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VF INVEST

OUR DIVIDEND STRATEGY

Financial Freedom Through Dividends

In This eBook:

THE DIVIDEND STRATEGY
Security + Dividend = Passive Income

DIVIDEND: STABILITY FOR THE PORTFOLIO
High inflation and growing uncertainty make dividend stocks more attractive.

HIGH DIVIDEND – A WARNING SIGN?
What makes a good dividend stock.

THE DIVIDEND STRATEGY

Security + Dividend = Passive Income

The fundamental prerequisite for any success, especially in the stock market, is setting the right goals. That's why I would like to explain today what you can expect from my dividend strategy — and why this strategy is not only promising but also particularly transparent and easy for you to implement.

RATIONAL THINKING IS THE BASIS FOR SUCCESS

Basically, every person acts according to the economic principle. Trust your gut feeling when it tells you that a promise in an ad sounds too good to be true. The same applies to investing: effort and result must be in an optimal relationship to each other in order to maximize profit and use one's resources as efficiently as possible.

DISTINCTION BETWEEN MINIMUM AND MAXIMUM PRINCIPLE

With the minimum principle, a goal is given and should be achieved with as little effort and resources as possible. The maximum principle aims to achieve the best possible result using limited resources. Applied to investing, these principles can be translated into risk and return.

Important: Just like with any economic principle, these laws cannot be overridden!

Risk and return are always interconnected — if you increase your target return, the risk of your investment automatically increases. Investors lose billions every year by believing promises that claim otherwise.

ATTRACTIVE DIVIDEND YIELDS

You can put together a dividend portfolio with a current yield of eight percent without much effort. For a portfolio worth $150,000, that would generate payouts of $12,000 per year — or $1,000 per month. Sounds tempting?

But please don't forget the rule of risk and return! At present, you'll only achieve an eight percent yield if you compromise on company-level safety and have very limited geographic diversification. In other words, you're almost exclusively invested in U.S. stocks — and in companies whose share prices, and in some cases even their dividends, are highly volatile.

SECURITY + DIVIDEND = PASSIVE INCOME

No investment in individual stocks is completely risk-free. That's why, in the dividend portfolio, we focus on the safety of the dividends. As genuine quality companies, most of the stocks in the portfolio also show relatively stable price trends over time.

But for passive income, the main focus is on the reliability of the payouts, which will increase over the years — and with them, our passive income. That's what it's all about!

As a safety-conscious investor, ask yourself this simple question before every purchase:

Do I absolutely need this company's product — or could I live without it? This mindset helps you build a portfolio for the long term — one that lets you worry less about daily price fluctuations.

DIVIDEND: STABILITY FOR THE PORTFOLIO

High inflation and growing uncertainty make dividend stocks more attractive.

The world has become more uncertain. This applies not only to geopolitics, but also to the economic environment. The global economy and markets are being shaken by shocks like the COVID pandemic and the war in Ukraine. Added to that are the challenges of climate change and disruptive political figures like Donald Trump. Together, these developments call into question two key foundations of stable economic and market development in recent years: globalization and cheap energy supply.

STOCK MARKET VOLATILITY IS INCREASING

This not only dampens economic growth but also causes inflation rates to rise sharply. Such an environment hasn't been seen since the 1970s. It’s no surprise that comparisons are being made to the “stagflation” of that era. As back then, fluctuations in economic growth and inflation are increasing. An unstable economic environment also brings greater stock market volatility than we have become accustomed to in recent years.

SECURITY IS GAINING IMPORTANCE AGAIN

The dramatic rise in inflation has forced central banks to rethink their approach. Interest rates have increased significantly, especially in the U.S. The end of the long-standing low-interest-rate policy by central banks is having a major impact on stock valuations. Future earnings are discounted more heavily with higher interest rates, and high debt levels lead to greater price markdowns. So-called growth stocks, for example in the technology sector, are now valued lower.

As a result, companies with currently high cash flows and proven business models that promise reliable earnings are now being valued more highly. This applies to classic dividend stocks. With the end of the central banks' low-interest-rate policy, an exceptional phase in the markets is coming to an end—one that is unlikely to return anytime soon.

