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SOPHISTICATED INVESTOR

Long live dividend yield!

Payments offer more accurate portrayal of growth

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LOS ANGELES (CBS.MW) -- Earnings are dead! Earnings are dead! Long live dividend yield!

That's the meaning some gleaned from Federal Reserve Board Chairman Alan Greenspan's remarks when he spoke about the state of the U.S. economy before Congress last week.

"Earnings are very difficult to estimate," Greenspan said. "... cash dividends are not."

More than half the companies accused of financial fraud in shareholder class action lawsuits last year have been forced to restate their earnings, says Rep. John LaFalce (D-NY). Moreover, some 500 firms were accused of financial fraud last year, according to the Securities Class Action Clearinghouse, which is run by Stanford University's school of law.

And at a time when more questions are surfacing about companies' financial procedures, a return to dividend payments and analysis could offer a more accurate portrayal of a company's growth pattern.

"Earnings are always provisional," Greenspan said.

The call for dividends

Dividends are the amount of earnings a company pays to its shareholders in cash. Younger, faster-growing companies typically reinvest all their earnings to expand. And, as we all know, fledgling companies with ambitious growth plans have been the rage for the past two decades.

Yet with mismanagement, fraud, and earnings manipulation, expansion among these younger companies seems to have been far down on the corporate checklist.

That's why a clarion call for dowdy days of yesteryear is in order. Greenspan himself has trumpeted the call: "This goes back 50 years, grant you. But people bought stocks for dividends; they did not buy them for earnings. And one of the problems that we did not have back then is earnings manipulations were not very important because nobody cared," he said.

Today, we care. Day by day, as the Dow Jones Industrial Average falls fast, we all care to find a bottom.

Today, the dividend yield for all U.S. equity is just above 1 percent, compared to 5.15 percent in 1926, according to the

A return to dividend-paying stocks

Chicago-based research firm Ibbotson Associates.

That means we've traded value for growth. And in some ways we are merely looking at stock price versus total equity return. In stock analysis, this is called capital share price appreciation, where the emphasis is solely on the capital gain in stock price.

The mass market methodology of only looking at stock price gains and losses is wrong. A look at total equity return is needed. After all, a gain in stock price is only one measure of increasing equity return. A gain in dividend yield also increases a return on investment.

'Better than a money market'

Financial advisors are beginning to look at dividend-paying stocks again for just this reason.

"I recently put a client into a dividend-paying stock with a three-percent yield. I understand the volatility, but it's better than a money market," says William Guthrie, a certified financial planner with Schneider Downs Wealth Management Advisors in Pittsburgh, Pa.

"I think there's going to be more of a return to dividend-paying stocks."

The hitch with dividends is that they are taxed earnings to both the corporation and individual shareholder - a point Greenspan said should be rectified.

"The most fundamental aspect of this question really gets down to the double taxation of dividends and the issue of the integration of the corporate tax with the individual tax. And I think a lot of the columnists will tell you that that is an extraordinarily useful and efficient way, if you can do it, to put all of the tax burden on shareholders and not have double taxation of dividends through the -- taxing the corporation and then taxing the dividends again.

"My own impression is that we ought to have a very large expansion of Subchapter S corporations, which effectively would enable dividends to be paid out and effectively taxed only once," Greenspan said.

This columnist couldn't agree more.

Dividend payments at least put some earnings back into investors' pockets - where Corporate America has had its hands in for too long.

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