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Markets and Economies

Dividend Growers: A Less Volatile Approach to Building Long-Term Wealth

"Time in the market is more important than timing the market" is a concept that's especially relevant for those investing in quality stocks. Here's why.

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Key Takeaways

- Investors have historically shown a tendency to reduce equity exposure after market drawdowns.
- We believe that the long-term benefits of equity market compounding are powerful and attempting to time the market can result in less favorable outcomes.
- Identifying a diversified strategy that focuses on owning high-quality dividend-growth companies can provide investors with lower volatility, superior risk-adjusted returns, and perhaps lessen the tendency to reduce exposure to the market at inopportune times.

Buy low and sell high! This strategy has been preached since the beginning of investing. The thinking behind this maxim: When the equity market is expensive, investors should sell their winners and capture some of their hard-earned gains. When stocks are seen as cheap, often after a market downdraft, investors should increase their equity exposure and position themselves for future appreciation.

This approach is simple conceptually, yet it is much more complicated to execute in practice. Peaks and troughs are not necessarily foreseeable, and it is difficult to determine the duration of upward or downward moves in the equity market. This is why history has shown that those who stay invested, or those who invest at regular intervals, have had much better outcomes than those who tried to time the market.

Despite this evidence, investor behavior still shows a reluctance to stay invested in equity markets after periods of weak returns. Over the last 25 years, whenever major U.S. stock indexes had a double-digit drawdown over a quarter, it was common to see net outflows in the equity markets. In almost every instance, the market rebounded strongly over the following 12 months, meaning that some investors inverted the old cliché and "sold low," missing out on that recovery (Figure 1).

Figure 1. Investors Exiting the Market During Drawdowns Have Missed Out on Major Recoveries

Data for the S&P 500® Index for the indicated periods

Date	Quarterly Performance	Net New Flows ($M)	Subsequent 1-Year Return
2008-Q4	-21.94%	($44,346)	26.46%
2020-Q1	-19.60%	($68,002)	56.35%
2002-Q3	-17.28%	($45,042)	24.40%
2022-Q2	-16.10%	($41,649)	19.59%
2001-Q3	-14.68%	($5,871)	-20.49%
2011-Q3	-13.87%	($42,385)	30.20%
2018-Q4	-13.52%	($23,825)	31.49%
2002-Q2	-13.40%	$7,984	0.25%
2001-Q1	-11.86%	$15,533	0.24%
2010-Q2	-11.43%	($10,945)	30.69%
2009-Q1	-11.01%	($21,820)	49.77%
	AVERAGE	**($25,488)**	**22.63%**

Source: Morningstar. Performance based on total return of S&P 500® Index in the periods following quarterly declines of 10% or more since Q4 2008.

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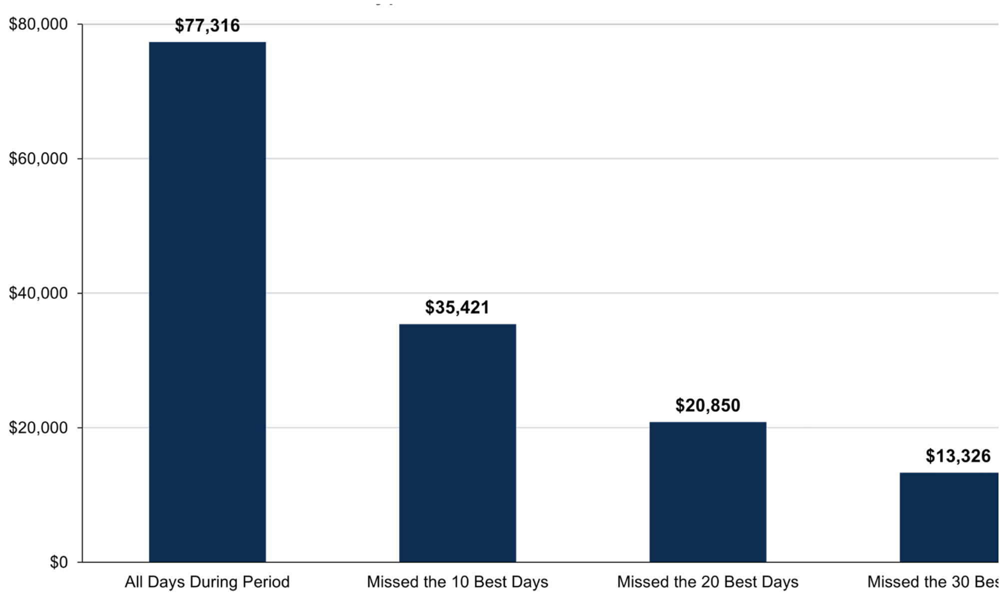
Why Staying Invested Matters

