DOW THEORY FORECASTS®

The power of reinvestment

Investors love dividends, especially in today's low-interest-rate environment. But investors who spend their dividends are giving up one of the biggest turbo-boosters to long-term investment returns — dividend reinvestment.

Since the beginning of 1926, the S&P 500 Index has delivered a price return of roughly 6% per year. Reinvest dividends, and the annual return jumps to nearly 10%.

Since Jan. 1, 2000, the S&P 500's annualized price return is just 2.3%, paltry by historical standards. However, had you reinvested dividends in the index, your annualized return would nearly double to 4.3%. That additional 2% per year may not sound like much, but it's huge. At 2.3% per year, a $10,000 investment in the S&P 500 at the beginning of 2000 would have grown to about $15,000. By reinvesting dividends, that $10,000 would be worth roughly one-third more, approximately $20,000.

We can best illustrate the value of dividend reinvestment using individual stocks — Apple (AAPL) and Comcast (CMCSa) — both with the longest tenures on our recommended lists. Comcast joined the Forecasts Long-Term Buy List in May 2009, and we added Apple to the Long-Term Buy list a year later.

Investors who bought $10,000 of Comcast when we first recommended it and reinvested dividends would have seen their holdings jump to roughly $48,000, 16% more wealth creation than investors who spent the dividends. Apple's return gap was more muted — dividend reinvestment boosted the $10,000 investment to nearly $29,000, versus less than $27,000 for those who didn't reinvest. Of course, Apple didn't pay a dividend until mid-2012.

Where does dividend reinvestment get its power?

• It keeps your cash working in the market. Stocks have increased approximately three out of every four years since 1926, and dividend reinvestment exploits that upward bias.

• It forces investors to buy stocks when they are down — an underappreciated benefit because the reinvestment translates into more shares when prices are low. While investors know they should buy low, many have trouble pulling the trigger; dividend reinvestment eliminates the need to make a decision.

The volatile, low-return stock markets of the last two years scream out for a strategy that exploits market volatility. Review your investments, and if you don't need the cash flow, reinvest the dividends. You can easily reinvest in stocks or mutual funds held by your broker. Or you can use dividend reinvestment plans, which in many cases allow reinvestment at little or no charge.