

Don't put your stock dividends all in one basket



Q: I'm going to retire and I've accumulated individual stocks that pay dividends. One stock is 40% of my portfolio and I assume that the dividends, plus my Social Security, will generate enough income that I won't have to sell any stocks. Do you think this is a viable strategy?

A: One of the principles of the Prudent Investor Rule is that sound diversification is fundamental to risk management. How would you have felt if your 40% position was in Lehman Brothers or Enron? Several sources identify a concentrated position as any single holding that exceeds 10%.

If you have the right stocks, planning to live off the dividends may work. But how do you know that you have the right stocks? Was

Johns Manville or Bethlehem Steel or GM the right stocks back in their heydays? These were all Dow components, and you know there are only 30 stocks in the Dow Jones Industrial Average.

Dividends are not guaranteed. When you are holding a stock that flat-lines, the dividends are often the first to go (after the CEO).

Chasing yield can lead to higher risk if you're focusing on specific sectors (such as financials and utilities) which results in reduced diversification.

Why are you restricting yourself to only taking income from your portfolio? Why not consider the appreciation as well and look at the total return? Are you confusing these dividends with your old pay check?

Consider controlling taxes; ordinary dividends are always taxed at a higher rate than long-term capital gains.

Interest rates are so low right now that many people are avoiding bonds and replacing

them with dividend-paying stocks. If you're using this strategy, be sure to keep several years of living expenses in CD's or cash so you won't have to sell stocks during a market correction.

Consider reducing your holdings so none of your individual stocks make up more than 10% of your portfolio. Dividends are an important part of the total return but should not be the single criteria for stock selection or retention.

Sound diversification, total return, tax management and an appropriate withdrawal plan will provide you with a viable retirement income strategy. Consult your advisors and make a plan. You'll have a more peaceful retirement.

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