Here’s What You Need to Know about Dividends

In November 1999 tech stocks with no dividends seemed like a sure bet. Despite the hype, I was still doing my best to encourage my readers to stick the principles of dividends and compounding. Here’s what I wrote then:

> ### *Historically, Dividends Provide Much of Total Return*
>
> *What about the base for the economy and the stock market in general? As I’ve written often, the two are inexorably linked. After all, could stocks on average outrun the performance of all the companies that jointly contribute to our country’s gross domestic product? No. and, here’s why.*
>
> *Over seven decades, from 1926 to 1997, U.S. nominal gross domestic product (non-inflation adjusted) grew at a compounded 6.4% per year. Over the same period, the return on stocks due to price appreciation (dividends not considered) was a compounded 6% per year. The fit is almost exact. I know you’re thinking that the stock market must have done better than that, but it did not.*
>
> *Investors, however, did better due to the average annual compounded 4.6% return paid to shareholder from dividends. The total return from (1) price appreciation and (2) dividends was an average compounded 10.6%, but remember, over 43% of total return came from dividends. Sadly, today’s investors have almost completely forgotten about dividends. Perhaps with the average yield on stocks about 1.5%, instead of the historical 4.6%, there is some reason not to spend much time on dividends. Nonetheless, most investors are unlikely to see stock price appreciation that outruns nominal GDP growth over*

time.

You can read more about the benefits of dividends in your portfolio in, [Dividend Investing: A Primer], a white paper on the subject produced by my family run investment counsel firm, [Richard C. Young & Co., Ltd.]

What Are You Getting Paid?

It's a seemingly simple question, what are you getting paid? Most people can recall their weekly or monthly employment income without hesitation, but do you know what your portfolio is paying you quarterly? If you aren't focused on generating income from your investment portfolio, you may want to adjust your strategy. In April 2006 I discussed the importance of getting paid, now. I wrote:

> ***Pay Me Now***
>
> *When you invest in portfolio securities, your first question should be, what am I getting paid? I do not want you investing your serious money in securities that pay you neither interest nor dividends. Do not put your hard-earned capital at risk with the view of buying a portfolio security today and selling it to someone else tomorrow at a higher price. To me, this is speculation, not investing. Go with what you know by not only demanding to be paid, but by also holding your taxes and transaction costs to a minimum, as I do. Trust me, over time, the penalty of taxes and transaction costs is a brutal killer for most investors. Think reverse compounding here.*
>
> *OK, so compound interest and dividends must underpin your*

investment thinking. Albert Einstein described compound interest as “the greatest mathematical discovery of all time.” Ben Franklin wrote on compound interest, “’Tis the stone that will turn all your lead into gold.” Charlie Munger, longtime partner to Warren Buffett, wrote, “Understanding the power of compound return and the difficulty getting it is the heart and soul of understanding a lot of things.”

Ben Graham Speaks

In almost each of my strategy reports over the decades, I’ve written about the power of dividends. Mr. Value Investing, Ben Graham, devoted a ton of ink to the subject. In fact, B.G. wrote, “One of the most persuasive tests of high quality is an uninterrupted record of dividend payments going back over many years.” Graham believed that “the defensive investor might be justified in limiting his purchases to those meeting this test.”

The Winning Investment Technique Used by Queen Elizabeth I

Two years ago I told readers the story of John Maynard Keynes’ lectures on compound interest in the late 20s. Keynes told the story then of Queen Elizabeth I and her impetuous and insightful use of compounding to build the British Empire. I wrote:

Compound Interest, the Foundation of an Empire

In a series of lectures and papers in 1928, John Maynard Keynes traced England's success from the late 16th century, starting with a treasure Francis Drake had stolen from the Spaniards in 1580. Keynes was writing at the height of the British Empire, and he chalked England's success up to compounding. He wrote, "In that year he [Drake] returned to England bringing with him the prodigious spoils of the Golden Hind. Queen Elizabeth was a considerable shareholder in the syndicate which had financed the expedition. Out of her share she paid off the whole of England's foreign debt, balanced her Budget, and found herself with about £40,000 in hand. This she invested in the Levant Company—which prospered. Out of the profits of the Levant Company, the East India Company was founded; and the profits of this great enterprise were the foundation of England's subsequent foreign investment. Now it happens that £40,000 accumulating at 3.25 per cent compound interest approximately corresponds to the actual volume of England's foreign investments at various dates, and would actually amount today to the total of £4,000,000,000 which I have already quoted as being what our foreign investments now are. Thus, every £1 which Drake brought home in 1580 has now become £100,000. Such is the power of compound interest!"

