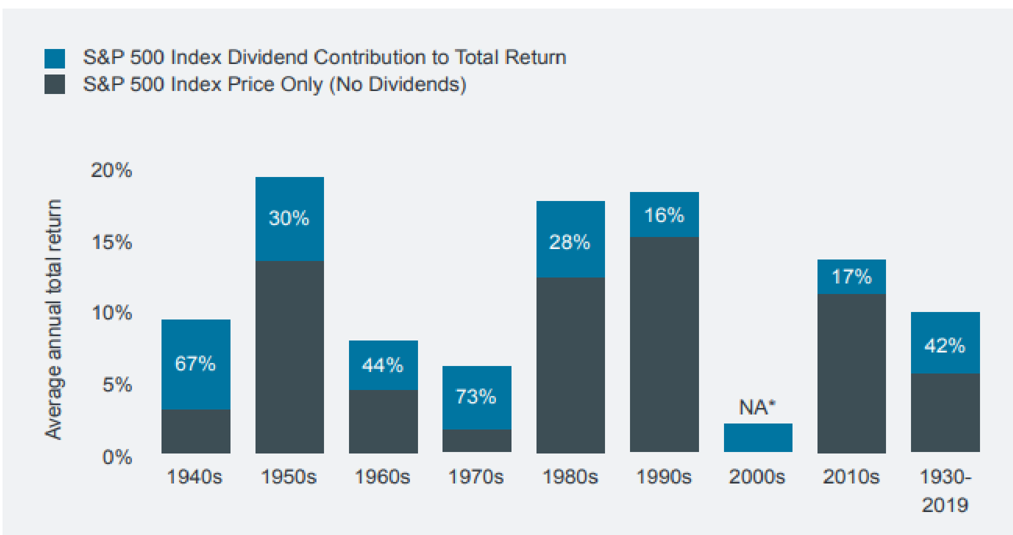
The Many Benefits of Dividend Growth Investing

September 2022

Dividends are an often overlooked driver of stock market returns. This is particularly true when equity markets are on the upswing. Other than possibly at a convention of retirees, when was the last time you heard someone bragging about the dividends in their stock portfolio? Yet, companies that consistently pay and grow their dividends have historically outperformed non-dividend stocks over a full market cycle. This is not entirely surprising. The ability to pay and grow a dividend is a strong sign of financial health. It demonstrates the companies' ability to earn a return over cost with enough cushion to return cash to shareholders. Companies that not just maintain but grow their dividends are able to grow both the top *and* the bottom line.

Contribution Can Vary

The role of dividends in equity total return varies over time, largely reflecting current interest rates and the outlook for economic growth. During the high rate & high inflation 1970s, dividends contributed 73% of the S&P 500 total return. During the ultra-low rate, high growth 2010s, that number fell to 17%. Over the entire measured period from 1940-2019, dividends accounted for 42% of total return, a figure that may surprise many.



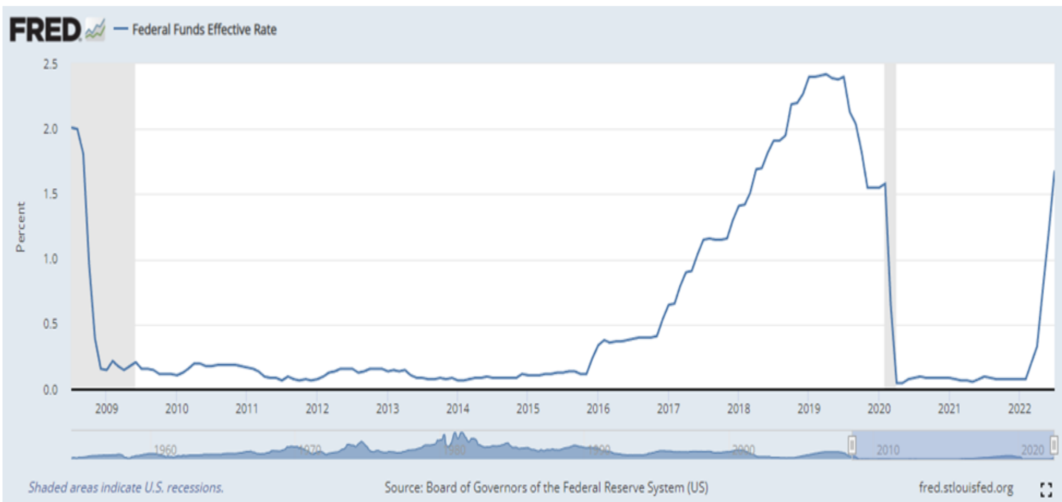
*Source: Morningstar./Hartford Funds. 02/2020 S&P 500 Index is a market capitalization weighted price index composed of 500 widely held shares. *Total return for the S&P 500 Index was negative for the 2000s. Dividends provided a 1.8% annualized return over the decade.*

In addition to a large contribution to total return, growing dividends have provided investors benefits that include income for retirement, an inflation hedge, reduced portfolio volatility, and reduced reliance on market timing for wealth creation. Investing in dividends is not as simple as "set it and forget it", however, as owning stable and growing dividends will produce far superior returns to dividends that are reduced or eliminated.

