Evolutions:
Crawford Dividend Growth Strategy

CRAWFORD
INVESTMENT COUNSEL
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We recently wrote a brief piece on the origins of the Crawford Dividend Growth strategy. The basic approach came into being in 1971, over 50 years ago. The fundamental aspects of the approach were set out then, and while these have not changed, within the approach there have been several evolutions. Most of these have been voluntary, made in the interest of improving the approach, except for one change that was suggested by economic and market circumstances. For those interested, what follows is a chronological history of the approach and how it has evolved into its current, disciplined form.

CONSISTENT DIVIDEND GROWTH UNIVERSE. A few years after founding Crawford Investment Counsel and continuing to invest along the lines outlined in our recent piece, we established a formal universe of companies that were eligible for investment. The universe was made up of all companies that had raised their dividend for at least 10 consecutive years. By limiting purchases to companies within this universe, the process was codified into a more disciplined and well defined approach. By investing in these types of companies, we believed we would be able to enhance the rate of dividend growth from the portfolio. Setting the standard at ten years of uninterrupted annual increases, we discovered that there were about 400 companies that met this test. Desiring to know what results might have been achieved by investing in these companies only, we engaged an independent research firm to do a back study for us. These were the days before databases and computers were widely available, hence the necessity to have outside help on this project.

The results of the test were very promising. The returns that would have been generated over time were so powerful that we were reinforced in our conviction that consistent dividend growth was a factor that, over time, would contribute significantly to the total investment return. We studied all of the characteristics of a portfolio of such companies and appreciated the consistency of returns, downside protection and upside participation, and overall quality. Our endorsement of the universe of consistent growth companies demonstrated our belief that growing dividends told us many favorable things about these companies and that they lent themselves to long-term holding periods.

THE MODEL. Importantly, within this approach we were able to respond favorably to the original question, “Why not both?”, and provide both yield and growth to the return equation. The next evolution was to develop a system of ordering the factors of return and provide a structure to our

decision-making process. Hence, we developed a simple model that ranked all of the companies in the consistent dividend growth universe by three things: dividend growth, dividend yield, and relative dividend yield. The value aspect was expressed in terms of relative dividend yield, that is, how high the yield on a stock was relative to its history. If it was higher, the stock would have been depressed on a historical basis, something we could evaluate on a fundamental basis to determine why the stock was depressed. The model helped us identify companies that had a favorable combination of all three of the desired factors. All models are by definition imperfect, but if used wisely as a complement to a basic approach they can point investors in the right direction where fundamental research can verify the objective results of the model. This is how we used the model.

OUTSIDE CONFIRMATION. As time went on and the firm developed, we began to tell our story to a larger audience. We approached the investment management consulting community in an effort to raise our profile among institutional clients. One of the larger consultants in our country, who will remain nameless, took a hard look at our approach and found favor with it. They were impressed with the way we approached the investment question, saying, “You really cut the apple differently.” This was in reference to our emphasis on dividend growth as a driver of appreciation over time and the emphasis on quality. In our words, this translates to, “rising income gives value to stocks.” It was this same consultant that made what has endured as one of our favorite descriptions of our process: “It is simple but elegant.”

We were also fortunate to be able to engage the services of Peter Bernstein, noted author and investor, with whom we had developed a personal relationship. In essence, we were seeking validation of our philosophy and process from a giant of the investment industry. We not only asked Peter to review our entire approach, but we also asked for his suggestions on how to improve the execution of our process, which he did in some detail. This engagement served us well and deepened our conviction that we were on the right path and that our process could indeed stand up to the test of scrutiny and time.

DIVIDEND GROWTH ADJUSTMENT. The next evolution in the history of the Dividend Growth approach was not planned or initiated by us. When the financial crisis of 2008-9 occurred, its most severe impact was among finance companies. Many of these companies suffered greatly in the crisis and were forced to cut or eliminate their dividends. The universe thus began shrinking by a considerable amount, so much so that we felt that with the reduced number of companies it would no longer be possible to reasonably diversify a portfolio. As a proactive measure and in order to be able to effectively implement the strategy, we decided to change the requirement of dividend increases for at least ten consecutive years to a slightly lower standard of ten years of paying a consistent dividend. Thus, the requirement for inclusion in the universe of candidates was no dividend cut and to at least maintain the dividend for ten consecutive years. This enlarged

the universe to a sufficient number from which to make our selections and provide adequate diversification. This standard remains as our practice today, although we continue to have a preference for those companies that raise their dividends each year.

When something new is established, even if it is sound, it is not often a finished product. That was certainly the case with our Dividend Growth strategy. The important thing is that it was established on strong fundamental grounds. The idea of owning dividend-paying stocks and purchasing them when they represent value is classic investment philosophy. Add in the focus on quality and the process is enhanced. These fundamental elements of our approach remain as the hallmarks of our Dividend Growth strategy. Over the years the process has evolved without losing its original, grounding instincts. It is what we do at Crawford. And, there is always room for improvement, something we strive for every day. No doubt there will be further evolutions in the future.

Through the years we have been challenged by difficult economic and market conditions. By sticking with our knitting, that is, consistently employing the strategy on behalf of clients and never wavering in our belief in its efficacy, our clients have been rewarded with lower-risk, high-quality returns.

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