The goal of investing is long-term wealth creation. This wealth creation is highlighted by two distinct phases. The first phase is wealth accumulation. Historically speaking, equities have been one of the most compelling asset classes to help build long-term wealth. While the percentage of one's allocation to equities depends on their own time horizon and goals, we believe it is imperative to be steadfast in whatever that equity allocation is supposed to be. If we look at the last 25 years, missing the best 10, 20, or 30 days in the market had a profound impact on an investor's portfolio (Figure 2). For example, if you missed the 10 best-performing days in the U.S. equity market, you would have a portfolio less than half the size of someone who remained fully invested in equities.

Figure 2. Equity Investors Who Stayed the Course Have Benefited the Most

Hypothetical growth of a $10,000 investment in the S&P 500® Index from January 1, 1998, to December 31, 2024



Source: Standard & Poor's and Lord Abbett. Returns are measured based on the S&P 500® Index from January 1, 1998, to December 31, 2024.

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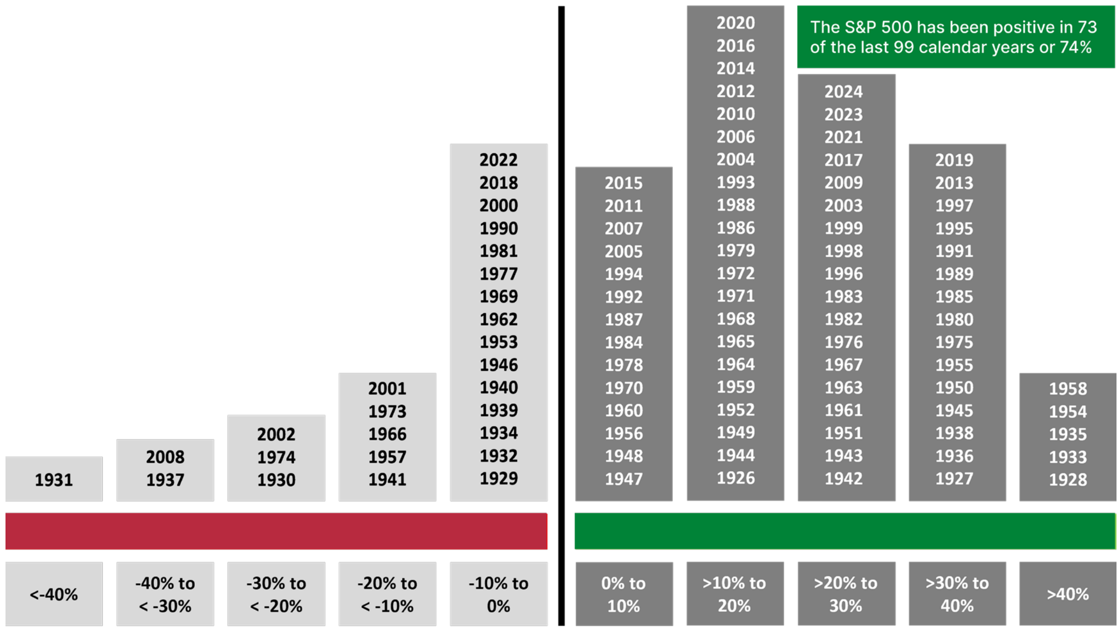
If we are focused on long-term wealth creation, then we should measure returns over longer periods than a few days, one quarter, or even one year. Looking at annual returns of the S&P 500® Index since 1926, we can see that returns have been positive almost 74% of the time (Figure 3). Over five-year rolling periods, this increases to 88%. Over 10-year periods, returns were positive 94% of the time. This further demonstrates the impact of remaining invested in equities through full market cycles; it has been rare to experience losses when measuring returns through such a long-term lens.

