



Looking For A Retirement Income? Here's Where I Think Is The Perfect Place To Start

Description

Deciding where to invest in order to generate a retirement income can be challenging. Investors are unlikely to want to take a significant amount of risk, since their retirement portfolio must be able to provide them with a long-term income. However, its returns must be sufficient to counter the threat of inflation.

With that in mind, investing in [dividend stocks](#) could be a shrewd move. They may offer more risk than some assets in terms of their volatility, but their higher returns could provide a healthy income for retirement.

Risks

In terms of the risks of investing in stocks, the economic cycle is an ever-present danger. Over the history of the stock market, it has experienced ups and downs. In future, this trend is very likely to continue, which means that a retiree with a portfolio of stocks may see paper losses at times over the long run.

This in itself is not a major problem for an investor who is not looking to sell. Certainly, paper losses can be frustrating, but as long as the companies in question are able to continue to pay growing dividends, their falling market valuations are somewhat irrelevant to an income investor in older age.

Of course, it is crucial to diversify away company-specific risk. Buying stocks in a variety of sectors and geographies can help to de-risk a portfolio yet further, although in reality the volatility of the stock market is likely to remain.

Returns

While other assets such as cash and bonds may offer less risk than stocks in terms of their price volatility, where they lack appeal is in terms of their return prospects. That's especially the case at a

time when a loose monetary policy has caused bond yields to fall and the interest rate on cash to remain at a low ebb. Simultaneously, low interest rates and the impact of quantitative easing could cause a spike in inflation over the coming years. This could mean that the returns from bonds and cash falls in real terms over the long run.

In contrast, stocks have a much better ability to outpace inflation. Companies are often able to pass higher input costs on to their customers, and this can mean that dividend growth remains ahead of inflation over the long run. With life expectancy on the rise, an individual may realistically be retired for 30 years or more. In that time, a failure to at least match inflation when it comes to income can lead to financial challenges in older age.

Long-term potential

While investing in dividend stocks may seem to be a risky move compared to buying bonds or holding cash, the reality is that it offers an appealing risk/reward ratio for the long term. Having a variety of dividend stocks within a portfolio could lead to company-specific risk being diversified away, while stocks can offer better protection against the harmful effect of inflation in the long run.

As such, buying dividend stocks when in retirement could be a shrewd move. While no investment is perfect, it may be the best opportunity relative to other assets.

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Date

2025/08/25

Date Created

2019/03/16

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