A Top Canadian Dividend Stock to Start Your TFSA

Description

Young Canadian savers are trying to figure out how they can set aside some serious cash to fund their retirement. This wasn't an issue for previous generations, who have generous pensions and significant home equity to use as a safety net.

Today, defined benefit pensions are becoming rare, and new home buyers in Canada face the possibility of seeing little or no growth in the value of their property over the next 20 years.

Fortunately, young investors have one savings tool at their disposal that wasn't available to their parents or grandparents at the same age.

It's called the Tax-Free Savings Account (TFSA).

Canadian investors now have up to $52,000 in TFSA contribution room available, which is enough to start a nice self-directed retirement portfolio that can grow significantly over time.

How?

The TFSA protects all income and gains from the taxman, which means investors can take the full value of dividends and invest in new shares. This sets off a powerful compounding process that can turn a modest initial sum into a significant cash stash over the course of a few decades.

When the time comes to use the money, all of the capital gains are tax-free.

Which stocks should you buy?

The best companies have strong track records of dividend growth and tend to be market leaders in industries that have significant barriers to entry.

Let's take a look at **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) to see why it might be an interesting pick.

Wide moat

CN is the only railway company in North America that can offer its customers access to three coasts. That's a nice competitive advantage, and it is unlikely the situation will change.

Why?

The odds of new tracks being built along the same routes are pretty slim, and railway merger attempts tend to run into serious regulatory roadblocks.

CN still has to compete with trucks and other rail operators on some routes, so the company works hard to be as efficient as possible. In fact, CN often posts the best operating ratio in the industry and is widely viewed as the best-run company in the sector.

CN generates significant free cash flow and returns healthy portions to shareholders through dividend increases and share buybacks.

The yield is only 1.5%, but CN has a compound annual dividend growth rate of about 16% over the past decade.

What about returns?

A $10,000 investment in CN 20 years ago would be worth about $293,000 today with the dividends reinvested.

The bottom line

There is no guarantee CN will deliver the same returns over the next two decades, but the strategy of buying quality dividend-growth stocks and investing the dividends in new shares is a proven one.

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