3 Things About Dividend Investing Every Retiree Should Know

Description

Retirees deserve to enjoy their golden years. It'd be smart to get their money to continue to work for them when they don't work anymore.

Because of low interest rates, many retirees or near-retirees have put more of their money into the market to aim for higher returns. These investors have gravitated more towards dividend stocks to earn a steady income.

Here are three things about dividend investing that every retiree should know.

High yields: Too good to be true?

If you see a yield that's +7%, you should be suspicious about its sustainability. Although not all high yielders will cut their dividends, when the market is commanding a higher yield from a stock, that indicates the stock is risky.

Cominar REIT (TSX:CUF.UN), the largest commercial property landlord in Quebec, is popular among income investors. However, Cominar's share price has been in a general decline for five years.

The decline has at least partly to do with the REIT's expanding payout ratio, which was about 95% five years ago and was over 100% last year. The large payout ratio is due in part to the company selling some of its properties, which resulted in a reduction in cash flow generation.

Cominar's +11% yield seems attractive, but with its payout ratio estimated to continue to be more than 100% this year and next year, retirees should look for safer yields elsewhere, even though that may mean a smaller yield.

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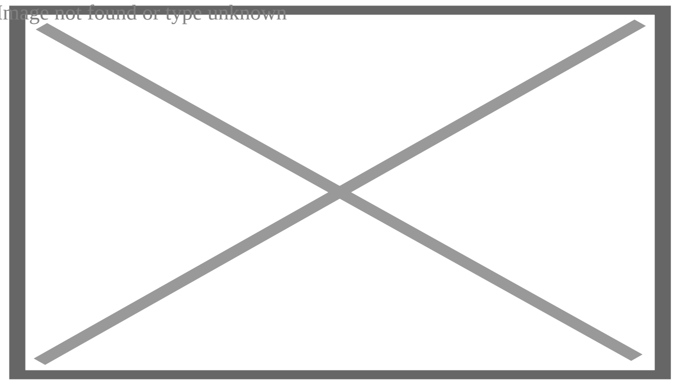

Dividend-growth stocks typically offer safer yields

Dividend-growth stocks that are sustainably growing their dividends generally offer safer yields than stocks that maintain but don't increase their dividends.

Dividend stocks with growing dividends should be growing their earnings per share (EPS) or cash flow per share over time, and their payout ratios should be in line with, if not lower than, its peers'.

For example, you'll find that Canada's Big Five banks, including **Royal Bank of Canada** (TSX:RY)(NYSE:RY), have payout ratios of about 50% and are expected to grow their EPS by at least 5% per year in the next few years.

The growing earnings make the banks more profitable and their dividends safer. In fact, the growing earnings allow the banks to grow their dividends over time. Royal Bank offers a safe 3.6% yield, and it can grow its dividend at least 5% per year.

Low yields: Higher growth, higher returns?

Low-yielding dividend-growth stocks may deliver higher dividend growth and ultimately higher total returns than higher-yielding stocks in the long run.

For example, **Alimentation Couche Tard Inc.** (TSX:ATD.B) has delivered annualized returns of 36% and annualized dividend growth of 31.7% in the last five years. However, it only yields 0.6%, so it wouldn't even be on the radars of most retirees who seek income.

In comparison, Cominar and Royal Bank had annualized returns of -3% and 16% and annualized dividend growth of 0.4% and 9.3%, respectively, in the same period.

Investor takeaway

Know what type of dividend stock you're buying. Each one will behave differently as the examples have shown.

Chances are that you're going to hold different types of dividend stocks (high yield and slow growth, moderate yield and moderate growth, or low yield and high growth) for different purposes in your diversified dividend portfolio.

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