Episode 32: Three Key Reasons Why Investing for Dividends as a Retirement Income Strategy is a Mistake

Bob French 00:00
The purpose of Retire with Style is to help you discover the retirement income plan that is right for you. The first step is to discover your retirement income personality. Start by going to risaprofile.com/style and sign up to take the industry's first financial personality tool for retirement planning.

Alex Murguia 00:42
Hey, everybody, welcome to Retire with Style. I'm Alex, and I'm here with Wade, foul. We're getting ready to roll another one. Wait, what are we going to talk about today?

Wade Pfau 00:57
We're going to talk about a very popular topic on if you ever read an article on Yahoo Finance or anything like that about the 4% rule, and then read the comments. You'll read a number of comments and say, What is this 4% Rule nonsense, I've put together a portfolio of dividend paying stocks giving me a 6% dividend yield, the 4% rule is meaningless. And so we're going to be talking about this idea of investing for income. leaning into higher yielding dividend paying stocks or with bonds, it's the same sort of conversation around higher maturity, longer maturity or credit risk, to seek out a higher yield, and how that may not ultimately really create additional value for the retirement plan. It's popular in comment sections on finance articles. But it's not been an issue that's been really analyzed or explored in terms of the historical data in the same way that the 4% rule has. And where economic theory really points to the idea that no, there really shouldn't be anything, they're leaning into higher yielding stocks and bonds should not give you a higher withdrawal rate for regard to and just It's the basic matter.

Alex Murguia 02:13
Just to recap this way, this is also part of the previous stuff that we've been talking about, where we got into why 4% rule may actually be too high. And so this episode is it's nothing really against the 4% as it relates to the total return. But a lot of folks take this 4% rule and impose upon it a dividend strategy to to get that 4% Or even higher, as we pointed out, correct?

Wade Pfau 02:39
Right, we're in a series of probably three episodes talking about why the 4% rule might be too high, or what that really means is where when you change assumptions behind the 4% rule, you might end up with a lower withdrawal rate number. Now later on, we'll talk about there's a whole host of reasons why the 4% rule might be too low. But in particular, today, what we're talking about is the 4% rule assumes

you have a total market portfolio, you invest in total market stock and bond indices, you invest for total returns, you don't worry about the breakdown between cash flows kicked off of the portfolio, in the selling of principal defend retirement expenses. And the violation of that assumption that we're talking about today is no you you move away from total returns, you lean into higher yielding

Alex Murguia 03:28
Wow the word violation. Wade, sounds serious,

Wade Pfau 03:32
violating the assumption.

Alex Murguia 03:35
What Why do you think this is just anecdotally, based on your experience read in Why do you think it's such a popular idea? Income investing, investing for dividends, investing for yield, as opposed to thinking the portfolio as a whole or whatnot? What's your take on that?

Wade Pfau 03:56
Well, I think it can just intuitively sort of make sense that if I can put together a portfolio that's kicking off 6% income, and I never have to sell a share, why wouldn't that be a better retirement strategy? I just think intuitively it sounds appealing. Now, the the issue is, is it actually going to work better, but I think intuitively it sounds good. Yeah.

Alex Murguia 04:19
No, I've debated that myself. Oh, what do I think? Oh. No, I, I I actually I agree with you. 100%. I also think it's one of these things from a bygone era error. Well, I don't know which word is appropriate, maybe both era. And by that, I mean, you know, when stocks really used to kick out dividends A while back, you know, many, many times it was higher than than bonds at a certain point. It kind of flipped the other way around. But it seems to me and the old school way investing was just thought like that, you know, get good quality stocks that kick up a dividend and from that dividend, you get your cash flow? I don't I don't see that to be the case that much anymore. But there's something there that has remained. And frankly, I think the Wall Street uses that. And many advisors use that. And many reporters use that as almost like a gimmicky is too strong of a word, but almost like a way to, to get eyeballs or to attract certain strategies that, you know, from an economic standpoint, there's nothing wrong with them. But by the same token, there's nothing good with me that you know, by good, I mean, there's nothing above and beyond why you should use them relative to other strategies. If anything, it limits the purview of potential other investment strategies we'll we'll get into but we this, we see this quite quite a bit this, this whole investing for income, versus just a total return approach.

