3 Quick Tips for Beginner Investors Interested in Dividend Stocks

Description

Are you excited to buy your first dividend stocks and start earning passive income? If so, make sure you check out these three tips first.

Long-term investing in dividend stocks

I can't stress enough that investors should focus on the longevity of the underlying businesses of stocks. That is, focus on investing for the long term, because short-term market volatility can distract investors from the goal of making money.

About a third of long-term market returns come from dividends, and you need to hold shares of stable dividend stocks to get dividend income. So, it makes sense to plan to hold shares for a long time. It's also less workload for you to have a long-term mindset so as to reduce the churn on your portfolio.

For example, an investor who'd bought $10,000 of **Royal Bank of Canada** (TSX:RY)(NYSE:RY) stock 15 years ago would have tripled their money by now, including receiving about $7,682 dividends. In that period, the leading Canadian bank increased its earnings per share by roughly 7.2% per year and dividend per share by about 6.4% annually.

Recall that 15 years ago was 2007, which was right before the global financial crisis market crash, during which Canadian banks (RBC stock included) lost as much as 50% of their market value. Those were some of the scariest times in the stock market, but it was also a great opportunity to gobble up shares of quality businesses. Investors with a long-term investing mindset made lots of money from buying then.

Diversify

It wouldn’t be smart to hold your entire dividend portfolio in Canadian bank stocks like RBC stock, no matter how much you trust them. What are some other possible businesses that you expect to become more profitable over time and be able to continue paying out healthy and higher dividends?

The idea of diversification is to spread your money across quality businesses in different sectors and industries — businesses that are exposed to different risks so their stocks won’t move in tandem. You can explore utilities, telecoms, energy infrastructure, and real estate investment trusts (REITs), which are good places to seek dividend income.

Depending on your financial goals, financial advisors would probably advise you to diversify your investment portfolio across different asset classes, too, including fixed-income assets and real estate. Fixed-income investments are sensitive to changes in interest rates. Therefore, they tend to move differently from common stocks.

Pay reasonable valuations for your dividend stocks

While investing for the long haul and diversifying your investments help you to ride through market volatility, new investors should still be careful not to overpay for investments. If you overpay for dividend stocks, you’ll reduce your expected dividend income and total returns potential.

On the contrary, despite feeling butterflies in your stomach, during a market crash, it could be the best time to buy stocks on the cheap. In the short run, stocks could appear risky, but from a long-term view, they could be substantially undervalued.

How does the valuation of RBC stock look now? At $132 and change per share, it trades at about 11.9 times its earnings. It’s essentially fairly priced and can deliver total returns of about 7-10% annually in the long run. It pays a yield of about 3.6% today.

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