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Time to Let the Dogs Out

By Mike Hogan

Dow Dogs, big and small -- and new ways to buy 'em.

IT'S THAT TIME OF YEAR AGAIN: Time to let the old dogs out and some new ones in. The first week of January marks the changing of the sled team for those who follow the Dogs of the Dow investing model.

A no-brainer value play popularized by asset manager Michael O'Higgins in his 1991 book *Beating the Dow* (www.ohiggins.com), the Dow dividend approach simply dictates buying equal-dollar amounts of the Dow's top 10 dividend yielders at the beginning of the new year. You adjust the mix to incorporate the latest dividend leaders every January thereafter.

The long-running Dogs of the Dow Website (www.dogsofthedow.com) claims this strategy has delivered an average annual total return (income and capital appreciation) of 17.7% since 1973, beating the 30-stock Dow Jones Industrial Average by about six points. But even if one can expect that kind of return, note that it's still an average; the Dogs have taken their lumps, the same as other investing models, especially in 2005. Once a Dogs fancier, the Motley Fool (www.fool.com) fell out of love with the strategy after extensive back-testing of the stocks' performance showed their gains were closer to two points above the Dow. The Fool Website's still a good place to find an even-handed review of the strategy.

The pejorative connotation of the dogs comes from the fact that these stocks' share prices generally lag in the year leading up to their selection. The thought is that any company can suffer a down year, but these largest of large-caps are a relatively safe bet to rebound. General Motors (ticker: GM), whose 10.29% yield topped the list in 2006, is one of the warm-puppy stories. It still had a place on the list in 2007, with a still-generous 3.26% yield and, by the market's Octoberfest celebration, its share price had rallied about from \$13 to \$43. Citigroup (C), on the other hand, is a good example of how a large-cap gets thrown in the doghouse.

With a plummeting 2007 share price but toothsome 6.49% yield, the big bank is the odds-on favorite to be the leader of the pack in 2008, according to Barron's sister company, Dow Jones Indexes (<http://djindexes.com>). The keeper of these indexes, Dow Jones doesn't wrap up the dividend-leaders list until year's end for its own version of the Dogs: the Dow Jones High Yield Select 10. But at this writing, other would-be bow-wows include Pfizer (PFE); Altria (MO); Verizon Communications (VZ); General Motors; AT&T (T); DuPont (DD); JPMorgan Chase (JPM); Home Depot (HD); General Electric (GE) and Merck (MRK).

You've probably already identified a downside to this approach: Who can afford to buy 10 large-caps at one sitting?