Keynes opined "the power of compound interest over two hundred years is such as to stagger the imagination." You, like me, may not be a fan of the great body of Keynes' work, but on compound interest, there is no doubt he was correct.

The Historical Primacy of Dividends

In July 2011 I wrote:

> *On page 480 of 1962's Security Analysis by Graham, Dodd, and Cottle, I underlined the above header. Since that time, I must have worn out a thousand red pens underlining books, but rarely are they investment books. I have never required another book on investing. I have since read a handful of other books on investing that I have found somewhat useful, but it has been a couple of decades since the last one. And I have no need to add to the list. Successful investing is to me more an art than a science. And intuition plays a big part. Since I graduated from Babson College with a BS in investments in 1963, I have relied on the wisdom outlined in the paragraph headed "Historical Primacy of Dividends." In chapter 35, the authors explain, "For the vast majority of common stocks, the dividend record and prospects have always been the most important factor controlling investment quality and value. In the majority of cases, the price of common stocks has been influenced more markedly by the dividend rate than by the reported earnings."*

Dividends are still the ultimate way to value common stocks. You have no control over the ups-and-downs of stock prices, but every quarter when you receive a dividend payment, that's a real return. And when you put those cash payments to work on compounding, it only gets better.

At Richard C. Young & Co., Ltd., we craft custom portfolios of dividend paying stocks for our clients. Each portfolio is filled with stocks that not only pay regular dividends, but which also have a history of increasing those dividends.

If you would like to learn more about the Retirement Compounders Portfolio strategy, [sign up for the Richard C. Young & Co., Ltd. monthly client letter] (free, even for non-clients). There my son Matt, President and CEO of the family run investment counsel, spends time each month explaining our strategy, including the historical primacy of dividends.

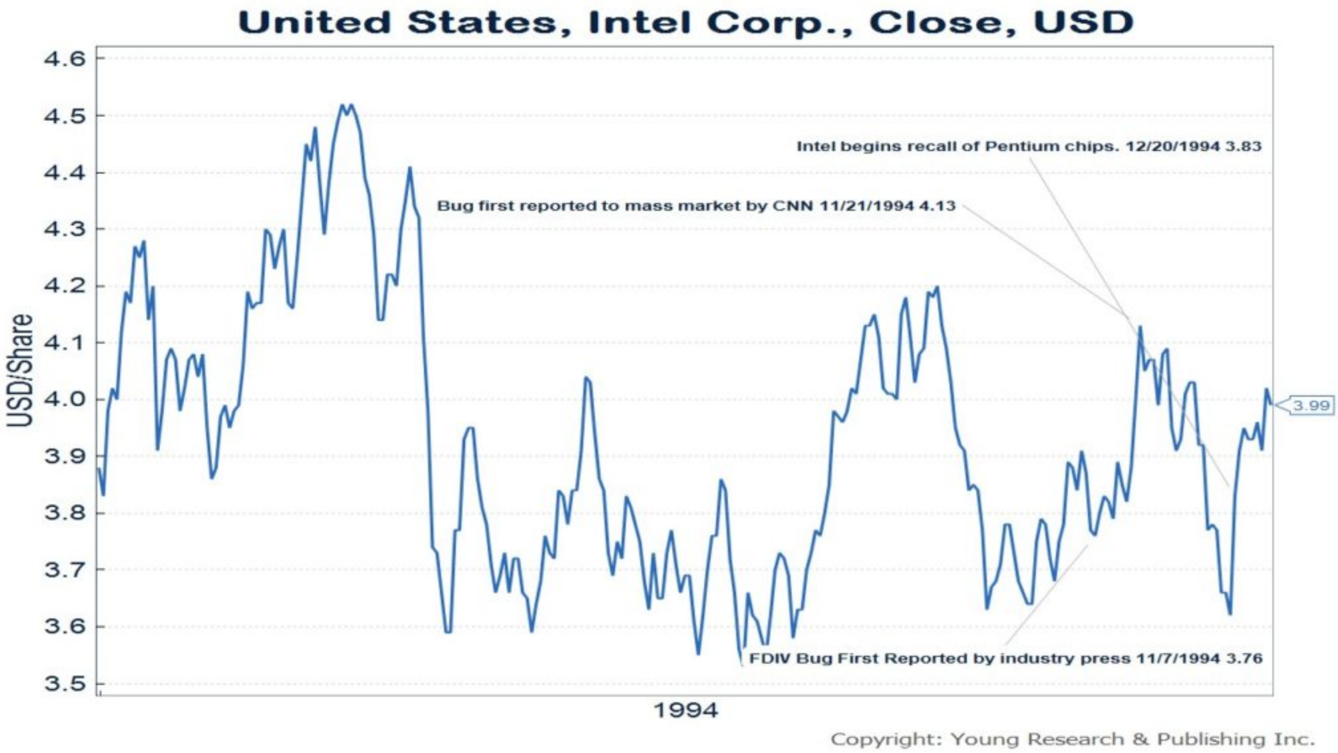
Is Your Investment Game Plan Ready for Action?

