Passive-Income Seekers: Watch Out for the Great Dividend Reset

Description

If you're like me, you've been steadily building a passive-income portfolio based on the most robust dividend stocks. Relying on dividends from major corporations to support your lifestyle is a time-honoured way of retiring early. It's also an excellent way to build wealth if you intend to retire later and can reinvest the dividends.

However, the economic situation has heightened the level of risk these dividend-paying companies face. Here's why investors should brace for a grand dividend reset in 2020 and 2021. You may want to restructure your passive-income plan accordingly

Economic divergence

The pandemic-driven lockdown has impaired the tangible economy and boosted the intangible economy. Software and services saw a big boost during the lockdown, while real estate and oil stocks plunged. Unfortunately, the latter group has been more generous with shareholder dividends.

Shopify, for example, pays no dividend. This is because the company aggressively reinvests all its earnings to fuel hyper-growth. Other software and tech stocks do the same and offer little to no return.

However, real estate investment trusts, banks, and energy companies are usually the best passive-income stocks. That's because they pay the highest dividends. However, since banks face a mortgage crisis, malls are shut, and demand for oil is lower, all these companies could face lower profits this year.

Passive-income impact

If the economy continues to drag like this, these companies could be forced to cut or suspend their dividends. This is already happening. 33 stocks have cut their dividend this year. This includes passive-income favourites like **Suncor** and **Laurentian Bank**.

Meanwhile, real estate investment trusts like **Morguard REIT** and **H&R REIT** have cut their dividends too. **American Hotel Properties**, previously one of the highest dividend-paying stocks on the market, has suspended its dividend entirely.

Investors should watch out for more REITs and dividend stocks to join this list in the coming months. **Enbridge** currently offers a 7.47% dividend yield, but its payout ratio is 329%. If earnings don't improve soon, the company may be forced to slash the dividend

What can you do?

Focusing on debt and the dividend-payout ratio is usually a good idea for passive-income investors. A company that is conservative with its cash, that has a resilient business model, and that has low interest burden can sustain its shareholder rewards through this crisis.

Royal Bank of Canada offers a sizable dividend yield: 4.5%. Its payout ratio is just 0.54, which means nearly half of annual earnings are saved. Canada's largest bank also has a robust balance sheet and low risk, according to banking experts. This means it can face a downturn in the economy and the real estate market.

You can probably seek out other stocks with high dividend yields, low debt, and conservative payout ratios. Adding these to your portfolio, while eliminating the risky ones, should cement your passive income for the long term.

Bottom line

33 companies have cut their dividends, and many more could make the same difficult choice. Investors should consider replacing risky dividend stocks with robust businesses to save their passive income from the Great Dividend Reset.

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vraisinghani