

A Primer on Dividends

When looking for income-generating investments, some investors turn to dividend-yielding stocks.

When a company makes a profit, that money can be put to two uses:

1. It can be reinvested in the business.
2. It can be paid out to the company's shareholders in the form of a dividend, a taxable disbursement typically made quarterly or monthly.

Dividend Ratios

Investors track dividend-yielding stocks by examining a pair of ratios.¹

Dividend per share measures how much cash an investor is scheduled to receive for each share of dividend-yielding stock. It is calculated by adding up the total dividends paid out over a year (not including special dividends) and dividing by the number of shares of stock that are outstanding.

Dividend yield measures how much cash an investor is scheduled to receive for each dollar invested in a dividend-yielding stock. It is calculated by dividing the dividends per share by the share price.

Other Dividend Considerations

Investing in dividend-paying stocks can create a stream of taxable income. But the fact that a company is paying dividends is only one factor to consider when choosing a stock investment.

Dividends can be stopped, increased, or decreased at any time. This is unlike interest from a corporate bond, which is normally a set amount determined and approved by a company's board of directors. If a company is experiencing financial difficulties, its board may reduce or eliminate its dividend for a period of time. If a company is outperforming expectations, it may boost its dividend or pay shareholders a special one-time payout.

When considering a dividend-yielding stock, focus first on the company's cash position. Companies with a strong cash position may be able to pay their scheduled dividend without interruption. Many mature, profitable companies are in a position to offer regular dividends to shareholders as a way to attract investors to the stock.

Qualified dividends are taxed at a maximum rate of 20%. Ordinary dividends are taxed at the same rate as federal income taxes, or between 10% and 37%. State income taxes also may apply.²

Be cautious when considering investments that pay a high dividend. While past history cannot predict future performance, companies with established histories of consistent dividend payment may be more likely to continue that performance in the future.

In a period of low interest rates, investors who want income may want to consider all their options. Dividend-yielding stocks can generate taxable income, but like most investments, they should be carefully reviewed before you commit any dollars.

Keep in mind that the return and principal value of stock prices will fluctuate as market conditions change. And shares, when sold, may be worth more or less than their original cost.

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1. Investopedia.com, July 28, 2025
2. Investopedia.com, January 22, 2025

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