McCarthy Asset Management, Inc.
Personalized Wealth Management

THEME: DIVIDEND-PAYING STOCKS

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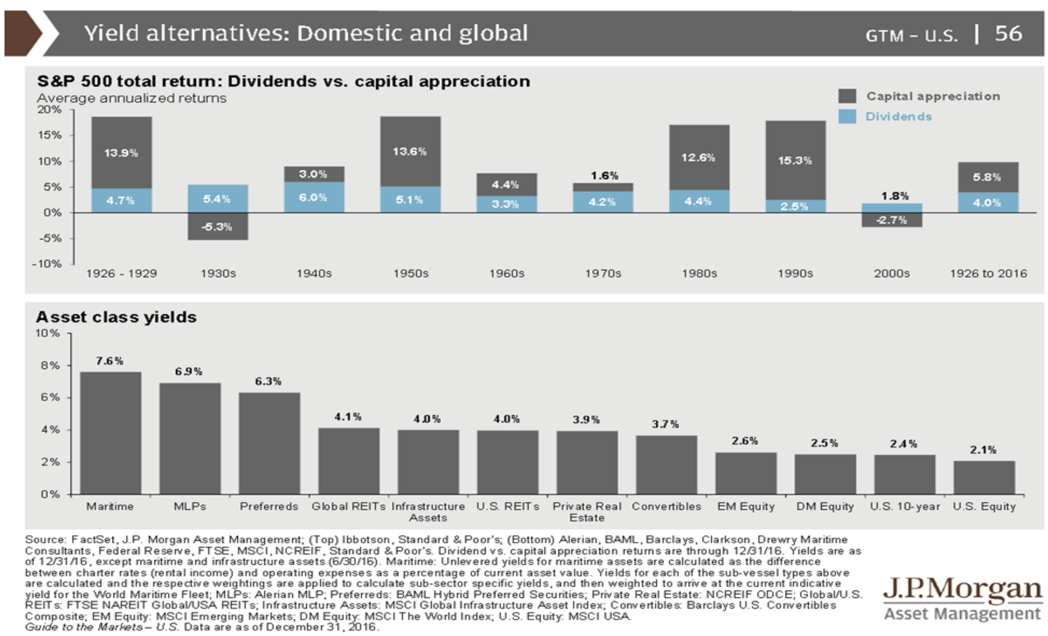
"While they can have periods of underperformance, historically, stocks that pay a dividend have outperformed non-dividend paying stocks."

McCarthy Asset Management, Inc. is an independent, fee-only investment advisory firm that has been helping people invest wisely for over fifteen years. Our mission is to help you better understand and improve your financial situation. We specialize in Retirement Planning, Portfolio Management and Tax Planning.

For a number of years, an important focus for MAM has been on mutual funds and ETFs that invest in dividend-paying stocks. For instance, the ETF Vanguard Dividend Appreciation (symbol VIG) was added to portfolios in November of 2009 and the ETF Schwab U.S. Dividend Equity (symbol SCHD) was added in November of 2012. Other dividend-focused funds used in portfolios include American Funds Capital World Growth & Income, American Funds Income Fund of America and Matthews Asia Dividend Investor. The purpose of this article is to explore the rational and benefits of investing in dividend-paying companies:

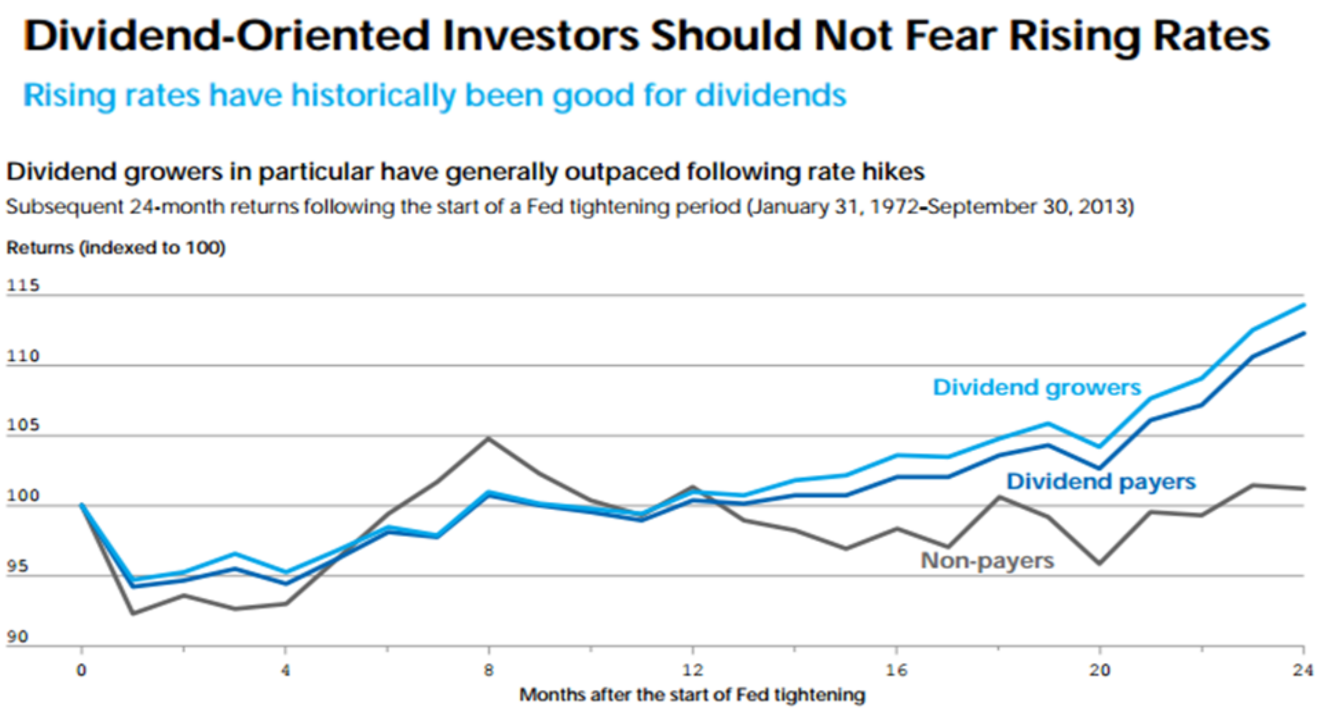
- **Dividend income and its reinvestment have comprised a significant portion of long-term stock gains.** As can be seen in the column on the upper right in the J.P. Morgan chart below, from 1926 through 2016, stocks returned 9.8% per year. Over 40% of that annual return, or 4.0%, was from dividends, with the remaining 5.8% from capital appreciation.