Figure 3. Through the Decades, Staying in the Market Has Built Wealth

Yearly return data for the S&P 500® Index, 1926–2024



	Number of Periods			Percent of Periods	
	Positive	Negative	Total	Positive	Negative
Calendar Year Returns	73	26	99	73.7%	26.3%
Rolling 1 Year Returns, Monthly	892	291	1183	75.4%	24.6%
Rolling 5 Year Returns, Monthly	1004	130	1134	88.5%	11.5%
Rolling 10 Year Returns, Monthly	1016	58	1074	94.6%	5.4%

Source: Standard & Poor's and Lord Abbett. Returns are measured based on the S&P 500® Index from January 1, 1926, to June 30,2025.

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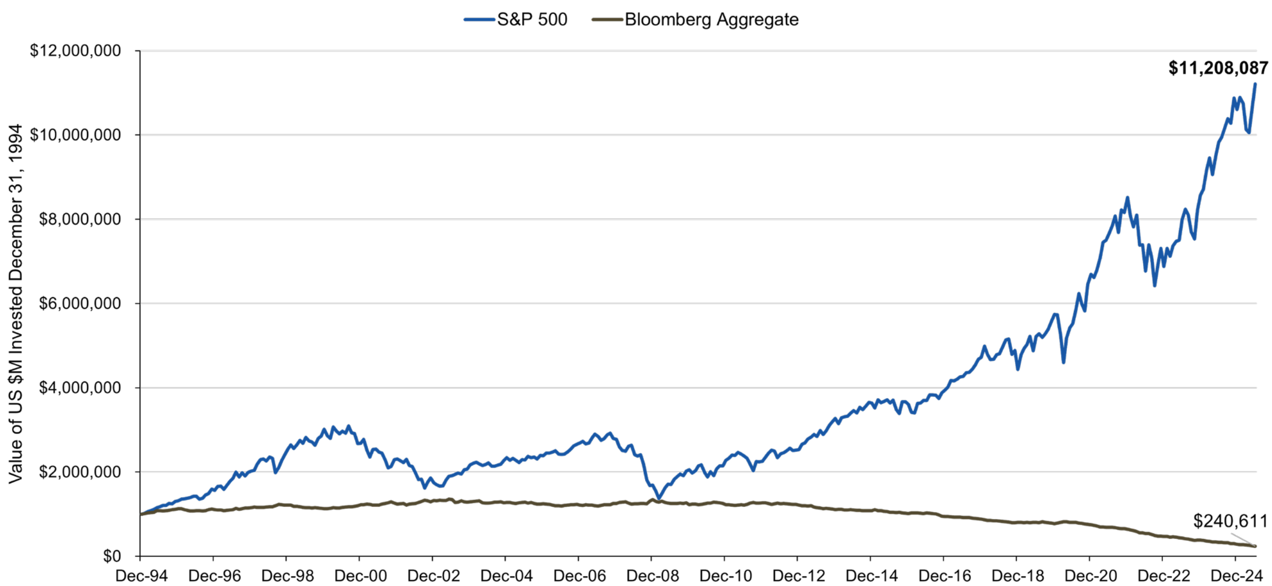
The second phase of long-term wealth creation is wealth preservation during retirement. Over the last three decades, investors have experienced three major market downturns: the 1999-2000 "tech bubble," the global financial crisis of 2008–09, and the onset of the COVID-19 pandemic in early 2020. In each of these periods, investors fled from equity markets in an attempt to preserve assets. Yet, a hypothetical investment in the S&P 500 versus a fixed-income alternative, the Bloomberg US Aggregate Bond Index (with 5% withdrawals adjusted for inflation), shows two entirely different retirement outcomes (Figure 4). One investor is making ends meet, while the other has a lot of flexibility in their retirement lifestyle and estate planning.

Figure 4. How Two Different Retirement Portfolios Have Fared Over the Past 30 Years

Hypothetical growth of a $1,000,000 investment in the S&P 500® and Bloomberg U.S. Aggregate Bond Indexes from December 31, 1994, assuming annual 5% withdrawals, to June 30, 2025



Source: Standard & Poor's and Lord Abbett.

