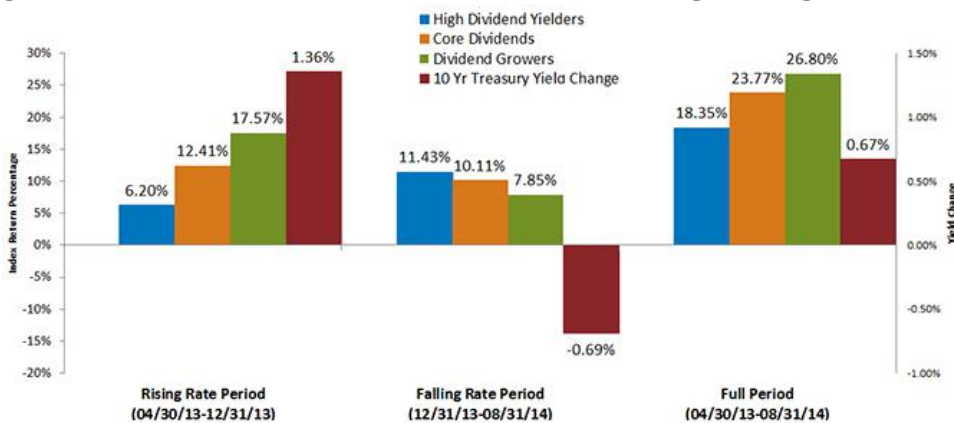


# HOW DIVIDEND GROWERS CAN HELP WITH RISING RATES

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In May of last year, longer-term [interest rates](#) in the U.S. rose considerably on just a hint that the [Federal Reserve \(Fed\)](#) might begin scaling back its bonds purchases. Then, at the beginning of 2014, interest rates fell due to weaker U.S. economic data and [deflationary](#) concerns in Europe. These two periods caused interesting differences in performance—and as the Fed plans to end its [asset purchase program](#) in October and prepares for a potential rate hike in mid- to late 2015, we think the lessons from these recent performance divergences can be important for shaping equity allocations. So let's take a look at how the movement in [Treasury yields](#) has impacted various income-oriented investment strategies. The chart below shows the performance of various equity indexes during the rising interest rate period (4/30/13–12/31/13) and the declining interest rate period (1/1/14–8/31/14). I selected this time frame as the 10-year [yield](#) rose by 136 [basis points \(bps\)](#) during the rising rate period and then began a steady decline—losing 69 bps. Overall, the 10-year yield rose by 67 bps.<sup>1</sup> For the period, I looked at the [high dividend yielders](#)<sup>2</sup>, [core dividends](#)<sup>3</sup> and the [dividend growers](#)<sup>4</sup>

Index Performance During Rising and Falling Rate Periods



Sources: WisdomTree, Bloomberg, 4/30/13–8/31/14. Past performance is not indicative of future results. You cannot invest directly in an index.

And here's what I discovered:

- **Dividend Growers Outperformed over Periods of Rising Rates:** As interest rates began their climb in 2013, dividend growers outperformed dividend yielders and core dividends.
  - **High Dividend Yields Outperformed during Falling Rate Period:** As interest rates generally declined in 2014, dividend yielders outperformed. In fact, dividend yielders and core dividends indexes outperformed the [S&P 500 Index](#) (up 9.89%). Lower-yielding dividend growers lagged in the first eight months of the year.
  - **Dividend Growers Outperformed over the Entire Period:** Yields rose by 67 basis points over the full period, and during that time, dividend growers outperformed both yielders and core dividends.
- Consider Focusing on Dividend Growers** Given the prospects of rising interest rates in 2015, and the fact that dividend growers outperformed during these periods, we think it would be wise for investors to consider dividend-growth-focused indexes. So, what should you look for in a dividend growth index? In our opinion, screening dividend-paying equities based on earnings growth and quality factors provides substantial sector differences compared to a broadly focused index or an index that screens based on dividend yield. This is important as we expect the higher growth expectations and increased exposure to [cyclical sectors](#) could become more desirable with improving economic activity and rising rates.

<sup>1</sup>Source: Bloomberg, 4/30/13–8/31/14. <sup>2</sup>References the WisdomTree Equity Income Index.

<sup>3</sup>References the WisdomTree LargeCap Dividend Index. <sup>4</sup>References the WisdomTree U.S. Dividend Growth Index.

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## DEFINITIONS

**Interest rates** : The rate at which interest is paid by a borrower for the use of money.

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.

**Deflation** : The opposite of inflation, characterized by falling price levels.

**Asset purchases** : The Fed purchases longer-term securities issued by the U.S. government and longer-term securities issued or guaranteed by government-sponsored agencies such as Fannie Mae or Freddie Mac.

**Yield** : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

**Basis point** : 1/100th of 1 percent.

**Qualified dividends** : Dividend paid by corporations meeting certain criteria defined by the Internal Revenue Service and therefore eligible in certain instances to be taxed at rates below a tax filer's tax bracket on ordinary income.

**S&P 500 Index** : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the United States economy.

**Cyclical sectors** : Consumer Discretionary, Energy, Industrials, Materials, Financials and Information Technology sectors.