

# A Deep Dive on the Dividend Dance

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We recently talked about a [new strategy](#) that aims to avoid the tax drag associated with receiving distributions in taxable brokerage accounts. In partnership with Compoundr & F/m Investments, Nasdaq launched the Nasdaq Compoundr U.S. Aggregate Bond™ Index (NCPAG™) and the Nasdaq Compoundr High-Yield Corporate Bond™ Index (NCPHY™), which are tracked by [CPAG](#) and [CPHY](#), respectively. In today's report, we review the strategy and walk through how the rotation works, step-by-step.

## How does the strategy work?

The [Nasdaq Compoundr indexes](#) attempt to mimic total returns without incurring potential [distribution tax drag](#).

For each index, there is a:

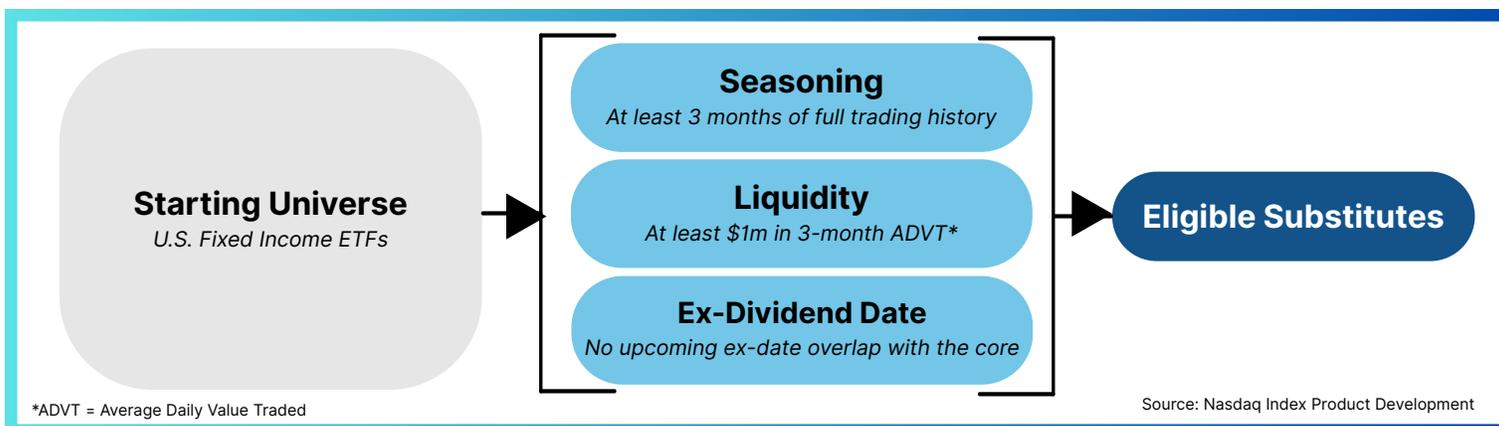
- **Core Holding:** the primary index constituent. The index will hold one or more of these 'core' exchange traded funds (ETFs) the majority of the time, except for the rebalancing window.
- **Substitute Holding:** the temporary index constituent. On the other hand, the index will hold at least one 'substitute' ETF during each core holding's ex-date period.

For the purposes of the analysis below, we focus on NCPAG, whose core holding is AGG. As of this writing, AGG's most recent ex-date was 9/2/2025.

Each time a core holding trades [ex-dividend](#), the index must find an eligible substitute to rotate into. As summarized in **Chart 1**, the [index rules](#) state that eligible substitutes must be U.S.-listed fixed income ETFs, that:

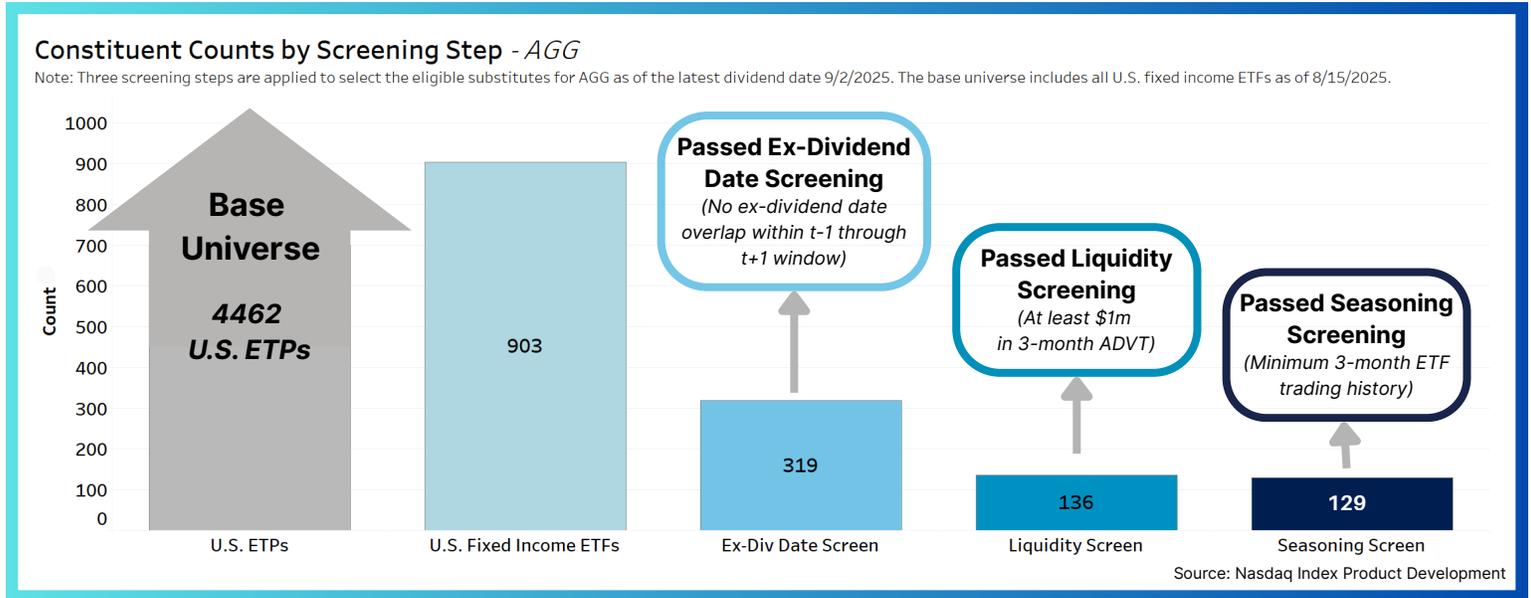
- have traded at least three full months (Seasoning Screen),
- have traded at least \$1m per day on average over the last three months (Liquidity Screen), and
- don't have an ex-date that overlaps with that of the core holding (Ex-Dividend Date Screen)

Chart 1: Nasdaq Compoundr Screening Methodology



For the September 2025 rebalance, there were over 4,000 U.S. ETPs, around 900 of which were classified as fixed income (**Chart 2**). The majority of fixed income ETFs shared an ex-date of 9/2/2025. However, there were around 300 that did not. After applying some additional screens (for the purposes of trading), there were 129 funds that could potentially be considered for inclusion as a temporary substitute.

