INCOME FOR INCOME
INCOME FOR GROWTH

If Einstein described compound interest as "the most powerful force in the universe", its about time it was applied outside of just bank accounts and interest bearing deposits. Compounding is equally applicable to the share market, with reinvested equity income (dividends) working to grow your investment in a similar way. So equity income portfolios are not just for income investors – equity income can also generate growth.

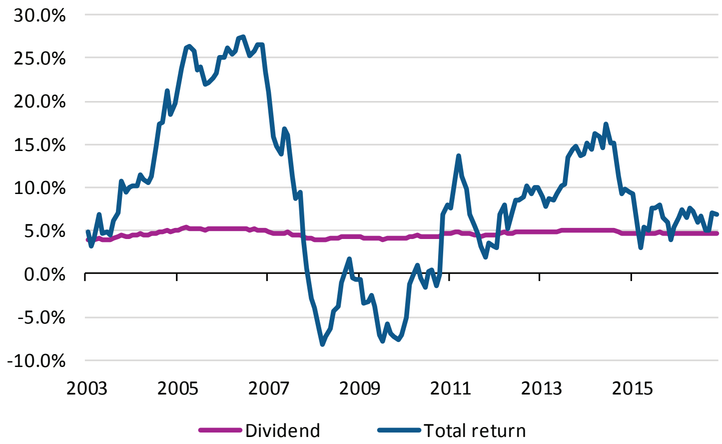
Compound dividends

Just as interest paid into your bank account earns more interest, share market investors can choose to reinvest their dividends back into the market to enhance returns. Reinvested dividends not only earn more dividends, they also help to grow the capital you have invested. This provides a larger base on which you can potentially earn further capital gains and dividends. So reinvested dividends are a powerful source of investment growth.

Dividend share of total returns

Dividends also comprise a significant portion of total share market returns, hence they are just as important to growth investors as they are to income investors. As the chart below shows, dividends are the stable, reliable portion of total returns as they are nowhere near as volatile as capital gains.

Australian sharemarket – rolling three year returns



Source: Bloomberg, 21 Nov 2017

They also play a number of different roles over the economic cycle. In periods of strong capital gains (eg 2004-07), dividends enhance total shareholder returns. In downturns like the Global Financial Crisis (2008-09), solid dividends help offset capital losses, cushioning the negative impact on investors. In periods of relatively low capital gains (eg 2015-16), dividends actually comprise the "lion's share" of total shareholder returns.

The imperative of income growth

Investors seeking income – whether for income's sake or for growth - should focus on solutions that can provide a sustainable, growing and real (after inflation) income stream, while also protecting their capital base. A successful equity income fund needs to target quality companies whose dividends are generally expected to increase and use active management of company selection to ensure the potential for long-term capital growth, which increases the value of units for the investor.

Legg Mason's equity income specialist

The **Legg Mason Martin Currie Equity Income Fund** (Fund) has both these attributes as well as several other proprietary strategies to generate reliable income growth:

- A unique distribution each year that re-invests net realized capital gains back into additional units, thus growing the investor's capital base and providing stable cash distributions.
- A natural bias to companies in sectors that match consumer spending patterns, providing a natural inflation hedge – as prices increase consumers will pay more while investors can expect higher dividends.
- A transparent and cost effective portfolio that focuses on company dividends and does not use derivatives to generate income.

The Fund is rated highly by research houses. It has a strong performance track record in that it delivered investors a total return (net of fees) of 12.6% pa over the past five years[1] and is ranked in the first quartile in its peer group over both 3 & 5 years.[2] The Fund is expected to provide a dividend yield of 6.9% (grossed up for franking credits) over the next 12 months on a forward-looking basis.[3]

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