History has a way of repeating itself. In early 1995 I wrote about a math professor named Tom Nicely, who worked at Lynchburg College. Nicely was examining prime numbers using a group of five personal computers. While four of the computers gave Nicely the correct answer to a problem, 1.2126596294086, the fifth turned up a slightly different answer, 1.212659624891157804.

The cause of the fifth computer's error was the Intel Pentium processor installed on it. Nicely called Intel to explain, but was given the cold shoulder. Next, he did something which at that point was still novel, he asked for help on the Internet. Others checked Nicely's work and came back with the same results, confirming his conclusions.

Intel had already known about the problem since May when one of their own researchers had discovered it, but only after they had been backed into a corner by independent confirmation did Intel acknowledge Nicely's research. The company even offered him a consulting job.

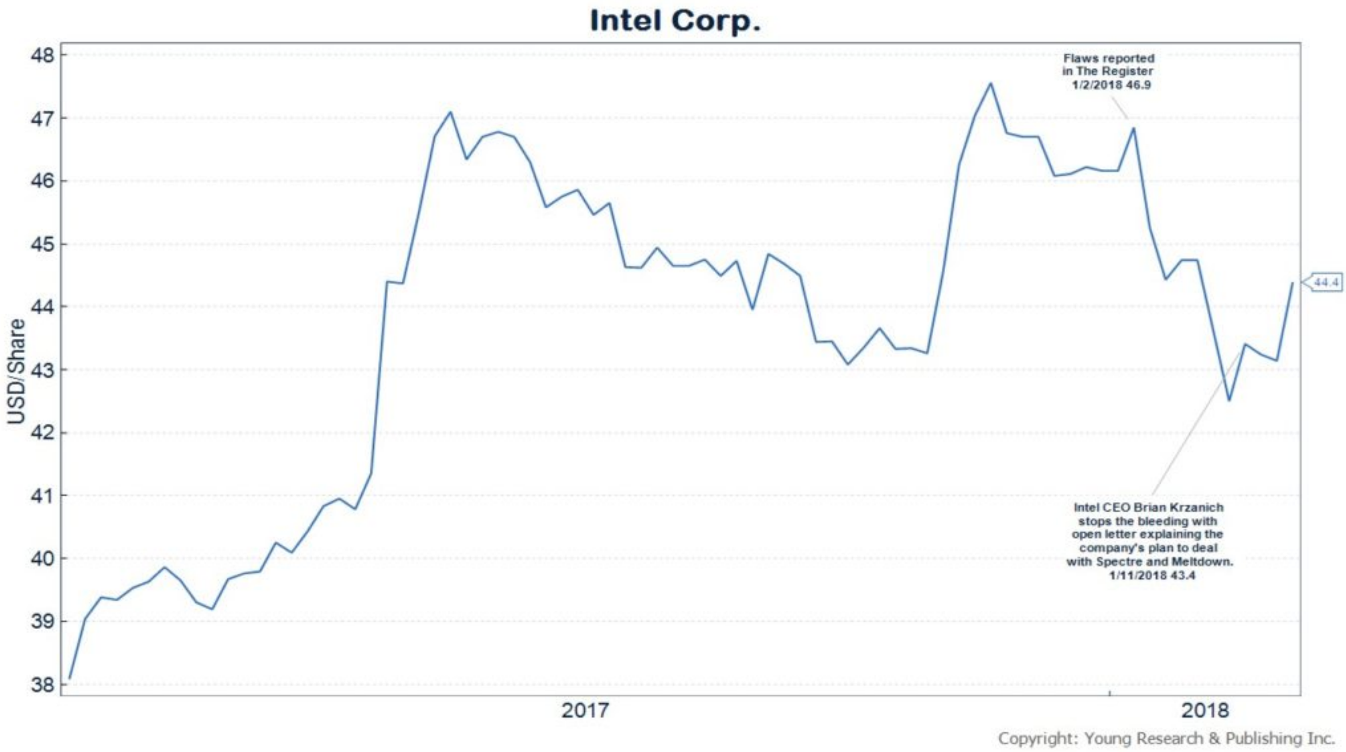
The bug was first reported in an industry journal known as *Electronic Engineering Times*, but when it was reported by the mass media on CNN on November 21, 1994, the stock dropped over 12.3% in a little less than a month. The stock only began gaining again after Intel offered a recall on December 20th.



