

The COMPASS Chronicle

July 2014

Vol. 4 No. 7

"Morningstar's Best Client Newsletter"

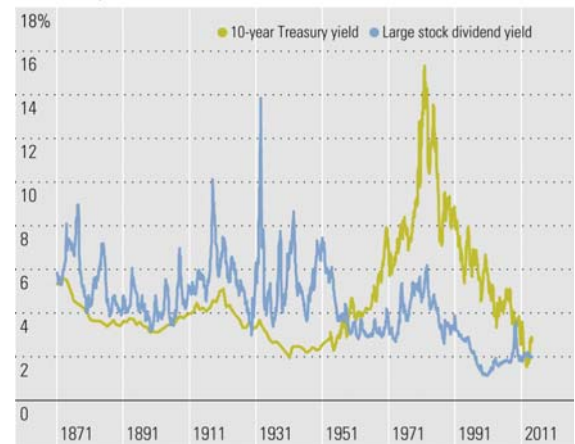
Large Stock Dividend Yield Versus 10-Year Treasury Yield

- ▶ In an article back in October 2011, COMPASS highlighted the fact that the S&P 500's dividend yield was greater than the 10-year Treasury yield.
- ▶ As we stated then, "when this has occurred in the modern era, stocks significantly outperformed bonds during the following 1 - 3 years."
- ▶ Since October 2011, the S&P 500 has gained more than 75%. While stocks are no longer inexpensive on an absolute basis, they remain cheap relative to bonds.

In the recent context of likely-to-rise-at-any-time interest rates, it may be interesting to take a look at the historical relationship between stock and bond yields. As illustrated in the image, stock dividend yields were much higher than 10-year government-bond yields before 1957, with dividend payouts a form of compensation for the additional risk of investing in stocks.

In the more modern period, this relationship has changed. As capital appreciation became a bigger driver of stock performance, bonds became the main engine for potentially steady income generation. After 10-year Treasury rates significantly declined following the 2008 financial crisis, stocks yielded more than 10-year Treasury bonds for the first time since 1957. Recent rising interest rates, however, have pushed government yields above stock dividends once again.

Stock and Bond Yields
January 1871–March 2014



Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. Stocks are not guaranteed and have been more volatile than the other asset classes. Dividends are not guaranteed and are paid solely at the discretion of the stock-issuing company. Government bonds and Treasury bills are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest. U.S. government bonds may be exempt from state taxes and income is taxed as ordinary income in the year received. With government bonds, the investor is a creditor of the government. In general, the price of a debt security tends to fall when interest rates rise and rise when interest rates fall. Securities with longer maturities and mortgage securities can be more sensitive to interest-rate changes.

Data: Large stock dividend yield is represented by monthly S&P Composite Index. 10-year Treasury yield is based on the monthly yield of 10-year government bonds. Both indexes are from Robert J. Shiller's Data Library



Louis E. Conrad II, CFA
President

lconrad@compassinvest.com
(978) 254-7040
www.compassinvest.com

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