How Young Investors Can Build Retirement Wealth

Description

The security of work and the generosity of company pension programs used to make saving for the gold years a relatively non-essential practice.

However, full-time jobs with a generous defined-benefit pension as part of the package are becoming increasingly rare, and many young Canadians are now forced to take retirement planning into their own hands.

The traditional approaches, such as buying an income property or a home and relying on an increase in value could still work, but high prices are making houses less affordable and the potential for a significant price drop makes that strategy less reliable than in the past.

Another option to consider involves holding top-quality dividend stocks inside a TFSA and allocating the distributions to buy additional shares.

The benefit of this strategy is that it doesn't take up much of your time and the compounding element of the process can turn small initial sums into a significant pile of cash over the period of two or three decades.

The great thing about the TFSA is that none of the distributions or capital gains that are generated are taxed. Yes, you get to keep it all!

Let's take a look at one company that might serve as a good model for identifying attractive stocks for a TFSA retirement fund.

CN

Canadian National Railway (TSX:CNR)(NYSE:CNI) serves a key role in the workings of the Canadian and U.S. economies. The company has tracks that connect to three ports and transports everything from raw materials to finished goods.

The nature of the railway industry makes it unlikely that competing tracks would ever be built alongside CN's existing routes, so the company has an advantage that is quite secure.

Nonetheless, CN makes the required investments to ensure it has the right infrastructure in place to meet growing demand. In 2019, CN is spending about $4 billion on new locomotives rail cars, technology, and network improvements.

The business consistently earns strong profits and generates healthy free cash flow. Profits make their way back to investors in the form of share buybacks and dividend increases. CN's compound annual dividend growth rate over the past 20 years is about 16%.

Long-term investors have done well with the stock. A $10,000 investment in CN two decades ago would be worth about $195,000 today with the dividends reinvested.

The bottom line

While CN might not deliver the same returns over the next 20 years, the strategy of buying top-quality dividend stocks and using the distributions to purchase new shares is a proven one for building wealth.

CN is just one of a number of **TSX Index** stocks that have helped make buy-and-hold investors rich.

CATEGORY

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