Wade Pfau 05:51
I think there could be a behavioral piece to where people generally don't like having to spend down their nest egg or they don't like to sell shares to fund retirement expenses. And so behaviorally, it kind of feels like the idea of spending your paycheck. Well, if you put together a portfolio that's providing you this paycheck of interest and dividends, you're not having to sell shares, there could be a degree of

comfort in that or reassurance that I'm not going to spend down my assets because I'm not selling my asset. And so certainly, that could be part

Alex Murguia 06:24
of what if you don't mind, though, taking us through the calisthenics of, of why do we say that there really is no benefit from taking income in the form of dividends, versus just creating your own dividend by just selling shares yourself to, to, you know, to raise cash? What why is that? Why is there no benefit one way or the other?

Wade Pfau 06:48
Well, at the basic finance theory, kind of the value of a stock is the present value of its future dividends. And I don't know if this is always commonly or always understood, but when a dividend is paid, the stock price reduces by the amount of the dividend. Now, at the end of the day that the dividend is paid, that may not be an exact thing, because there's capital gains and capital losses going on every day. But the stock price falls by the amount of the dividend. And that's where nothing in a pure economic sense has changed between having a higher price stock that didn't pay a dividend or a stock that reduced in price by the amount of the dividend paid.

Alex Murguia 07:30
So that's important if you if you had, so you think about a way to saying if you had 100 shares of a stock, and they're priced at $20, you effectively have $2,000, that your portfolio is worth $2,000. Now you can sell a certain amount, you can sell $100 worth of it. And there you have it, but let's say the stock, you know, you have 100 shares and the issue $1 in dividends, you know, all of a sudden that price goes down to $19. And they've all those, the company has effectively kicked out to you by $1, share in for dividends 100 bucks. So it's effectively the same thing. So you shouldn't there isn't one Yeah, the $1 either if it comes through dividends, or if it comes through capital gains, is economically the same, not without any tax considerations. I'm not, you know, ordinary dividends, qualified dividends. I'm not going to get into that right now. But that's depending on your holding period. But effectively, it's the same economic transaction.

Wade Pfau 08:33
Right. Right, without taxes. And that's the other thing. I mean, taxes actually weaken the case for the dividend paying stocks, but ignoring taxes. Yeah, it doesn't really matter how you extracted that portion of your assets, whether it was through a dividend or whether it was through selling shares you, you have the same number of shares, but they're worthless after the dividend is paid.

Alex Murguia 08:54
Yeah. So So conceptually, what really is going on there, and that's where we want to make sure that you're making the right decisions. And so when you get, you know, presented with these dividend strategies with these sort of things, I'm not sure they're necessarily an improvement worth worth versus what could be done from a total return standpoint. And I would go so far as to say as you're limiting your opportunity set in which you can extract ongoing equity premiums over the long term. Now, that's that's as it relates to stocks real quick in terms of bonds. We see this a lot in McLean, where someone comes in with these bond portfolios, especially as returns have, you know, as yields have gone down,

although they're heading back up, where, you know, over the long term there, there really is a little bit of a premium for maturity for extending maturities. But once you get past a certain point, there's not much there. And there is a little bit of a term premium, but it's nothing. It's nothing to go crazy about right. And so the danger that happens is there's this There's this desire to start chasing yield. There really is. And when you start, like just, when you start thinking about it in terms of mental accounting, like yield, this bond is gonna give me 5%. And you know what, that's 1% over the 4% rule. So that's a heck of a deal. There's a danger to do that. And ultimately, what happens is you're really taking more outsize risks than you wanted to to begin with. Now, this is separate from time segmentation, where you're matching liabilities, exactly. You know, this is this is where we're sticking to the total return probability safety for probability optionality side of the quadrant right now. And so from that vantage point, fixed income, should serve as more of a ballast, and you shouldn't even it shouldn't be a consideration from the standpoint of taking distributions from it or not, it really serves as a balance to the equity portion. So you really want to sort of watch yourself when it comes to that. Wait, it you I've heard you say this, and it merits saying and again, what's what's an analogy that folks use? That I think I've heard, I heard it years ago, and I've never forgotten it, and I use it quite a bit when it comes to earmarking dividends versus a total return approach, you know, and I'm thinking precipitation here. What's, how does that analogy go? Because I think that's something that really hits home whenever I hear it.

