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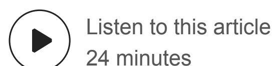
RETIREMENT | COVER

Yes, You Can Retire on Dividends. 10 Stocks to Build an Income Stream for the Long Haul.

By Lawrence C. Strauss March 26, 2021 6:00 am ET

illustration by Doug Chayka



Bob Baker, a retired aerospace engineer, regularly taps his small pension and Social Security income to help cover his living expenses.

But he also relies on a steady dose of stock dividends, something he started to zero in on when he retired in 2015. "Once I fully understood the significance of dividends from quality companies, a priority focus for me was not to have to sell any shares of any holdings," says Baker, 72, who lives in northern Virginia with his wife.

Dividends from his retirement accounts are transferred every month into a taxable account to cover required minimum distributions, or RMDs—which kick in after a retiree hits 72, up from age 70½ previously. His holdings include PepsiCo (ticker: PEP), CVS Health (CVS), and Prudential Financial (PRU)—longtime dividend payers that sport yields well above the S&P 500 index's average of about 1.5%. The yield on the dividend stocks in his portfolio was recently 4.5%.

The notion of using dividends in retirement, either as a way to complement other financial assets, as Baker does, or perhaps rely on them for an even larger percentage of income, is drawing plenty of interest these days. Yields on many traditional income investments are now near historical lows, and the onus increasingly is on individuals to secure their postcareer income. The strategy has spawned something of a movement,

encompassing investors of all ages and levels of sophistication. There are Facebook groups devoted to the topic along with blogs, newsletters, books, and various other platforms.

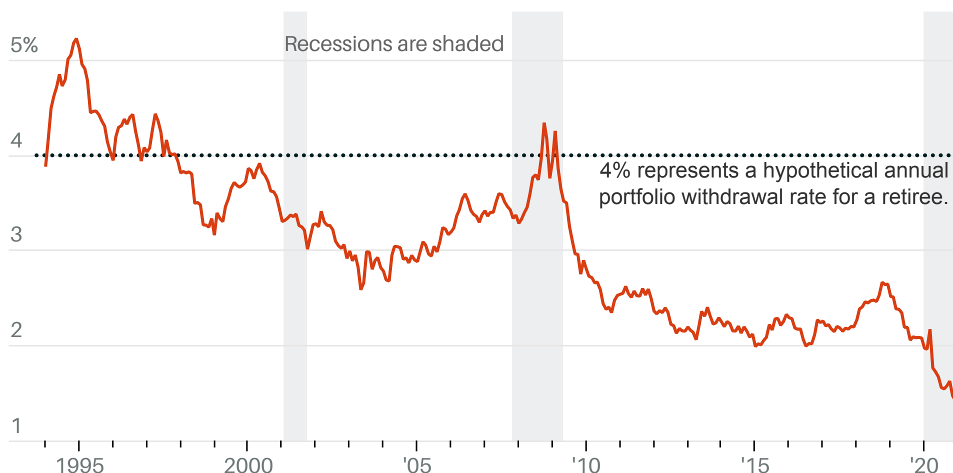
But these investors are not your GameStop traders or momentum players. They are in many cases diligent investors adopting sound strategies to build a portfolio for the long haul, investing sometimes $100 here or $50 there. They're more like modern-day moms and pops.

"A big appeal of dividends is really that it's kind of psychologically easier to stay the course," says Brian Bollinger, who in 2015 founded Simply Safe Dividends, which includes a monthly newsletter and tools for do-it-yourself dividend investors. "You are focusing on building this growing income stream regardless of market conditions."

Indeed, during last year's pandemic-driven market rout and subsequent strong rally, dividend stocks lagged, and a number of big names cut or suspended their payouts. From when the market reached its prepandemic peak in February 2020 through the end of the year, the S&P 500 Dividend Aristocrats returned 8.1%, dividends included. Those companies, which have paid out higher dividends for at least 25 straight years, trailed the S&P 500's 12.7% return over that stretch.

Yield Shortage

The yield of a 50-50 portfolio of stocks and bonds, once a reliable source of income for retirees, has dwindled to below 2%.



Source: Vanguard

But last year's selloff and relative underperformance offered a chance for nimble dividend investors to add to holdings they considered to be undervalued. If you missed out, however, it's not too late: Below, we identify 10 stocks with solid yields, consistent payouts, and seeming durability.

