Retirees: 1 Trick to Max Out Your Passive Income With Dividend Stocks

Description

The stock market's recent challenges mean that a number of stocks have relatively high dividend yields at the present time. As such, many investors may be seeking to improve their passive income through purchasing high-yielding stocks.

While this can be a sound strategy, considering a company's dividend prospects over the long run could be a better idea. A high yield today may not translate into a growing and sustainable passive income in the coming years.

As such, focusing on dividend prospects, rather than solely on dividend yield, could be a shrewd move – especially after the market crash.

Dividend prospects

The dividend prospects for any business can be measured by their affordability, as well as by their potential to rise over the long term. In terms of affordability, there is little point in buying a stock with a high yield when its dividend payments are unlikely to be met over the medium term.

Therefore, assessing a stock's headroom when making its shareholder payouts is a worthwhile move. This can be achieved by dividing net profit by dividends paid to determine how many times a company is able to make its shareholder payout. A figure of less than one suggests that dividends could be reduced in the near term.

As well as checking the affordability of a company's dividends, it makes sense to consider their growth potential. This is arguably more subjective than considering dividend affordability, since it hinges to a large extent on the future profitability of the company in question. However, by considering its operating environment, past dividend growth, and the attitude of its management team towards reinvesting profits, it is possible to ascertain the likelihood for dividends to rise at a fast pace over the long term.

Buying opportunities

Clearly, at the present time the prospects for dividend stocks are relatively challenging. Investors may become cautious about the affordability and growth prospects of dividends across a range of companies.

However, history shows that while economic challenges can be painful in the short run, the global economy has always recovered from recessions to return to growth. Therefore, today could be a good buying opportunity while many stocks have high yields and low valuations. They may still be able to post resilient shareholder payouts and raise them at an above-inflation pace over the coming years.

Relative appeal

Certainly, there may be less risky means of generating a passive income at the present time. You are less likely, for example, to lose money on cash or bonds. But those assets also fail to have the passive income potential of stocks, and would require a larger amount of capital to produce a similar income level due to their lower returns.

As such, now could be the right time to buy dividend shares to enjoy a relatively high passive income. By assessing their dividend prospects, in terms of affordability and growth potential, you can enjoy a higher income return.

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peterstephens