

Why does a Credit Rating Matter for Dividend Investing?

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SUMMARY

- In our view, a credit rating is a measure of financial robustness and a proxy for quality, reflecting a firm's proven results and history of prudent capital deployment.
- We believe that deep fundamental credit research is well equipped to identify firms that are of robust quality, defensive, and able to at least sustain, and ideally grow dividends over the long term.
- Credit research is inherently focused on downside risks and is a valuable addition in identifying firms that can be considered high quality dividend payers.





We believe that a credit rating is an all-encompassing indicator that provides more information than many other singular metrics. In essence, at its most broad definition, the credit rating is a signal that reflects the overall financial and business risk of a given firm and is a proxy for a firm's overall quality.

There are three primary proof points around the relevance of a credit rating in identifying strong dividend payers:

- 1 Companies with high credit ratings are likely to focus on growth of dividends paid per share, avoid reducing dividends, and be reluctant to change dividends that may have to be reversed in the future.¹
- 2 Companies that access public debt markets are concerned about the signals that their dividend policies send to the market. These firms are likely to exhibit Litner-style² dividend smoothing that is less influenced by short term earnings.³
- 3 Overleveraged firms are less likely to increase dividends and are more likely to decrease them.⁴ Highly leveraged firms are more likely to have lower credit ratings.⁵

While at first glance a credit rating seems simple, there are a plethora of inputs involved in assigning a credit rating, which necessitates regular due diligence using careful quantitative and qualitative analysis by a credit analyst with expertise in each firm's particular industry. Scale, diversification, capital structure, financial policy, management, as well as their competitive positioning and any industry risk factors, are ultimately incorporated into the analyst's view on their rating. Evaluating the impact of these factors on balance sheet strength, cash flow stability, and a firm's desire to maintain or improve its credit rating, is intuitively linked to a firm's dividend stability.

A credit rating is directly related to the overall quality of a firm. Breckinridge maintains proprietary credit ratings that, when assessed in addition to other key inputs, contributes to our identification of high-quality dividend payers that we believe are more likely to sustain and grow dividends over time.

Philosophically, credit research places an emphasis on a firm's proven results and history of prudently deploying capital. We believe that deep fundamental credit research is well equipped to identify firms that are of robust quality, defensive, and able to at least sustain, and ideally grow dividends over the long term. Credit research is inherently focused on downside risks and is a valuable addition in identifying firms that can be considered high quality dividend payers.

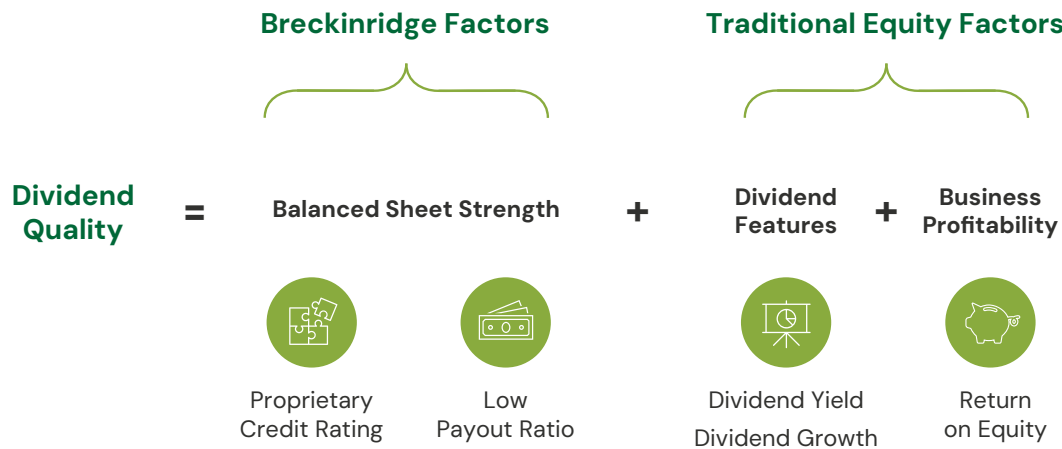
1. Alon Brava, John R. Graham, Campbell R. Harvey, Roni Michaely, "Payout Policy in the 21st Century," *Journal of Financial Economics*, September 2005.
2. Litner-style dividend smoothing refers to a behavioral model of corporate dividend policy introduced by economist John Litner in the 1950s. It is a foundational concept in financial economics for understanding how firms decide on dividend payouts over time.
3. Varouj A. Aivazian, Laurence Booth, Sean Cleary, "Dividend Smoothing and Debt Ratings," *Journal of Financial and Quantitative Analysis*, June 2006.
4. Armen Hovakimian, Ayla Kayhan, Sheridan Titman, "Credit Rating Targets," presented at the NBER Corporate Finance Meeting, 2009.
5. Ibid.



The Breckinridge High Quality Dividend Strategy and Sustainable High Quality Dividend Strategy utilize our proprietary credit ratings assigned by our in-house credit analysts. The strategies incorporate our credit rating as a scored factor when seeking to identify strong dividend-paying firms. When included with additional factors such as low payout ratios, elevated but not risky dividend yields, high dividend growth rates, and strong return on equity – it has the potential to better identify firms that exhibit strong dividend quality.

DEFINING DIVIDEND & QUALITY

We believe that the addition of credit quality to more commonly used equity factors offers a more comprehensive approach to identifying dividend paying companies with financial strength.



For illustrative purposes. Source: Breckinridge Capital Advisors, as of September 30, 2025.

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BCAI-BCAI-10102025-xOns4wbq (10/15/25)

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