A key force behind the burgeoning interest in retiring on dividends is ultralow interest rates. Even though the 10-year U.S. Treasury yield has touched 1.7% in recent days, passing the S&P 500's average yield, interest rates remain low by historical standards. Other traditional income—generating investments like certificates of deposit and corporate bonds are also trading with historically low yields.

"It used to be that retirees could live off the cash flows from a portfolio," says Colleen Jaconetti, head of investment research at Vanguard Institutional Investor Group. "So, you never really had to think about where it came from."

She points out that in early 1995, a 50-50 stock and bond portfolio yielded a little more than 5%, above the 4% annual portfolio withdrawal rate that some advisors and investors use as a starting framework in retirement. That portfolio's yield had fallen to 1.4% at the end of 2020.

Such paltry yields can make dividend stocks an attractive investment centerpiece for retirees. They can offer nice yields, and unlike fixed bond coupons, dividends can grow to hedge inflation, which many experts expect to tick up.

"People generally say that the sweet spot is somewhere between 2.5% and 4.5%" for dividend yields, "and I'm right in the middle of that at 3.6%," says Dave Van Knapp, an active dividend-growth-investing blogger and investor who relies heavily on dividends in retirement.

The 74-year-old Van Knapp, who worked in legal publishing, not only promotes the investment strategy but also shows it in action, posting one of his portfolios on a website called Daily Trade Alert. That portfolio—which had increased more than threefold from when he set it up in 2008, to $151,854 recently—has 28 stocks. They include Johnson & Johnson (JNJ), PepsiCo, and Procter & Gamble (PG). He uses Social Security and a pension to complement his dividend income streams.

"A lot of times, when people say I want to live off income in my retirement, many, many people—and the investment industry does this—immediately translate that to bonds," says Van Knapp. "One of the breakthrough concepts of this [strategy] is that you can generate equity income."

One thing to keep in mind is that by eschewing bonds and focusing solely on stocks, investors are discarding an asset class that can provide important portfolio diversification.

There are many ways to build a portfolio of dividend stocks, one of which entails assembling a collection of blue-chip issues, as Van Knapp's portfolio does. Investors, however, need to consider the pros and cons of relying heavily on dividends in retirement—and there's no shortage of each.

MORE READING

Barron's covers dividend stocks and income investing regularly in our Income Investing column. Here are some recent postings:

"If you have a large enough portfolio, then buying a blue-chip amalgamation of companies like Procter & Gamble, Kimberly Clark, and so forth that produces enough income for you—you're golden," says Charles Lieberman, chief investment officer at Advisors Capital Management. "The conceptual issue is, do you buy a diversified portfolio and peel off assets on a regular basis in order to get cash,

REITs' Reversal Shows You Can Win for Losing, at Least in the Short Term

Bank Stocks Could Be a Good Option for Income Investors. Here Are 5 Places to Start.

Here Are 4 Tech Stocks That Offer Solid Yield and Dividend Growth

or do you invest for income and live off the income?"

Many investors and financial advisors favor a total-return approach, in which a saver assembles a portfolio of growth stocks and dividend payers—and often bonds and other asset classes—and sometimes sells off assets in retirement to raise cash. Relying largely on stock dividends in retirement, to them, isn't a feasible approach to amassing the principal necessary for a retirement that could last 30 years or more.

"I don't hear any advisors saying, 'How do I build a dividend-paying portfolio that is going to cover 100% of my client's income needs?' " says Katherine Roy, chief retirement strategist at J.P. Morgan Asset Management. "I just see so many more advisors building diversified portfolios that are oriented toward income, but they are looking for that growth potential, as well."

Jaconetti, too, is skeptical, pointing out that stocks with yields of 3% to 4%, though deemed attractive and safe by some investors, can pose a lot of risk, lead to overly concentrated portfolios, and create capital losses.

"At any given time, there's no way to say whether growth or value is going to outperform," Jaconetti adds. "It's not that you can't have a lot of diversification within value. But you are most likely underweighting growth. And if growth is outperforming, then you are going to end up underperforming."

Still, several of the retirement dividend-investing practitioners *Barron's* spoke with believe that it's possible to actively manage a portfolio of dividend stocks for long-term capital return while minimizing the attendant risks.

> **"Once I fully understood the significance of dividends from quality companies, a priority focus for me was not to have to sell any shares of any holdings. "**

— Retired aerospace engineer Bob Baker, 72

Jenny Van Leeuwen Harrington, CEO and portfolio manager at Gilman Hill Asset Management, aims for a 5% yield plus capital appreciation in the firm's equity income strategy. "You can get the 5% yield, but it doesn't come easy or at a superlow cost" that an equity income exchange-traded fund charges, she says. "You need to work for it."