Wade Pfau 11:21
I'm not exactly sure what analogy really

Alex Murguia 11:23
the one about No, well, I'm sorry, like water from a well. It's

Wade Pfau 11:28
may be new to me. Oh, really?

Alex Murguia 11:28
Okay.

Wade Pfau 11:30
Why don't you? Why don't you?

Alex Murguia 11:35
Effectively, if you think about it like this, you know, dividends, there's many ways you can you can create a distribution amount, right? You can get it from wherever, right? So think about water in a well, right, you're taking water from oil. So it's very similar to taking this sustainable distributions, right? You don't concern yourself when you're taking water from a well, if the water came from snow, if it came from rain, if it came from morning dew or whatnot, you just are concerned that there's water there, you're not like you don't have a special bucket, that's just going to pick up rainwater, a special bucket that's just going to pick up snow, a special bucket that's just going to pick up morning dew or whatnot, you're just taking it from the well, it's that's the way I view, the ability to take sustainable withdrawals from your portfolio, I'm less concerned, I'm not concerned at all, frankly, whether if it's coming from a dividend, or it's coming from capital appreciation, and I'm just cutting a slice of that appreciation for

myself. And that's that's a better way of looking at this than to getting into the game of mental accounting with dividends. Now, some of you may point out, well, there's been studies about this, right? There's been studies about this, how they do relative to others, I mean, popular book was the dividend aristocrat, things along those lines. And what you'll see over the long term, that there is no above average return provided by dividend stocks relative to the factors that they are naturally exposed to. And what I mean by that is, you know, you're able to assess how much value stocks bring to the table, or you know, what the expected return is of a stock based on a few factors, right, their market beta, their exposure to size, small cap stocks, and up from larger cap stocks, their exposure to value, value stocks tend to outperform growth, your stocks, their exposure to momentum, their exposure to a quality factor, which is a relatively new one. And this, this determines roughly 95 98% of the expected variability, fall stock market returns. And so when you look at dividend stocks, you know, they have a little bit more exposure to quality, they have a little bit more exposure to value, but you can capture that passively without having to go all in into dividend stocks. And so a way of saying that there's there's many stocks in the stock market that have these types of exposures that don't provide dividends, you know, but they have the same expected return as dividend stocks. So why would you reduce your opportunity set within the investable universe by just focusing on dividend stocks, it would be akin to, you know, I want to there's their stocks A through Z, they all have the same expected return. But you know what, I'm going to invest just in stocks A through M, and stocks N through Z, I'm going to forget about why because they don't start with if they don't start with the letter A through M. That really is the case there's no above and beyond reason why dividend stocks will outperform other stocks that have similar exposures to these risk factors. Wade, you want to go into that a little bit?

Wade Pfau 14:40
No, I think that makes a lot of sense. And it's, again, what I've also seen kind of explained about this is with when you lean towards yield, you're trading current income for risk to future income because like you're saying you're moving away from the total market portfolio now. The total market portfolio pay as dividends and interest, it's just they may be lower than the spending goal. And that's the difference is when you shift away from the total market portfolio, lean into dividend paying stocks or higher yielding bonds, you're moving into riskier sectors of the market, ultimately, and you might get more income today. But the if the total returns are equal or less than the, for this sub sector of the market that you're going into, over the long term, you're not going to be in a better position, a lower total return, doesn't matter how high the dividend yield is, you're gonna spend on that asset base quicker. And that really is the concern with these sorts of income investing type strategies.