Here We Go Again

Today Intel is in a somewhat similar, though not exact, position. A group of researchers connected by the Internet, have exposed a much larger flaw in Intel’s processors, and now the company needs to deal with the fallout.

The issues, known as Spectre and Meltdown, could potentially be used by hackers to attack computers using Intel processors. The news was again first reported in an industry journal, the *Register*, out of the U.K. But in today’s rapid information world, it didn’t take much time to disseminate to the market. Intel’s share price dropped over 9.2% in eight days.



Only after CEO Brian Krzanich wrote an [open letter] to the tech industry explaining Intel's next steps were investors willing to climb aboard Intel once more.

Do You Have a Game Plan?

I do not relay this story to you to shame Intel. What I want you to see here, is that companies often undergo rough periods. The tech industry in particular is prone to volatility thanks to complex products and low barriers to entry. The unexpected happens, and without a game plan you may see a lot of your own money wiped off the board quickly.

My game plan for decades has been one laid out first by Ben Graham in the *Intelligent Investor*. Graham wrote, "One of the most persuasive tests of high quality is an uninterrupted record of dividend payments for the last 20 years or more. Indeed, the defensive investor might be justified in limiting his purchases to those meeting this test." I would add to Graham's astute analysis that focusing on companies dedicated to increasing dividends helps as well.

What are Your Goals?

Another factor in investing is understanding the business you are investing in. Not many investors today can honestly say they understand what the Spectre and Meltdown flaws in Intel's chips really are. Are you prepared to invest in a company that builds a product you don't understand and can't explain? These shares are no doubt appropriate for some portfolios, but if risk avoidance is one of your goals, understanding the company from top to bottom is a good place to start.

I practice risk avoidance in all aspects of life, and especially in investing. If you are in or nearing retirement and are looking to relieve the burden of the work that must be done to minimize risk in your investment portfolio, I urge you to visit the website of my family run investment advisory, Richard C. Young & Co., Ltd. You can sign up for our client letter, free even for non-clients, to get a better idea of the principles used to make investment decisions.

Originally posted on January 19, 2018.

How Pennies Can Win the War

Back in January of 1987, Ronald Reagan gave a State of the Union address in which he lamented the brutal war being waged by the Soviet Union on the people of Afghanistan. Behind the scenes though, Reagan was operating what has become popularly known as "Charlie Wilson's War."

Reagan and his supporters in Congress, including Charlie Wilson, were sending Stinger missiles to the Afghans fighting against the Soviets. Those missiles cost pennies on the dollar compared to the Soviet MI-24 Hind gunships they were used to target with a lethal 79% successful kill rate.

