

Client's Corner

The Delightful Stickiness of Dividends

HERE'S A QUESTION FOR YOU: IN RETIREMENT, WHEN YOU GO to the supermarket, what will be the single most important variable in your financial life?

Hint: it won't be the total value shown on your brokerage account statement. That's because you don't actually bring your account values to the supermarket. *You bring your income.* Indeed, whether your account values are going up or down in any given month is all but irrelevant. The critical financial issue is binary: (a) is your income adequate to your spending needs, and (b) is that income rising through time to offset inexorable increases in your cost of living (aka inflation)?

With those as your tests of a lifestyle-sustaining income, a fixed-income approach may not inspire a lot of confidence. That's because bonds, CDs and savings accounts aren't yielding very much, and haven't been for some time. Meanwhile your cost of living continues to escalate. Indeed, just at the moment inflation is (and ought to be) a pressing concern.

Mainstream equities have a better income story to tell.

Here's a [link](#) to the chart of S&P 500 earnings and dividends prepared annually by Dr. Aswath Damodaran, professor at NYU's prestigious Stern School of Business. It's worth several looks.

Set aside if you can the fact that it shows the S&P 500 rising almost 65 times, from 58 in 1960 to 3,756 at the end of 2020. Even set aside the fact that the earnings of the Index grew from \$3.10 in 1960 to a pandemic-suppressed \$138.12 last year. Impressive as these numbers surely are, they're irrelevant to the line of inquiry we're pursuing here, which is entirely focused on *income*.

When we narrow our focus in just that way, we find that the cash *dividend* of the S&P 500 grew, in the 61 years under study, from \$1.98 to \$56.70. That represents a compound annual growth rate of 5.8%. Much more to the point, it's an increase in the cash income from mainstream equities of about 29 times *while the Consumer Price Index went up just less than nine times*. (Source: the U.S. Bureau of Labor Statistics, as reported by InflationData.com.)

This is, in the broadest sense, what we require of our retirement income: that it goes up, and that over time it can increase at a rate that outpaces our loss of purchasing power.

But even *that* isn't the narrow point of this essay, which is the relative *stickiness* of dividends: their historical tendency, during difficult times, to go down a whole lot less than do stock *prices*.

The fact is that established dividend-paying companies—which make up about 85% of the S&P 500—hate like the dickens to cut dividends, even when earnings are taking a hit and stock prices are swooning for a season or two. You can see this all throughout Professor Damodaran's data; I would simply draw your attention to the three worst stock market declines in these 61 years.

- Between January 1973 and October 1974, the S&P 500 Index declined about 48%. But as you see, on an annual basis, the dividend didn't go down *at all*.

- Between March 2000 and October 2002, the S&P 500 went down about 49%, but the dividend contracted a mere 2% from 2000 to 2001. It was already rallying in 2002, and was in new high ground by 2003.

- Between October 2007 and March 2009, in the Global Financial Crisis, the Index went down 57%. The dividend declined quite a bit less than half that, at 23%. It recovered smartly thereafter, and by 2020 had very nearly doubled its 2008 peak.

Now, a 23% hit to the dividend was certainly no walk in the park. But you'll note that it was by far the largest dividend cut in these six decades. And compared to a 57% price decline, it was at least *relatively* mild. What it demonstrates quite clearly is that retirees living on equity dividends should always have a couple of years' living expenses in reserve to see them through—a point that can't be overstressed.

Finishing up this analysis with the plague year 2020, we note that the Index was (however briefly) down 34%. But the dividend typically gave ground far more grudgingly—down 3.6% on the year. It's ticking up strongly as I write.

As a general statement, then: people have a tendency to obsess far too much about short-term changes in their account values—and pay far too little attention to the long-term trajectory of their dividend income. Which is probably a mistake, because *it's the latter they're going to be living on*.

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