

S&P 500 Dividend Aristocrats

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- Since 1926, dividends have contributed to approximately one-third of total return while capital appreciations have contributed two-thirds. Therefore, both sustainable dividend income and capital appreciation potential are important to total return expectations.
- Managers use stable and increasing dividends as a sign of confidence in their firm's prospects, while investors consider such track records as a sign of corporate maturity and strength.

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- The S&P 500 Dividend Aristocrats Index measures the performance of the S&P 500 index constituents that have followed a policy of consistently increasing dividends every year for at least 25 consecutive years.
- The S&P 500 Dividend Aristocrats Class of 2009 includes 52 securities diversified across 10 sectors. The constituents have both growth and value characteristics.
- The composition of the S&P 500 Dividend Aristocrats contrasts with that of typical dividend oriented lists and benchmarks that have high exposure to Financials and Utilities sectors and have a steep value bias.

Introduction

Dividends have fascinated investors and theorists since the origin of modern financial theory. As such, voluminous research has been written on various topics related to dividends and dividend paying firms. Despite inconclusive evidence of whether or not dividend paying firms are better investments or whether or not dividends are more important risk factors than size, sector or other fundamental metrics, the undisputable fact remains – dividend yield is an important component of total return.

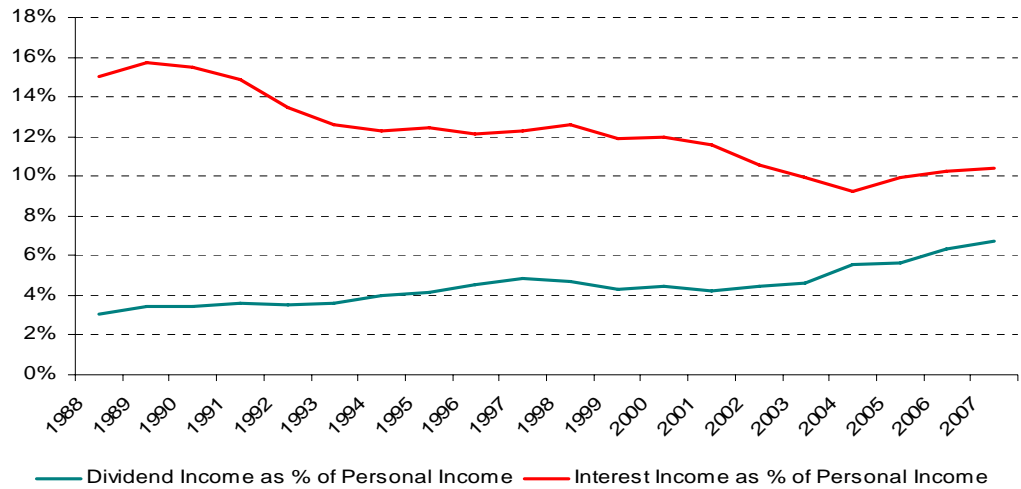
In this paper, the S&P 500 Dividend Aristocrats Class of 2009, a list of S&P 500 constituents that have increased their dividend payouts for 25 consecutive years, is introduced and discussed.

Importance of Dividends

Dividends are an Important and Growing Portion of Personal Income

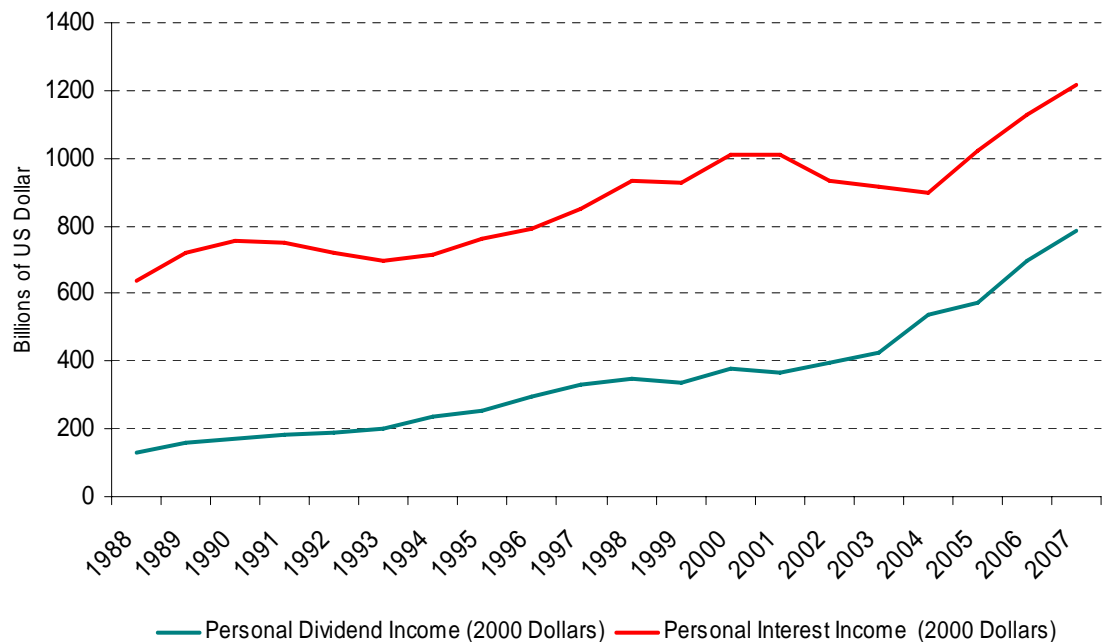
The percentage of the dividend income as part of personal income has steadily increased over time making dividends an important source of income. In 2007, dividend income comprised 6.7% of per capita personal income in the United States, compared to 4.8% ten years prior and 2.8% twenty years prior. During the same period, the source of income from capital markets, interest, steadily shrunk from 15.03% in 1988 to 10.41% in 2007. The value of total dividend income in 2000 has increased significantly from US\$ 129.7 billion in 1988 to US\$ 785.8 billion in 2008, representing over 600% growth. Interest income, on the other hand, grew only 189% during the same period. Exhibits 1 and 2 chart the growing importance of dividend income versus interest income. As equity ownership becomes even more ubiquitous, and a growing number of retiring Americans seek income-generating assets, the importance of personal dividend income will increase.

