



3 Simple Steps to Make a Reliable Passive Income From Dividend Shares

Description

Dividend stocks can provide a robust and highly appealing passive income over the long run. Of course, they can experience periods of volatility and financial challenges. Therefore, diversifying across a range of businesses within a portfolio is a sound move.

Furthermore, focusing on companies that have relatively dependable business models can help to reduce risk further. And, by assessing a company's [dividend affordability](#), you may be able to obtain a more resilient income stream that is less impacted by the ups-and-downs of the economic cycle.

Diversity

Perhaps the most obvious way to increase the reliability of a passive income from dividend stocks is to diversify. This helps to reduce company-specific risk, which is the potential for difficulties experienced by a single stock to impact negatively on your wider portfolio.

Furthermore, diversifying among different industries and regions can be a sound move. Globalization may mean that there is more correlation between the economic performances of different regions, but it may still be worth buying stocks that have exposure to different countries to reduce your exposure to local risks.

In addition, buying shares in companies that operate in different industries could make it easier to overcome risk factors such as changing consumer tastes and evolving technology. This could lead to a more robust income stream in the long run.

Defensive business models

The type of company held within a portfolio may also impact on how reliable its dividends will be in the long run. While cyclical companies may offer high and growing dividends during bull markets, their income potential in recessions may be severely impacted by their reliance on the performance of the economy.

As such, focusing your capital on companies which have defensive characteristics and that are less reliant on the economy to generate growth could be a worthwhile move. They may not produce rapid dividend growth as per some stocks, but their long-term dividends could be higher due to them offering modest but consistent year-on-year growth.

Dividend affordability

The affordability of a company's dividend can have a significant impact on the likelihood that it will grow, or even be maintained, in the long run. For example, a business that has a significant amount of headroom when making its dividend payments each year may be less likely to experience difficulties in affording it. By contrast, a company that pays out most, or even all, of its net profit as a dividend could struggle to maintain it over a prolonged period.

Therefore, checking a company's dividend payments versus its net profit, or even its free cash flow, could provide guidance on its affordability. Clearly, operating conditions can change and may impact positively or negatively on its ability to make dividend payments. But through focusing your capital on stocks with modest dividend payout ratios, it may be possible to reduce your risks in terms of generating a more robust passive income.

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