



## Use Covered Calls and This Utility Stock to Create Your Own 22.9% Dividend

### Description

Covered calls can be a very useful tool in an investor's arsenal. Especially during periods of tumultuous markets, like we're seeing today.

Here's how they work. The first step is to own the underlying stock. Without doing that, a covered call isn't possible. Next, you sell a call option, a move that generates income today but in exchange for creating a sell obligation in the future. The sell obligation will be at a certain price at a certain date, which is referred to as the strike price.

The trade has two possible outcomes. Either the stock trades below the strike price on the magical day, or it goes higher and you're forced to sell. Ideally, a stock will trade under the strike price, meaning you'll still own it and you're free to do another covered call trade. If the stock rallies and you're forced to sell, you've still locked in a profit.

Normally, this move can net an investor anywhere from 0.5% to 1% per month, assuming you do the trade with one of Canada's many [monthly dividend](#) stocks. But recent volatility has made the covered call game much more lucrative. You can own relatively boring stocks and use them to collect some serious yield. We're talking anywhere from 20% to 30% annualized.

Let's take a look at one such stock, **TransAlta Renewables** ([TSX:RNW](#)). Here's how you can turn this steady dividend payer into something that generates an annualized income of 22.9%. No, that's not a typo. It really has that potential.

### Why TransAlta Renewables?

There's little doubt about it. The future of power generation will come from renewable energy.

TransAlta Renewables has solid portfolio filled with environmentally friendly power-generation facilities. The portfolio includes 44 different natural gas, wind, hydro, and solar powered assets that collectively generate more than 2,500 MW of energy.

The company hasn't expanded much over the last few years, but that should change in 2020. It is finishing a development project as we speak, a series of wind farms that should add between 5% and 10% to the bottom line this year. This could very well translate into the company's first dividend increase since 2017.

This fat current dividend — the stock yields 6.4% today — is one of the things that makes TransAlta Renewables a great covered call candidate. And the company's ex-dividend date is April 14, meaning if you get in today, you'll be able to take advantage of this situation very soon.

## Covered call yield of 22.9%

Remember, the first step of a covered call trade is to own the underlying stock. By doing so with TransAlta Renewables, you've already locked in a 6.4% yield.

Thanks to the recent market volatility, selling a call option will generate some serious income. As I type this, the company's \$16 call option trades for \$0.20 per share. Remember, the stock currently trades at \$14.58 per share. The strike date on this trade would be April 17, minimizing the time risk here.

In other words, if you buy TransAlta Renewables stock today and write a covered call option on it, you'll generate \$0.27833 per share in income, minus any commissions on the trades. Assuming you can do this trade every month, that works out to an annualized yield of 22.9%.

## The bottom line

The [market crash](#) isn't just creating situations where investors can buy solid long-term stocks for their portfolios. It's also creating an interesting opportunity to engage in some smart covered calls.

One key for this strategy is buying excellent stocks to begin with. That way, you won't be tempted to sell when the covered call strategy goes against you.

It might take a little work, but this is a pretty interesting way to goose your portfolio's yield. This could be especially lucrative for retirees or other folks looking to live on their passive income. If that's you, you owe it to yourself to explore this unique investment strategy a little further.

### CATEGORY

1. Dividend Stocks
2. Investing

### TICKERS GLOBAL

1. TSX:RNW (TransAlta Renewables)

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