Should You Buy TD Bank (TSX:TD) Stock for its 4.9% Dividend Yield?

Description

Dividend stocks are a tried-and-test method to supplement your income. Stocks with high dividend yields and with a sustainable payout ratio can help generate a stable stream of predictable and recurring income.

While high dividend yields are attractive, the company should be able to keep paying dividends across economic cycles. Investors need to consider several factors including dividend stability, growth, and payout ratios before taking a position in a dividend stock.

The recent market uncertainty due to the COVID-19 pandemic has dragged shares of banking giants, including **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD), lower. TD stock fell from $77.72 in February to a multi-year low of $49 in March. It's currently trading at $65 per share, which means its dividend yield stands at a tasty 4.9%.

TD Bank has paid dividends since 1998

TD Bank has paid dividends to investors for 22 consecutive years. Its trailing 12-month dividend per share has increased from $0.21 in 2000 to $3.11 per share today — an annual growth rate of over 14%. In the last five years, TD Bank has increased dividends at an annual rate of 9.23%.

If you'd bought 1,000 TD Bank shares for $7.53 per share back in September 2000, you would have generated $210 in annual dividend income. TD stock has gained 11.4% annually and your investment worth $7,530 in 2000 would have ballooned to $78,600 today, after accounting for dividend reinvestments.

Similarly, if you invest $10,000 in TD stock today, you will rake in $490 in annual dividends. After accounting for reinvestments, these payouts will increase to $2,500 per year in the next 20 years if the company grows its dividends by 9% per year. We can see how dividend-growth stocks can effectively turn a 4.9% yield to 25% over the long term.

TD stock remains an attractive long-term option

When the economy is in a recession, bank stocks come under pressure, as interest rates are lowered and unemployment spikes. This increases the risk of mortgage, consumer, and enterprise defaults, resulting in a sell-off in banking stocks.

However, when the economy recovers, banks profit profoundly, which enables them to increase dividends and generate capital gains.

TD Bank is one of the top financial companies in North America and has delivered high-quality earnings growth to investors. It has already gained 35% since March 2020, and while the stock will be range bound in the near term, it offers significant upside potential for long-term investors.

Yes, the effects of the COVID-19 pandemic are severe, but TD Bank has a strong balance sheet, a huge market presence, and enough liquidity to help it through the crisis. Company performance will be subdued in the next 12 months due to rising provisions for credit losses and weakening margins. But there is an opportunity for plenty of upside when the economy rebounds.

The Foolish takeaway

Fool contributor Joey Frenette noted, “Today, TD stock trades at a crisis-level discount that I don’t think will be around once this pandemic subsides.” The Canadian banking giant has survived multiple recessions, increased dividends at an enviable rate, and managed to outpace the broader markets since the start of this millennium.

While growth stocks are always attractive due to their potential to generate multi-fold gains, you should also invest in blue-chip stocks such as TD Bank.

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