## Chart 2: Security Counts by Screening Step

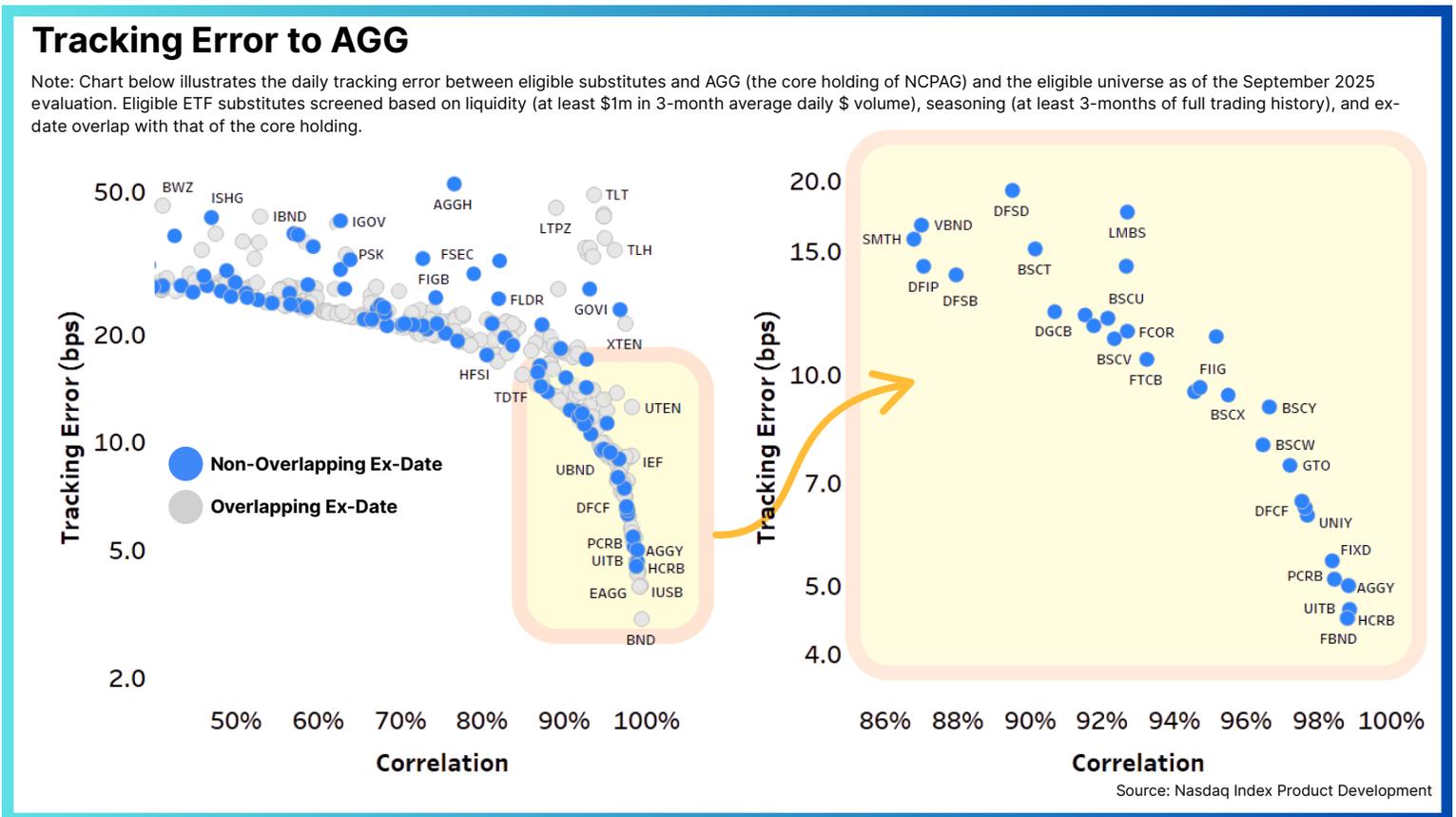


## Selecting a substitute

So, how does the index decide which of the 129 eligible funds to select for temporary inclusion? The key to ensuring the strategy maintains AGG-like returns on ex-date is that the substitute has a very similar risk and return profile to AGG.