BOND YIELDS ARE RISING

Even safe government bonds are once again generating returns in this environment. However, due to persistently high inflation, real returns in some bond markets remain negative—and this may well continue. Government debt is still growing, and countries must remain solvent. Central banks are, in effect, forced to maintain low real interest rates over the long term to support this.

In recent years, bonds were no longer a real alternative to stocks. That may now be changing with the rise in yields. Over decades, bonds and stocks have competed for investors' attention. Whenever risk-free U.S. Treasury bonds yielded more than 4% above the inflation rate, it often marked the beginning of a major capital shift away from stocks. But, as mentioned, we are far from that scenario. High real yields on government bonds would put massive pressure on the financial system.

STOCKS VS. BONDS

Investors should also remember that there is a fundamental difference between bonds and stocks. Bonds are debt capital lent out for a predetermined period. Stocks are equity capital permanently invested in a company. A shareholder is a co-owner, not an external creditor.

The difference can have significant impacts. On one hand, shareholders have a say in company decisions because they generally have voting rights at the annual general meeting (this does not apply to preferred shares). This puts them in a stronger position than bondholders.

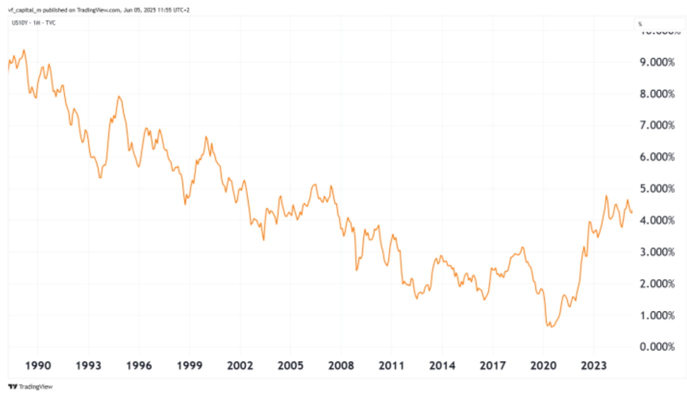
RISK OF INSOLVENCY

However, in the event of insolvency, this advantage turns into a disadvantage. As co-owners, shareholders are last in line when it comes to distributing remaining assets. Bondholders are ahead, since they are creditors of the company. Their risk is therefore lower than that of shareholders.

In return, their upside is limited: they receive only the fixed interest payments during the bond's term and the principal back at maturity. Shareholders, on the other hand, receive no guaranteed payout. But as part-owners, they benefit directly from the company's success, which can lead to rising stock prices and/or dividend payments—or losses, if business results decline.

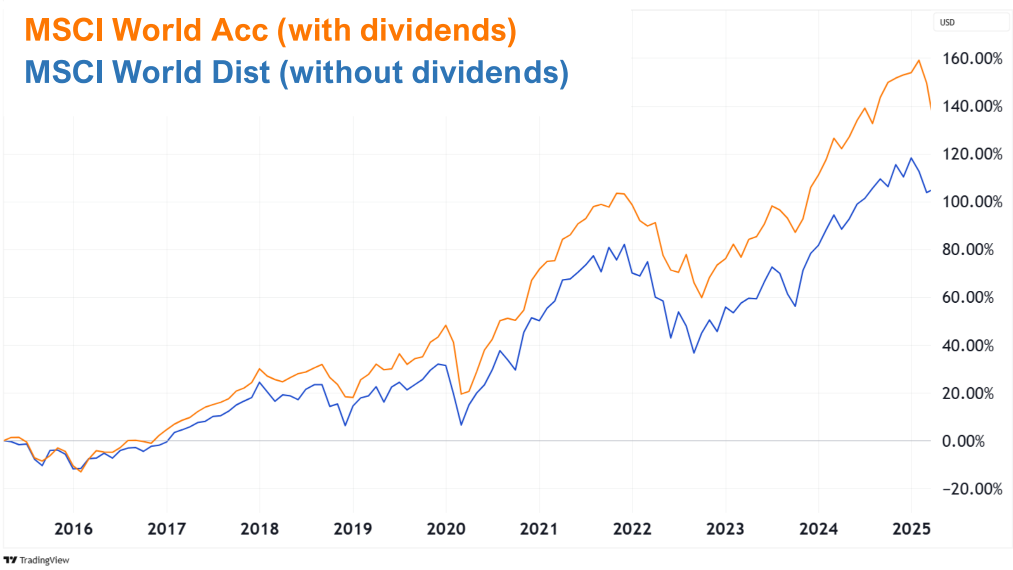
Bond Yields on the Rise?

