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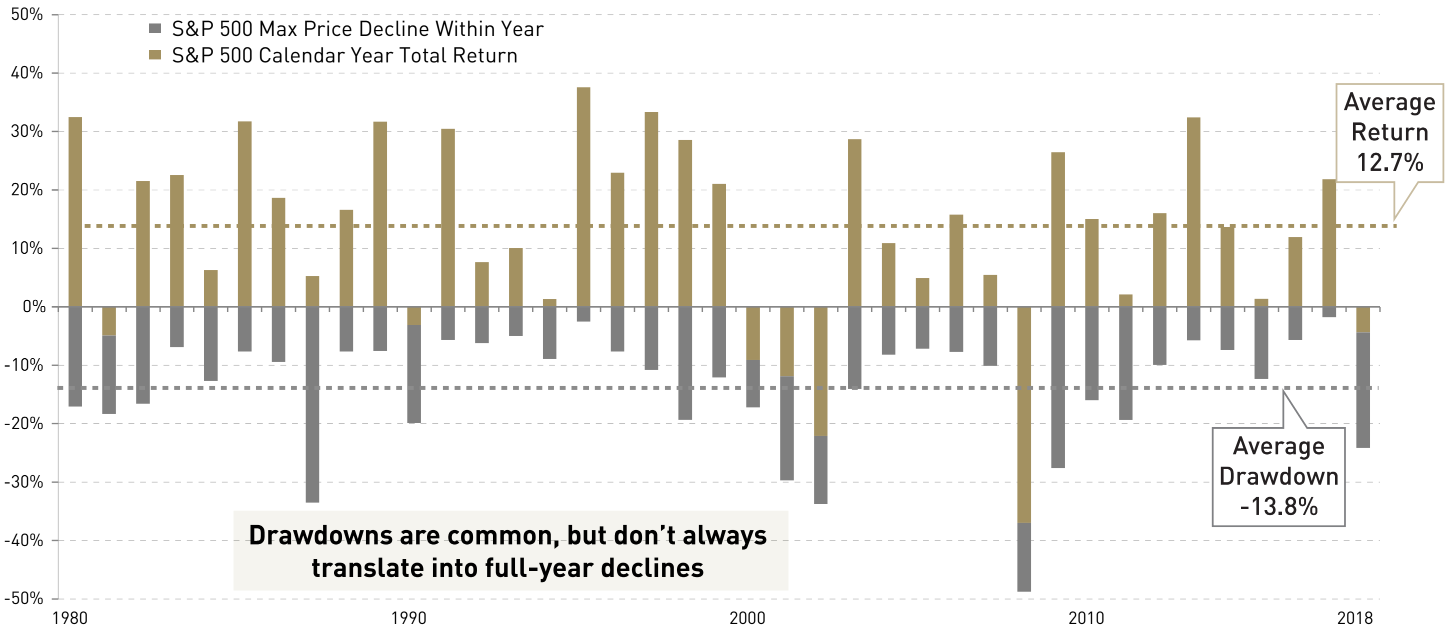
# MARKET VIEW

## DIVIDEND-GROWTH STOCKS: AN ALTERNATIVE TO MARKET TIMING

*Instead of jumping in and out of stocks, investors may be better served by understanding the types of equities that historically have performed relatively well during bouts of market volatility.*

### CHART 1. SHORT-TERM MARKET DECLINES ARE NORMAL

ANNUAL TOTAL RETURNS VERSUS MAXIMUM PRICE DECLINES (AS OF DECEMBER 31, 2018)




Source: Morningstar.

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**Past performance is not a reliable indicator or guarantee of future results.**

## IN BRIEF

- Retail investors pulled nearly $20 billion out of equities in December 2018, missing out on the best January in U.S. equities in 30 years.
- Investors were responding to an uptick in volatility and concerns of an end to the long-running bull market.
- Investors would have been better serviced by investing in dividend growers, which historically have performed relatively well during bouts of market volatility.

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After a December that marked the worst month for U.S. equities since the Great Depression, the U.S. equity market (as measured by the S&P 500® Index) experienced a robust rebound in January 2019, returning 8.01% - its strongest month since October 2015 and only the sixth time that U.S. equities have returned more than 8% in a month since the market bottom in March 2009 (out of 119 months), according to Standard & Poor's.

Unfortunately, many investors missed out on the best January in 30 years. Retail investors pulled nearly $20 billion out of equities (mutual funds and ETFs) in the month of December, according to Morningstar, (the ninth largest month of equity outflows since the market bottom in March 2009).

As we discussed recently, it is no secret that market timing is an inherently difficult task for investors at all levels of sophistication, yet many still find themselves susceptible to the market timing trap and its potentially severe repercussions. Just missing the 10 best days in the market over the past 25 calendar years would have reduced returns by more than 50%. Missing the 20 best days was even worse, reducing returns by 69%, while being absent for the 30 best days would have cost a staggering 80%, according to Morningstar.

With the uptick in volatility over the past year, and driven by fears that the nearly decade-long bull market is nearing its end, it has become common for investors to treat bouts of volatility as an imminent sign of a prolonged bear-market (while fundamentals may still suggest otherwise). Instead, investors may be wise to remember that intra-year market pullbacks are not uncommon; in fact they happen almost every year as shown in Chart 1.