Exhibit 1: Dividend Income as Percentage of Personal Income



Source: Bureau of Economic Analysis

Exhibit 2: Dividend and Interest Income (in 2000 US Dollars)



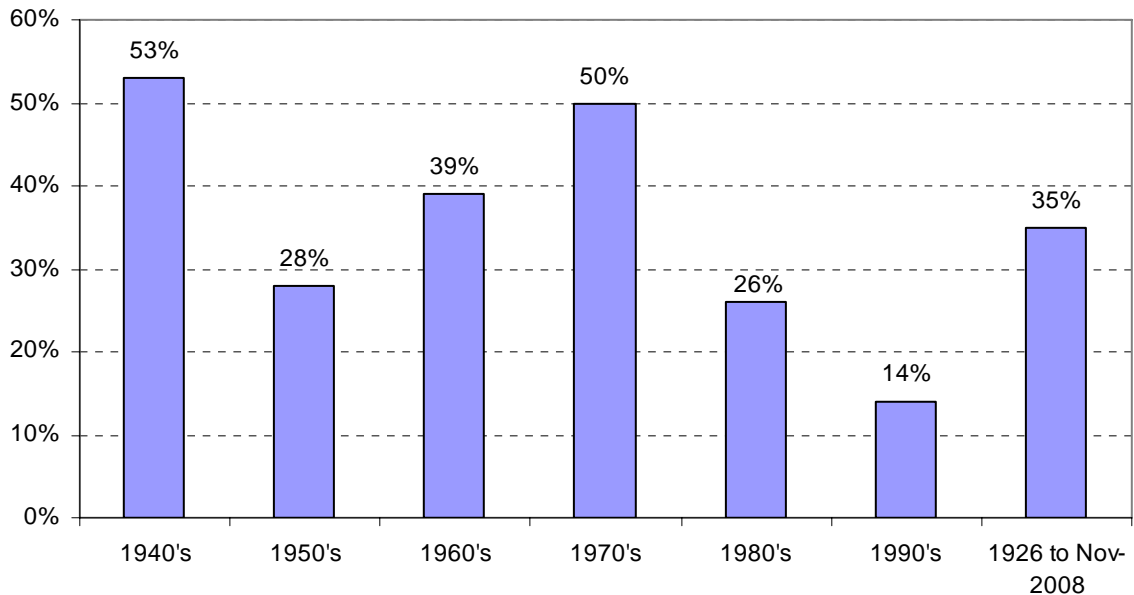
Source: Bureau of Economic Analysis

Dividends Contribute to More than One-Third of Long-Term Total Return from Equity

Historically, dividends have contributed approximately one-third of total equity return. Exhibit 3 plots the contribution of dividends to the average monthly

total return of the S&P 500 through several decades.¹ From 1926 to November 2008, dividend income constituted 35% of the monthly total return of the S&P 500.

