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FINANCIAL PLANNING NOTES
CLIENT NEWSLETTER

IN THIS ISSUE:

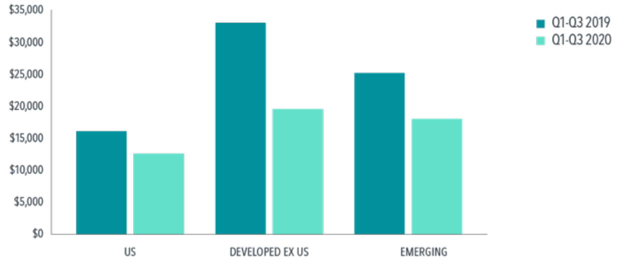
COVID EXPOSES RISK OF DIVIDEND STRATEGY

Many investors view dividend payouts as a reliable source of income. However, those expecting to receive consistent dividend income may have been surprised to see lower-than-expected dividend payouts following the onset of the coronavirus pandemic, when both market volatility and market declines were extraordinary. In reality, recent and historical data show that changes in dividend policy are common, especially during times of higher uncertainty.

Aggregate dividend payouts fell meaningfully in the first three quarters of 2020 compared with the same period in 2019. **Exhibit 1** shows the dividends earned from a hypothetical $1 million investment in U.S., developed ex U.S., and emerging markets in both periods. Developed ex U.S. markets showed the most drastic change with a 41% decrease. Dividend payments in emerging markets decreased by 29% and in U.S. markets by 22%.

EXHIBIT 1

DIVIDENDS FROM A HYPOTHETICAL $1 MILLION INVESTMENT



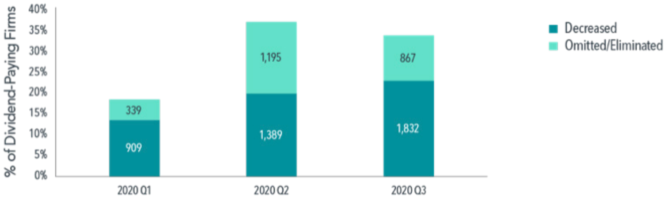
Past performance, including hypothetical performance, is no guarantee of future results.

Globally, large firms have historically had the highest propensity to offer dividend payouts,[1] but even successful, established firms were not immune to the economic consequences of a global pandemic. A few examples help illustrate this point. Harley Davidson (HOG) has been paying dividends to shareholders since the 1990s. In April 2020, the motorcycle manufacturer slashed its dividend from $0.38 per share to just $0.02, a 95% decrease.[2] Gap Inc. (GPS) suspended its dividend payments until at least April 2021[3] after the economic downturn left the clothing brand with particularly poor revenues.

Harley Davidson and Gap were not the only firms to change their dividend policies. As shown in **Exhibit 2**, 38% of firms in global markets (2,584 companies) that were expected to pay dividends, consistent with their payout history, instead decreased, omitted, or eliminated their dividend payments in the second quarter, more than doubling the 1,248 firms that made similar changes to their dividend policy in the first quarter of the year. The trend continued into the third quarter: 2,699 firms made such changes.

EXHIBIT 2

DIVIDEND POLICY CHANGES IN GLOBAL MARKETS (% OF DIVIDEND-PAYING FIRMS), 2020

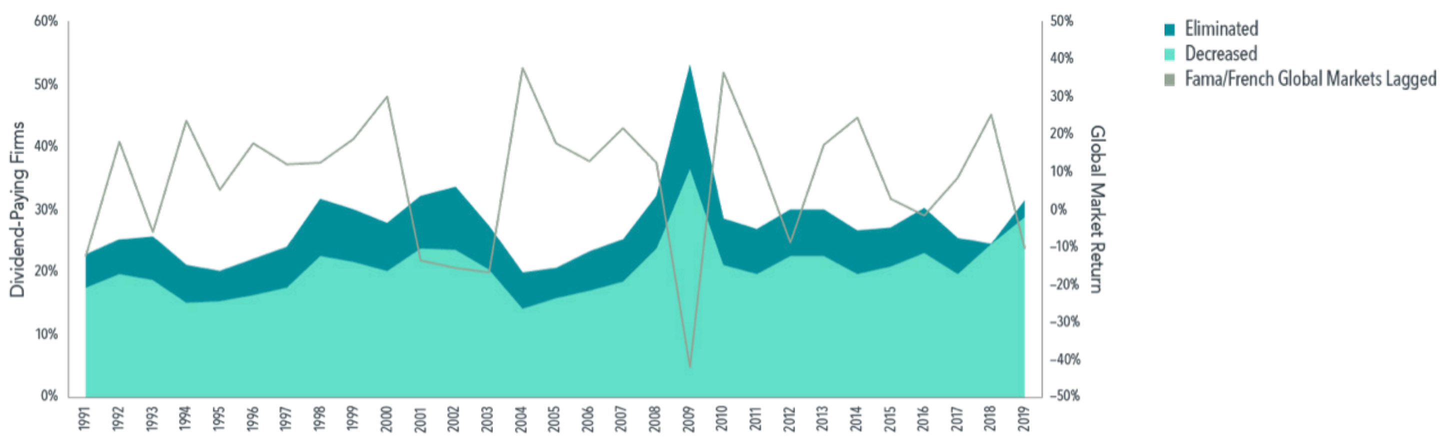


Source: Calculated by Dimensional from Bloomberg data. Dividend-paying firms include all firms that have paid a dividend in the preceding 12 months and were expected to pay a dividend in the current quarter.

