TFSA Investors: 2 Dividend Stocks Paying Sustainable 7% Yields

Description

For TFSA investors, finding a good dividend stock is a good way of securing recurring income, and it becomes tax-free when it is held inside of a TFSA account. For dividend investors, these stocks can secure a steady stream of income, while investors looking for stock appreciation can use the dividend as a safety net to offset any losses, which is particularly important this year when the TSX has not been providing strong returns.

I have two stocks listed here that provide strong 7% yields that TFSA investors looking for either capital appreciation or dividend income can benefit from, while also adding some diversification.

First National Financial Corp. (TSX:FN) provides mortgages to both residential and commercial segments. The company also invests in short-term mortgages. With interest rates rising, First National could stand to benefit by taking advantage of higher spreads, and although it may lose customers that are now unable to get mortgages because of the higher rates, those customers would have been high risk, and the increased spreads could offset a lot of that lost revenue anyway.

First National currently pays a dividend of over 7% per year, and the payouts are made on a monthly basis. In the past four quarters, the company has posted earnings per share of $3.73, which makes the payout ratio for First National just 50% of its net income. If that weren't good enough, consider that the company also annually grows its dividend, and since 2012, payouts have increased by over 42%. That means if you buy the stock today and hold it, in five years you could be earning 10% in dividends on your initial investment if the company follows a similar pattern in hiking its payout.

Medical Facilities Corp. (TSX:DR) has interests in entities that, by and large, own either specialty surgical hospitals or ambulatory surgery centres. These hospitals and surgery centres are in many states across the United States. Health care is a necessity, and investing in this company provides some stability for investors looking for recession-proof-type investments.

Currently, the stock pays monthly dividends of $0.0938, and although the company hasn't had a dividend hike in five years, with an annual yield of over 7.4%, I'm sure investors will be able to look past that. With earnings per share of $0.99, the company is currently paying out over 113% of its net income. However, Medical Facilities also has a lot of non-cash expenses that drive down its net income and won't reflect its true ability to meet dividend payments.

If we look at dividend payments as a percentage of cash flows, we see a more sustainable payout ratio. In the past 12 months, the company paid $26 million in dividends, or just 29% of its cash flow from operations and 59% of free cash flow.

When looking at a company's payout ratio, you need to consider if it has a lot of non-cash items in its net income. If the company has a lot of depreciation expenses, then that might be a hint that using net income to calculate the payout ratio is likely not going to be helpful in assessing if the company can afford its current dividend.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:DR (Medical Facilities Corporation)
2. TSX:FN (First National Financial Corporation)

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