Exhibit 3: Dividend Income as a % of the Monthly Total Return of the S&P 500



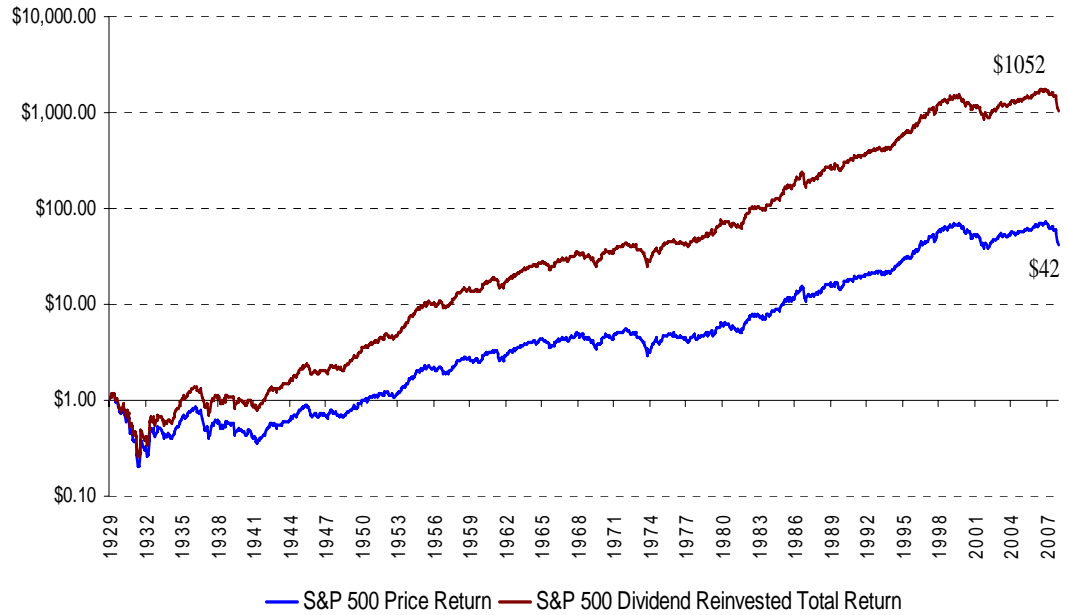
Source: Standard & Poor's.

Compounding Effect of Dividend Income

Another important aspect of dividends can be observed through the effect of compounding, as illustrated in Exhibit 4 and 5. Excluding dividends, a US\$ 1 investment made in the S&P 500 on January 1, 1930 would have grown to US\$ 42 by the end of 2007. During the same investment horizon, a US\$ 1 investment with dividends reinvested would have yielded US\$ 1052. Exhibit 5 plots this compounding effect for the S&P 500 over several time horizons. The plotted figures are averages for every continuous investment horizon, over each time period based on monthly data for the last 50 years, ending in 2007.

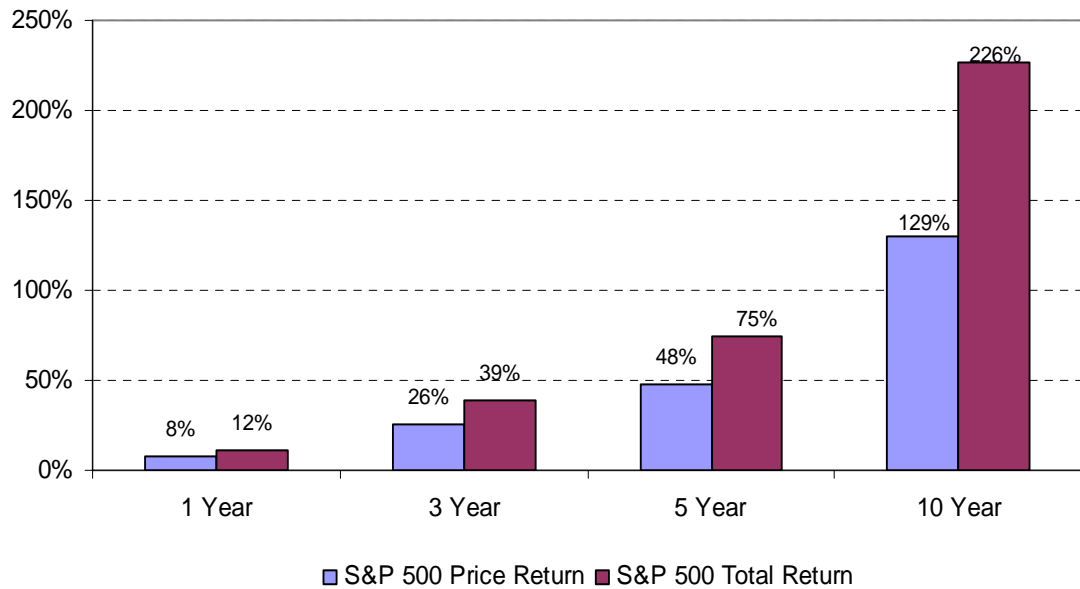
¹ The S&P 500 did not actually have 500 stocks prior to 1957, and was known as the S&P Composite Index. However, for simplicity's sake we use the term "S&P 500" throughout this paper.

