3 Reasons Dividend Growth Is the Best Way to Invest

Description

The best dividend stocks are the ones that can offer both a high yield and consistent growth. In other words, a dividend stock that expands payouts by 5% annually is better than a dividend stock that provides a 5% dividend yield forever.

Here are my top three reasons why this difference is critical and why you should look for dividend-growth stocks to add to your portfolio right away.

Dividend stocks replace fixed income

“Dividends have been an increasingly important source of investment income, as bond yields have plummeted in recent years,” says Jack Ablin, chief investment officer from Cresset Capital, in a recent note to investors. According to Ablin, central banks across the world (including the Bank of Canada) have pushed interest rates far below the yield on these stocks.

That means investing in telecom giant **BCE** (TSX:BCE)(NYSE:BCE) for its 5.87% dividend yield is obviously a better idea than leaving cash in your savings account. Even the best savings accounts in Canada don’t offer returns anywhere close to dividend yields.

Capital appreciation

If you’d invested $10,000 in BCE stock in 2009, 11 years ago, it would be worth over $21,300 today. That’s a decent return, but nowhere close to what some tech and hyper-growth stocks offer.

However, BCE’s true capital return is hidden. The company has increased its dividend every year over the past 11 years. This growing dividend means you receive a nearly 12% yield on your original $10,000 invested in BCE stock. Reinvesting these dividends over time to buy more BCE stock would boost your returns tremendously.

This hidden dividend-growth factor is the secret sauce of some of the world’s most successful investors. Warren Buffett has built the bulk of his fortune by focusing on these stocks. Some research by Standard & Poor’s indicates that 40-50% of the stock markets total return over time is hidden in this dividend-growth phenomenon.

Dividend stocks are reliable

Some dividend-growth stocks have a better streak of accelerating dividends than BCE. These companies that can boost payouts for decades are known as “Dividend Aristocrats.” Dividend Aristocrats have a record of increasing dividend payouts per year consistently for the last 25 years.

Investment legend Peter Lynch called them “the dividend achievers” in his book. That’s because companies that can reliably boost earnings and offer consistently expanding shareholder rewards, year after year, are truly special.

If BCE can sustain its dividend-growth pace for the next 14 years, it could secure this coveted title of “Dividend Aristocrat.” Of course, with 5G on the horizon, BCE seems destined for better growth ahead. That means now is probably the best time to get into the stock.

Bottom line

A dividend stock that is growing is better than a static stock. These companies have demonstrated an ability to expand shareholder returns consistently. Dividend growth is responsible for the bulk of stock market returns.

Which is why investors should focus on stocks like BCE, which has high yields and better growth prospects than most public companies.

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