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Regardless of whether an investor is in the accumulation phase or the preservation phase, it's worth repeating that it is important for investors to focus on "time in" the market as opposed to "timing" the market.

Weathering Tough Times with Dividend Growers

We believe a thoughtful and diversified approach is vital to weathering periods of market drawdowns. It is important to remain invested in the equity markets, as the potential for long-term growth can lead to a larger nest egg in retirement. Yet, it is sometimes inevitable for emotional decision-making to take over during uncertain time periods. We think one way of alleviating this stress is by selecting a portfolio that has demonstrated lower historical volatility. If we look at the last 50 years of data, high-quality companies that are initiating and growing dividends have had higher returns and lower volatility than the equal-weighted S&P 500® Index as shown in Figure 5.

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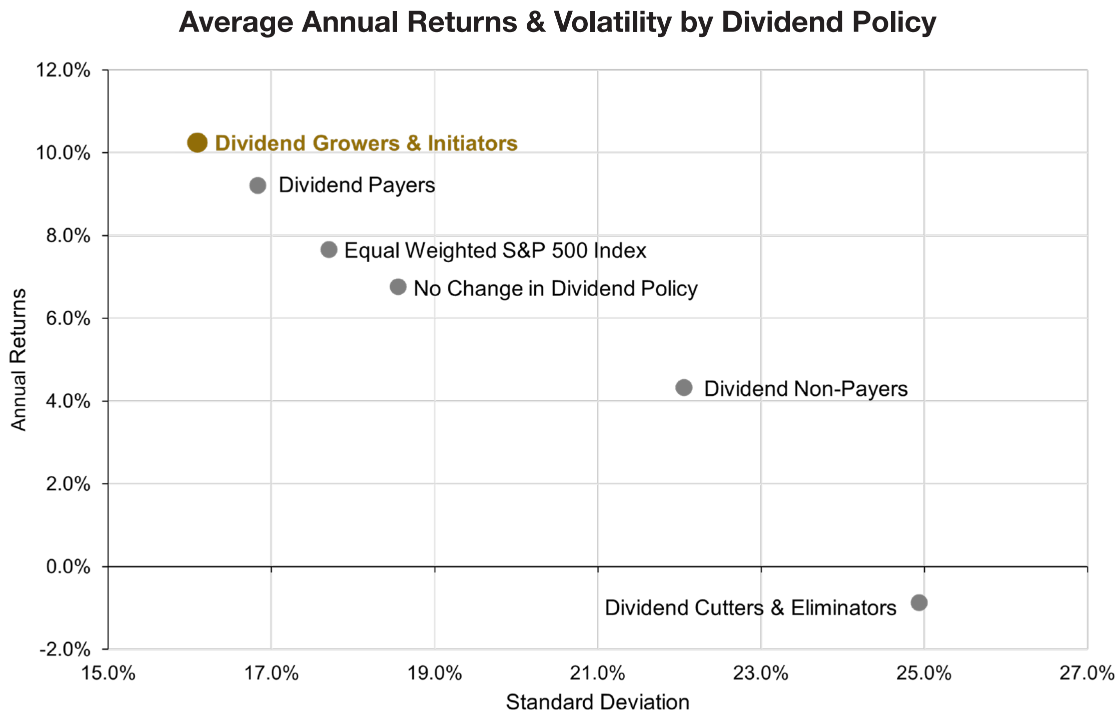
Figure 5. Dividend Growers Have Offered Higher Returns with Less Volatility

Data for the S&P 500 Index, January 31, 1973–December 31, 2024



Source: Ned Davis Research. Latest available full-year historical data.

Dividend policy: A stock is classified as a dividend payer if it paid a cash dividend any time during the previous 12 months; a dividend grower if it initiated or raised its cash dividend at any time during the previous 12 months; and a non-dividend payer if it did not pay a cash dividend at any time during the previous 12 months. A company's dividend payments may vary over time, and there is no guarantee that a company will pay a dividend at all.

Standard deviation is a statistic that measures the dispersion of a data set relative to its mean. The higher the standard deviation, the further the observed data are from the mean.