She cites Verizon Communications (VZ), IBM (IBM), and SL Green Realty (SLG) as examples of what she considers sound companies with attractive yields of at least 4.5%.

Still, she says, relying solely on stock dividends in retirement isn't for everyone. "It depends on the amount and what your spending is. That's the equation," says Harrington.

Consider, for example, a retiree whose portfolio totals $200,000. A 3% yield on that would produce $6,000 a year—not very much, though it could be supplemented by Social Security or other income, if available.

A $1.5 million portfolio, at a 3% yield, would generate annual income of $45,000, which, if combined with other sources like Social Security, could be sufficient.

Higher yields, of course, are alluring to some investors, but they can signal value traps —where a stock that appears cheap can trade at depressed levels or decline for an extended period of time. Such stocks are the subject of much debate in dividend-investing circles, but investors should do their due diligence before deciding whether a high-yielding stock is worth the risk.

“Only fundamental analysis reveals the real why [for a high yield] and if it’s a temporary dislocation or a real permanent decliner,” says Harrington, who adds that her clients “find emotional comfort in the consistency of those dividends.”

Ultimately, an income-dependent retirement strategy isn’t foolproof or something to set and forget.

“It still requires care,” says Lieberman. “Inevitably, there will be downdrafts in the market, and inevitably there will be a company or multiple companies that at some point cut their dividends, so then you have to adapt.”

Reliable Retirement Returns

These are the types of companies that can offer retirees durable dividends and potenial growth.

Company / Ticker	Recent Price	Dividend Yield	Market Value (bil)	Return Since 1/31/2020	5-Year Dividend Growth Rate*
AT&T / T	$29.99	6.9%	$215.4	-14.5%	2%
Coca-Cola / KO	51.52	3.3	222.0	-8.0	4
Consolidated Edison / ED	73.43	4.2	25.1	-17.9	3
International Business Machines / IBM	130.62	5.0	116.7	-3.1	5
Johnson & Johnson / JNJ	161.91	2.5	426.3	12.4	6
Kellogg / K	62.59	3.7	21.3	-5.7	3
Procter & Gamble / PG	132.56	2.4	326.4	9.0	3
SL Green Realty / SLG	70.02	5.2	4.9	-18.5	8
U.S. Bancorp / USB	53.47	3.1	80.3	5.0	11
Verizon Communications / VZ	57.01	4.4	236.6	0.2	2

Data as of 3/24/21. *Annualized

Source: FactSet

Another factor to consider before pursuing a dividend-focused portfolio for retirement: Not every retiree or saver has the desire, prowess, or time to regularly focus on a stock portfolio. Using mutual funds or a financial advisor can make a lot more sense, their fees notwithstanding.

But managing a portfolio of dividend stocks works well for some investors.

"The key consideration was to have a comfortable income stream and not have to liquidate any equities in my portfolio to do so," says Baker, the former aerospace engineer. "I tend to go into my portfolio every day. I'm retired. I have the time, and I enjoy doing it."

Dividend-paying stocks can make a lot of sense for retirees, many of whom face "very difficult investment decisions," says David Katz, chief investment officer at Matrix Asset Advisors, pointing to low bond yields and rich valuations as major headwinds.

Certain dividend stocks, he says, "should allow for a healthy and growing income stream and reasonable portfolio growth over time" while providing some downside protection when needed.

Based on input from Katz and other financial pros, as well as our own research, *Barron's* came up with a portfolio of 10 dividend-paying stocks that retirees should consider.

AT&T

AT&T (T) is one of the more-discussed stocks among dividend investors, as its yield, at about 7%, is much higher than most U.S companies. A concern that many investors have is the company's hefty debt load.

Such a high yield can be a reason for investors to exit, but the entertainment, tech, and telecom conglomerate has a long history of paying a dividend—it's a member of the S&P 500 Dividend Aristocrats—and some analysts like its content library and foray into streaming.

Company executives are showing their support for the dividend. In a March 12 release outlining the company's strategy and financial outlook, CEO John Stankey said in part that AT&T is "committed to sustaining the dividend at current levels and utilizing cash after dividends to reduce debt." Chief Financial Officer John Stephens expressed a similar commitment to the dividend at a conference on March 8. "With $26 billion of free cash flow after [capital expenditure], there's plenty of money to pay out the dividend," he said.

The last time the company declared a quarterly dividend increase occurred in December 2019, more than a year ago, boosting it by a penny, to 52 cents a share. But AT&T looks like it's on course to at least sustain the dividend.