Yield on 10-Year U.S. Treasury Bonds



While bondholders don't necessarily have to keep an eye on market prices—since they typically receive 100% of their investment back at maturity—stockholders are much more affected by price fluctuations, as the stock price represents a key part of their total return. When a dividend is paid out, that money leaves the company, often leading to a corresponding drop in the share price—a drop that must first be recovered, ideally through strong business performance and future profits. That's why stocks offer greater potential returns than bonds, but also come with greater risks. Investors should therefore be especially selective when choosing dividend stocks—to avoid any unpleasant surprises.

MSCI World With and Without Dividends



Dividends are an important factor for successful investing. This profit-sharing significantly contributes to overall returns—and therefore to the success of an investment—and provides shareholders with a welcome income stream that can be used to supplement retirement or pay for the next vacation. Ideally, dividends are reinvested into stocks to generate even higher returns through the power of compound interest and to maximize one's personal income stream.

HIGH DIVIDEND – A WARNING SIGN?

What makes a good dividend stock.

Dividends are profit distributions — and for that, a company must first generate profits. Of course, dividends can also be paid out when companies are making losses, but doing so consumes substance and weakens the company over time. That is not a promising strategy.

Net Income vs. Free Cash Flow

Net income shouldn't be overestimated either. Since the revision of accounting standards (IFRS 16) a few years ago, its significance has declined. Profit and loss statements now also include valuation changes — i.e., write-ups or write-downs on securities or subsidiaries — which can cause large swings in reported earnings. Nonetheless, the principle remains: dividends must be earned. That's why the focus should be on free cash flow — a metric that reflects the result after all operating expenses have been paid. Free cash flow is then available for acquisitions, stock buybacks — and for dividends.

Coca-Cola vs. General Electric

Let's take a look at two well-known U.S. corporations: Coca-Cola and General Electric. Both were long considered among the most attractive dividend stocks in the world. For Coca-Cola, that's still true — but not for GE. In early 2005, General Electric was the most valuable company in the world. But then came a prolonged decline. In 2018, GE — the last original member of the Dow Jones — was dropped from the index. It then had to sharply cut its dividend, losing its status as a Dividend Aristocrat — a double blow for the industrial icon. Still, many investors remained loyal to GE. Even as the business deteriorated and the stock price kept falling, the dividend yield looked attractive — but it was a trap.

In 2018, GE's dividend yield climbed to over six percent — based on the payout from the previous fiscal year. No surprise there: when share prices drop but dividends remain unchanged, the yield rises. That lured many dividend hunters into holding or even buying more GE shares. But this should serve as a clear warning to all investors: Dividend yield says little about a company's health.

If business performance weakens and the stock price plummets, the yield rises artificially — until the dividend is eventually cut or eliminated. Then investors are left with the wreckage of a failed investment. That's exactly what happened with General Electric: By 2018, the dividend was halved, and shortly after, nearly wiped out.

In April 2024, the company finally pulled the emergency brake: the remaining GE conglomerate was broken up into three independent companies: GE Aerospace, GE Healthcare, and GE Vernova.

Dead Weight Doesn't Belong in Your Portfolio

Many investors fear losses so much that they ignore clear warning signs and hold onto failing stocks.

The brain plays tricks — convincing them that a loss only becomes real once the stock is sold. And as long as dividends are being paid, they cling to the idea that things aren't so bad. Especially since falling prices make yields look even more attractive. But investing requires objectivity and honesty.

Even the best investors in the world are wrong nearly half the time — the key difference: they cut losses early and let winners run. Average investors do the opposite: they hold onto losers and sell winners too early. The result? A significantly below-average return.