Alex Murguia 15:47
No you're absolutely right. And there's risk, there's risk in the in the concentration factor in from a concentration point of view. And again, I believe I said it earlier, but like 60% of US stocks do not issue dividends, 40% of international stocks, don't pay dividends. And so you're really excluding them. And so you could say, well, I don't need that, you know, what if I get 10, good dividend paying stocks, then I feel good about that. Or if I get 20, good dividend paying stocks, and I feel good about that. And now then it's just basic portfolio construction one on one, as much as you feel good about the dividends. I mean, you're taking an exorbitant amount of risk relative to your retirement safety to put to put your whole entire income strategy on just 10 stocks or 20. stocks or what have you. And at that point, you know, ignore all the studies that Wade has done that has done on the 4% rule, or that, you know, we've

just brought up because the reality is it doesn't apply, if you just have 1020 stocks. I mean, it's hard enough to get a sustainable control hurry with 3000 stocks. All right, Wade, I mean, you want to maybe

Wade Pfau 16:54
right here, you're not using the assumptions of the 4% rule. There's the tracking error, you're not the 4% rule is based on total market portfolio returns, you're not using that assumption. So you can't rely on that research. Yeah, to know what a sustainable spending strategy when

Alex Murguia 17:12
because, you're not diversifying away from company risk at that point. And that's, that's the risk that you're not necessarily compensated for. And we can't, you know, we, it's too much noise at that point to really make any conclusions with regards to what the sustainable withdrawal rate is. And that's very important. I mean, you can take these, these, these assumptions, but it really goes down to having a market portfolio. And that was one of the reasons why in the previous episode, we said why may be by may be too high of 4% rule may be too high, because investors kind of muddy things up a bit. And this is one of the prime ways to muddy things up where you sort of think to yourself, well, you know, what, I'm gonna back into a 4% rule by looking at dividends. And if you know, what if I get stocks that effectively pay 4%. And it's 30 of them. So you know, what, I'm diversified? Not really, you know, you're diversified in the sense that maybe the standard deviation equates to what the market standard deviation is, but that the, the tracking error is going to be immense. And the opportunity cost is, you know, you're not going to be diversified across all the industries, etc, etc. And so it's troublesome in there and by concentration, ask yourself, what are the companies that issue dividends, and again, there's nothing wrong with dividends, we don't want to sort of paint them in a bad picture. It's just when you're trying to capture market returns, you have to expose yourself to market returns. And the sustainable withdrawal rate strategies are based on capturing market returns efficiently. Another thing Wait, that I just wanted to point out is, there is and you pointed out there there's there's a little bit of a behavioral sort of thing going on here. And it's interesting, because there's been studies by Chevron and Statman, that that really begins to point this out, because I think what you're referring to is there is no economic reason why a dividend is better than just taking a you know, selling, selling and taking the game and creating your own dividend. There shouldn't be a one better than the other, if you will. Well, I would say the sustainable the total return is better. But you know, the economic the dollar is the same from from any pile right. And and ceferin and Statman point out. And I don't know, I don't have enough conversation of backdrop to point this out. And I think they're just posing this as well, but it's an interesting concept. And what dividends do provide is this ability to control to control spending a little bit what they start saying is, well, you know what, we have trouble as human beings delaying gratification. I only have that problem with marshmallows on the table. But that's that's it. No human beings have trouble with delaying gratification. So what the dividend a dividend policy does do is it kind of does it for the person, it kind of just, you know, the person doesn't really have to sell the person doesn't have to buy, it just stands back and wait for that dividend check to come in in cash and takes it. And so it's really a matching of a cash flow piece that that seems to kind of have a lot of interest with folks in terms of doing that. And that may be I'll take a step further, that might be maybe why sometimes folks get an advisor, because they effectively function as that person cutting that check. And sending the two of them were the person who doesn't have to do anything themselves. What do you think about that way?

Bob French 20:42
If you're looking for more personal advice, please know that our show is sponsored by McClean Asset Management. Learn more at McLeanam.com. That's McLeanam.com. McLean Asset Management is a wealth management firm where we help you design and implement the right retirement plan for you.

