Cash Dividends vs. DRIP: 2 Different Approaches to Passive Income

Description

There are a lot of different ways to start a passive income. The more capital you have, the more "passive-income-creation" options you can choose from. But capital is not the only variable necessary in identifying the right passive-income strategy. You have to look at your short-term and long-term passive-income goals, your risk tolerance, and a number of other factors before you take the right approach to passive income.

Similar to different strategies, there are different types of assets you can choose from. Dividend stocks are a common choice, and if that's the asset you are going with, there are two different passive-income approaches that you might consider.

A passive stream for the present with cash dividends

If you have an adequate amount of capital at your disposal, and you have identified safe, reliable dividend stocks, you can start a healthy passive income to augment your primary income. One such stock would be the energy king **Enbridge** (TSX:ENB)(NYSE:ENB). The pipeline giant of North America that's responsible for moving a sizeable portion of the total oil and natural gas in the region is also one of the most beloved Dividend Aristocrats in Canada.

Not only does the company almost always offer a mouthwatering yield, but time and time again, despite the harshest market conditions, the company keeps rewarding its investors with generous dividends. It even raised its payouts by a significant margin in 2021 after suffering a brutal pandemic year, which was especially difficult for the energy sector.

If you invest a sizeable amount of capital in the company, say $100,000, you can start a passive-income stream of about $6,310 a year. That's over $500 a month — quite a sizeable sum for completely hands-off passive income.

A passive-income stream for the future with DRIP

Relatively few people have enough free cash set aside to create sizeable passive-income streams that can actually help them with their regular expenses. And if they can make do without the small amount of dividend income, they can produce with their relatively small capital, a better use would be the DRIP.

With this approach, you can keep growing your stake in a good dividend payer, and when it comes the time to start taking their dividends in cash, you will receive a much healthier sum than would have been possible with your capital.

An example would be **Telus** (TSX:T)(NYSE:TU). If you had invested $10,000 in the company exactly 15 years ago to buy about 705 shares, you would have grown your stake to about 1,348 shares by now and your financial stake to over $41,000. At $1.31 per share in yearly dividends, this comes out to about $1,765 in dividend income.

That's more than one-fourth the yearly income with just one-tenth of the capital invested. And that's disregarding the capital appreciation.

Foolish takeaway

It's important to note that your choice of the dividend stock can significantly alter the "fate" of your passive income, regardless of the approach, so be careful with the companies you bet on. The TFSA is the no-brainer option for the first passive-income approach, and it would also be a smart choice for the second one, thanks to the accessibility it offers.

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adamothman