

'Dogs of the Dow' add quality to your portfolio

By Lauren Rudd

Having taught students at all levels, from college to adult education, I have learned the value of repetition. So let me state once again, investing is not difficult. Anyone with a modicum of common sense should have no difficulty building a successful portfolio.

Yes, it is that easy and no, you do not need professional advice or specialized computer software or expensive newsletters and whatever else is being touted these days by those claiming to have an "inside track."

Unfortunately, there are still those who continue to look for Wall Street's Holy Grail, that flawless method for deciding which stocks to buy and when. Regrettably, there is no Holy Grail, and to make matters worse, Wall Street offers no guarantees. Yet, there are those individuals for whom the search has become an obsession, while for others it is a hopeless crusade. In either case, their frustration leaves them vulnerable to the vultures that prey on the uninformed.

Meanwhile, you can dramatically increase your probability of investment success if you pay attention to two simple rules.

The first is that the higher the return, the higher the risk. The second is that capital appreciation takes time. Like baking a cake or brewing beer (as a matter of disclosure, I have never done either), capital appreciation cannot be rushed. Over time, a portfolio with quality ingredients can and will produce outstanding results.

Furthermore, there is one method anyone can use to build a decent portfolio, in a period of about 20 minutes. Your total commission cost, using a discount brokerage house, should not exceed \$45 and you do not have to look at your portfolio for a year.

Developed by money manager Michael O'Higgins, the often maligned methodology is referred to as the Dow 5 theory or Dogs of the Dow and it was originally described in his book "Beating the Dow," (Harper Collins Publishers, 1991). The strategy limits your selection of possible

investment candidates to the 30 companies that make up the Dow Jones industrial average.

As Mr. O'Higgins points out, these companies are among the most widely held, widely analyzed and widely publicized companies in the world. They are also among the largest and strongest of the world's corporate giants. Combined, the 30 Dow companies have assets of more than a trillion dollars and more than 4.5 million employees.

These companies may gain, lose, spin off, acquire, merge, rename themselves, reorganize, or even drop out of the Dow, but they are an integral and vital part of our economic system. In one form or another, they are here to stay.

The Dow 5 theory consists of selecting the five lowest priced Dow 30 stocks out of the 10 with the highest dividend yield. You buy an equal dollar amount, not an equal number of shares, of each of these five companies and hold the shares for one year. On the anniversary of your purchase, you again identify the five lowest priced stocks out of the 10 with the highest yield and adjust your portfolio accordingly.

For 2006, the total return for the Dow 5 was 42 percent. The S&P 500 had a return of 15.8 percent, Fidelity Magellan (FMAGX) 7.2 percent and the Vanguard Index 500 (VFINX) 15.6 percent.

Does the Dow 5 theory work every year? No, it does not. For 2007, the return on the Dow 5 was only 3.1 percent, while the S&P had a return of 3.5 percent, Fidelity Magellan 3.3 percent and the Vanguard Index 3.6 percent.

Want some longer-term numbers? In the past 15 years through 2006, the average annual return on the Dow 5 was 15.9 percent, while the S&P returned 12.0 percent, the Magellan 10.9 percent and the Vanguard Index 11.9 percent. Not bad for an annual 20 minute investment of your time.

Please note that your particular year can start at anytime. The current Dow 5 stocks are: AT&T, GE, Citigroup, GM and Pfizer. Their average dividend yield is 4.71 percent.

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