How I’d Turn Cheap Shares Into a Lasting Income Stream

Description

Buying cheap shares to make a passive income stream may not sound like an appealing idea to some investors. For example, they may think that today’s cheap stocks are priced at low levels because of their weak business models or poor financial outlooks.

While in some cases that may be true, in others it is far from the truth. Some low-priced shares can offer affordable dividends, growth potential and may contribute to a dependable passive income stream over the long run.

Identifying high-quality cheap shares

Assessing which cheap shares are high-quality companies may be a prudent first step in creating a long-lasting passive income. A good starting point to achieve this aim may be a company’s annual report. It provides guidance on the financial position of a business, as well as other facts and figures that may shine a light on the reliability of its dividend. For example, a company that has low debt levels and a dividend that is covered more than once by net profit may offer a robust passive income outlook.

Furthermore, a company’s latest investor updates paint a picture of its overall strategy. This may be especially relevant at the present time, when a number of industries are experiencing major changes. If company management has a flexible strategy that can adapt to what could be a very changeable period in the coming months, it may stand a better chance of delivering improving financial performance. This could mean that it has investment potential versus other cheap shares.

Dividend growth potential

Annual reports and investor updates can provide insight into the dividend growth prospects of cheap shares. For example, a business that pays out a small proportion of profit as a dividend may be able to raise shareholder payouts in future without necessarily increasing profitability. Similarly, a companywith a sound strategy that is set to enter a new market may be able to produce improving financial performance that results in strong dividend growth.

Dividend growth could become increasingly important in the coming years. The scale of monetary policy stimulus enacted in recent months suggests that a period of higher global inflation would not be a major surprise. As such, cheap shares that can produce dividend growth may become more valuable in the eyes of investors. This may mean they offer capital growth prospects, as well as an attractive passive income outlook.

Diversifying to create a passive income stream

Of course, some cheap shares could deliver poor returns in the coming years. Even if they have solid financial positions, a competitive advantage and sound dividend prospects, unforeseen events may hold back their financial prospects.

As such, it is crucial to diversify across a wide range of businesses. This could lead to less risk, as well as higher returns in the long run.

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