Dividend Growth Investor's Instablog

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The Dividend Investment Journey **0 comments**

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Most investors have specific goals in mind they pick a certain strategy to utilize. They then get to pick strategies that could help them achieve those goals. The end result from this exercise is that too often investors end up bailing out on strategies at the worst possible times. The reason for that is that they weren't prepared for the rocky rides that would ultimately lead them to reach their goals later.

Some investors are comfortable utilizing strategies that deliver small positive results to them in a consistent manner. Dividend investing is one such strategy, where investors are frequently rewarded for holding a portfolio of the best dividend stocks, by receiving dividends. Selling covered calls is another example of a strategy where investors are rewarded frequently with small gains.

Other investors however are more comfortable to shoot for the big payout coupled with a lot of small losses. The big payout could erase any small losses previously incurred. Purchasing out of the money call or put options, which is what Nassim Taleb does, or purchasing speculative biotech stocks hoping for a positive FDA announcement are two examples of such approaches.

It is important to understand your strategy very well in order to make sure that it fits your investor profile. Dividend investing is a pretty slow and sometimes boring process of selecting companies that have raised distributions for a define set of years, provided that they are trading at attractive valuations. It involves a little bit of work when dollar cost averaging at regular intervals, rebalancing portfolio weightings and reinvesting dividends selectively. Other than that however it is nothing “exciting” to talk about in the first few years of employing this strategy. Only after a few years later however, as the stream of dividend income becomes larger and exceeds what you could be making at a part time job, does the enterprising dividend investor begin to see a material effect of employing this strategy.

In the meantime the boredom could play mind tricks on dividend investors, which are constantly bombarded with news about the stock market and the economy. Sometimes the information overload could generate intense urge for meaningless action, which would be disastrous to investment returns over time.

For example, some investors consider yields on cost of 10% as a pretty good thing. The way that most novice investors deal in attaining this goal however is by purchasing companies yielding 10% or more, without checking the fundamentals and sustainability behind this dividend payment. Back in the summer of 2008 Bank of America (BAC) was yielding over 10% on several occasions. Investors hoped that the dividend won't get cut and that a rise in the stock price would bring the yield back to normal levels. Little did they know that the company would cut dividends twice in 6 months and end up yielding less than 0.25%.

The strategy that has worked best for many dividend growth investors is to purchase stocks in strong brand names such as Procter & Gamble (PG), Johnson & Johnson (JNJ), Wal-Mart (WMT) and Pepsi Co (PEP). Such stocks have the ability to generate strong earnings growth, which then trickles back to increased dividend payments. Some investors still ignore such investments however, since they have dividend yields of 3% - 4%. What these investors fail to see is that if these companies could grow their distributions at least at a rate of 7% annually, they would end up doubling their distributions every decade. A 4% yielder with sustainable dividend payout ratio today would likely generate an 8% yield on cost after ten years.

The following dividend aristocrats are good starting positions for many dividend investors:

Johnson & Johnson (JNJ) engages in the research and development, manufacture, and sale of various products in the health care field worldwide. This dividend aristocrat has increased distributions for 47 years in a row. (analysis)

PepsiCo, Inc.(PEP) manufactures, markets, and sells various snacks, carbonated and non-carbonated beverages, and foods worldwide. This dividend aristocrat has increased distributions for 37 consecutive years. (analysis)

The Procter & Gamble Company (PG) engages in the manufacture and sale of consumer goods worldwide. The company operates in three global business units (GBUs): Beauty, Health and Well-Being, and Household Care. This dividend aristocrat has increased distributions for over 53 consecutive years. (analysis)

Wal-Mart Stores, Inc. (WMT) operates the largest chain of retail stores in various formats worldwide. This dividend aristocrat has consistently increased distributions for 35 years. (analysis)

At the end of the day, what truly matters is that you reach your financial goals, not when you started investing or how fast you were going. There truly aren't any short cuts to investing other than the fact that slow and steady always wins the race, while the hare would most likely spend most of their time catching up.

Full Disclosure: Long JNJ, PEP, PG and WMT

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