Coca-Cola

In the 1970s, Coca-Cola (KO) ran a series of TV advertisements built around the mantra "Coke adds life." The beverage behemoth has added a lot of yield over the years, as well, and it continues to do so—with its stock recently yielding 3.3%.

Coke managed to keep its quarterly dividend at 41 cents a share last year, even though the pandemic took a big toll on restaurants, one of the company's key sales channels.

Coke earned an adjusted $1.95 a share in 2020, down from $2.11 the previous year, as sales fell 11%, to $33 billion. Analysts polled by FactSet expect sales to rebound this year to $36.7 billion, still below 2019 levels, and for the company to earn $2.14 a share.

Coca-Cola maintained its dividend during the pandemic, a testament to its durability even in rough times.
George Frey/Bloomberg

Despite the headwinds, Coke's board in February declared a quarterly dividend of 42 cents a share, up by a penny, or 2.4%. The company paid out $7 billion in dividends to shareholders last year—including BerkshIre Hathaway's Warren Buffett, who has famously enjoyed the company's products, and dividends, for years.

In an investor presentation last month, Coke listed continuing to increase its dividend as its second-highest capital-allocation priority after reinvesting in its businesses.

The stock is down about 5% this year, dividends included. Still, the company should be a big beneficiary of the economy's reopening, and its payout history bodes well for the long term.

Consolidated Edison

Utilities are often lauded by investors for their durability, resiliency, and big yields. The pandemic has posed a big test for the sector, however, and Consolidated Edison (ED), whose regulated utility footprint includes New York City as well as nearby Westchester and Rockland counties, was no exception.

The company earned an adjusted $4.18 a share last year, down 5% from $4.38 in 2019, on an operating revenue decline of about 3% to a little more than $12.2 billion.

Still, ConEd's "regulated utility distribution business will still contribute over 90% of adjusted earnings over the next five years," wrote Morningstar analyst Charles Fishman recently.

Regulated utility businesses are generally regarded as durable and resilient, helping to fuel increases in earnings and dividends.

ConEd has boosted its dividend for 47 straight years, most recently in January to $3.10 a share annually, up by four cents, or 1.3%. That's below the 3.5% dividend increases the company has averaged in recent years, Fishman observes, "and we expect this level of increase over the next several years due to the economic impact of Covid-19."

But he calls the dividend secure, "considering the conservative strategy of the company's nonutility businesses and the favorable regulatory framework for its New York utilities."

Katz believes that the "stock will probably get a lift as a reopening play and a New York City recovery."

IBM

IBM shares have returned about 5% this year, slightly ahead of the S&P 500, but they've been a laggard over longer periods owing to disappointing financial results, including weak revenue growth.

But the company has been trying to change that. In 2019, for example, IBM acquired Red Hat, which offers customers a hybrid cloud platform, for about $33 billion using a combination of debt and cash. Red Hat's sales grew 18% on a normalized basis in 2020, CEO Arvind Krishna told analysts in January. That should help solidify the dividend and grow it modestly.

Gilman Hill's Harrington sees Red Hat's "hybrid cloud IT strategies" becoming "an increasingly meaningful driver of total revenue growth" for the company. It's "a stock everyone loves to hate," she says, "and, as a result, [it] has been written off."

On the plus side, the stock yields 5%, and the company has said that it's committed to the dividend. IBM earlier this year was admitted to the S&P 500 Dividend Aristocrats—demonstrating the consistency of dividend growth that retirement savers and retirees need for the long haul.

Johnson & Johnson

With its diversified mix of businesses, Johnson & Johnson throws off a lot of free cash flow, giving it the wherewithal to maintain its dividend and boost it through thick and thin.

Case in point: Last April, as the pandemic was forcing many companies to slash or eliminate their dividends, J&J declared a quarterly payout of $1.01 a share, up 6% from 95 cents. This came even as one of its key business units, medical devices, came under pressure as customers put off elective surgeries due to the pandemic.

Last year, the company, whose businesses also include consumer products and prescription drugs, paid out about $10.5 billion in dividends, or roughly half of its free cash flow.

Morningstar analyst Damien Conover likes J&J's "diverse revenue base, a developing research pipeline, and exceptional cash flow generation"—three attributes that should support the dividend and keep it growing.

Kellogg

Kellogg (K), whose signature brands include Special K, Rice Krispies, and Pringles, has lagged behind the market this year with a flattish return. But the company's foundation looks sound, helped by its plant-based proteins under the Morningstar Farms Incogmeato label and others.