Wade Pfau 21:05
Yeah, yeah, for somebody who's, I mean, there's many examples of this kind of, I'm worried about overspending. I don't feel like I have the willpower to control that. So I might just overpay taxes is a forced way to get that tax refund that I'll then save, or in this context. I don't have the self control. But if I can just frame things as I'm allowed to spend my dividend, and I'm not allowed to sell any shares. That could be a way to just create that generate the the behavioral commitment, the general idea of, okay, this is how much I'm allowed to spend. Now, you could deviate and spend more, but at some level, you kind of just okay, here's a rule that I'm going to apply to my situation, I'm allowed to spend dividends, I'm allowed to spend interest, I'm not allowed to sell shares. And that can help me to avoid overspending. Souza, so I can imagine that some people might employ that sort of behavioral trick. And that might be why they liked dividends and interest

Alex Murguia 22:05
sort of to you from profligacy to some extent. I don't know. I mean, the way I would see it in the way I've spoken is, to me, it's like allowing a board that say, these companies are made up of boards and the boards, you know, implement dividend policies. It's like allowing a board to kind of determine what your income should be. And this board knows nothing about you. You know, and I'm like, why, why would you do that? Yeah, I mean, I got past my allowance, you know, when I was I don't know, at 10 years old, right? After that, you know, I can I can manage. It's one of those things. But yeah, I guess it helps for some folks. And this is where I think it still goes back to that old way of thinking. And by old way, I don't mean like, this is your dad's Oldsmobile, or this kind of stuff. I just think it's a bygone era where it was kind of unknown way. But science moves forward. You know, through much of the research being done through ways research, you know, there's there's ways that point out, there's optimal ways to do this from a total return strategy. And if you're agnostic, as you should be to where the money comes from, think about the precipitation example. It shouldn't matter at all. I mean, I think, I think you do yourself a favor by just getting out of that mindset, frankly, because it's mental accounting, that can be very tricky. Another another thing that these guys point out, Wade, is that okay, that's from the I'm gonna give you guardrails. So spend what your dividend is, and that's quote, unquote, your allowance. But there's a there's a loss aversion piece to this, that that is interesting, as well.

Wade Pfau 23:41
Yeah, that people don't like experiencing losses. And if I'm investing with a total return portfolio, and the market is down, that could force me to realize a loss, that makes me very sad. The dividend and the dividend investing approach kind of gives you a backdoor to not have that mental image because the market may be down, but I'm just spending my dividends I'm not selling at a loss. I don't have to deal with this psychological dissatisfaction of selling at a loss.

Alex Murguia 24:13

Again, going back to what you said in the beginning, it's really the same thing because the dividend reduces the price per share by the dividend. So it's kind of a funny, a funny thing. You really are, but you're not, you know, that can be.

Wade Pfau 24:28
Yeah, and it'd be interesting if economists always like to come up with these explanations that intuitively make sense. But whether or not people are actually this is they may not even necessarily verbalize it, but they're implicitly behaving this way. It's just internally this is what they're doing. I don't know it seems kinda like a stretch,

Alex Murguia 24:47
but no, I see this a lot. I see folks, I see this with prospects coming in. Not necessarily clients because clients you know, if they are going to be in the total return approach, it is a total return approach. We don't have like a dividend, a dividend strategy. There are some firms that do that. And they give it some acronym to sound off fancy or kind of like, this is our, you know, intellectual property dividend lever strategy. And I think that's a loaded garbage. Honestly, I know it is. I think it's just done to kind of appeal to your behavioral sensibilities, but there's nothing there's no there there, unfortunately. And I, you know, we don't do the handover heart, we're not going to do something just for that. We're going to do it if it makes sense from a planning from from the planning standpoint. And so I do think there's a lot there, because if you're just collecting dividends, then you can say to yourself, Well, I'm not really spending down principal. Right, in case in case you had started a 4% rule, right? The other piece is if it, if it goes up even better, right, it's like you're everything is gravy, you're playing with the houses money. But again, if it goes down, you don't feel like you're selling at a loss. And you know, going that losses are have a greater emotional valence than gains, I do think there that has something to do with it. You know, that sort of regret avoidance, if you will. But again, there's, there's this this is, you know, in this episode, there's a couple of points we really wanted to hit home on. Because this is something that it comes up a lot, it comes up a lot, you're going to read it, there's going to be some guy writing some book or woman writing a book about dividends or an article about it. And it shouldn't matter, it really should not matter. The reality is this, there's three main points $1, dividends, versus $1, from selling from selling an asset is the same thing. It's irrelevant. And frankly, you have more control of it, when it comes via total return approach. You know, frankly, we're all about being agnostic versus strategy and so forth. But a case, a strong case is made that a total return approach is just better, a better option for you then matching it to dividends. The second point,