Despite the regularity of intra-year market pullbacks, it is important to remember that equities still managed to finish higher in most of the past 90 years and have delivered returns greater than 12% nearly three-quarters of the time.

So what does this mean for investors who are nervous about increased volatility in the market? For those who lack clairvoyance, the historical return profile of the market suggests that moving to the sidelines in expectation of a drawdown—even if perfectly timed—may simply put an investor's long-term results at risk by missing a subsequent recovery.

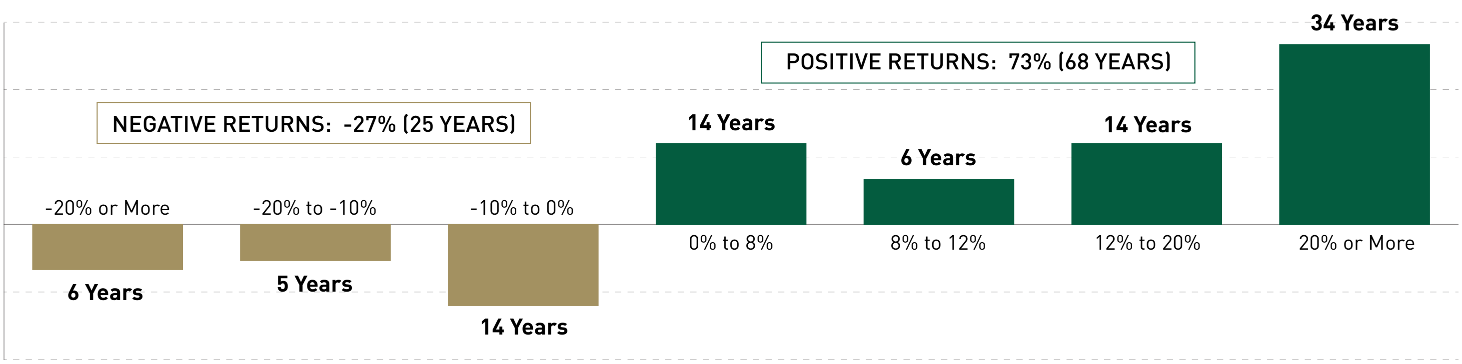
Instead of jumping in and out of stocks, investors may be better served by understanding the types of equities that have, historically, performed relatively well during bouts of market volatility. One such type is a company that has a historical track record of consistent dividend growth. As shown in Table 1 (on next page), stocks of such companies have tended to outperform amid market declines, capturing just 87% of market downside on average during each of the largest drawdowns over the past 10 years.

### Summing Up

For investors concerned about a potential market pullback, a steady allocation to dividend-growth stocks might help improve outcomes compared with precipitous, and previously futile, efforts to time market tops and bottoms. In this regard, dividend growers could offer a less stressful alternative during periods of market volatility. In particular, investors may wish to consider portfolios from active managers with deep experience in evaluating and selecting stocks with a strong dividend-growth pedigree— and the potential for continued dividend increases over the long term.

**CHART 2. SINCE 1926, POSITIVE ANNUAL RETURNS HAVE OUTNUMBERED NEGATIVE RETURNS, 68 TO 25.**

ANNUAL TOTAL RETURNS FOR THE S&P 500 INDEX, 1926-2018




Source: Morningstar, S&P Dow Jones Indices, and Lord Abbett.

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### TABLE 1. HISTORICALLY, DIVIDEND GROWERS HAVE OUTPERFORMED IN MARKET DECLINES

MAXIMUM INTRA-YEAR DECLINES OVER THE LAST 10 YEARS, START DATES INCLUSIVE, AND DOWNSIDE CAPTURE

| Max S&P 500 Annual Drawdown Period | S&P 500 Index Return | Dividend Growers[1] Downside Capture |
|---|---|---|
| 10/10/2007 - 11/26/2007 | -9.9% | **107%** |
| 01/02/2008 - 11/20/2008 | -47.7% | **85%** |
| 01/07/2009 - 03/09/2009 | -27.2% | **108%** |
| 04/24/2010 - 07/02/2010 | -15.6% | **80%** |
| 04/30/2011 - 10/03/2011 | -18.6% | **82%** |
| 04/03/2012 - 06/01/2012 | -9.6% | **67%** |
| 05/22/2013 - 06/24/2013 | -5.6% | **99%** |
| 09/19/2014 - 10/15/2014 | -7.3% | **77%** |
| 07/21/2015 - 08/25/2015 | -12.0% | **80%** |
| 01/04/2016 - 02/11/2016 | -10.3% | **49%** |
| 02/27/2017 - 04/14/2017 | -1.7% | **107%** |
| 01/26/2018 - 02/08/2018 | -10.2% | **97%** |

**Average Downside Capture 87%**

[1]Dividend growers are defined as companies in the S&P 500® Index or S&P 400® Index that have paid a dividend and increased their yearly dividend payout for 10 consecutive years.

Source: FactSet.

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**Dividend yield** is equal to the dividend divided by the stock price. Dividend yield is one measure of a stock's value. A high dividend yield may indicate that a stock is relatively inexpensive.

**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 non-dividend payer if it did not pay a cash dividend at any time during the previous 12 months.

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

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