Exhibit 4: S&P 500 Cumulative Return of US\$ 1 from 1930 - 2007



Source: Standard & Poor's. Returns are in USD.

Exhibit 5: Compounding Effect



Source: Standard & Poor's.

The S&P 500 Dividend Aristocrats

Dividend growth has been intricately linked to equity valuation since John Burr Williams' Dividend Discount Model in the late 1930's. As noted, managers use stable and increasing dividends as a signal of their confidence in a firm's prospects. Standard & Poor's has been identifying stocks with a long history of consistent dividend increases (which it terms Dividend Aristocrats) since the early 1970's. The S&P 500 Dividend Aristocrats Index is an index of stocks that follow a managed dividend policy. To be eligible securities must meet the following criteria:

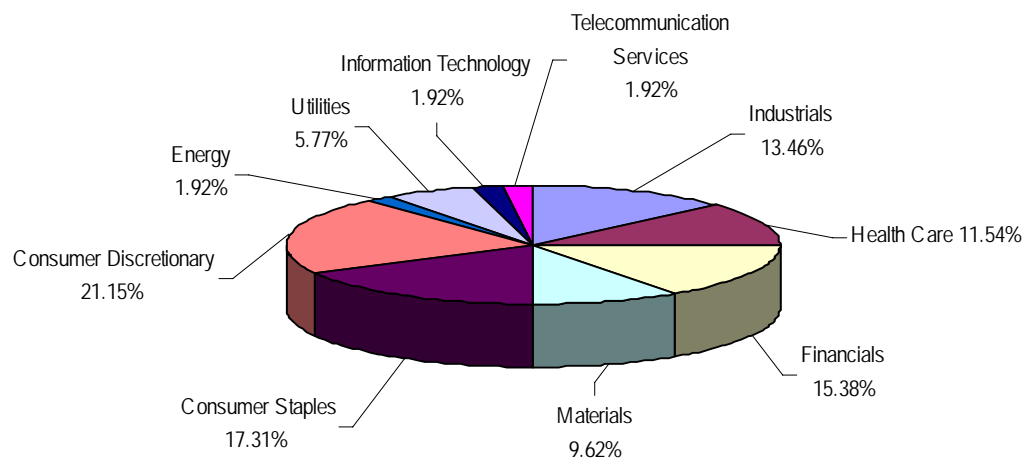
1. Be a member of the S&P 500 Index
2. Have increased dividends for at least 25 consecutive years

Constituents are equal weighted and re-weighted on a quarterly basis.

Sector Diversification

The S&P 500 Dividend Aristocrats Class of 2009 consists of 52 securities diversified across 10 sectors. Unlike many dividend yields based portfolios, which concentrate heavily on the Financials and the Utilities sectors to achieve the high yield, the S&P 500 Dividend Aristocrats are well diversified with no sector weighing more than 20%. Exhibit 6 illustrates the sector diversification of the S&P 500 Aristocrats as of the latest December rebalancing.