Wade Pfau 27:03
and we hinted at the tax issue, yeah, that's never really went that much in depth. But if your dividend is all the qualified dividends that are taxed at preferential rates, and you're spending it, because with any sort of retirement withdrawal strategy, you'd spend any dividends and interest first, and then if you needed more income, you'd sell some shares. So if it's all tax qualified dividends, and you're spending it all, it doesn't really make a difference. But if you're receiving more dividend than you might actually want to spend, even with a qualified dividend, you're still front loading taxes, because you're having to pay the tax on it, and then you might reinvest it. Whereas if it was unrealized, long term capital gains, you could defer the taxation longer. That's exactly right. And that's where the the, the when you overlay taxes, the dividend strategy looks less held in that regard.

Alex Murguia 27:57

Thats exactly right. And so that's the first point. And again, if you had to think of the the analogy that's sort of a transfer at the beginning, but it's effectively that well, think about, think about withdrawals as precipitate water, you're taking water from a well, you don't care about the sources of precipitation, you just care that the water is there, right? Same thing, you know, you don't care about snow, rain or morning dew, you just want water. Same thing when it comes to sustainable withdrawal rates, whether it comes to dividends, capital gains, as long as it's sustainable, you're golden, because economically, it's the same thing. The second point is, there's no extra added return for investing in dividend stocks, versus investing in stocks that are exposed to the same factors that do not pay a dividend. There's no magical, there's no magic of pixie dust on top of dividends, right, effectively, the expected return, the expected return of any stock could effectively be explained by their exposure to the market, their stocks, the exposure to size, their exposure to value, the exposure to momentum, their exposure to quality. So you can those stocks are plentiful within the market. And so why restrict yourself to just the ones that have dividends, that reduces your opportunity set, and it acts it creates concentration that you don't need and then it violates effectively the sustainable withdrawal rate strategies that we've been discussing. It just does. You know, and the third one is there's the third theme is there's a strong psychological component here. You know, the first one being that you know, it creates this, this this idea that you're not selling principle. You really are though unite that you really are but economically it's the same. So you need to disabuse yourself from that because it really it doesn't jive. It doesn't die from that and you know by but you know, you're not selling prints and the other piece As you're giving yourself kind of an allowance, these companies then through dividends, that's your lawn. So it kind of gives you that, that idea that, Oh, I'm not gonna spend more than what I get in dividends. So this is a three, the three reasons right off the bat, why? For us? I think when you get so focused on dividends, you start losing, you start, you know, losing the forest for the trees here a little bit. Wade.

Wade Pfau 30:23

Yeah, yeah, that's right. And we mostly focused on the stock side, we paid a little lip service to bonds. But it's the same situation there to that, if you're usually there's an upward sloping yield curve, which just means longer term bonds have a higher interest rate than short term bonds. But that's in large part because long term bonds are riskier, a small increase in interest rates, is going to lead to a bigger loss and a long term bond than a short term bond that could wipe out any of that additional yield quite quickly. And then with credit risk, it's you know, you're just taking on more risk, like junk bonds, or whatever the case may be, where you're seeking the higher yield, that is going to lead to more volatility, and not necessarily give you the kind of performance that you're really looking for in the long

Alex Murguia 31:12

You're 100% on target here. And you're right, we kind of bonds are boring, right? So we kind of always just give it lip service a little bit, but way to saying is very, very true. And and and I think more people actually come up to us with portfolios that are searching for yield on the on the credit side than on the high high dividend side. And so from this vantage point, another way of saying what we're saying is term premium, which is the longer out you go, the higher technically, you'll get a yield. But it's not that much once you get past four or five years, from a risk return from a return relative to the standard eight relative to the volatility that that underlying holding has, it's not worth it, it's it's actually less than what you would get from a efficient model kind of asset. It's actually very poor, you know, extending maturity, so it's not worth the extra bump in yield relative to the risk you're taking, even though you may save yourself it's a bond. Yeah, you know, it doesn't matter especially.

