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Give Me Dividends in Any Weather

The spring stock market rally has been powered partly by an acceleration in performance among lower quality companies – shades of 2013, in that regard – but altogether 2014 has turned a different dynamic of 2013 completely on its head.

Whereas low- or no-dividend stocks trounced higher-yielding shares last year, this year we're seeing the opposite result: stocks with above average dividend yields are beating low- or no-dividend stocks handily, turning in total returns more than one-and-a-half to three times better through May 31st . See the chart below, whose vertical bars show year-to-date total return for stocks grouped by dividend yield (the bottom row of numbers on the horizontal axis).

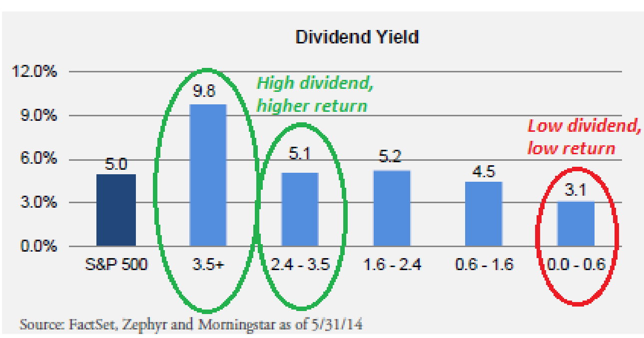

Chart source: Eaton Vance

For our income-tilting approach to equities, this has been a welcome change, and one that falls more within the channel of historic experience than outside it.

Did you know that of the eight decades from 1930 through 2009, dividends provided the only source of positive return in two of them (the 1930s and 2000s, when stock prices fell)? Or that in two of them (the 1940s and 1970s), dividends provided the bulk of total return? In other words, for half of the decades from the Hoover administration to the Obama administration, dividends delivered either the majority, or the entirety, of positive return.

Even in a period when yields have been measly by historic standards – the last ten years, 2004-2013 – dividends have been a positive differentiator. During this time, dividend-paying stocks beat the broad stock market 8.1% vs. 7.4%. What's more, they did so with less volatility (standard deviation 13.9% vs. 14.6%; numbers per Morningstar), especially welcome considering the wildly varying nature of the market across that period, an extraordinary cycle of bubble, bust, and recovery. Truly, dividends are your all-weather friend.

We associate the last two recessions with the two greatest stock market collapses since the Great Depression. During the March 2001-November 2001 recession, dividend-paying stocks outperformed the broad market by 5.4%. During the most recent recession dating from December 2007-June 2009, many companies had to cut their payouts; even so, dividend payers still did 5.7% better than the average stock (again, numbers per Morningstar).

OK, you might say, but deflation has been the boogey man of our last two recessions; *of course* steady income-producing assets did well in that slackening environment. But how about when inflation gets on the march? In our last episode of high inflation, from 1974-1980, dividends comprised over half of total return to US stockholders. They did the job then, too.

To us, cash dividends represent the most tangible, most reliable benefit of equity ownership: they are the transmission mechanism by which company management pushes out profits. They signal confidence, they substantiate corporate wherewithal, and they put cash in the pockets of the people companies are supposed to be working for: you, their owners.