BACKING WINNING COMPANIES

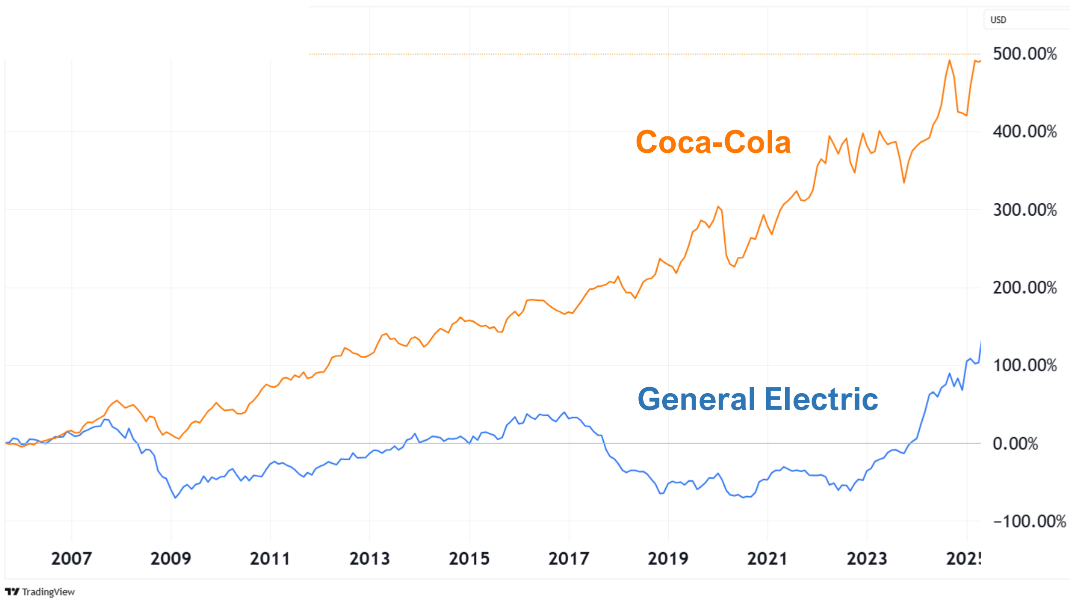
The key is to invest in successful businesses — companies that generate sustainable revenues and profits. Ideally, these firms have a wide economic moat that protects them from competitors. These enduring competitive advantages are what fuel steady earnings over time. What else matters? A seasoned, disciplined management team and a clear focus on shareholder value.

Take Coca-Cola as an example. Thanks to its powerful brand and smart corporate strategy, it consistently produces strong earnings. More importantly:
Its cash flow is robust enough to support dividend increases even in weaker profit years. Since 1988, Coca-Cola's dividend has never been cut — only raised. Yet in 2018, its dividend yield was "only" about 3.2% — roughly half the yield of General Electric at the time. Investors who chased high yields instead found themselves holding stocks like Daimler, Deutsche Bank, or General Electric. Too bad.

PAYOUT RATIO & DIVIDEND GROWTH

Instead of simply picking stocks with the highest dividend yield, investors should focus on other, more meaningful criteria. One key metric is the payout ratio, which indicates what percentage of a company's earnings is paid out as dividends. The higher the ratio, the less room there is for future increases. For example, with a payout ratio of 30%, a company can still raise its dividend even if profits stagnate, whereas a company already paying out 80% of its earnings has limited flexibility. Another important factor is dividend growth and the company's dividend history. If a company increases its dividend by 5% to 10% each year, the yield can keep pace with rising share prices. Over time, even a modest starting yield can develop into a powerful income stream and significantly enhance returns through the power of compounding. Dividend growth stocks are therefore the most promising long-term dividend investments.

GENERAL ELECTRIC VS. COCA-COLA (including dividend payments)



General Electric struggled for years with growing problems. Time and again, parts of the company had to be sold off to service its crushing billions in debt, while revenues collapsed. In contrast, Coca-Cola has remained consistently successful to this day. The beverage company has increased its dividend every year since 1988.