- **Dividend-paying stocks have delivered better long-term total return performance than non-dividend payers.** According to data compiled by Professors Fama & French, from 1927 to 2014, dividend payers rose 10.4% per annum compared to non-dividend payers, which rose 8.5% per annum. (See this article from The Motley Fool which is one of many I found that quoted these returns.)

- **Dividend income can provide valuable downside protection when stock prices are falling.** As can be seen in the chart above, since 1930 there were two decades when stocks had negative capital appreciation (i.e. the 1930s and 2000s). During both periods, dividend income provided important support to performance.

Dividend-paying stocks have performed well in past periods of rising interest rates as can be seen in the chart below from The Capital Group and Ned Davis Research. This is important because we are now in a period of rising interest rates.



Source: Capital Group; Ned Davis Research, Inc. © 2011 Ned Davis Research, Inc. Further distribution prohibited without prior permission. All rights reserved. Disclaimer is at www.ndr.com/copyright.html. For data vendor disclaimers, refer to www.ndr.com/vendorinfo. The chart is based on an equal-weighted geometric average of the historical total return of dividend-paying and non-dividend paying stocks. Dividend growers, payers, and non-payers are sub-components of the S&P 500 Index. The categories are created using actual annual dividends to identify dividend-paying stocks and are rebalanced annually. The dividend policy for each stock is determined on a rolling 12-month basis. The periods shown do not represent the full history of the S&P 500 Index. Start of tightening cycle determined as of the end of any month during which the Federal Reserve fi rst raised the target fed funds rate following a period of stable or declining interest rates; periods measure the 24 months following 1/31/1973, 9/30/1977, 9/30/1980, 9/30/1987, 2/28/1994, 7/31/1999 and 7/31/2004.

Our Services

Investment Management Services:

- MAM creates and manages customized investment portfolios based on each client's investment objectives, timeframe and risk tolerance.

Financial Planning Services:

- The Net Worth Analysis (NWA) tracks the accumulation of Invested Assets for pre-retirees and the retention of Invested Assets for retirees. Updated annually.
- "Retirement Analysis" a comprehensive analysis of your retirement goals, which produces easy-to-read, interactive working plan, stored in the cloud. Updated as needed for life events.

Tax Services:

- Clients have the option of utilizing the income tax services provided through the firm Stephen P. McCarthy, CPA. These services are offered at an hourly rate and may include:
    - Tax Return Preparation
    - Income Tax Projections
    - Tax Minimization Ideas
    - Tax Authority Representation

Other Services:

- MAM has retained several outside experts, whose services are available at no cost to our clients:
    - Medicare Planning– Eileen Hamm of Superior LTC Planning Services, Inc.
    - Long Term Care Planning– Allen Hamm of Superior LTC Planning Services, Inc.

Periods of Underperformance: There have been periods when dividend payers underperformed non-dividend payers. Typically, this has occurred at the start of a bull market when stocks are significantly undervalued. During this time, the riskiest stocks, which often don't pay a dividend, perform the best. This was the case starting in March of 2009 with the dramatic recovery in stock prices after the end of the financial crisis. Given the current bull market is now about to start its 9th year, this is an aging bull market with dividend payers likely to once again outperform.

The Best Dividend Stocks to Invest In: Which dividend-paying stocks perform the best? While it may be tempting to go for those paying the highest yield, this could lead investors to companies with little to no growth opportunities, or worse, ones in distress. Per studies from Ned Davis Research and others, over time the best performing stocks are those pay an increasing dividend. This is the focus of the two dividend ETFs (SCHD and VIG) used in MAM portfolios.