Investing Mentality: Short-term Pain Equals Long-term Gain

Description

When we go shopping, we want to buy things on sale. Somehow, this is different for the stock market. Generally, investors feel uneasy when stock prices go down and good when they go up.

We like to see our portfolio increase in value. However, if you're in the accumulation phase and you're buying shares sometime soon, you should root for lower prices.

Here's why.

Lower prices imply higher yield

For the dividend investor, lower prices imply higher yields. When **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) hit a share price of $73 in 2014, I was happy as a shareholder. It yielded 3.6% at the time with a quarterly dividend of 66 cents.

However, historically, it's known to reach yields of 4.4% or higher. Only two factors contribute to a higher yield: lower prices and dividend growth. Investors could have waited for lower prices or dividend growth to catch up before buying the shares.

Today, the shares have fallen under $62 with a yield of 4.5%. The shares now pay out a quarterly dividend of 70 cents instead of 66 cents.

Lower prices imply higher returns

Lower prices also imply higher returns. Now that Bank of Nova Scotia shares are under $62, it not only provides a higher yield than before, but it's also priced at a more attractive valuation.

When it was $73, it was priced at a price-to-earnings ratio (P/E) of about 13. Now it's priced at a P/E of 11. Paying a lower valuation for a quality business such as Nova Scotia Bank can only imply more upside in the future.

After all, the bank normally trades at a P/E of above 12, which would imply a fair value of about $70. As a result, the bank’s shares are discounted by over 11% today.

In conclusion

Total return is based on price appreciation and any dividend income. It doesn’t matter if you’re looking with the perspective of a total-return investor or a dividend investor; lower prices lead to higher returns. That’s why investors should fight that uneasy feeling and buy high-quality companies such as Bank of Nova Scotia when share prices drop.

Besides, dollar-cost averaging is a great method of buying more shares at lower prices to average your cost basis. The idea is to build a portfolio of quality businesses over the long term. As a dividend investor, that means a portfolio of quality dividend stocks that generates a growing income.

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1. Bank Stocks
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1. NYSE:BNS (The Bank of Nova Scotia)
2. TSX:BNS (Bank Of Nova Scotia)

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