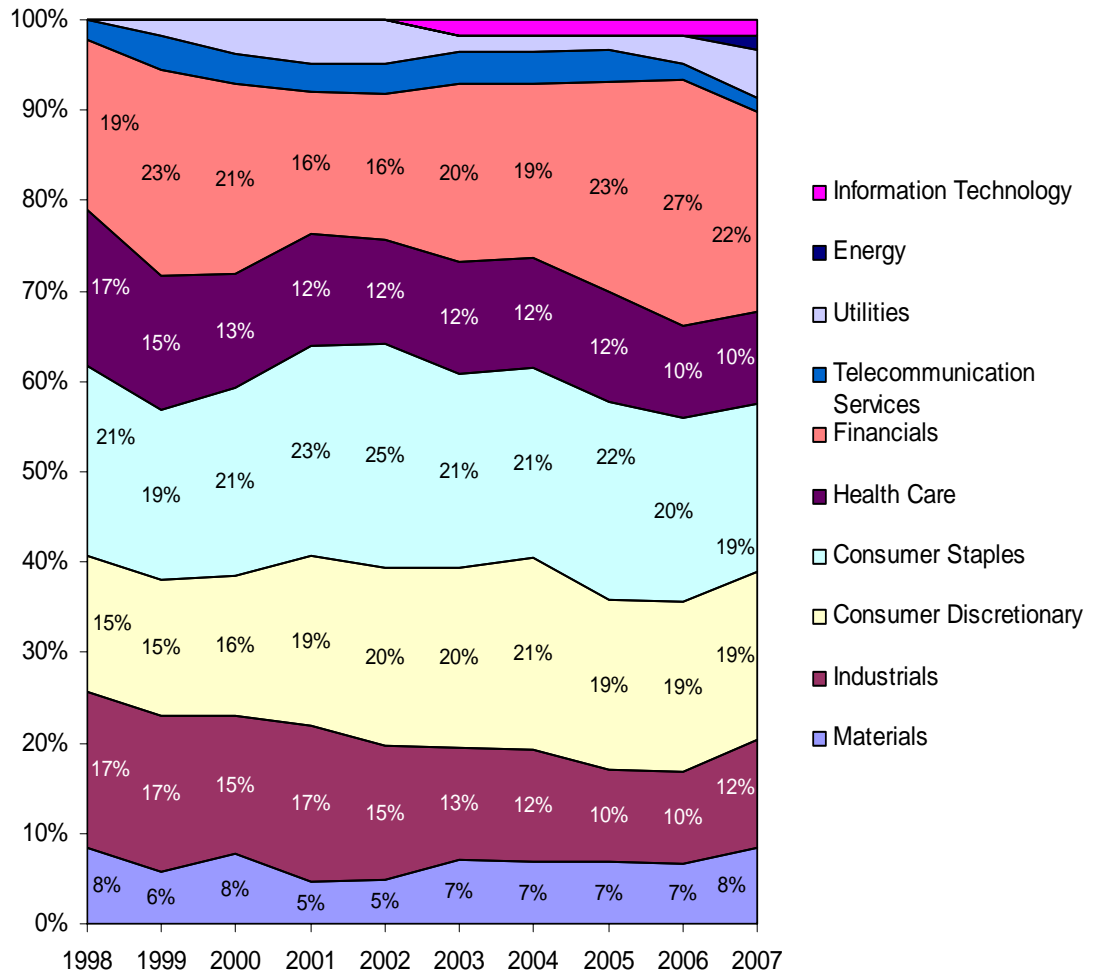
Exhibit 6: Sector Diversification



Source: Standard & Poor's. Data as of December 2008 rebalancing.

Since companies across sectors may follow a managed dividend policy and may exhibit consistent dividend growth, the S&P Dividend Aristocrats have drawn their constituents from a broad range of sectors through the index's history. Exhibit 7 charts the sector composition of the S&P 500 Dividend Aristocrats from year-end 1998 to year-end 2007.

Exhibit 7: Sector Composition of Aristocrats over Time



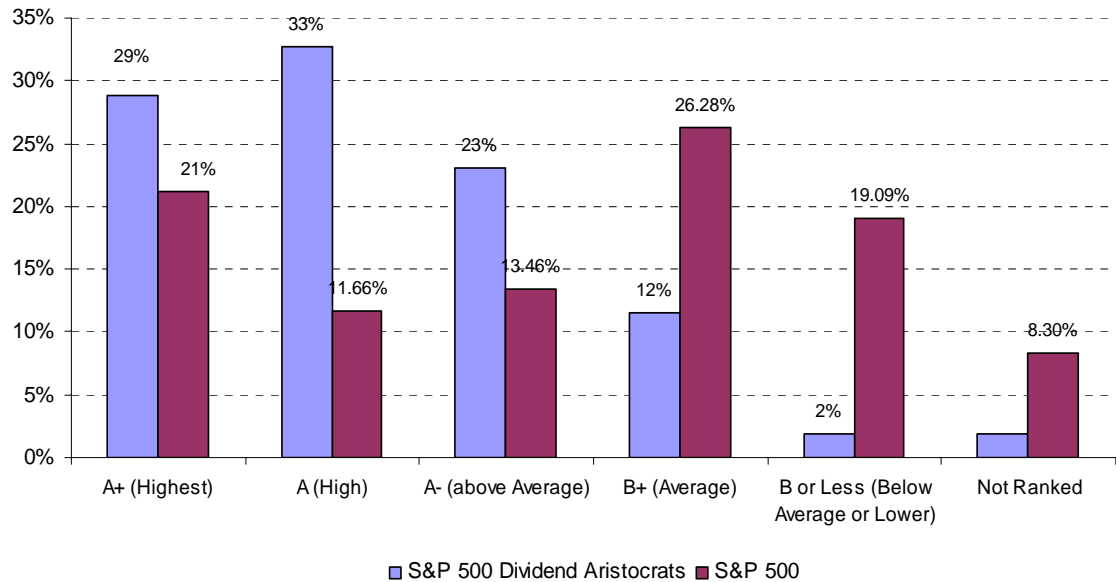
Source: Standard and Poor's. Percentages are as of year-end. Index composition prior to May 2005 is simulated.

Quality Rankings

Management's ability to maintain stable or increasing dividends indicate the quality of the firm's earnings and its growth prospects. For over 40 years, the S&P Common Stock Ranking Systems ranks stocks in categories based on the growth and stability of earnings and dividends. Exhibit 8 plots the distribution

of quality ranks of the S&P 500 Dividend Aristocrats Index constituents against those of the S&P 500 Index.

