Passive Income Investors: How to Find Top Stocks for Your Portfolio

Description

Investing in dividend stocks is a strategy employed by many Canadians. In fact, the concept of building a passive source of income is often what drives many individuals to invest in the first place. By building a portfolio of solid dividend companies, investors will be able to supplement and eventually replace their primary sources of income. Although dividend investing may be very popular, investors often fall victim to bad stocks. In this article, I discuss how to find top stocks for your portfolio.

An important quality

When choosing which dividend stocks to include in a portfolio, many investors often focus on a company's forward yield. This is calculated as the proportion of a company's share price that is paid out in dividends each year. While a high dividend yield suggests that investors may be paying less for a larger income, it's not the most important metric to consider.

Instead, investors should worry more about how long a company's been able to increase its distribution. This is important because dividend distributions that constantly increase will allow an investor's income to keep on pace with inflation (or even beat it). An example of a company that has consistently raised its dividend distribution is **Fortis**. With a dividend growth streak of 47 years, the company is known as a Canadian Dividend Aristocrat. This dividend growth streak is also the second-longest active growth streak in Canada.

Choose companies you're familiar with

There are many companies on the **TSX** that offer dividends. When you invest in a company, you become a part-owner of that company. Therefore, you should have a constant interest in following the growth and development of that company over time. Your job then becomes much easier if you stick to investing in companies you're already familiar with. By doing so, you ensure that you have a solid understanding of how the company makes money and its competitive landscape.

For example, if you bank with **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) and are pleased with its service, it would be a great idea to invest in the company. Luckily for you, the Canadian banking industry is highly regulated. This makes Bank of Nova Scotia even more appealing because these regulations make it difficult for new competitors to displace industry leaders. The Bank of Nova Scotia is another Canadian Dividend Aristocrat and also offers investors an attractive forward dividend yield of 4.38%.

One final metric to consider

Another metric that dividend investors should consider is a company's payout ratio. This is the ratio between a company's earnings and its dividend. Generally, dividend investors should look for payout ratios of 50% or less. The lower a company's payout ratio, the easier it'll be for that company to continue increasing dividend distributions in the future. This means that investors have a better chance of seeing a continually increasing source of passive income over time.

One company that stands out for its payout ratio is **goeasy** (TSX:GSY). The company currently maintains a payout ratio of 16.63%. Now, this may cause some investors to ask, "Does goeasy even raise its dividend?" You'll be surprised to hear that it does. In fact, it's known as a Canadian Dividend Aristocrat, after having successfully increased its dividend in each of the past six years. Over that period, goeasy's dividend has grown more than 600%! That makes the company's low payout ratio all the more appealing.

CATEGORY

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3. TSX:GSY (goeasy Ltd.)

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Date
2025/09/11
Date Created
2021/11/04
Author
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