No Savings at 40? I'd Buy Dividend Stocks to Retire on a Passive Income

Description

Having no savings at age 40 does not mean that a passive income in retirement is beyond your reach. After all, there are still likely to be more than two decades left for your capital to grow into a nest egg which can provide financial freedom in retirement.

In fact, through buying undervalued dividend shares and holding them for the long run, you could significantly improve your retirement prospects. With the stock market currently trading at a relatively attractive valuation, now could be the right time to kick-start your retirement plans.

Return potential

The return potential of the stock market is significantly higher than other mainstream assets. For example, indexes such as the S&P 500 and FTSE 100 have recorded high single-digit annual returns since their inception.

Certainly, they have failed to deliver consistent growth. However, at age 40 you have a long time horizon until you are likely to retire. This means that you may have the capacity to overcome short-term paper losses on your investments, in terms of having sufficient time for your stocks to recover.

By contrast, having cash savings or bonds could lead to disappointing returns – especially with interest rates being relatively low at the present time. In many cases, they may be unable to boost your spending power over the coming years, which may lead to a substantial difference in their return profiles compared to shares.

Dividend prospects

While buying growth shares may seem to be an obvious step to take when seeking to build a retirement portfolio, dividend shares could offer high total returns in the long run. In fact, a large proportion of the stock market's historic total returns have been derived from the reinvestment of dividends. Therefore, focusing your capital on dividend-paying stocks could be a means of obtaining an impressive return in the long run.

Moreover, dividend stocks could prove to be less risky than their growth counterparts. In some cases, dividends can provide guidance about the financial health of a business. They can offer a snapshot of the profitability of a company, as well as what its future performance may be. For example, a company that has a robust track record of dividend payments and is forecast to maintain its rate of dividend growth may prove to be a less risky purchase than a cyclical growth stock.

Buying opportunity

With investor sentiment currently relatively weak, now could be the right time to buy dividend stocks. Risks such as coronavirus and political uncertainty in the US may cause further share price declines in the short run. But investors who have long time horizons may have sufficient time for their holdings to recover from paper losses to post high returns in the long run.

As such, now could be the right time to start planning your retirement, with it being possible to generate a passive income in older age from a standing start at age 40.

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