Retirees: 3 Passive Dividend Investing Tips

Description

All passive income requires at least some initial work. I believe that dividend investing is as passive as earning income can get. Follow this checklist of three items to enjoy earning passive income from dividend stocks in retirement!

Retirees should do well by considering dividend stocks that have a track record of paying dividends. Make sure to check for dividend safety and invest for sufficiently high current yields.

Dividend safety

Different factors improve the dividend safety of a stock. Earnings or cash flow stability and growth are essential. Looking at the history of a business's earnings or cash flow can be telling in this aspect. For example, **Fortis** (TSX:FTS)(NYSE:FTS) stock's earnings have been highly stable through economic cycles and growing in the long run, because it's a regulated utility with predictable profits.

The financial position of the company is also important. You can quickly check the credit rating of a stock. (Fortis has a strong S&P credit ration of A-.) Otherwise, you can compare the current ratio and debt-to-assets ratio of a company to that of its industry. Generally speaking, the higher the current ratio and the lower the debt-to-assets ratio, the better. Utilities typically carry high debt on their balance sheet, because they usually have stable earnings.

Of course, retirees must track the payout ratio as well. How much is the company paying out as dividends from earnings or cash flow? Retirees should demand a margin of safety for this metric. Typically, the lower the payout ratio, the safer the dividend.

Dividend track record

Even when the dividends for a stock appear to be safe, management can still choose to cut the dividend. A dividend stock only has to pay out dividends that have been declared. However, if a dividend stock has a track record of paying out (ideally increasing) dividends, it'll more likely stick with the culture, even when there are changes in management. The longer the track record, the better.

For instance, having a super long dividend-growth streak like Fortis stock's 48 consecutive years of dividend increases is a reassuring track record for retirees.

"High" current yield

Retirees want high current dividend yields because they are living off of their dividends. Dividend income is a key component of their total income. How high must a dividend yield be to be considered a "high" yield?

Lowell Miller, the author of *The Single Best Investment*, believes a high yield is one that is 1.5 to two times that of the stock market's yield. You can probably find a free online version of the book, but you can also grab a hard copy of the book for reference if you prefer.

Currently, the Canadian stock market yields about 2.55%. So, a high yield is 3.8% to 5.1%. Fortis stock's yield is about 3.3%, so it doesn't make the cut for buying today. On further investigation, it's because the utility is fully valued now. In fact, the 12-month analyst consensus price target displayed on Yahoo Finance suggests there could be near-term downside of about 4% in the stock.

The Foolish investor takeaway

In retirees' journey for passive dividend income, it's essential to check for dividend safety and the dividend track record. When considering a buy today, look for "high" current yields and make sure you pay a reasonable valuation for your dividend stocks.

To protect your wealth and boost your overall income, you should seek a margin of safety for your purchases. The higher risk the stock, the bigger margin of safety you should seek. For a low-risk stock like Fortis, you might seek a minimum margin of safety of 10-20% before buying. That would imply a buy price range of approximately $49 to $55.

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