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Dividends pay real dividends

History shows dividends are a major contributor to total returns

Investors should consider dividends when building their portfolios. Although dividends are often viewed as boring, they can be quite glamorous given the potential they offer. And, as yield dwindles in the bond markets, it's increasingly important to consider alternatives for income portfolios.

History shows that dividends are a major contributor to total returns. According to a recent Guardian Capital LP report, 58% of the total returns earned in the MSCI World Index during the past 40 years came from dividends, making income as important as capital gains. Over the past 30 years, capital appreciation was responsible for only about a third of the returns, with dividend yield making up the balance.

Dividends are generally a more reliable contributor to total returns than price appreciation because companies must be on a solid footing to sustain dividend growth. Those with a track record of increasing dividends typically have a sustainable advantage and are doing well in their respective industries.

Many of the top dividend-producing stocks fall into defensive categories, notably financials, consumer staples, health care, and utilities. They are typically large, blue chip companies less volatile than their non-dividend paying counterparts. Their income stream helps mitigate potential price depreciation in their share prices.

The landscape for dividend investing is improving with many companies carrying high levels of corporate cash. We've witnessed more share buy backs, takeovers, and dividend increases. BCE, National Bank, and Baytex Energy Trust are among a few of the companies to raise dividends this past quarter. Most analysts expect the Big Five banks to raise theirs by 2012.

Demographics are also prompting a move to dividend investing. With the increasing scarcity of structured pension plans, many future retirees will have to rely on personal portfolios for retirement income. Those closer to retirement, baby boomers, are just as focused on it. Both groups want tax-efficient income and the Dividend Tax Credit helps satisfy that criterion. A 4% dividend generates roughly the same after-tax income as a 5.2 - 5.5% interest yield.

With equity markets slowing, investors should focus on total return, not just capital appreciation. Government bonds do not offer enough yield; corporate bonds present too much risk for the potential return; and money market instruments are yielding historically low rates. The current market environment makes dividend investing logical.

When evaluating dividend investments, place an emphasis on quality. Seek those that are positioned to withstand volatility; have a history of paying and increasing dividends; carry adequate

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amounts of cash; and have solid balance sheets. Buy high conviction, top quality names on market dips.

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