TFSA Investors: Use This Weird Trick to Really Supercharge Your Income

Description

Some impatient investors insist on more income than just regular dividends can provide.

These folks have a few different options, including venturing into the risky world of high-yield stocks, buying obscure ETFs that offer high payouts (but are difficult to understand), or even investing in odd assets like private mortgages.

There's an easier way. There's a little-known strategy that allows investors to easily increase their income from Canada's top blue-chip stocks. We're talking yields of 10%, 15%, or even close to 20%.

This strategy isn't very complex, either. Once you get the basics down pat, it's as easy as a few mouse clicks. The best part? It's allowed inside TFSAs. Let's take a closer look.

Covered calls

Covered calls are an easy trick you can use to really jump start your TFSA.

Here's how they work. You venture into the options market to buy an insurance product for a stock you already own. In exchange for agreeing to sell your shares on a certain day for a certain price, you receive a one-time payment.

It'll be easier if we look at a real-life example. Say you owned **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM), because, like me, you were attracted to the bank's growing presence in the United States, its cheap valuation, and its succulent dividend yield. The current payout is 5.7%.

As I type this, CIBC shares trade hands at $99.85 each, and the company has struggled for a few weeks now to surpass the $100 level for any sustained period of time. A stock trading sideways is the perfect choice for a covered call strategy.

The next step is to sell a CIBC call option and pocket the premium. We're going to use the September 20th $102 call, which would generate $0.80 per share in income in exchange for creating an obligation to sell the stock for $102 on September 20.

This trade has two potential outcomes. The first is CIBC shares trade under $102 each on September 20. This means an investor can keep the option premium and their shares. Or, if the stock trades above the $102 level, we're forced to sell for a slight profit, close to $3 per share. That's not a bad outcome for about 25 days. And remember, that's the worst-case scenario.

Annualized, this strategy used with CIBC shares can generate a 9.6% yield. Add in the company's generous 5.7% dividend, and we're looking at a total yield of 15.3% on an annual basis. That's some serious income.

How to do it inside a TFSA

There's really only one thing stopping someone from doing a covered call strategy inside their TFSA.

All you have to do is ask permission.

A normal TFSA account at a self-directed broker won't come with options trading privileges. Since most investors don't bother with options, it's not standard. You'll need to specifically tell your broker you want to trade options. This won't be any more difficult than filling out a short form.

The big advantage to doing this kind of trading inside your TFSA versus in a regular account is you won't have to worry about paying taxes. That alone is worth a lot.

If you pay 25% tax on your income, you'd have to earn 20% annually from a covered call strategy to net 15%.

The bottom line

If you're a retiree, this strategy should be especially interesting to you. It allows an investor to really supercharge their income in a tax-friendly way. And you can't beat the income it generates.

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