The easy money Fed policy of 2005-2008 resulted in widespread financial bubbles. When those bubbles burst in 2008, the world experienced the Great Recession. In an attempt to kick start the economy in 2009, the Fed once again drove borrowing costs to zero. This had the desired consequence of stimulating economic growth by lowering borrowing costs for consumers and businesses. Near-zero interest rates also spurred outsized returns in risk assets like stocks and housing. During the 2010's dividends only contributed 17% of total return.

More recently, The Fed has (for now) ended the period of "free money" in an attempt to rein in 40-year highs in U.S. inflation. As the U.S. enters a new monetary policy regime, the question becomes "What's next"?

U.S. Federal Funds Rate 2008-2022



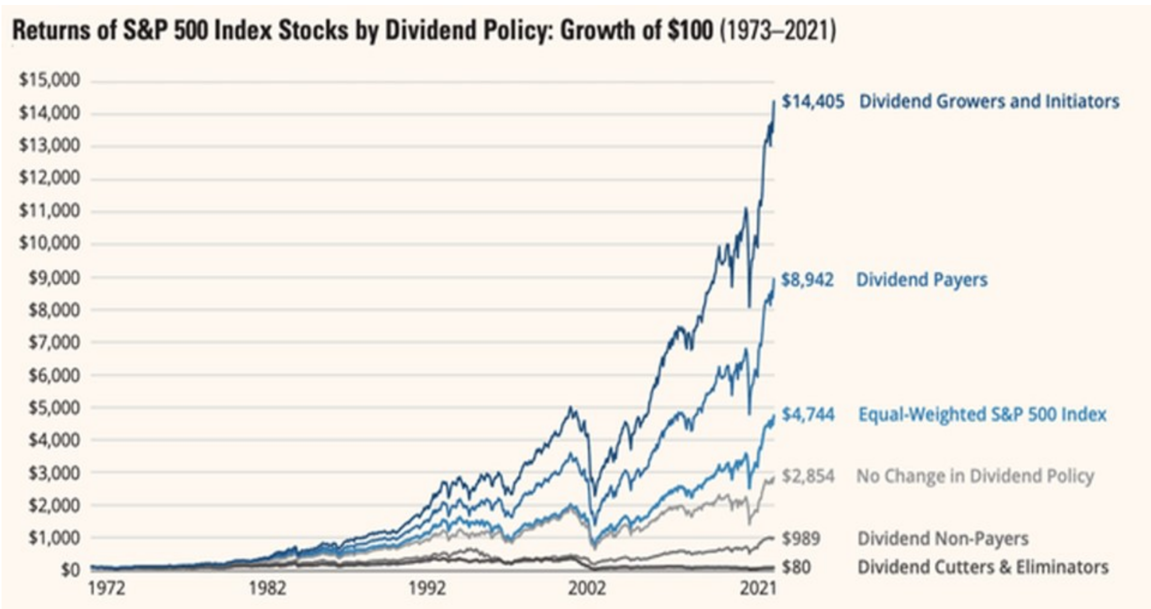
Forecasting future Fed moves as well as the direction of equity market moves is a difficult task. An old Wall Street adage warns investors "Don't fight the Fed". When the Fed is accommodative, stocks tend to rise. When the Fed is restrictive (higher rates), the economy is more likely to contract, dragging stock prices along. Given the difficulty of market timing, adding dividends to your portfolio has historically helped smooth returns, reducing the role of market timing in total return.

Different Types of Dividend Payers

Ned Davis research breaks the market into **Dividend Growers, Payers, No Change, Non-Payers, and Cutters.** Since 1972, owning Dividend Growers and Initiators has outperformed all other categories. Dividend Cutters and Eliminators have fared the worst. The differences in total return are non-trivial.

Some investors like to choose dividend stocks with the highest yield. But this approach fails to target two distinct dividend features: stability and growth. Often the highest paying dividend equities are those struggling to maintain their payout. Dividend cuts impact investors in two distinct ways. First there is a loss of income. Secondarily, share prices decline both before (in anticipation of) and after (reality sets in) the cuts.

