Six Income Rules Built for Markets Like These

20 August 2026

Key Takeaways

- **Think in dollars, not just yield.** For income-dependent investors, the key risk is not simply capital volatility, but whether the portfolio can generate a sufficient and growing dollar income stream over time.
- **Focus on dividend growth and resilience.** With cash and fixed income more competitive, the case for equity income increasingly rests on the ability of quality companies to grow dividends through durable earnings, pricing power and strong free cash flow.
- **Diversify beyond traditional income sectors.** A high-yielding stock or benchmark-heavy portfolio can leave investors exposed to concentrated risks. Resilient, growing income may increasingly come from a broader mix of businesses, including selected real assets and infrastructure.
- **Consider how returns are delivered.** Changes to the tax treatment of capital gains reinforce the value of understanding the mix between income and capital growth, while making stock selection more important than simply chasing headline yield.
- **Preserve the capital base that supports future income.** Becoming too defensive can reduce volatility, but it can also limit the growth needed to protect purchasing power and future income from inflation.
- **The current environment reinforces why these rules matter.** With reporting season providing fresh evidence on earnings and dividends, markets at elevated levels and the tax environment evolving, investors have good reason to revisit the principles that have guided our approach to equity income since 2010.

August reporting season is an important health check for Australian investors, and this year it is particularly relevant for those relying on their portfolios for income. We have just come through the end of FY26, advisers and investors are reviewing portfolio outcomes, and companies are providing fresh evidence on earnings, cash flow and dividends. At the same time, changes to the tax treatment of capital gains are adding another consideration to the way investors think about how their returns are generated.

Back in 2010, we challenged some of the traditional 'rules' of income investing when we first launched our innovative Australian Equity Income strategy. More than 15 years later, while the environment has changed considerably, our objective has not. Our motto has always been a **"Sufficient Income for Life"** — whether for retirees or other income-dependent investors such as charities and trusts.

As reporting season tests the resilience of earnings and dividends, markets remain elevated, and the tax treatment of investment returns evolves, now is a good time to revisit the six of the income rules that have guided our approach from the beginning.

Rule 1: Measure income in dollars, not just yield

My thinking about income investing became very personal around the time of the global financial crisis. My parents were retiring, and I spent a lot of time thinking about what they actually needed from their investments. What became clear was that to support their living expenses they needed an income stream that could be measured in dollars, not a percentage yield, and that they needed that income stream to grow over time.

That thinking really changed the way I thought about investment risk. For an accumulation investor, risk is often framed around movements in capital value. For someone drawing an income from their portfolio, there are other risks that can matter just as much: that the income is not high enough, that it fails to keep pace with inflation, or that too much of it depends on one company or sector.

That distinction is worth remembering when reviewing portfolios at financial year-end. A strong total return is welcome, but for an income investor there is another important question: How many dollars of income did the portfolio actually generate, and did that income grow?

A portfolio with an income tilt can help investors remain invested through periods of market volatility. Equities will always carry capital risk, but if the dollar income stream is sufficiently stable and growing, an investor may be less dependent on selling assets at an inconvenient time.

Since we launched the Australian Equity Income strategy in May 2010, and its sister strategies, Ethical Income and Sustainable Income in December 2015, approximately two-thirds of total returns have consistently come from their franked income streams[1].

Rule 2: Dividend growth matters as much as, or even more than, the dividend yield

For much of the past 10 to 15 years, income from equities has had a starting advantage over cash and fixed income because interest rates were so low. That advantage still exists in parts of the market, but it is narrower today.

With markets at record highs, and the ongoing inflationary environment, it is not simply the level of income, it is the growth in that income that investors need to really consider. It is important to remember that a fixed-income security may give an investor lower capital volatility, and a known level of income, but that income generally does not grow.

So, whereas fixed-income assets are giving no growth in a high inflationary environment, the dividend growth on our portfolio of quality defensive Australian equities has accelerated. There have been periods in the past where it was circa 3%, and we're now looking at 7- 8% annual growth in dividends in the current inflationary environment[2].

Rule 3: A high yield is only useful if it is resilient

Another income rule that investors need to revise is the focus on the high headline yields. A high yield can sometimes be a warning rather than an opportunity. If the market believes earnings are under pressure or a dividend may be cut, the share price can fall and mechanically push the yield higher. That is why we focus much more on the quality of the cash flow supporting the dividend.

The characteristics we look for are relatively straightforward: durable earnings, pricing power, strong free cash flow and the capacity to keep paying and growing dividends through different economic conditions. In FY26, quality defensive companies such as Aurizon Holdings, QBE Insurance Group, Woolworths Group and APA Group demonstrated a number of those characteristics, and helped us to post standout returns driven by income, despite the key Australian equity market drivers of AI and energy.

What I like about businesses of this type is that they are not necessarily relying on a strong consumer economy to generate cash flow. In many cases they have strong competitive positions, reliable demand or pricing mechanisms that allow earnings to hold up in a more difficult environment.

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[1] Source: ClearBridge; as of 30 June 2026. Data calculated for a ClearBridge Australian representatives account in A$ gross of management fee. Periods over a year are annualised. Assumes zero percent tax rate and full franking benefits realised in tax return.

