Insights, Tacit Thought | Weekly Investment Insights

# Dividend Aristocrats

Published on: 21 October, 2022 | Author: Investment Team

Dividends are a crucial component of any long-term equity strategy and, simply put, might be the only tangible return earned by the permanent owner of an equity asset. They significantly contribute to long term equity market performance (between 30% and 50% of total returns depending on the market in question) and excepting corporate action, drive capital appreciation by virtue of investors' expectations of future payments.

Standard & Poor's maintains an index of US businesses with exemplary dividend records, the 'Dividend Aristocrats'. The index tracks the performance of a sub-set of S&P 500 companies that have not only paid a regular dividend over the long term but have grown their dividend annually for the past 25 years. Despite the strict criteria, over 10% of the S&P 500 index constituents actually meet this criteria encompassing a broad range of sectors and industries.

Technology companies are notable by their absence from the index, but this is not a surprise to us. Many will think that as most IT or computing firms are young companies, they probably haven't been around long enough to meet the 25-year record required for inclusion in the index.  However, listed technology companies have roots dating back to the early 20th century; IBM listed in 1915. Maybe the more salient point is that technology changes at such a pace that most of these companies do not survive as independent businesses for as long a period as 25 years. The simple fact for this sector is that most tech companies have to reinvest retained earnings, either to take advantage of growth opportunities, or to protect themselves from the attack of disruptive developments.

So, what does 25 years of dividend increases actually tell us about a company's performance over that time, and does it give any clue as to its future? Looking at the long term performance of the whole Dividend Aristocrats index, it would seem that this group of companies have performed well. In the 32 years since the end of 1989 (the earliest available year that S&P provides data for), the index has produced a total return of 11.0% per annum, well ahead of the S&P 500 return of 8.3%.

Is this a surprise? Maybe not. A company that's been able to grow its dividend over such an extended time period might be expected to outperform the market.

Nothing about the future is assured however. Several companies have fallen off the index after long and venerable runs, indicating that aristocratic status today provides no guarantees for tomorrow. Looking back to the Index's composition ten years ago confirms that warning. Just under half (29) of the 61 companies in the index in 2012 have survived as dividend aristocrats today.

Clearly only the best are able to persistently withstand erosion from competitive forces over such a long time frame. At Tacit, we firmly believe that well managed companies with stable cashflows should form the core of all of our strategies. The statistics above only reaffirm our belief during volatile times such as now.

We held our inaugural 'Tacit Thought Live' event this week discussing our approach to investing, current issues including Gilt prices and our economic and strategic outlook. A recording of the event can be accessed here using passcode: !r+2cjH+