The mere pennies the U.S. was spending on the war against the Soviets really added up. The massive cost of the war was a major contributing factor to the eventual breakup of the USSR.

The same month Reagan gave his address, I was writing to subscribers to encourage them to realize the value of their hard-earned pennies.

That month I wrote:

> *I've told you about the vital importance of dividends and compound interest. At a 10% return, money doubles in only seven years. One member of the highly successful Rothschild family referred to compound interest as the eighth wonder of the world.*
>
> *I'll always remember Bob Rose's historic note in The Wall Street Journal a while back. Bob wrote, "Early in the last century, an English astronomer, Francis Baily, figured that a British penny invested at an annual compound interest of 5% at the birth of Christ would have yielded enough gold by 1810 to fill 357 million earths."*

When put into terms of earths worth of gold, it is easy to see the value of compounding. All the mined gold in the world today would fit into a 68-foot cube. The idea of 357 million earths volume of gold is incomprehensible, but it makes the point Baily was getting at. A small investment can generate a powerful return.

At the end of his speech, Reagan told the American people "my fellow citizens, America isn't finished. Her best days have just begun." It was true. American went on to win the Cold War, becoming the undisputed most powerful nation on earth. It all started with an investment of what seemed like pennies in Afghanistan.

If you harvest the power of compound interest, your best investing days have just begun as well.

The Most Important Thing in Investing

Back in 2006 I was celebrating 20 years of writing *Intelligence Report*. Debbie and I were in Vermont, and had just visited Vermont's Authentic Designs to purchase lighting fixtures. The shop uses 150 year-old machines to manufacture colonial and early American lighting fixtures. There, on one of the machines for all the craftsmen to see was taped a sign that read "Simple is Sophisticated."

After reading that taped up sign in Vermont all those years ago, I adopted "Simple is Sophisticated," as a personal mantra to keep me focused on the essential elements of my investment strategy. The most fundamental of these, and the one I have employed to the greatest benefit to myself, and hopefully to you if you have been a subscriber or client, is compound interest. Below you will read the story of how I have employed compound interest to the benefit of my grandchildren, and how you can do the same. I wrote back in May of 2006:

> ***Rich as Croesus***
>
> *I want you to begin on your quest for sophistication through simplicity by focusing laser-like on compound interest. Here*

is an amazing story. I call it my grandchildren's "rich as Croesus" strategy. (Croesus was the last king of Lydia from 560–547 B.C.)

When each of my four grandchildren was born, I opened accounts for them at Vanguard's TaxManaged Growth & Income fund. Each year, I deposit $10,000 (and yes, I know you can now give away $11,000/year tax-free). The money is invested with little in the way of long-term tax implications. Let me show you how compound interest works its magic.

Gettin' Rich Slowly

If you invest for a compounded rate of return of 10%, it's easy to think that your long-term return would be twice the return gained by investing at 5%. That is not the case—not by a long shot. Let's take a long-term look here, for that is my intention with my grandchildren. Investing $10,000 at 5% for 50 years gives them $115,000—a staggering sum, to be sure. But at 10%, $10,000 grows to a mind-boggling $1,174,000 (that's million). Double the growth rate to 20% (admittedly unrealistic, but useful in this example), your $10,000 would become a stratospheric $91 million (over 77 times the return). And you thought you understood compound interest?

You and Counterbalancing

As noted, a 20% annual return year after year is unrealistic. But you can achieve really terrific success, most conservatively, by counterbalancing your portfolio with fixed-income and common stocks. …

In 1989, the editors of Fortune published an article headed, "A Low Risk Path to Profits" profiling Loews Corp. money manager Joseph Rosenberg. Fortune noted that J.R. believed so fervently in the awesome power of compound interest that he carried a compound interest table in his pocket at all times.

> *Sayeth J.R., “It is the most important thing in investing.” As the article noted, it’s foolish to undermine the power of compounding by taking big risks that kick you out of the game.*

As Rosenberg noted then, compound interest “is the most important thing in investing.” If you want to succeed as an investor for your family, your grandchildren, or yourself, stay focused on the simple, yet sophisticated strategies that really make a difference.