Exhibit 8: Quality Rankings of the S&P 500 Dividend Aristocrats

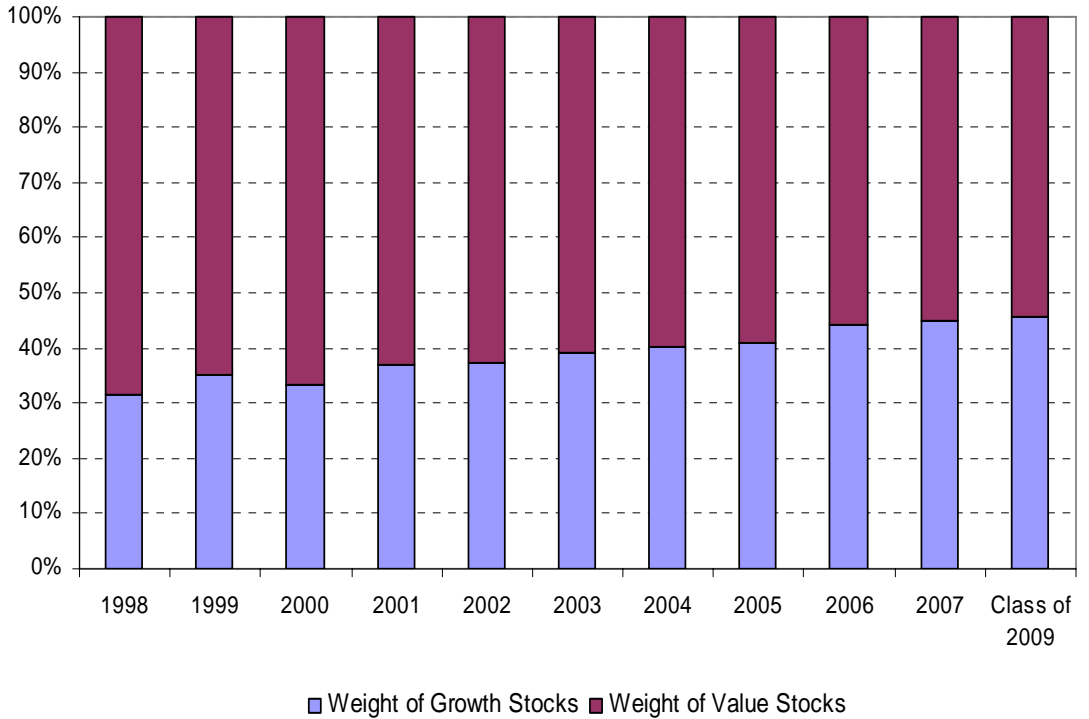


Source: Standard & Poor's. Data as of 11/30/2008.

Aristocrats Have Growth and Income Characteristics

Traditionally, income seeking portfolios tend to have value characteristics as investors lean towards securities with high dividend yield and lower price multiples. In contrast, the S&P 500 Dividend Aristocrats portfolio exhibits both growth and value characteristics. The Aristocrats are selected not only based on their consistent dividend payout level, but also on long-term dividend and earnings growth rates, as well as on profitability measures. Exhibit 9 illustrates the style breakdown of the portfolio composition in each of the last ten years.

Exhibit 9: The Growth and Value Characteristics of the S&P 500 Dividend Aristocrats

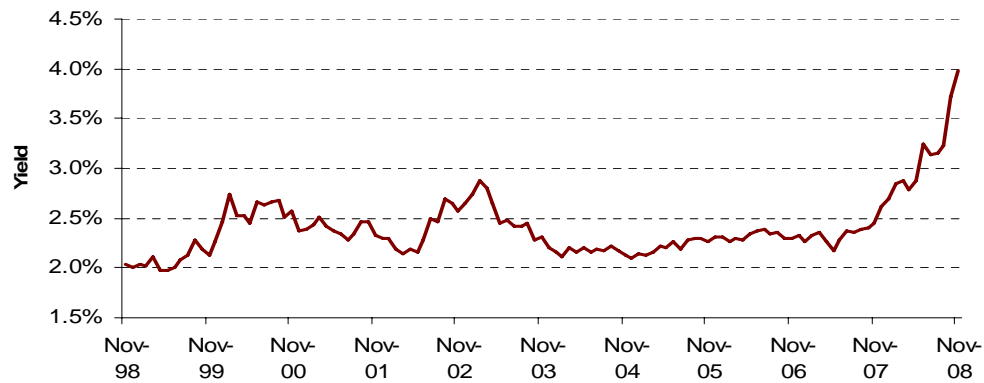


Source: Standard & Poor's. Based on the Style Weights for the S&P Americas BMI as of year-end 1998 -2007 and as of November 30, 2008. The growth and value scored prior to May 2005 are backtested.