[2] Source: ClearBridge, FactSet; as of 30 June 2026. Data calculated for a ClearBridge Australian Equity Income representative account.
Expected next 12 Months (NTM) data is calculated using the weighted average of broker consensus forecasts of each portfolio holding – because of this, the returns quoted are estimated figures and are therefore not guaranteed and may differ materially from the figures mentioned. The figures may also be affected by inaccurate assumptions or by known or unknown risks and uncertainties. In respect of the broker consensus data the number of brokers included for each individual stock will vary depending on active coverage of that stock by a broker at any point in time. A median of brokers is typically utilised. All estimates avoid stale forecasts which are removed after a certain number of days. Assumes zero percent tax rate and full franking benefits realised in tax return.

Rule 4: Don't mistake the index for an income portfolio

The S&P/ASX 200 is not constructed to provide an investor with a diversified income stream. Being a market-capitalisation-weighted index, it is heavily skewed towards certain sectors such as banks. Yield focused smart beta indices are also sector skewed given that banks have been traditionally high yielding stocks.

But think about what happened if around 30% of an equity allocation is concentrated in banks and something goes wrong with the domestic economy and bad debts rise. We are seeing signs already of this during the early parts of reporting season. An investor could find that a large part of their dividend income is exposed to the same correlated underlying risk. Income-dependent investors need far more diversification than that.

Commonwealth Bank of Australia (CBA) is a useful example of how the traditional income playbook can change. For a new investor, I don't think the right question is whether CBA has historically been a good dividend payer. The question is what are you are paying today for the expected dividend stream and how quickly that dividend can grow from here. That is one reason our exposure to banks is currently relatively low, at around 8%, with CBA representing only approximately 1% of the portfolio[3].

Listed real assets, which are not well represented in the index, are one area we continue to find more interesting for income. We generally maintain an allocation of around 10% because we like the quality and reliability of the cash flows and, in a number of cases, the ability to increase revenues and dividends through inflation-linked pricing. Stocks we like include selected retail REITs like Scentre Group and Vicinity Centres, and infrastructure businesses like Transurban Group, APA Group and Aurizon Holdings, where replacement costs, contractual pricing structures or strong market positions can provide attractive income characteristics.

Rule 5: Pay attention to how the return is delivered

The announced changes to capital gains taxation give investors another reason to think about the composition of their investment returns.

The conclusion isn’t that capital growth has suddenly become undesirable, or that investors should simply buy more high-yielding shares, rather that it matters how their total returns are delivered. As we mentioned earlier, skewing returns towards franked income has always been central to the way we think about our equity income portfolios. For an investor drawing an income from a portfolio, owning companies that generate resilient cash dividends means they are less reliant on selling assets and realising capital gains (that attract CGT) to meet their spending needs.

With franking, that income can also be particularly valuable for eligible Australian investors. Our internal analysis suggests that for investors seeking to draw income from their Australian equity portfolios outside the superannuation regime from 1 July 2027, the prospect of paying top-up tax each year to meet the new minimum 30% tax on realised capital gains will render fully-franked dividend stocks much more capable of producing better after-tax incomes than no-or-low dividend paying compounders. Furthermore, the much larger final capital gain that may be payable on selling a non-dividend paying stock only makes the headwind worse.

Changing tax considerations do not however change the investment fundamentals. If anything, they reinforce the importance of being selective. We still want businesses with strong free cash flow, pricing power and resilient earnings that can support their dividends through the cycle and grow them over time. That is where I believe active management matters.

Rule 6: Don't solve today's income problem by creating tomorrow's capital problem

A final risk that retirees need to be conscious of is becoming too defensive too early and removing the potential growth in the capital from their portfolio.

[3] Source: ClearBridge, FactSet; as of 30 June 2026. Data calculated for a ClearBridge Australian Equity Income representative account

If a more defensive portfolio, with a lower expected total return, only generates a total return that is close to an investor's draw down rate, there may not be enough growth left to protect the capital base and its future income generating ability against inflation over time.

If investors can generate a sufficient income to fund their needs without continually having to sell down capital, it can give them greater ability to remain invested in growth assets and participate in the long-term growth of those assets. And for younger retirees in particular, time is still on their side. A temporary equity-market dislocation does not necessarily have to change the long-term investment strategy if the portfolio continues to generate the income they require.

Reporting Season Is Reinforcing Our Non-Traditional Approach

The Australian investment environment today looks very different from the one we faced when we launched our Equity Income strategy more than 15 years ago. Cash and fixed income are more competitive. Parts of the equity market are trading at elevated valuations. The sources of market leadership have shifted. And changes to the tax treatment of capital gains are putting greater focus on how investment returns are delivered.

None of that changes the **Sufficient Income for Life** objective we set out with, or the rules that have been part of our approach since 2010. If anything, we think it makes the principles behind a diversified, resilient and growing income portfolio more relevant.

This reporting season, we have been looking for fresh evidence of which companies have the durable earnings, pricing power and free cash flow required to support dividends through different economic conditions — and, importantly, grow those dividends over time. The opportunities we are seeing across quality defensive companies reinforce why we believe a selective, non-traditional approach to equity income remains so important.

Explore ClearBridge's range of Australian Equity Income strategies, including Equity Income, Ethical Income and Sustainable Income, and learn more about our approach to building consistent and growing income streams **here**

About the Author

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