Compound Interest is Key

For prudent investors, the last three years have meant watching the so-called FAANG stocks (and other speculative shares) rise at a rate that is seemingly unbounded by profits or dividends. The FAANGs have gobbled up an ever-larger portion of the S&P 500 index total market capitalization. Four of the five largest companies in the S&P 500 are now FAANGs.

Today’s market environment feels similar to the late 1990s when speculation was dominant. To successfully navigate the environment then, I advised a focus on patience and compound interest.

> *Compound Interest Is the Key*
>
> *Legendary investor Phillip Carret used to say that investing genius consisted of one part patience, and one part compound interest. And Charlie Munger, Warren Buffett’s long-time partner, will tell you that he is rarely without a compound rate-of-return table. As Munger says, “Understanding both the power of compound return and the difficulty of achieving it is*

> *the key to investing."*
>
> *If you adhere to a base of value, keep your portfolio turnover low to cut costs and taxes, and rely on the miracle of compound interest, you will set yourself on the safest and surest course to profit both this year and in future years. Craft your portfolio with counterweight building blocks that allow you to ride out the vagaries of the marketplace.*
>
> *Last year was the third consecutive year that growth stocks outran value stocks. But remember, growth and value tend to produce similar returns long term. One sector is ahead for a period, then the other has its day. Back in the two-tier market of the early 1970s, growth stocks had a field day at the expense of value stocks. But over the next decade, it was another matter. Value stocks clobbered growth stocks, and it's value stock that are cheaper now in 2000.*

The same advice can be given today. Patience and compound interest never go out of style.

Dow Down Over 1,000 Points

What great news for me and for you if you are actually an investor. I mean a real, seasoned investor. One who embraces common sense, patience and the acuity that comes with decades studying the power of consistent cash flow matched with the most powerful word in investing: *compounding*.

My business is, as are my own portfolios, based on exactly these concepts. Market volatility has zero to do with dividends, interest (the source of cash flow), or compounding. Absolutely zero.

In that I have no plans to sell my major holdings (many owned for decades), I am not concerned about short-term market swings. What does cause me to pay close attention is the potential opportunity to invest my regular cash flow more advantageously than during periods of market buoyancy. That's just common sense, is it not?

So, let's look at some of the information I urge my clients to use to make steady, long-term investing decisions. Linked here is intelligence you can actually use to improve your long-term investment acuity.

The *Young's World Money Forecast* (my online home base for intelligence gathering) display looks at 10 blue-chip long time Dow dividend payers with solid dividend growth prospects. Keep this invaluable little menu at hand for regular reference during periods of opportunity brought about by normal and expected short-term financial markets volatility.

