

# The Dividend Effect

## Insulating Investors from Volatility

We have talked about the concept of *Dividend Integrity* and how this is a core element of our investment philosophy at Crawford Investment Counsel (Crawford). Since the firm's founding, we have utilized the dividend as an initial indicator of quality, believing a company's ability to pay, sustain, and raise its dividend can serve as a strong initial indicator of business strength. We have long believed dividends and quality are inexorably linked.

What has not been as well defined are the favorable outcomes produced by our focus on dividend-paying companies. Dividends can indicate consistent cash flow generation, low earnings variability, balance sheet strength, and shareholder friendly capital allocation policies. These factors often coalesce to provide investors with income and growth of income, reduced risk, a smoother ride, and ultimately a higher likelihood of earning positive returns. We like to call this the *Dividend Effect*, and below we will discuss its benefits in greater detail.

*Income.* When investing in dividend-paying securities, we see that income is generated regardless of what happens in the broader market. We believe this is valuable for a number of reasons, one of which is that income is positive each year and therefore softens a market decline. It reduces an investor's need to sell assets in a period of market distress like what we experienced in the first half of 2022. Withdrawals can put strain on a portfolio in a low return environment, and income can provide an important safety net for investors. In any market environment, we appreciate the dividend's contribution to the investor's spending ability.

*Growth of Income.* Rising dividends are one of the ways investors can benefit from the fundamental progress of the businesses they're invested in. We believe dividend increases can make a powerful impact on a portfolio if achieved regularly and over the long term. Dividend increases add up over time, compounding under the surface to the shareholder's benefit. For this reason, we place great significance on a company's dividend history when making investment decisions. For greater detail on dividend growth, see our piece *The Silent Factor*.

*Superior Pattern of Returns.* We believe that in certain market environments and return sequences, the pattern of returns earned can be more important than absolute returns. Investing in dividend-paying companies with high-quality attributes narrows the range of potential investment outcomes. Regardless of how the company performs, the dividend produces a nice recurring rate of investment return. In sum, we invest in what we see as more stable, consistent businesses to ensure a higher likelihood of success

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and improving the likelihood of positive returns. What's more, investors tend to appreciate dividend-paying stocks, especially those with high dividend yield in falling markets. All of this can provide downside protection and support performance in a time of turmoil.

*Total Investment Return.* Along with stock price appreciation, we believe dividends are an important component of total investment return. While we believe the components of the *Dividend Effect* outlined above are critical to investment success, we note that it is not simply the dividend that provides these benefits. Crawford's fundamental security research and selection process plays a large role in ensuring the benefits of *the Dividend Effect* are realized. We invest only in the companies we believe have the greatest chances of success. For us these are high conviction, stable, and growing businesses at attractive or reasonable valuations.

Our quest to achieve the *Dividend Effect* insulates our investors from much of the volatility typically associated with investing, empowering outperformance in periods of market stress and participation in strong markets. We hold our belief that dividends have a positive influence on a portfolio's risk/return tradeoff, and we appreciate that they provide investors with what we believe to be a stable and often growing stream of income.

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