Dividend cutters and eliminators have the worst historical performance since 1972. Those who simply maintain a consistent dividend have outperformed the equal-weighted S&P 500. But those returns pale in comparison to a portfolio of dividend growers and initiators. The ability to identify dividends that are both stable and growing places a premium on active portfolio management with a demonstrated ability to navigate dividend policies and trends.



Past performance does not guarantee future results. Indices are unmanaged and not available for direct investment. For illustrative purposes only. Data Sources: Ned Davis Research and Hartford Funds, 2/21.

Investing For Income And Growth

Dividend Growth investing offers investors some of the benefits of both dividend investing and growth investing. In addition to a history of superior total returns documented in the Ned Davis research, investing in a portfolio of dividend growers has offered other benefits.

Current Income. Both retirees and non-retirees seek income in their portfolios. For retirees, the need is more acute. Many advisors recommend removing no more than 4% from your retirement account annually during retirement in order to make the funds last. Some of that can reasonably be recouped from market appreciation. A 2008 study by Jack Gardner found the long-term outperformance of investing only in the 100 highest-yielding dividend stocks in the S&P 500, would allow retirees to increase annual portfolio withdrawals to 5% and still maintain the portfolio in perpetuity.

Potential Inflation Hedge. For much of the 2010s, fixed income yields were at historic lows. Recent higher yields allow investors to lock in more income. But what about inflation? If your bond portfolio yields 4%, but inflation is running at 5%, your future purchasing power is declining. This is where growing dividends can help fight inflation. Dividends that grow offset inflationary pressures and allow you to maintain purchasing power.

Reduced Volatility. More research from Ned Davis shows that dividend growers have historically delivered lower market volatility, as measured by the standard deviation of returns. Lower volatility reduces the importance of market timing and fosters more patient investors. Reducing the emotional highs and lows that results in fewer market timing decisions has the impact of increasing returns (and stress!) over time. Said differently, market timing is not easy.

Average Annual Returns and Volatility by Dividend Policy
(3/31/72–12/31/19)

	Returns	Beta	Standard Deviation
Dividend Growers & Initiators	12.87%	0.92	15.61%
Dividend Payers	12.79%	0.98	16.36%
No Change in Dividend Policy	11.85%	1.13	17.92%
Dividend Non-Payers	8.57%	1.13	24.33%
Dividend Cutters & Eliminators	10.88%	1.23	24.08%
Equal-Weighted S&P 500 Index	12.29%	1.00	16.98%

Data Sources: Ned Davis Research and Hartford Funds, 2/20. Dividend policies shown are for stocks in the S&P 500 Index.

Fostering A Long-Term Investing Mind Set

The single biggest enemy of creating wealth through investing is human emotion. Fear drives investors to sell when prices are falling. Greed causes investors to pile in at the top. Dividend investing helps foster a long-term investing mindset. When you adopt a long-term, value-oriented dividend growth mindset, it becomes easier to grow your wealth and income over time. Take Warren Buffett's advice:

"Owners of stocks, however, too often let the capricious and often irrational behavior of their fellow owners cause them to behave irrationally as well. Because there is so much chatter about markets, the economy, interest rates, price behavior of stocks, etc., some investors believe it is important to listen to pundits – and, worse yet, important to consider acting upon their comments.

Those people who can sit quietly for decades when they own a farm or apartment house too often become frenetic when they are exposed to a stream of stock quotations and accompanying commentators delivering an implied message of "Don't just sit there, do something."

Owning a portfolio of dividend payers and/or dividend growers can simultaneously add income to your portfolio, protect against inflation, and reduce volatility. All of which can change your focus from daily stock charts to long-term wealth creation.

For more information, contact:
Curt Pabst, Managing Director
713-952-3550
cpabst@eagleglobal.com

Disclosures

Eagle Global Advisors, LLC is a registered investment adviser located in Houston, Texas. The views expressed are those of Eagle Global Advisors, LLC and are not intended as investment advice or recommendation. This material is presented solely for informational purposes, and nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. No recommendation or advice is being given as to whether any investment or strategy is suitable for a particular investor. Information is obtained from sources deemed reliable, but there is no representation or warranty as to its accuracy, completeness or reliability. All information is current as of the date of this material and is subject to change without notice. Third-party economic, market or security estimates or forecasts discussed herein may or may not be realized and no opinion or representation is being given regarding such estimates or forecasts. Certain products and services may not be available in all jurisdictions or to all client types. Unless otherwise indicated, Eagle Global Advisors' returns reflect reinvestment of dividends and distributions. Indexes are unmanaged and are not available for direct investment. Investing entails risks, including possible loss of principal. Past performance is no guarantee of future results.