Wade Pfau 32:13
Yeah. Well, that's come up in past episodes to where like all of the bill, bank and style research on historical data, its intermediate term US government bonds, where the sweet spots according the highest withdrawal rates, historically, and that's about a five Yeah, once you get past that, once you get past that the volatility doesn't compensate for the tumor. I mean, the yield doesn't compensate for the extra volatility.

Alex Murguia 32:36
Now you may ask yourself, why did have bonds going out that way, that long, who would buy them, those are people that are trying to do different things with their portfolio, like insurance companies trying to immunize their liabilities in the future, etc, you know, think things like that. The other piece is credit, oh, I'm gonna go instead of AAA, I'm gonna do double A I'm gonna do whatever, right. And again, this is in the frame of mind of total return. And so here, fixed income should again be seen as the ballasts to your portfolio, if you're doing a total return, you shouldn't try to think, Okay, I'm gonna take this from fixed income this from stocks, because it's the whole Well, the example again, is precipitation, right. And so what happens with credit premium, you may think everything is good, but what happens is over the long term, when there's moments of dislocation, and that's another way of saying stuff hits the fan, when things just go all out. It's really the high quality, high credit stuff, short term that really remains, the other stuff starts acting a lot more like equities. So all these years that you thought you were getting this sort of, you know, faux safety returns, you know, it just takes one six month period one one week period, to just blow that all up. And that's why you don't get this sort of efficient risk return trade off either for extending not just term, but credit quality. And so you don't want to do that within this within this dividend mindset because it's very easy to fall into the trap of, hey, this triple A corporate bond or whatever is paying 4% But this double B is paying 7% It's only one letter, you know what I'm getting? Yeah, that guy No, no, you don't want to do that at all because it's it's when you need that security dislocation occurs. And and where are you at that point then okay, you still have that dividend but the actual value just dropped you know by orders of magnitude. And, and there it is. Now, we wanted to we wanted to take time we were thinking to wait an hour debating, okay, do we include this as a bunch of others? We wanted to just take time and just discuss this one alone because we feel it's important this this is something that comes up quite often in terms of this dividend dedic dedicated portfolios when it comes to total return. And so I wait I feel good about it. anything we've discussed? Is there anything we may have missed?

Wade Pfau 35:03
No, I think we covered it. And so kind of leading into the next episode, we'll have one more on why the 4% rule might be too high. And that relates to the 4% rule ignores taxes, it assumes you're willing to spend your assets down to zero, and it assumes just 30 years, which may not always be a long enough time horizon. And then we'll have to that we'll get into why the 4% rule might be to be optimistic. This was an important. This is an important topic that actually doesn't get a lot of coverage other than people always just saying, Well, I invest for income. So I, this whole 4% real conversation is nonsense. And so

it was worth unpacking that a little bit today. So thank you for that. Alex. You're the one who pushed to have a more of a unique episode on this topic. So it was a good idea

Alex Murguia 35:50
Alright Wade. Well, thank you, everyone, and we'll catch you next week, right?

Wade Pfau 35:58
Yep, thanks. See you next week.

Bob French 36:00
Wait and Alex are both principals in McLean Asset Management and Retirement Researcher. Both are SEC registered investment advisors located in Tyson's Virginia. The opinions expressed in this program are for general informational and educational purposes only and are not intended to provide specific advice or recommendations for any individual or on any specific securities. To determine which investments may be appropriate for you, consult your financial advisor. All investing comes with the risk including risk of loss. Past performance does not guarantee future results.