

Dividends: Worth a closer look

3rd Quarter, 2010

Compelling yields

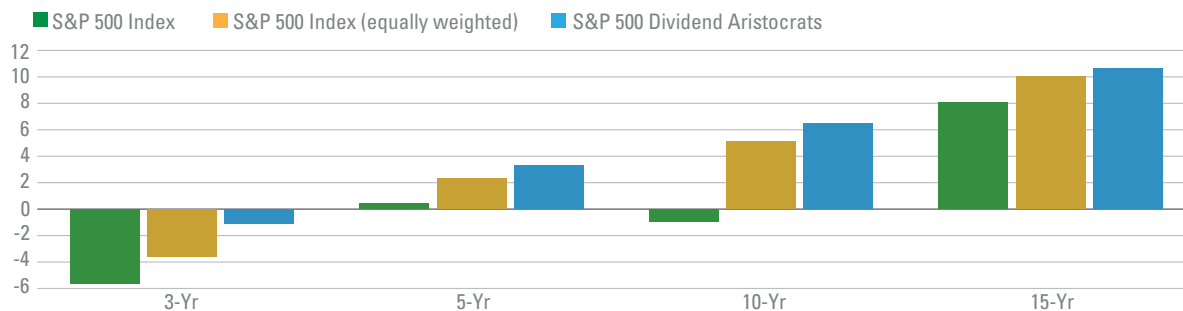
Many stocks today offer compelling dividend yields relative to Treasuries — some say the best advantage since the 1950s. In fact, as of 9/30/10, the S&P 500 dividend yield is 2.03%, with the 3-month T-bill yielding 0.16%, 2-year T-notes yielding 0.42% and 5-year T-notes yielding 1.27%. What's more, cash on corporate balance sheets is at high levels rarely seen — in other words, many companies are in good financial shape to increase dividend payouts and respond to arising growth opportunities.

A long-term track record of higher returns and lower risk

Companies with a long history of growing dividends have produced a favorable risk/reward profile over time, holding up better on the downside and producing better results on the upside as well. As evidenced in the illustration below, the S&P 500 Dividend Aristocrats Index (companies in the S&P 500 Index that have increased the dividend payout for at least 25 consecutive years) have provided higher returns with less risk than the S&P 500.

Turning to dividend-paying stocks during times of economic uncertainty is not a new concept. However, it's one that seems especially relevant now, with the dividend yields of many stocks providing a relatively attractive alternative to the historically low yields delivered by bonds.

Average annual total returns and risk as of 12/31/09



Standard deviation as of 12/31/09 (%)	S&P 500 Index	S&P 500 Index (equally weighted)	S&P 500 Dividend Aristocrats
	3-Year	15.26	24.91
5-Year	13.07	20.02	15.39
10-Year	15.21	19.04	14.76
15-Year	14.99	17.60	14.27

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Dividend-paying stocks offer many potential benefits for investors. Hersh Cohen, Chief Investment Officer and Senior Portfolio Manager, ClearBridge Advisors sees many reasons to look closer at dividends as an investment opportunity:

- **A signal of quality:** Consistent dividend growth can be confirmation of a firm's "quality" status, as it shows the company's ability to consistently increase cash flow over time.

"When we look at our companies, we see many of them in the best financial shape in decades. Cash on corporate balance sheets is at levels rarely seen. Dividends have been raised, often sharply, for many. Coming out of the worst recession of our lives, we cannot help but believe that these high-quality companies offer the best values in the financial spectrum."

- **A source of income:** In today's current economic environment, where bond yields are at historic lows, stock dividend yields can be relatively more compelling, especially for stocks with low price-to-earnings (P/E) ratios.

"We believe it will take longer than is generally expected to return to 'normal,' and prefer to take our risks in more established companies that have come through this debacle in superior shape. When we are asked how to get more income with no risk, we reply that it is impossible. However, by stepping up to great companies, one can possibly get better returns with some risk. We like the trade-off."

- **A cushion from volatility:** Compared to the overall market, dividend-paying stocks have a history of lower volatility, which means they can provide stability to an equity portfolio.

"Clearly, stocks have inherent risks and volatility, but sometimes the risk/reward pendulum favors stocks. We can buy a variety of stocks with current dividend yields that we believe can grow over time, well above the risk-free rate of return. That is a rare occurrence, one we have not seen since the 1950s."

- **A growing option for retirement:** Dividend-paying stocks can help to provide income needed in retirement.

"All investors, regardless of their age or financial goals, need investments that produce income. Income can also enhance your portfolio's total return potential and help to temper volatility. And with a population of nearly 80 million baby boomers starting to retire, this need for income will become even stronger. With longer life expectancies and the potential for rising inflation, income-seeking investors will need to make sure their money continues to grow."

Take a closer look

There are many reasons to take a closer look at dividend-paying stocks — as a cushion from volatility, for income — just to name a couple — but also consider that dividends, reinvested and compounded over time, have provided a significant contribution to total return. For example, with dividends reinvested, the S&P 500 produced a cumulative total return of 393.4% during the 20-year period August 31, 1990 through August 31, 2010. Excluding dividends, price appreciation in the S&P 500 for the same time period was just 225.3% — a difference of \$16,810 on an original \$10,000 investment.

Making the most of the "dividend opportunity" requires stock selection expertise and active portfolio management.

Important information

The views expressed are those of Hersh Cohen as of September 14, 2010 and are subject to change based on market and other conditions. These views may differ from the views of other portfolio managers or the firm as a whole, and they are not intended to be a forecast of future events, a guarantee of future results, or investment advice. The information contained should not be used as the sole basis to make any investment decision. The statistics have been obtained from sources believed to be reliable, but the accuracy and completeness of this information cannot be guaranteed.

For more information about how you can access the experience and investment solutions that ClearBridge Advisors offers, please contact Andy Goldsmith or Sean Oakes at 1.800.691.6960, or visit us at www.ClearBridgeAdvisors.com