Warm regards,

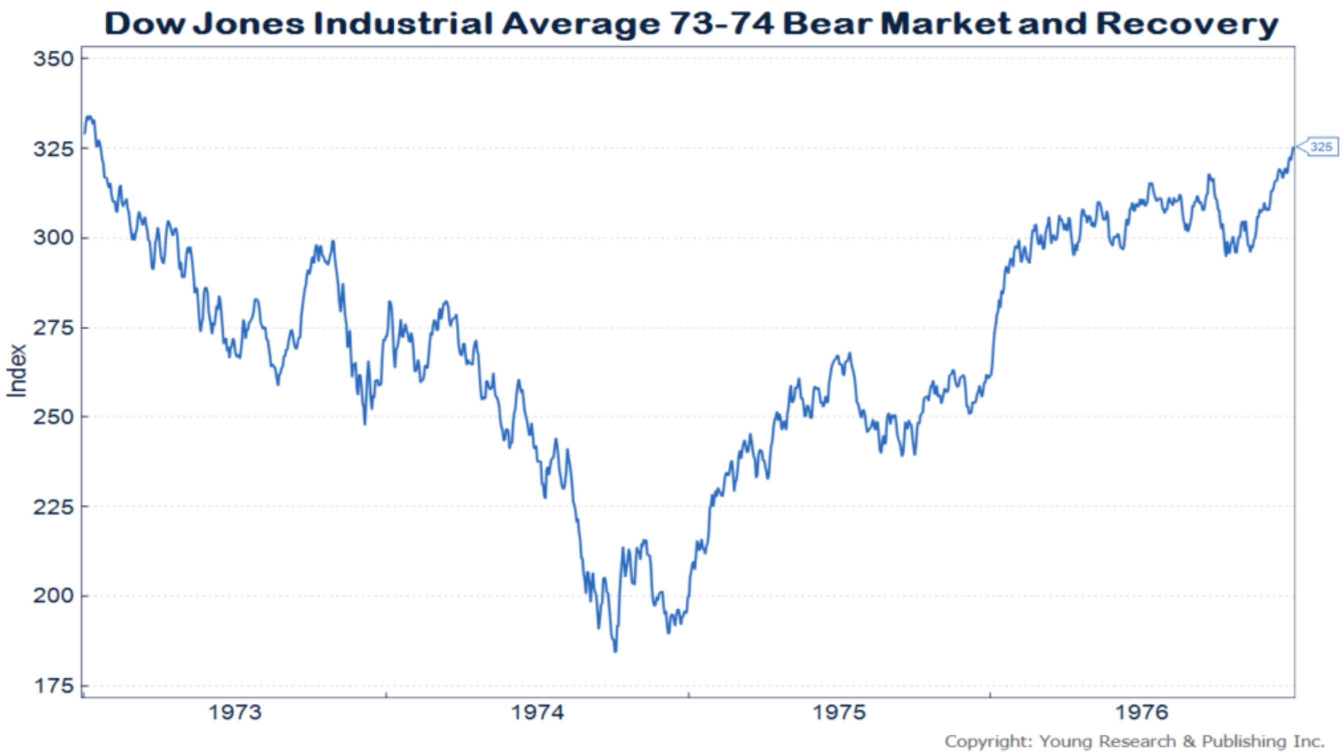
Dick

Rising Dividends: Decades of Focus on a Winning Strategy

In 1987, I sat down with Bill Lippman for a conversation about L.F. Rothschild Fund Management's "Rising Dividends Fund." Bill had been the founder and president of the Pilgrim Group mutual funds for 25 years before he sold the firm. Bill then moved over to the New York based, L.F. Rothschild Fund Management, at the time a new subsidiary of L.F. Rothschild investment bank. (The Rising Dividends Fund would later become the Franklin Rising Dividends Fund, which still trades today, though this is not a recommendation to buy).

The Rising Dividends Fund focused on what I have been recommending to my readers for years; solid companies with strong records of increasing dividend payouts. I have been focused on dividend payments since my days at Babson reading Ben Graham and David Dodd.

Bill was interested in rising dividends as a way to protect his fund's owners from experiencing the type of punishment in their portfolios they felt in the bear market of 1973-1974. Those unhappy days of "stagflation" saw unemployment of 8.5%, CPI increases of up to 11%, and a drop in the Dow Jones Industrial Average of 46%. Afterward, investors were not eager to have their savings ripped apart again. The pain was so bad that even in 1987 when Bill and I discussed his Rising Dividends Fund, the lessons of 73-74 were still remembered well.



When we talked, Bill said “In 1973-1974, we had a really bad market. It was a disaster…and it went on and on for a couple of years. It seemed like it would never end. One then asks, ‘Is there a better way?’ As it turns out, yes, there is a better way. You must have a philosophy, and you must stick to it. Don’t be the victim of the latest hot story that comes off the tape. And that’s what we did that was different. We evolved a philosophy that made sense. We selected companies that increased dividends and had low debt and low P/Es. We wanted a solid game plan that we could follow with comfort through good markets and bad.”

My focus for you today, just as it was in 1987, is on quality dividends from companies that are dedicated to increasing their payouts. As part of the RCs program at Richard C. Young & Co., Ltd., and in my recent coverage of the Dow stocks here on *Youngsworldmoneyforecast.com*, I consistently focus on finding companies that do just that.

Another thing Bill said in our discussion that really resonated with me was a piece of advice he gave to all investors “Put down in writing what you really believe in, and then stick to it.” I encourage you to do that right now. Don’t wait until later, or let inertia allow you to forget. Do it right now. Write down what you want to accomplish by investing, and how you plan to do it. Then stick to it.