The company notched organic sales growth of 6% in 2020, lifted by gains across all of its regions globally and its four major product categories: snacks, cereal, frozen food, and noodles. That helped offset headwinds that included Covid-19 and divestitures.

What's more, Kellogg paid a quarterly dividend of 57 cents a share throughout the pandemic-challenged year, and it plans to boost it by a penny in the second quarter. The stock was recently yielding 3.7%.

"This means returning more cash to share owners, and it reflects our confidence in the business," CFO Amit Banati told analysts during the company's fourth-quarter earnings call in February.

The company earned $4.03 a share on an adjusted basis last year, up fractionally from $4 in 2019, and the FactSet consensus for this year is $4.01 a share. It recently fetched 15.3 times its FactSet consensus adjusted 2021 profit estimate.

Katz describes Kellogg as a "top-tier consumer-staples company selling at a very attractive valuation."

Procter & Gamble

P&G, a consumer-products giant whose brands include Bounty paper towels and Charmin toilet paper, proved its dividend mettle in 2020.

Last April, it declared a quarterly payout of 79.07 cents a share, an increase of 6%. The stock yields 2.4%.

Operating chief Jon Moeller told analysts in January that the company had built momentum before the pandemic. That gave P&G confidence, he said, "to increase our

dividend at the highest rate in many years, even as we struggled with new Covid realities."

The company ultimately benefited from heady sales of lockdown items such paper towels. Analysts surveyed by FactSet expect the company to earn $5.70 a share in its current fiscal year, which ends in June, up from $5.12 last year—testament to P&G's durability and the health of its dividend.

SL Green Realty

Real estate investment trusts, which are required to pay out at least 90% of their taxable income as dividends, are popular among income investors. This REIT could prove particularly popular postpandemic.

SL Green, which owns a lot of high-profile Manhattan office buildings, is down 18.5% since last January, before the pandemic began. The company has been hit as tenants grapple with weak occupancies and many employees continue to work from home a year into the pandemic.

"People were worried about workers never coming back to work in offices in New York City. I think that's very unlikely," says Charles Lieberman of Advisors Capital Management.

He views SL Green as a good way to play the economy's reopening. SL Green shares have been on the road to recovery, returning about 15% this year alone. The stock was recently yielding 5.2%.

In March, in addition to declaring a monthly dividend of 30.33 cents a share, the company issued a special dividend of just under $1.70 a share for a total dividend of $2 a share. However, the special was paid in the form of the company's stock—though shareholders could ask to be paid fully in cash.

U.S. Bancorp

Shares of U.S. Bancorp (USB) have returned about 15% this year, and around 75% over the past year—and they may have room to run.

Katz calls it a "top-tier super-regional bank" that's well capitalized with a strong loan portfolio and good credit quality. "We expect them to fully benefit from an improving economy and a steepening yield curve."

The bank has several segments, giving its revenue mix some diversification: corporate and commercial banking; consumer and business banking, wealth management and investments; payment services, including for credit and debit cards; and treasury and other support for companies.

The stock pays a quarterly dividend of 42 cents a share, for a yield around 3%. And that's not all. Even though the stock has a double-digit return this year, it hasn't done quite as well as peers such as Truist Financial (TFC) and KeyCorp (KEY). "It's due for a catch-up trade higher," says Katz.

Verizon Communications

The stock, which yields 4.4%, changes hands a reasonable 11 times the $5.06 FactSet consensus adjusted 2021 profit estimate. That estimate is up 3% from the $4.90 per share earnings last year.

“Consensus is for low-single digits earnings growth, but we think that will prove too conservative and hasn’t adjusted for management’s revenue-growth guidance,” says Harrington.

The company’s guidance includes 2%-plus annual service and revenue growth this year and 3%-plus in 2022 and 2023.

Verizon “should benefit from an improving economy and 5G rollout,” says Katz. He adds that it “can comfortably manage through the cost of the recent and very expensive spectrum auction” for government-issued licenses that allow telecom firms to increase their network capabilities.

At its investor day earlier in March, Verizon said that it was committed to its dividend, which it listed as its second capital-allocation priority after investing in the business. Verizon’s most recent dividend increase was last September, when it went to 62.75 cents a share, up 2% from 61.5 cents.

If the company can hold true to its commitment, that should keep the dividend rising and make the stock one that can be relied on for income in retirement.

Write to Lawrence C. Strauss at lawrence.strauss@barrons.com