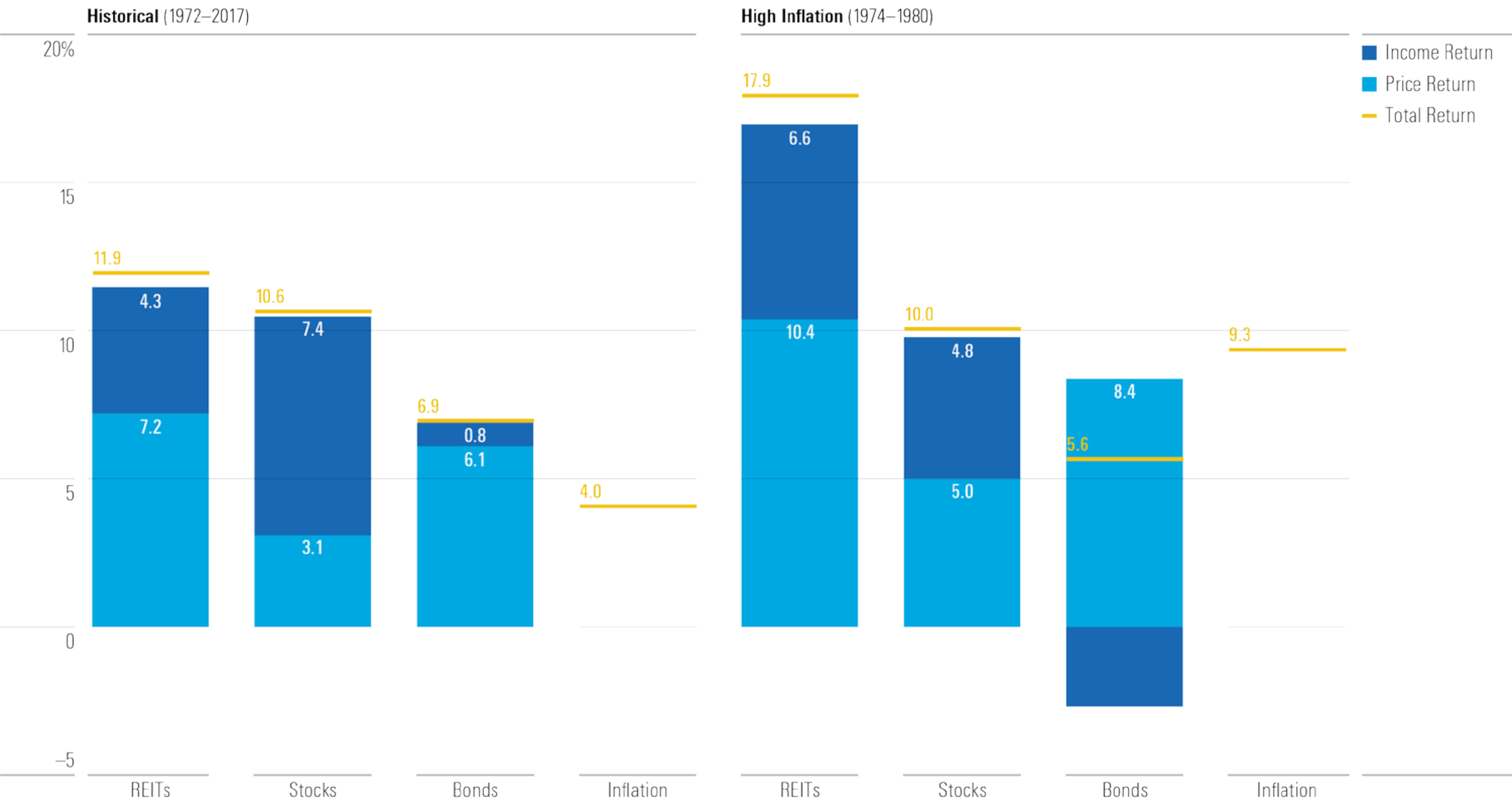
Dividends and Inflation

Stocks, bonds, and REITs, 1972–2017



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As an investor nearing retirement, you may ask whether an allocation to dividend-paying stocks or REITs in your retirement portfolio will help counter high inflation. Examining stock and REIT returns during periods of high inflation may help answer this question. Investors often think of stocks and REITs as a capital appreciation vehicle or a tool for growing portfolio wealth. Little do some investors realize, however, that dividend-paying stocks or REITs can also be an income tool. This is especially relevant for investors seeking to manage their portfolios in retirement, when the need for current income takes precedence over the need for capital accumulation.

The image illustrates the income potential for bonds, REITs, and stocks historically (1972–2017) as well as during a period of high inflation (1974–1980). The figures in the bars represent the portion of total return that can be attributed to income return (versus capital appreciation). While stocks and REIT prices tend to be volatile, dividends serve as a stable component of total return and may provide better inflation protection compared to bonds. Between 1974 and 1980 (high inflation), the average rate of inflation was 9.3%, much higher than the historical rate (1972–2017) of 4.0%. During this time, bonds yielded 8.4% from income, but prices declined by 2.7%, resulting in a total return of 5.6%—way short of inflation. On the contrary, stocks returned a total of 10.0%: 5.0% from dividend income and 4.8% from price return, outpacing inflation for this time period. The income return of REITs alone was 10.4%, higher than the 9.3% rate of inflation. REITs returned a total of 17.9% for this time period.

Dividend-paying stocks and REITs can serve as part of a growth investor's strategy, while also helping to seek the income return requirement for income-oriented investors. These investments can also play an important role in retired investors' portfolios because of their high potential to generate income.

Dividends are not guaranteed and are paid at the discretion of the stock-issuing company. Diversification does not eliminate the risk of experiencing investment losses. An investment cannot be made directly in an index. Government bonds are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest, while stocks and REITs are not guaranteed. REITs are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure. It is important to note that REITs may not be suitable for all investors.

About the data
REITs are represented by the FTSE NAREIT All Equity REIT Index®, stocks by the Ibbotson® Large Company Stock Index, bonds by the 5-year U.S. government bond, and inflation by the Consumer Price Index.

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