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EXPLAINS: Dividends & Distributions

Dividends and distributions play an important role in the world of investing, offering the potential for investors to receive a stable and reliable income stream.

WHAT ARE DIVIDENDS AND DISTRIBUTIONS?

Dividends are payments by a company out of its profits to investors who own shares in the company. A dividend is usually paid in the form of cash or in additional shares of the company.

Distributions are payments made by a 'Fund' like a managed fund or an exchange-traded fund (ETF) to an investor. The Fund may receive the dividend payment from the companies it is invested in, this then typically forms part of a distribution paid to investors by the Fund. A Fund distribution can include dividends, interest and foreign income for example. The Fund may also make gains or losses on investments sold. The Fund may also offer a distribution reinvestment plan, where an investor can elect to buy more units in the Fund rather than taking a cash distribution.

Both involve the distribution of income however, a dividend comes from individual companies to the shareholders, whilst a Fund itself receives dividends from companies they invest in.

WHAT ARE THE BENEFITS?

Dividends and distributions are a fundamental aspect of investing, offering investors potential benefits of a consistent income stream and investment growth.

A consistent income stream

A company's ability to pay dividends depends on its earnings. Strong and consistent earnings growth may result in higher and more sustainable dividend payments. Other factors, like the profitability of the company, cash flow, debt obligations, economic downturns and market volatility can also have an impact on dividend payments.

A Fund's ability to pay a distribution is based on the income generated in the Fund. The overall income generated by the various assets in a Fund's portfolio, including both dividend-paying and non-dividend paying companies, contributes to a Fund's distribution payments. The income may also include realised net capital gains resulting from the sale of investments by the Fund or a capital loss on the sale of assets. Market volatility and the economic landscape may also have an impact on a Fund's ability to pay a distribution.

Potential for investment growth

By understanding the types of income payments such as dividends and distributions, their benefits, and the factors that influence these payments, investors can make informed decisions to help them build and grow an investment portfolio suited to their needs. Over time, dividends and distributions, when reinvested can take advantage of compounding and help build wealth. When investors reinvest their dividends or distributions, it allows investors to accumulate more shares in a company or units in a Fund over time and potentially benefit from compounding returns.

EXAMPLES OF TYPES OF DIVIDENDS AND DISTRIBUTIONS

Cash dividend - This is the most common type of dividend. Shareholders receive a cash payment for each share of a company they own. Cash dividends are usually paid on a regular basis, such as half-yearly or annually.

Stock dividend - Instead of a cash payment, shareholders receive additional shares in a company. For example, if a company declares a 5% dividend, you would receive an additional 5 shares for every 100 shares you already own.

Special dividend - Companies may sometimes distribute a special dividend in addition to their regular dividend payment. These are often one-time payments and can result from exceptional earnings or other unique circumstances.

Cash distribution - This is profit earned by a Fund and paid to investors. A Fund will earn income from its investments, such as dividends, interest or foreign income. The Fund may also make gains or losses on investments sold.

Capital gains distribution - This is a payment by a Fund to investors, when a Fund has sold a security in its portfolio and it has been sold for more than its original price. There are short-term and long-term gains. Short-term gains include gains on securities held for one year or less, while long-term gains include gains on securities held for more than a year.

COMMON DIVIDEND AND DISTRIBUTION TERMS

Dividend Reinvestment Plan (DRP)	A dividend reinvestment plan (DRP) is the process where investors can reinvest their dividend back into the company to obtain additional shares. This allows investors to accumulate more shares over time and potentially benefit from compounding returns.
Distribution Reinvestment Plan (DRP)	A distribution reinvestment plan (DRP) is the process where investors can use their distributions to obtain additional units in the Fund. This allows investors to accumulate more units over time and potentially benefit from compounding returns.
Dividend yield	A financial ratio expressed as a percentage, that indicates the annual value of dividends an investor receives relative to its share price. To determine a dividend yield, divide the dividend amount per share by the price per share. For example: x company share price = \$100, annual dividend per share = \$2.00. $\$2.00/\$100 = 0.02$ (2%).
Declaration date	The date that a company or fund announces the next dividend or distribution payment to investors.
Ex-dividend date	The cut off date for an investor to purchase shares in a company in order to receive the next dividend payment.
Record date	The official date on which a shareholder must own shares in a company in order to receive dividend payments or units in a fund in order to receive distribution payments.
Dividend payment date	The date an investor is paid their dividend.

We scour the world for the best companies that we believe have a sustainable competitive advantage that will compound returns for our investors over the long term.

At Magellan, we believe that successful investing is about finding, and owning for the long term, companies that can generate excess returns on capital for years to come. We seek to do this by investing in highly rated quality global and infrastructure strategies, while minimising the risk of permanent capital loss.



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