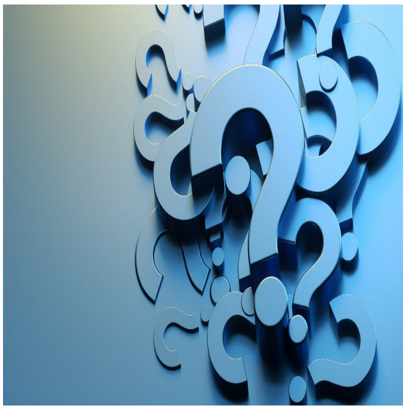

Dividends or Capital Growth: What Should Be Your Passive-Income Priority?

Description

For a lot of people, the primary reason to create a passive-income source is to augment the primary income. Because starting a passive income that can replace the job, business, or pension-based income would require substantial capital, which not many investors have access to. That's partly because when most people think of a passive income via stocks, they think of dividends, especially when they are learning to invest.

And if you wish to create a $50,000-a-year "passive" income through dividends, even with a generous dividend portfolio that yields about 7%, you will have to invest $715,000. And since three-quarters of a million is the amount most investors *strive* for and is not the capital they have to start investing, dividend-based passive income usually just supplements the regular income rather than replaces it.

But you can create a relatively "thicker" passive-income stream via growth stocks, but that requires a different approach.

Passive income through growth stocks

Let's say you have about $50,000 capital to invest, and instead of going through the usual dividend-for-passive-income route, you decided to invest it into a growth stock like **Thomson Reuters** (TSX:TRI)(NYSE:TRI) — ideally, a few years *before* you need to start a passive income. The company has grown about $50,000 in the last five years, and if it can replicate the feat again, you will be sitting on $100,000 in about five years from now.

If you liquidate your whole stake, you will have your capital ($50,000) back, and you will also have $50,000 in the form of returns that you can now use as passive income. You can use it to augment your passive income by a significant sum of $10,000 a year, or you can replace a year's worth of your primary income (or shorter duration), assuming it's around $50,000, with your passive/investment income.

The company also pays dividends, and if you can lock in the current yield of 1.5%, you will also get an additional $3,750 (at least, since it's an aristocrat) via dividends over the five-year period.

Passive income through dividends

If you invest the same sum ($50,000) in a reliable dividend stock like **Telus** (TSX:T)(NYSE:TU), which currently offers a 4.4% yield, you will get $2,000 a year. The sum will increase slightly every year, since Telus is an aristocrat and grows its payouts. Even a 7% increase a year will make the sum $2,140 next year.

One benefit is that it starts paying dividends right away, and you won't have to wait to get your capital and passive-income sum back. But if we apply the same five-year approach on Telus, which has grown its value by about 35% in the last five years, you will get about $67,500 by selling your stake, plus about $11,000 (a rough estimate) in dividends over five years.

However, you may achieve better results by investing in a dividend-growth stock that offers a better growth and dividend combination. Also, reinvesting your payouts can grow your stake till you need to start receiving those dividends for passive income.

Foolish takeaway

Both approaches are useful, depending upon your passive-income goals and financial reality. If you want to start a passive income right away and have more capital to work with, a great dividend portfolio is your best shot. But if you are working with limited capital, growing it via a growth portfolio to build a nest egg for later might be a good approach for you.

CATEGORY

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