No Dividend? No Problem: How to Get Passive Income From ANY Stock!

Description

Did you know that you can generate passive income from any stock whether or not it pays a dividend?

Not many people know this, but it's true.

Most people think that dividends and capital gains are the only sources of income from stocks, but in fact, there are many more. In this article, I will explore one option for generating passive income from stocks whether or not they pay dividends.

Covered calls

Calls are a type of financial derivative where the buyer pays for the right to buy an asset at a pre-determined price (called the "strike price"). The buyer pays the seller a premium in exchange for agreeing to sell the asset in the future. The buyer has the right to buy but isn't obligated to do so. The seller ("writer") has an obligation to sell–though the option may not actually be exercised, in which case the seller just pockets the premium. If an option does not hit its strike price then the buyer won't exercise it.

A covered call is a call option where the seller owns the asset underlying the option. So, the seller does not risk paying out huge amounts of cash to pay off the buyer–the sale is "covered," hence the name.

The way you generate income from covered calls is by being the "seller" in the transaction described above. You own 'X' amount of shares and you write calls based on those same shares. If the stock never hits the strike price, you pocket the premium. If it does, then your shares get called away and you also pocket the premium. Either way, that premium is yours to keep, like a "homemade dividend."

How much you can earn

The amount you can earn from writing covered calls depends on the option premium. If you write 100 calls at a premium of $2, you get $200. Your shares may get called away if the stock hits the strike price. So, while there's income to be gained here, there is also a cap on your potential return.

Not approved for options trading? Not a problem…

One obstacle to covered call writing is that your broker may not have approved you for it. Options trading is considered high risk, so not everyone is allowed to do it right away. Covered call writing in itself is not risky–it actually reduces volatility–but brokerage accounts don't have permissions for just covered calls and nothing else. If you want to write covered calls, you need full permission for options trading.

Fortunately, you can get your covered call exposure through ETFs like the **BMO Covered Call Banks ETF** (TSX:ZWB). These are ETFs that have covered calls "under the hood." The portfolio managers buy a portfolio of stocks–in ZWB's case, bank stocks–and write covered calls on them. The covered calls serve as a form of yield enhancement; that is to say, they increase the yield. ZWB is built on high-yield stocks. The covered calls take the yield even higher.

As a result, the fund yields an astounding 5.55%. That's a much higher yield than you'll get on most stocks alone. You do pay for that yield in the form of a fairly high 0.72% MER. Nevertheless, the payout is very high even with all the expenses taken out.

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