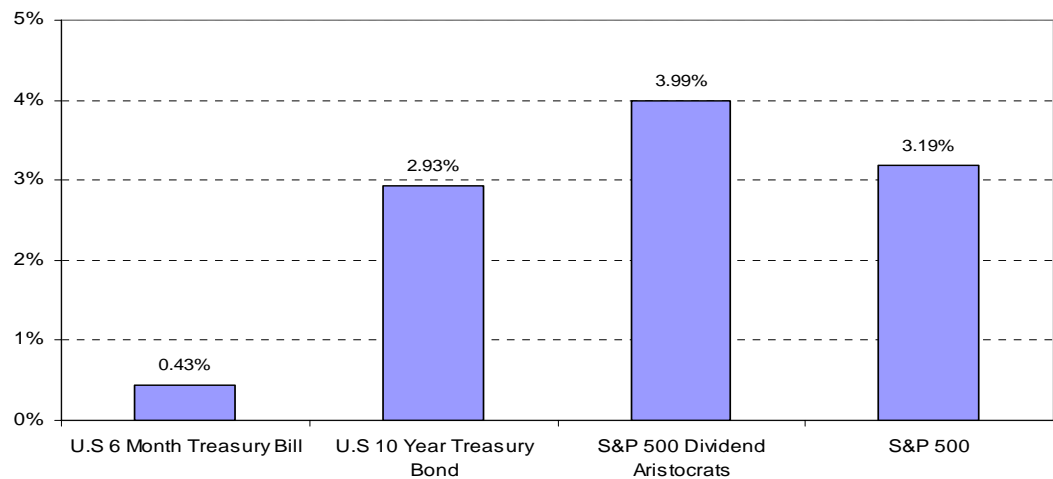
Current and Historical Yield

As shown in Exhibit 10, the S&P 500 Dividend Aristocrats Index has consistently delivered yields in the range of 1.98% to 4% over the last ten years.

Exhibit 10: Historical Yield



Source: Standard & Poor's. Yields before May 2005 are backtested.

Exhibit 11: Current Yield

Source: Standard & Poor's. Data as of 11/30/2008.

Risk/Return Profile of the S&P 500 Dividend Aristocrats

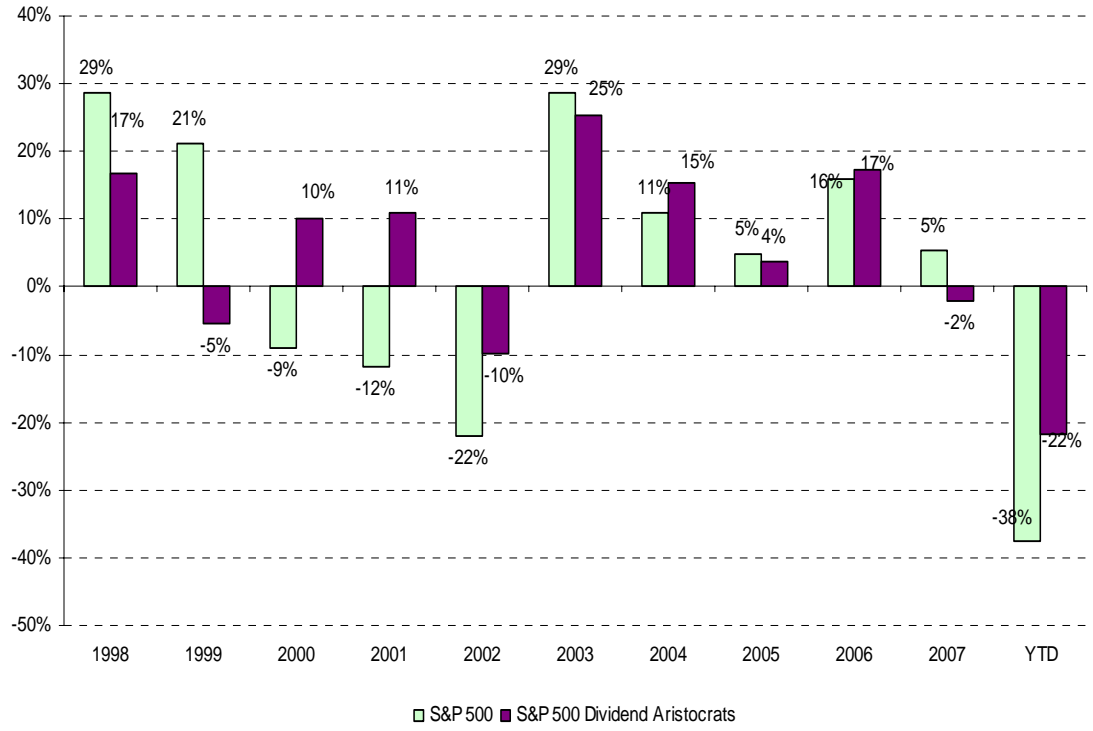
Historically, the S&P 500 Dividend Aristocrats have outperformed the S&P 500 and the S&P 500 Equal Weight indices with lower volatility. Exhibit 12 compares the performance characteristics of the S&P 500 Dividend Aristocrats against those of the S&P 500 and the S&P 500 Equal Weight indices. Exhibit 13 plots the historical annual performance of the S&P 500 Dividend Aristocrats against the S&P 500.