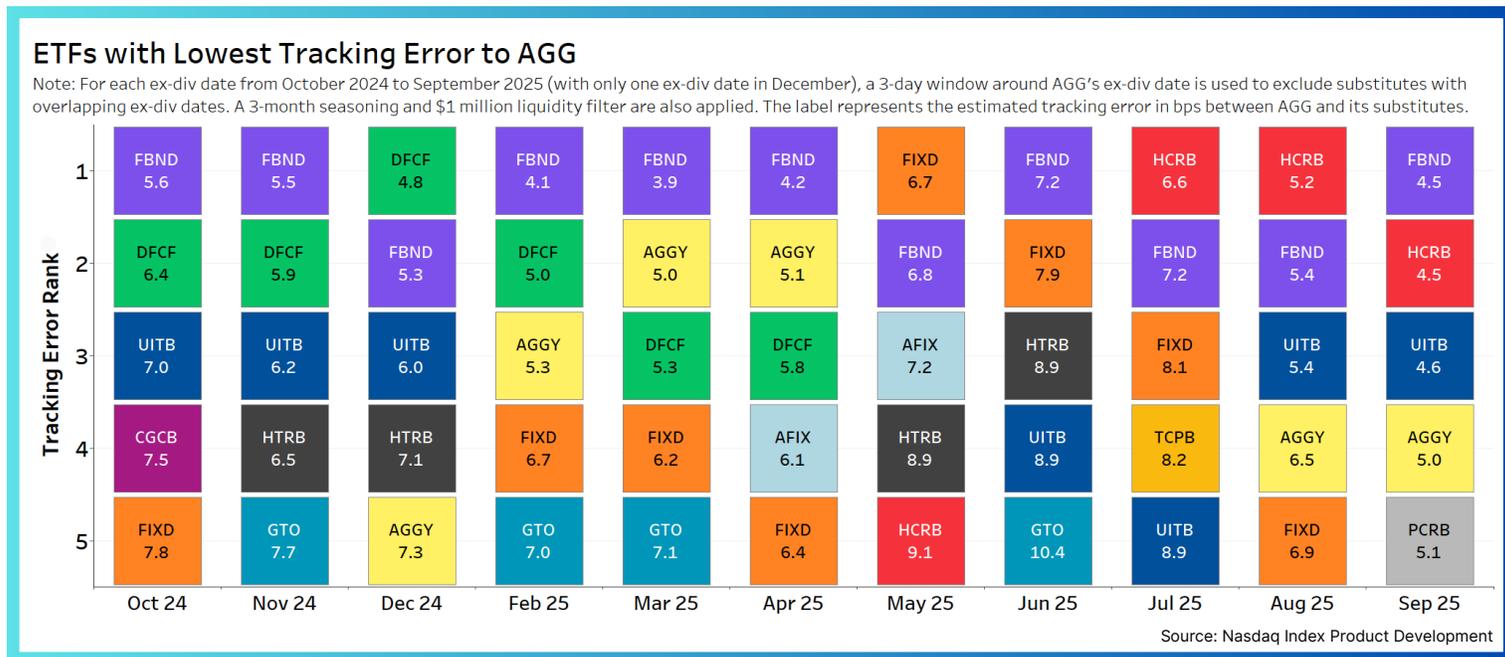
**Chart 3** shows a sample of fixed income ETFs and their tracking error and correlation relative to AGG. The blue dots are potential substitutes because they do not share an ex-date with AGG. In this case FBND, HCRB, and UITB have the lowest daily tracking error to AGG, and therefore make for the best potential substitutes.

## Chart 3: Substitute Tracking Error with AGG



In fact, **Chart 4** shows that on a historical basis, FBND has consistently ranked in the Top 5 for best substitutes. We also see that the Top 5 eligible substitutes have generally remained consistent, although they may sometimes switch between rankings.