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While this chart shows a slight deviation between dividend growers and dividend payers, in recent years, we've seen a higher dispersion. Since 2020, the markets have endured a COVID-19 shutdown, the inflation-driven correction of 2022, a narrow market rebound led by mega cap tech names, and tariff uncertainty due to a volatile trade war. In Figure 6, we examine how three indexes performed across these events, one of which is dividend-growth focused, and the other two centered on high dividend yield. The S&P U.S. Dividend Growers Index significantly outperformed the two yield-focused indexes while displaying much lower volatility. While dividend payers across the board provided strong downside capture, we can see that dividend growers didn't sacrifice on the upside to accomplish this, which resulted in stronger absolute and risk-adjusted performance.

Figure 6. Dividend Growers versus High Dividend Yield

Return and Risk Data for S&P U.S. Dividend Growers, Dow Jones U.S. Select Dividend, and S&P High Yield Dividend Aristocrats

Time Period: 3/1/2020 – 6/30/2025

	S&P US Dividend Growers	DJ US Select Dividend	S&P High Yield Dividend Aristocrats
Cumulative Return	104%	81%	69%
Standard Deviation	15.44%	18.66%	17.02%
Sharpe Ratio	0.76	0.54	0.50
Upside Capture	85.10%	78.00%	76.60%
Downside Capture	84.70%	84.10%	88.20%

Source: Morningstar, Standard & Poor's, Dow Jones Indices. Latest available historical data. Capture ratios are relative to the S&P 500® Index. The S&P U.S. Dividend Growers index tracks U.S. companies that have increased their dividend per share for at least 10 consecutive years while excluding the top 25% highest-yielding eligible companies. The Dow Jones U.S. Select Dividend Index consists of the top 200 companies based on dividend yield in the Dow Jones U.S. Index. The S&P High Yield Dividend Aristocrats is a dividend-yield-weighted index of stocks in the S&P Composite 1500 that have increased their dividend per share for the last 20 consecutive years.

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Lower volatility may mean investors will be less likely to reduce equity exposure following a market drawdown. In a sense, if the drawdown is less severe or perhaps just lower than the overall S&P 500, an investor may be less likely to reduce equity exposure at an untimely moment. The outcome of owning a lower-volatility portfolio of dividend growth companies may mean not only superior risk-adjusted returns but also a better "lived outcome;" one that is devoid of the risk of market timing that can limit long-term returns. Such an approach may leave investors in a better position to grow their wealth over the long term—and provide themselves with a more assured financial future.

Glossary & Index Definitions

Dividend policy: A stock is classified as a dividend payer if it paid a cash dividend any time during the previous 12 months; a dividend grower if it initiated or raised its cash dividend at any time during the previous 12 months; and a non-dividend payer if it did not pay a cash dividend at any time during the previous 12 months.

Downside/Upside capture: These ratios measure a manager's performance in down or up markets relative to a particular benchmark. A down market is one in which the market's quarterly (or monthly) return is less than zero; an up market is greater than zero. For example, a downside capture ratio of 50% means that the portfolio's value fell half as much as its benchmark index during down markets.

Sharpe ratio is calculated by taking an asset class's (or portfolio's) excess return above the risk-free rate and dividing it by the standard deviation of its returns. The greater the Sharpe ratio, the better the risk-adjusted performance has been.

Standard Deviation measures the dispersion of data from the mean. Applied to a rate of return, standard deviation is an indication of an investment's volatility.

The **Bloomberg US Aggregate Bond Index** represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment-grade, fixed-rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

Bloomberg Index Information
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The **Dow Jones U.S. Select Dividend Index** aims to represent the U.S.'s leading stocks by dividend yield.

The **S&P 500® Index** is widely regarded as the standard for measuring large cap U.S. stock market performance and includes a representative sample of leading companies in leading industries. The S&P 500 Equal Weight Index (EWI) includes the same constituents as the capitalization-weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight—or 0.2% of the index total at each quarterly rebalance.

The **S&P High Yield Dividend Aristocrats Index** is designed to measure the performance of companies within the S&P Composite 1500 that have followed a managed-dividends policy of consistently increasing dividends every year for at least 20 years.

The **S&P U.S. Dividend Growers Index** is designed to measure the performance of U.S. companies that have followed a policy of consistently increasing dividends every year for at least 10 consecutive years. The index excludes the top 25% highest-yielding eligible companies from the index.

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