Exhibit 12: Risk/Return Characteristics

	<i>S&P 500</i>	<i>S&P 500 Equal Weight</i>	<i>S&P 500 Dividend Aristocrats</i>
Returns			
3 Year	-8.67%	-11.44%	-3.32%
5 Year	-1.39%	-1.74%	2.39%
10 Year	-0.93%	2.37%	3.73%
15 Year	6.47%	7.33%	9.2%
Standard Deviation			
3 Year	15.26%	17.97%	12.44%
5 Year	13.07%	15.66%	10.69%
10 Year	15.21%	17.11%	12.9%
15 Year	14.99%	16.16%	12.94%
Sharpe Ratio			
3 Year	-0.81	-0.84	-0.56
5 Year	-0.34	-0.31	-0.06
10 Year	-0.28	-0.05	0.04
15 Year	0.17	0.21	0.41

Source: Standard & Poor's. Data as of 11/30/2008. Returns are in USD. Index returns prior to May 2005 are backtested.

Exhibit 13: Historical Annual Performance



Source: Standard & Poor's. Data from 1998 to 11/30/2008. Index returns prior to May 2005 are backtested.

S&P 500 Dividend Aristocrats Class of 2009

	Ticker	Name	Sector
1	MMM	3M Company	Industrials
2	ABT	Abbott Labs	Health Care
3	AFL	AFLAC Inc.	Financials
4	APD	Air Products & Chemicals	Materials
5	ADM	Archer-Daniels-Midland	Consumer Staples
6	ADP	Automatic Data Processing Inc.	Information Technology
7	AVY	Avery Dennison Corp.	Industrials
8	BCR	Bard (C.R.) Inc.	Health Care
9	BBT	BB&T Corporation	Financials
10	BDX	Becton, Dickinson	Health Care
11	BMS	Bemis Co.	Materials
12	CTL	Century Telephone	Telecommunication Services
13	CB	Chubb Corp.	Financials
14	CINF	Cincinnati Financial	Financials
15	CLX	Clorox Co.	Consumer Staples
16	KO	Coca Cola Co.	Consumer Staples
17	ED	Consolidated Edison	Utilities
18	DOV	Dover Corp.	Industrials
19	EMR	Emerson Electric	Industrials
20	XOM	Exxon Mobil Corp.	Energy
21	FDO	Family Dollar Stores	Consumer Discretionary
22	GCI	Gannett Co.	Consumer Discretionary
23	GE	General Electric	Industrials
24	GWV	Grainger (W.W.) Inc.	Industrials
25	TEG	Integrys Energy Group, Inc.	Utilities
26	JNJ	Johnson & Johnson	Health Care
27	JCI	Johnson Controls	Consumer Discretionary
28	KMB	Kimberly-Clark	Consumer Staples
29	LM	Legg Mason	Financials
30	LEG	Leggett & Platt	Consumer Discretionary
31	LLY	Lilly (Eli) & Co.	Health Care
32	LOW	Lowe's Cos.	Consumer Discretionary
33	MTB	M&T Bank Corp.	Financials
34	MCD	McDonald's Corp.	Consumer Discretionary
35	MHP	McGraw-Hill	Consumer Discretionary
36	PEP	PepsiCo Inc.	Consumer Staples
37	PFE	Pfizer, Inc.	Health Care
38	PBI	Pitney-Bowes	Industrials
39	PPG	PPG Industries	Materials
40	PG	Procter & Gamble	Consumer Staples
41	STR	Questar Corp.	Utilities
42	ROH	Rohm & Haas	Materials
43	SHW	Sherwin-Williams	Consumer Discretionary
44	SIAL	Sigma-Aldrich	Materials
45	SWK	Stanley Works	Consumer Discretionary
46	STT	State Street Corp.	Financials
47	SVU	Supervalu Inc.	Consumer Staples
48	TGT	Target Corp.	Consumer Discretionary
49	USB	U.S. Bancorp	Financials
50	VFC	V.F. Corp.	Consumer Discretionary
51	WAG	Walgreen Co.	Consumer Staples
52	WMT	Wal-Mart Stores	Consumer Staples

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