Chart 4: Historical AGG Substitutes

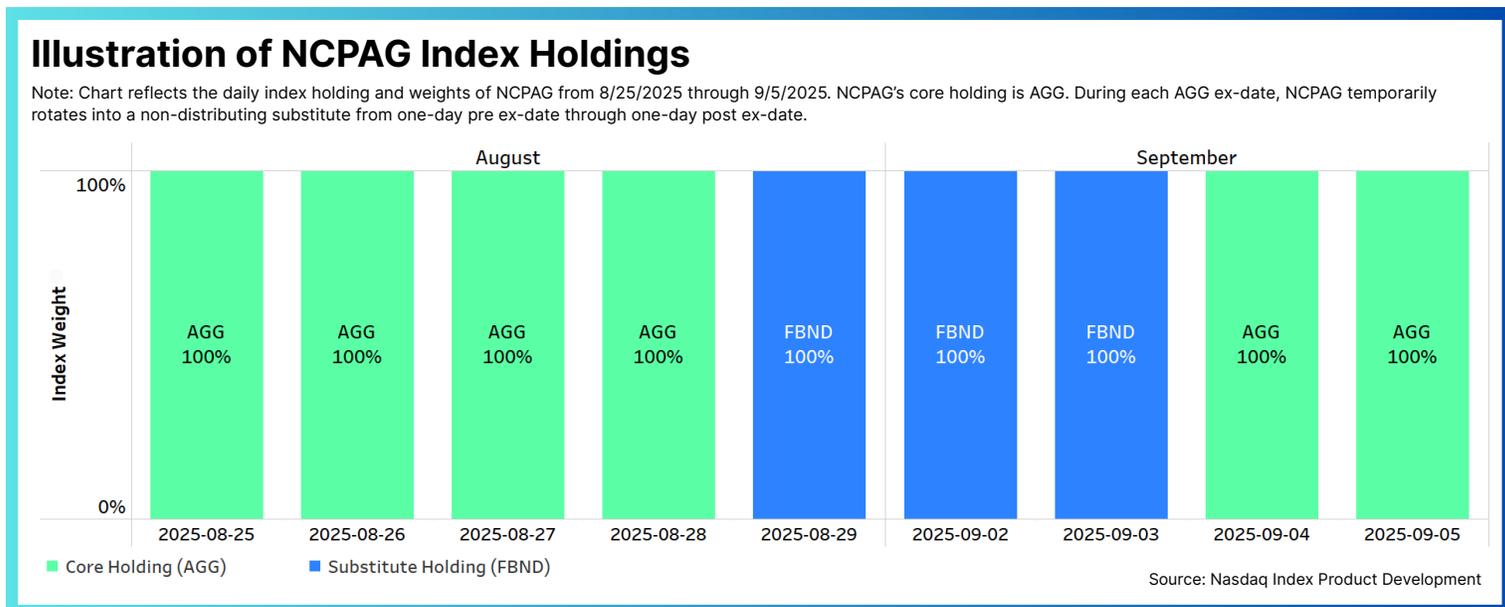


## The live switch

As we've discussed previously, the index will only hold the substitute security for a temporary period, during the core holding's ex-dividend date. The index switches to its substitute one day prior to the core holding's ex-date, and continues to hold the substitute through one day post ex-date. This is to give the ETF which is tracking the index enough time to make the required change.

**Chart 5** shows how in the days leading up to AGG's ex-date, NCPAG held exactly one constituent – AGG. However, from 8/29/2025 (ex-date minus one) through 9/3/2025 (ex-date plus one), the index switched to FBND.

Chart 5: NCPAG Index Holdings



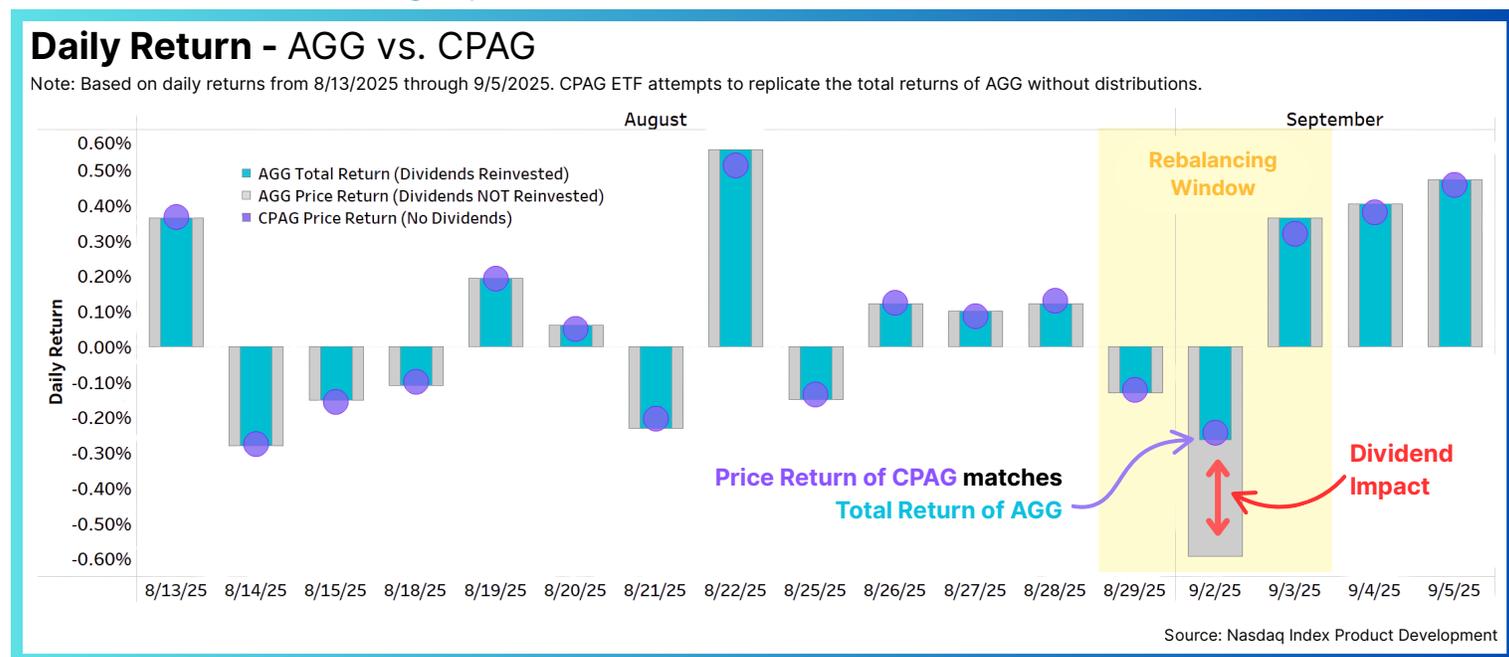
So, as we see above, the index rotates from core, to substitute, then back to core; this is what we call the “dividend dance.” In doing this, the index successfully avoided AGG’s dividend, but was able to maintain AGG-like exposure.

## How did the ETF do?

It’s important to note that it is not possible to invest directly in an index. However, the [F/m Compoundr U.S. Aggregate Bond ETF \(CPAG\)](#), is designed to track the Nasdaq Compoundr U.S. Aggregate Bond™ Index (NCPAG). So, how did CPAG’s (the ETF’s) first live rebalance go around AGG’s September ex-date?

We see below that the price return of CPAG (purple dot) matched the total return of AGG (blue bar) well during this period (**Chart 6**). Also note the disparity between AGG’s total return (blue bar) and AGG’s price return (grey bar) on 9/2. This disparity reflects the downward adjustment in price due to the monthly distribution.

Chart 6: CPAG vs. AGG During September Rebalance



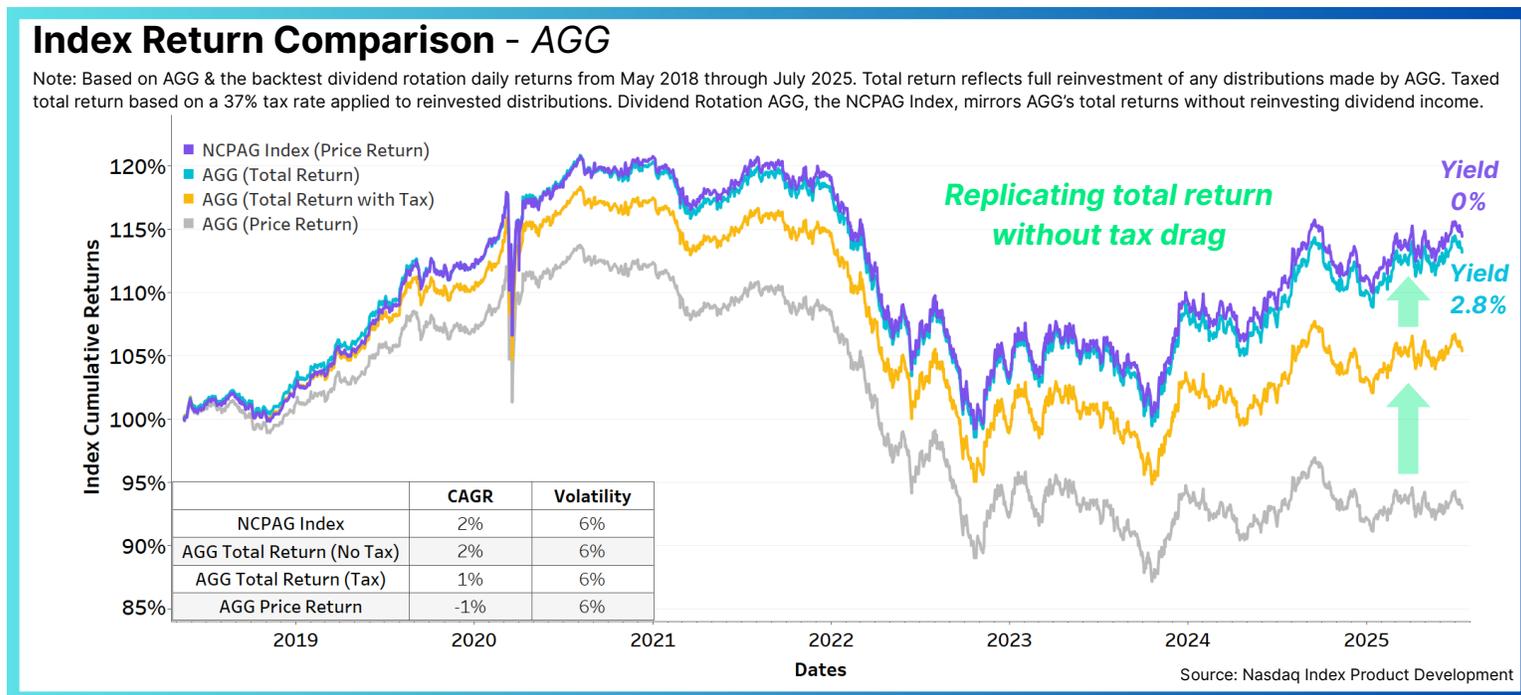
Overall, **Chart 6** above suggests that the index (and therefore the ETF tracking) achieved its goal – maintain AGG-like total returns without receiving and reinvesting a distribution.

## What to expect for the future?

Given the limited live history, we can analyze the backtested index performance to get a sense of how this strategy might continue to perform in the future.

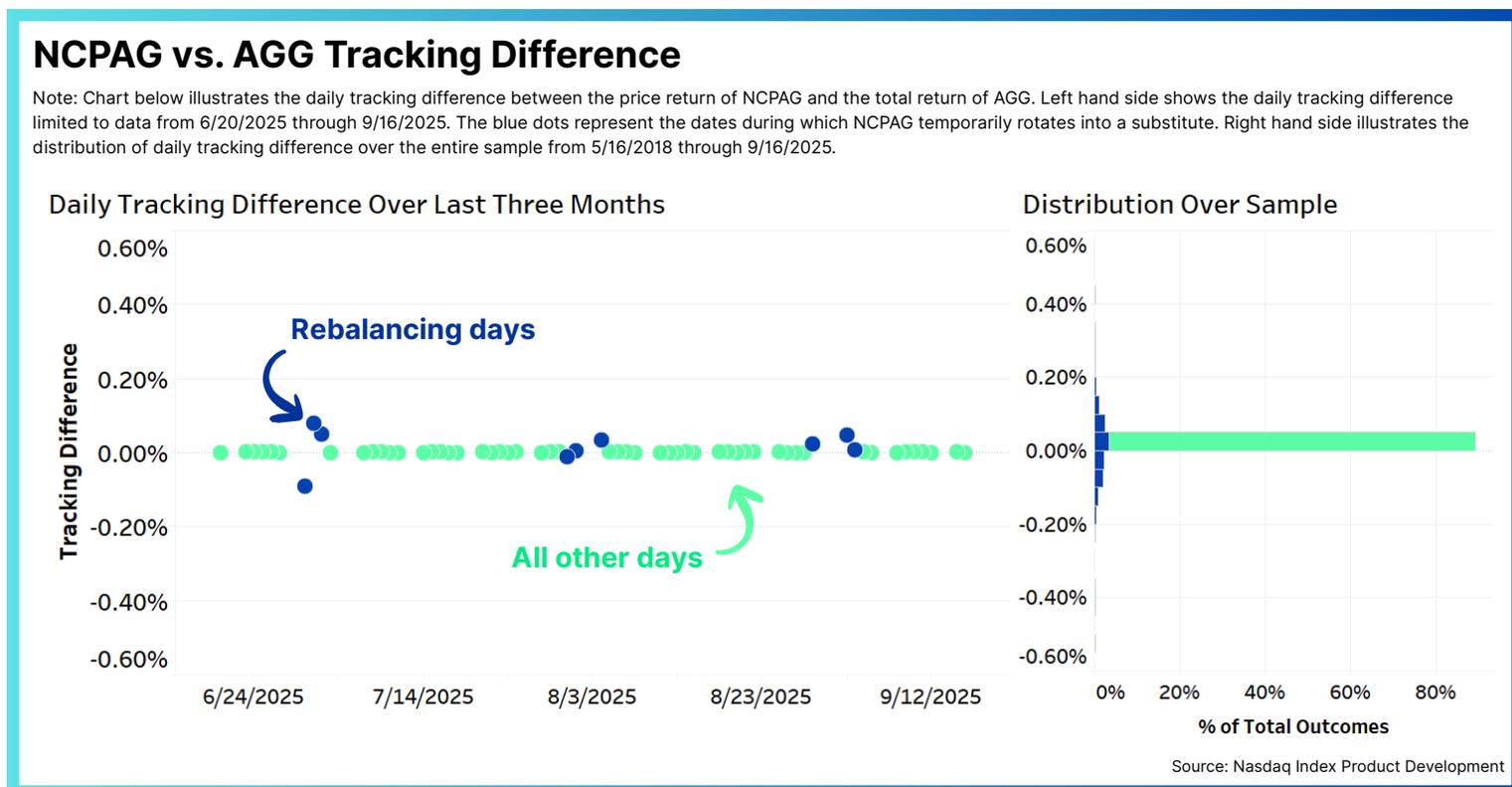
Based on backtested index performance, over the long-term, cumulative *price* returns of the NCPAG index have generally matched the cumulative *total* returns of AGG (**Chart 7**). We also estimate that monthly tracking error has generally been around 40 basis points (bps) over the entire backtest.

Chart 7: Backtested NCPAG Performance



However, given that the index holds the core holding the majority of the time, tracking error is only expected to occur during the three-day rebalancing window. For example, **Chart 8** illustrates the daily tracking difference between the price return of NCPAG and the total return of AGG. The left side shows that non-zero tracking difference only occurs when the index rotates into the substitute (blue dots). On all other days (green dots), tracking difference is 0, since the index is simply holding the core ETF. Thus, in aggregate, the daily return profile should almost always match that of AGG (right side of Chart 8).

Chart 8: Historical Tracking Difference Between NCPAG and AGG



## Conclusion

Overall, dividends can sometimes result in a drag on performance. Using a systematic set of rules, the Nasdaq Compoundr indexes attempt to reduce this friction so that investors can continue pursuing their long-term financial goals, in a seamless and efficient manner.

For more information on the Nasdaq Compoundr Indexes, please visit:

<https://indexes.nasdaqomx.com/Index/Overview/NCPAG>

Read more related research here:

- [The Dividend Drag Dilemma](#)
- [Total Return without the Dividend?](#)
- [The Residual Tax Burden of US ETFs - Whitepaper](#)

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