While these dividend cuts may come as a surprise to some investors, history buffs may recall that, in 2009, Harley Davidson announced it was cutting dividend payouts from $0.33 per share to $0.10, a 70% decrease.[4] In fact, during the Great Recession, significant changes to firms' dividend policies spiked throughout global markets. **Exhibit 3** displays Fama/French global market returns for 1991–2019 with a one-year lag and the proportion of dividend-paying firms that eliminated or decreased their dividend payouts. In 2008, for example, the global market was down more than 40%, and the following year, many firms made changes to their dividend policies. The historical correlation between global market returns and dividends that are eliminated or decreased may suggest that firms are more likely to alter their dividend payouts during times of market instability.

EXHIBIT 3

GLOBAL MARKET RETURNS AND DIVIDEND CHANGES



Note: Global Market return is free-float market cap weighted average of Fama/French Developed Markets and Emerging Markets Indexes. See Index Descriptions in the disclosures for descriptions of Fama/French index data.

Source: Calculated by Dimensional from Bloomberg data. Past performance is no guarantee of future results. Dividend-paying firms include all firms that paid a dividend in the prior calendar year.

The first three quarters of 2020 remind us that dividend payouts can be inconsistent, particularly in volatile markets. Hence investment strategies that focus on income derived from dividends may not serve investors who need a steady income stream and, moreover, might not be the most effective way to pursue long-term wealth growth. A more reliable approach is to structure equity asset allocation around the characteristics that research demonstrates drive long-term higher expected returns—namely size, relative price, and profitability—while maintaining broad diversification across names, sectors, and countries.

—Dimensional Fund Advisors

Footnotes:

1. Stanley Black, "Global Dividend-Paying Stocks: A Recent History" (white paper, Dimensional Fund Advisors, March 2013).
2. Harley-Davidson, Inc., "Dividends & Stock Splits," investor.harley-davidson.com/stock-info/dividends-and-stock-split.
3. Gap Inc., "Gap Inc. Provides Update In Response To Covid-19 Outbreak," news release, March 26, 2020, investors.gapinc.com/press-releases/news-details/2020/GAP-INC-PROVIDES-UPDATE-IN-RESPONSE-TO-COVID-19-OUTBREAK/default.aspx
4. Harley-Davidson, Inc., "Dividends & Stock Splits."

THE UPS AND DOWNS OF CREDIT CARDS

One of the easiest ways to get in big financial trouble is to fund your lifestyle on credit—by running up big balances on your credit cards, up to maxing them out.

For many reasons (loss of job, health emergencies), a line of credit can be a last-resort lifeline, but for many others, it is an "unforced error" as they say in tennis, a big financial mistake.

Annual interest rates average around 18% for credit cards,[1] and many are well over 20%. Run up a few thousand dollars on a card like that and your monthly debt service (interest charges) will soon become a sizable part of your budget.

Your best choice, then, if you find credit card cash has become a necessity, would probably be a card with the lowest interest rate you can find, mindful that it might have a larger annual fee than other cards. A card with a very low introductory fee can save you big dollars if you feel confident you can pay off the debt within the six-month or one-year period—but be careful. Once that intro period expires, the rate will rocket up.

On the other side of the plastic, there are perks to using credit cards if you can pay off the balance each month. Most cards offer rewards for usage, from airline miles to free fill-ups to cold hard cash back. You don't get any of that when you use your debit card, write checks, or pay with cash.

Choosing the best card depends on your preferences and expenses, as different cards offer different levels of reward on particular categories of purchases. For example, the American Express Gold Card gives 4x rewards on restaurant charges and 3x rewards on air travel, so if you travel and dine out a lot (in a normal year), that might be a good choice.

Here are a few cards and their rewards, per thepointsguy.com:

Card	Rewards	Annual Fee
Amex Gold Card	4x restaurant, 3x airlines	$250
Citi® Double Cash Card	2% on all purchases	$0
Ink Business Preferred	3x business categories	$95
Amex Blue Cash Preferred	6% supermarket and streaming, 3% gas	$95
Chase Freedom Flex	5% on rotating categories, 3% dining/pharmacy	$0
Wells Fargo Propel Amex	3% dining, gas, travel, streaming	$0
Capital One Savor	4% dining, entertainment, 2% grocery	$95

Other terms and conditions and restrictions may apply. Always read the terms and conditions provided by the card issuer.

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One type of card I excluded from the list is the travel miles card, like Capital One Venture Rewards. My research tells me those rewards are not always what you expect, as blackout dates and small inventory can make it very difficult to redeem your points for flights you want on dates you want. Plus, the issuer reserves the right to change the redemption values at any time. Imagine finally saving up 60,000 points for your dream trip and being told it now costs 90,000.

My advice is avoid miles rewards with a good old-fashioned cash-back card. And tell Jennifer Garner, "Its none of your business what's in my wallet."

—Steve Tepper

Footnotes:
1. wallethub.com