

Looking for Dividend Growth with Rising Rates

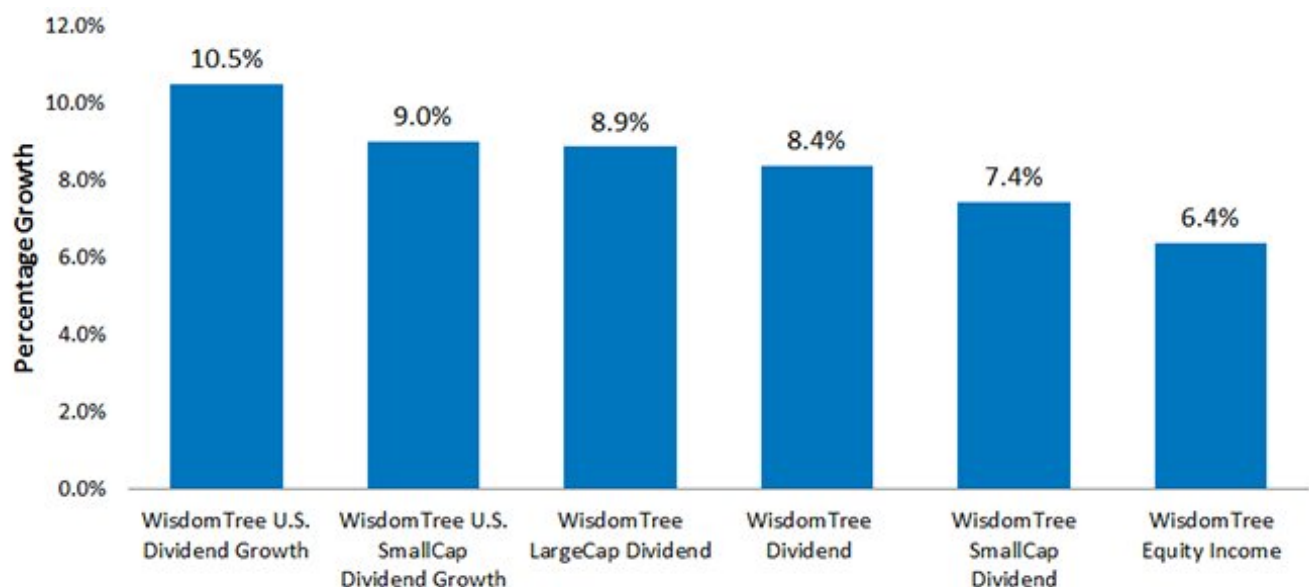
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In a previous [blog post](#), I wrote about the impact rising interest rates had on dividend-paying equities over this past year. Rising interest rates are bad for current holders of bonds—but potentially make bonds more attractive for new investors as well as more competitive with stocks for current income. If one wants to focus on equities for their income potential, the dividend growth prospects are becoming a more important component of the returns—as equities not only offer the current dividend but also the future growth potential. Bonds, of course, offer just a fixed income stream—by their definition as vehicles that provide fixed income payments. For those looking for dividend growth potential, WisdomTree created a new series of Indexes in 2013 to reflect those stocks we believe have the best prospects for raising their dividends based on growth and quality factors. As of our latest Index rebalance, the data shows these dividend growth stocks displayed above-average dividend growth over the last year, compared to some of our higher-yielding dividend Indexes. In the chart below, I look at the median *Dividend Stream*® growth of constituents of various WisdomTree Indexes as of the most recent annual rebalance screening date.

Dividend Growth Comparison



Sources: WisdomTree, Bloomberg. Dividend growth percentage above is the median Dividend Stream growth of Index constituents as of the 11/30/13 screening, from 11/30/12 to 11/30/13.

Past performance is not indicative of future results. You cannot invest directly in an index.

- **Dividend Growth Indexes Recorded Higher Growth** – Both the WisdomTree U.S. Dividend Growth Index (WTDGI) and the WisdomTree U.S. SmallCap Dividend Growth Index (WTSDG) saw higher *Dividend Stream* growth over the period shown above compared to the broader WisdomTree Dividend Index (WTDI).
- It is impressive to note that WTDGI and WTSDG each saw a 1.6 point advantage compared to the WisdomTree LargeCap Dividend Index (WTLDI) and WisdomTree SmallCap Dividend Index (WTSDI), respectively, the Indexes closest to them in terms of size capitalization. It is important to note that both WTLDI and WTSDI are broad dividend Indexes that do not focus specifically on dividend growth.
- **Dividend Growth Indexes Saw Higher Growth Than Yield-Focused Index** – WTDGI and WTSDG had an advantage of over 4 and 2.5 points, respectively, compared to the WisdomTree Equity Income Index (WTHYE). Although WTHYE's median dividend growth lagged over the period, it is important to remember that WTHYE screens for securities with higher dividend yields instead of focusing on future growth potential, so the Index will typically have a higher dividend yield than WTDGI and WTSDG.

Dividend Growth Indexes Tend to Provide Different Exposures WisdomTree believes the combined ranking of earnings growth and quality factors is a key element of our dividend growth methodology process of identifying stocks with the highest potential to increase dividends. It is important to understand that screening dividend-paying equities based on earnings growth and quality factors can create an index with substantial sector differences compared to a broadly focused index or an index that screens based on dividend yield. **The Growth Sectors:** WisdomTree's [dividend growth Indexes](#) are currently over-weight in the more cyclical sectors such as **Information Technology**, **Consumer Discretionary** and **Industrials**, compared to broad and yield-focused dividend indexes. **The Higher-Yielding Sectors:** On the other hand, yield-focused indexes are typically over-weight in defensive sectors, for example **Utilities** and **Telecommunication Services**, which are characteristically some of the highest-yielding sectors, compared to the broad or dividend growth indexes. **Conclusion** There is no question that investors are drawn to the idea of dividend growth—potentially even more than in the past, due to rising interest rates. While there is no way to know with certainty what will happen in the future, I believe that our dividend growth methodology shows that it can help identify stocks with above-average prospects for dividend growth—as it did at the last rebalance. I believe this dividend growth potential becomes even more important if we continue to see a rise in interest rates like we witnessed in 2013.

Important Risks Related to this Article

Dividends are not guaranteed and a company's future abilities to pay dividends may be limited. A company currently paying dividends may cease paying dividends at any time. Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. In addition, when interest rates fall, income may decline. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline.