Want to Make Money? Focus on Dividend Yields

Description

Do you want to make money in good and bad economic times? Look for businesses with long histories of profitability that are priced reasonably, if not relatively cheaply, today.

Buy quality companies when they offer yields that are at the high ends of their historical yield ranges. When their yields are relatively high, this may indicate that their shares are cheap or they raised their dividends.

Cheap share prices and high dividend yields mean high income and high total returns. However, investors should only shop for great businesses that remain profitable even in bad environments.

Apple Inc. (NASDAQ:AAPL) has outperformed the general market in the past five-, 10-, and 15-year periods. It just hiked its dividend by 9.6%. This year marks its fourth consecutive year of dividend increases. Its yield of 2.4% is at the high end of its historical yield range. This indicates its shares may be undervalued.

In fact, Apple shares have fallen 10% in the past two days. At under US$95 per share, it trades at about 11 times its earnings, which is discounted for an A-grade company that generates lots of cash every quarter and tends to outperform the market.

Canadian Western Bank (TSX:CWB) is a well-run regional bank. It last experienced a huge dip in the financial crisis of 2008 and 2009. Back then, its earnings per share (EPS) fell 2% from the fiscal year 2007 to 2009, but its shares fell more than 60% because of the recession.

This time, its share-price decline is different. Due to low oil prices, its shares have fallen at a slower pace over a longer period of time. The bank's EPS fell 5% in the fiscal year 2015, has been flat so far this year, and is expected to resume growth next year.

Whether growth resumes or not, it's a fact that the bank's earnings haven't declined by a lot, while its share price has fallen 30% from a high of $40 per share in 2014 to under $28 per share today.

After the huge dip, the bank trades at 10.6 times its earnings. And its dividend yield is historically high at 3.3% compared to the yield it had for most of the decade, which was below 2.6%.

Canadian Western Bank continues to be profitable and rewards shareholders. It has increased its dividend for 24 consecutive years. And its payout ratio of 35% remains sustainable.

Conclusion

Buying great businesses on dips works best if the companies have a history of increasing their dividends because a threshold dividend yield unique to each company helps put a base on their share prices.

For example, Apple has support between the 2.5% and 2.9% yield range and Canadian Western Bank's recent performance indicates it has strong support at the 4.5% yield. That translates to a price range of US$79-92 per share for Apple and $21 per share for Canadian Western Bank.

Even if you buy their inexpensive shares today, investors can experience gains of 36% for the tech giant and 39% for the bank when they trade at their normal multiples.

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1. Bank Stocks
2. Dividend Stocks
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1. Editor's Choice

TICKERS GLOBAL

1. NASDAQ:AAPL (Apple Inc.)
2. TSX:CWB (Canadian Western Bank)

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