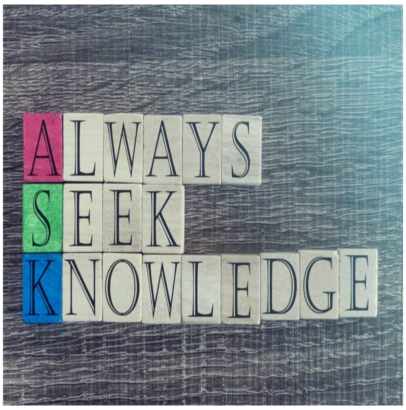

A Complete Guide to Investing in Dividend Stocks

Description

The stock market offers a boatload of options for all types of investors with different risk profiles. Today, I will talk about dividend stocks — Warren Buffett's favourite stocks, and mine, too. An equity share gives the shareholder a right in the company's net profit. As an equity shareholder, you can earn from capital appreciation or dividends. Capital appreciation is a fancy term for an increase in share price and is a forte of growth stocks. Dividend stocks are the ones where the company directly pays a share of profit through monthly or quarterly dividends.

Dividend investing basics

A company pays dividends from its free cash flow (FCF). This means only those companies that have stable cash flow can pay dividends. Hence, you will rarely see small tech companies or airlines paying dividends, as their cash flow fluctuates. Mostly traditional capital-intensive companies with little competition and high demand pay dividends. Real estate, energy, utilities, financial, telecommunication, materials, and industrial are sectors where you can find Dividend Aristocrats.

How to identify a good dividend stock

Unlike growth stocks, dividend stocks are less complex. Past performance does not guarantee future growth, but in the case of dividend stocks, dividend history shows the company's stability. Any dividend-related decision is at the management's discretion. The management first allocates the cash to invest in the business, repays any urgent debts, and then pays dividends.

When researching dividend stocks, look at the company's last five to six years of FCF. Then look at its ability to continue generating stable cash flow for the coming years. This will ensure the company's future dividends. Also, look at its dividend-payout ratio, which tells how much net income the company has paid as dividends.

Enbridge: A dividend stock for beginners

For instance, **Enbridge** (TSX:ENB)(NYSE:ENB) is a pipeline operator that has a history of paying a quarterly dividend for over 40 years. It has been increasing dividends at a compounded annual growth rate (CAGR) of 10% for the last 26 years. How does it manage to grow dividends?

Enbridge invests millions of dollars in building pipelines. Once these pipelines are operational, Enbridge signs long-term contracts to transmit oil and natural gas in return for toll money, which increases at regular intervals. This ensures regular cash flow, which it uses to build new pipelines, reduce debt, and pay dividends. The addition of new pipelines and an increase in toll rate lead to cash flow growth and, therefore, dividend growth.

Enbridge's robust cash-focused business has helped it pay dividends every year, and it will continue to pay dividends as long as its pipelines are functional. Its dividend could be affected if any of its major pipelines are destroyed because of natural or manmade calamities. Its dividend growth could slow, as it becomes increasingly difficult to make new pipelines. Unless there is a major incident, like when **TC Energy** cancelled its Keystone XL Pipeline, Enbridge's dividend is safe.

When do companies cut dividends?

As dividends are paid at the management's discretion, you will see many companies cut dividends during crises to preserve cash for the hay day. For instance, **Suncor Energy** (TSX:SU)(NYSE:SU) slashed dividends by 55% in May 2020, as the pandemic reduced oil price below the cost. All oil companies faced massive losses, as there wasn't enough demand, and they were selling oil below the production cost. Suncor slashed its dividend, as there was uncertainty around how long the pandemic-induced lockdown would last.

When do companies grow dividends?

A company increases dividends when it finds a new recurring cash flow stream. It sometimes pays special dividends if it sees a windfall gain in a particular year.

But there are Dividend Aristocrats that do not want to taint their history of paying regular dividends. Hence, they pay dividends, even if their profits fall or if they face temporary losses. For instance, **SmartCentres REIT** maintained its annual dividend, even when the pandemic reduced its 2020 FCF by 14%.

Now that you know how to look or dividend stocks, here is a list of top dividend stocks to begin investing.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing
4. Personal Finance

TICKERS GLOBAL

1. NYSE:ENB (Enbridge Inc.)
2. NYSE:SU (Suncor Energy Inc.)
3. TSX:ENB (Enbridge Inc.)
4. TSX:SU (Suncor Energy Inc.)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
3. Msn
4. Newscred
5. Quote Media
6. Sharewise
7. Smart News
8. Yahoo CA

PP NOTIFY USER

1. kduncombe
2. pujatayal

Category

1. Dividend Stocks
2. Energy Stocks
3. Investing
4. Personal Finance

Date
2025/07/17
Date Created
2021/08/25
Author
pujatayal