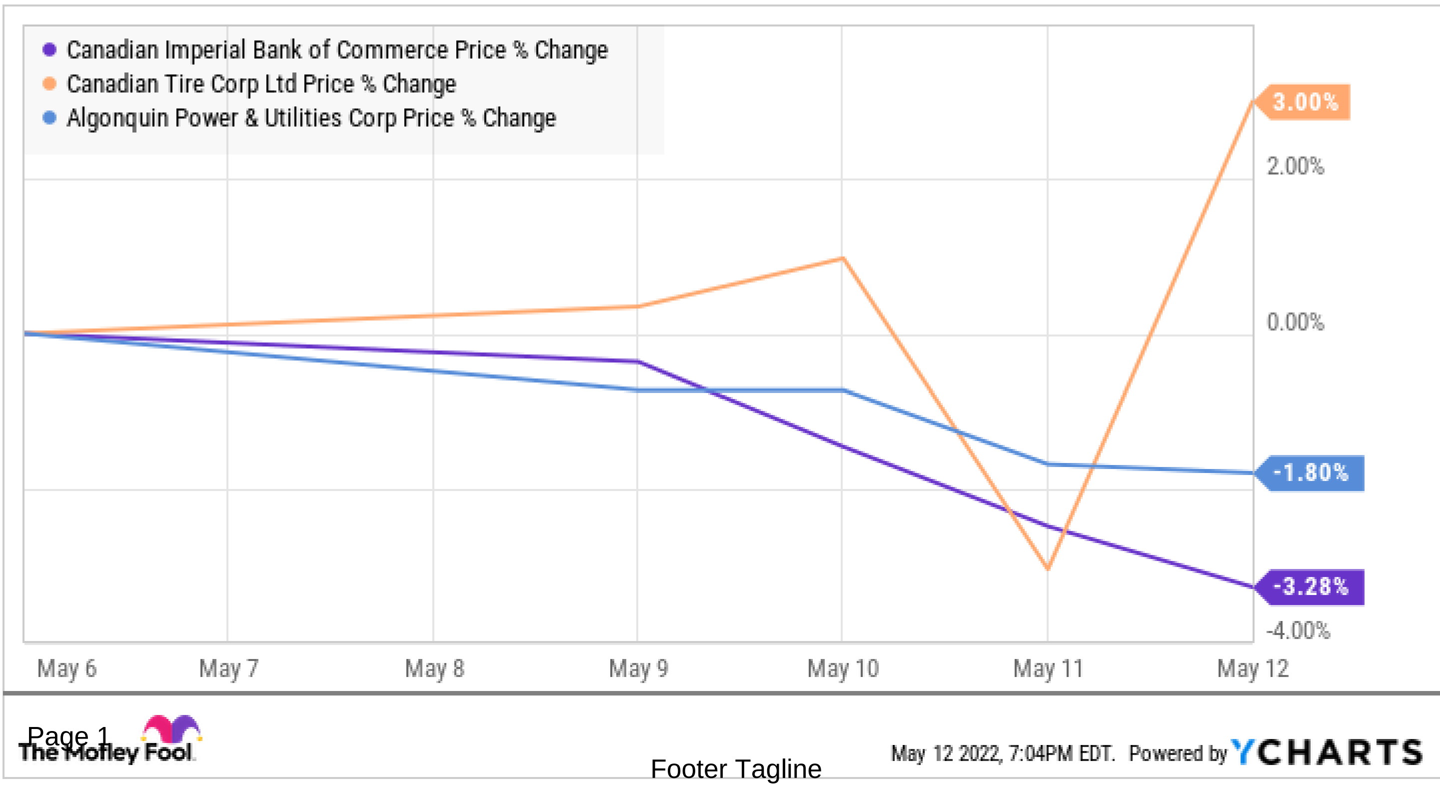
New Investors: How to Get a Pay Raise Every Year

Description

As the current stock market downturn shows, stock prices are unpredictable. Therefore, you can't reliably predict that you can make money from stock price appreciation without speculating on what stock prices may do. Another way of making money from stocks is through dividend income. New investors can increase their odds of getting a pay raise every year by investing across a diversified portfolio of carefully chosen quality dividend stocks.

For example, just last week, I wrote that three dividend stocks, **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM), **Canadian Tire** (TSX:CTC.A), and **Algonquin Power & Utilities**, are good to consider this month. In the last week, their stock prices have move up and down, as shown below. They move seemingly to the tune of news or market sentiment in the short run. So, it's quite pointless for new investors to look too closely into the short-term price movement. However, in the long run, you can expect them to move with the fundamentals of the underlying businesses. If the companies make more money on a per-share basis over time, you can expect their share prices to move higher over time.



In the graph above, Canadian Tire is the only stock that's up in this period. It turns out that the solid dividend stock raised its dividend by 25% and, consequently, popped 6% on Thursday! This is surprising news, as the company announced the dividend increase, which is for September, ahead of time. Perhaps, in this market downturn, management is trying to demonstrate the company's strength and stable financial position. The dividend increase surely did boost investor confidence, at least, in the short term.

So, how *do* you get a pay raise every year?

How new investors can get a pay raise every year

Businesses in the same industry are exposed to similar risks. When these risks play out, their earnings can be meaningfully impacted. Therefore, buying and holding a basket of diversified dividend-growth stocks increases your likelihood of getting a pay raise from dividends every year.

For instance, when the macro risks are heightened to a certain level for the Canadian economy, the regulator, the Office of the Superintendent of Financial Institutions (OSFI), would restrict the federally regulated financial institutions from increasing their dividends. So, around the time of the global financial crisis in 2007 and the COVID-19 pandemic in 2020, CIBC and its peers only maintained their dividends.

Looking at individual dividend stocks, new investors can go through the following checklist to increase their chances of getting dividend increases. First, the dividend stock should have a track record of maintaining or increasing its dividend. Of course, increasing dividends healthily is always preferred, but any stock that's able to even maintain its dividend safely is praise-worthy.

Second, the more stable the stock's earnings or cash flow is, the better. For example, utility stocks like Algonquin have pretty stable earnings to protect their dividends. Typically, the more the unpredictability of profits, the lower the payout ratio should be. This is why cyclical companies like dividend-paying industrial stocks typically have low payout ratios.

If you're not sure what is considered a healthy payout ratio of a company, observe the payout ratios of its peers. It should align with the industry payout ratio.

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2. TSX:CM (Canadian Imperial Bank of Commerce)
3. TSX:CTC.A (Canadian Tire Corporation, Limited)

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Date
2025/08/18
Date Created
2022/05/15
Author
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