3 Reasons Why Dividend Shares can Boost Your Passive Income in 2020

Description

Generating a passive income has been relatively challenging over recent years. Assets such as bonds and cash have failed to offer strong after-inflation returns in many cases, with this trend having the potential to persist during 2020.

As such, now may be the right time to consider buying dividend shares. In many cases they offer high yields which could improve as the world economy delivers a continued rise in GDP.

Low valuations

Despite the stock market having experienced strong growth since the global financial crisis, many stocks continue to trade on low valuations. Investors appear to be concerned about risks such as political uncertainty in the US, which could negatively impact on the global growth outlook.

As a result, many companies currently trade on modest valuations and offer high dividend yields. In many cases, their yields are above their long-term averages, since they have been able to pay rising shareholder payouts as a growing world economy has catalysed their top and bottom lines.

Investors may, therefore, be able to build a diverse portfolio of stocks that offers a high income return, as well as capital growth.

Dividend growth

As well as offering high yields, dividend stocks could deliver a rising income stream for their investors. The prospects for the world economy suggest that, while risks are present, GDP growth could continue to be strong in 2020. This may positively impact on the financial performance of a wide range of businesses, which then enables them to generate higher levels of profit and pay a rising dividend.

In many cases, dividend growth could prove to be ahead of inflation. This may increase your spending power and enable you to enjoy greater financial freedom over the long run.

Improving the chances of this happening can be achieved by assessing the prospects for a business to raise dividends. For example, considering its dividend coverage ratio (which is calculated by dividing net profit by dividends paid) and management attitudes to rewarding shareholders can provide an insight into the likelihood of future dividend growth.

Interest rate outlook

With interest rates being relatively low, generating an inflation-beating income return from other assets such as cash and bonds has become more difficult. Rising bond prices and lower savings interest rates mean that many income investors are struggling to generate a return that increases, or even maintains, their spending power each year.

Looking ahead, the pace of interest rate rises could prove to be relatively slow. This could lead to continued challenges for savers and bondholders over the coming years. Although a loss of spending power is a gradual process which may not be noticed over a short timeframe, over the long run it can be detrimental to your lifestyle.

Takeaway

Now may be the right time to seek out the higher income returns which can be generated from dividend stocks when compared to assets such as bonds and cash. In addition, income shares could provide dividend growth which significantly boosts your passive income in 2020, and in the coming years.

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