Yield Alert: Get a 18.5% Income Stream From This Unloved Asset

Description

There's a little-known income investing technique that investors are using to generate eye-popping yields. We're talking payouts of 10%… 15%… or even more on an annual basis.

No, that's not a typo. In fact, we'll be looking at how you can use this method to generate an 18.5% annual return using an unloved asset class that looks poised to return to glory.

Does that sound interesting? Of course it does! Let's take a closer look.

A covered call approach

The strategy is a covered call approach, and it works a little something like this. The first step is simple. You must own the underlying stock.

We'll use **Chartwell Retirement Residences** (TSX:CSH.UN) for today's example. I like Chartwell today because it's still beaten up — thanks to COVID-19's impact on the seniors living sector — and it offers a robust dividend yield, a payout that looks to be safe.

The next step is to venture into the options market. What we want to do for a covered call trade is to sell a call option, a contract that gives the buyer the right to buy a stock at a certain price on a certain day. Since we're selling the option, we're on the other side of the trade. We have an obligation to sell the stock at a certain price on a certain day.

As I type this, Chartwell shares trade hands for approximately $10 each. The best call option to sell would be the July 17th $11 option, which means we've created an obligation to sell shares at $11 each on July 17. In exchange for taking on that risk we're paid $0.10 per share.

This trade has one of two conclusions. If Chartwell shares stay about the same or fall a little bit, the option expires worthless. After all, the person on the other side of the trade is silly to buy at $11 if the market price is still $10. The other outcome is Chartwell shares rising above $11 each. This means we'd be forced to sell our Chartwell shares for $11 each, which would lock in a 10% profit on the capital gain alone. That's not a bad outcome for just a month.

How to collect an 18.5% yield

We must remember that a covered call trade has two sources of income. You get paid immediately for selling the call option. But since you'd own the underlying stock, you'll get a dividend payment too.

As I type this, Chartwell offers a 6.5% yield on its monthly dividend alone. The covered call option pays $0.10 per share, which works out to a 12% annualized yield. Combine the two and we get an 18.5% income stream.

Ideally, you'd like Chartwell shares to trade around $10 each indefinitely. It would be easy to sell call options and pocket the premium. Unfortunately, the market doesn't often work that way. You'll likely end up having to sell your shares at some point. But being forced to take a profit isn't the worst outcome in the world.

And remember, even if you're forced to sell at a profit, there's nothing stopping you from doing the exact same trade month after month. Covered calls aren't a particularly difficult strategy, and they work well during periods of excess volatility — just like we're seeing today.

The bottom line on this income stream

Covered calls are an excellent way to goose your passive income. Just be warned: the strategy will involve a little bit of work. Perhaps the best way to play it is to use a covered call ETF instead.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:CSH.UN (Chartwell Retirement Residences)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
3. Msn
4. Newscred
5. Sharewise
6. Yahoo CA

Category

1. Dividend Stocks
2. Investing

Date

2025/08/13
Date Created
2020/06/20
Author
nelsonpsmith