How to Make $5,000/Year in Tax-Free Dividends

Description

There's nothing like some solid dividend income to help boost your portfolio. Whether you're looking to add to your savings or need the money for some other purchase, an extra $5,000 can go a long way. I'll show you how you can make that by investing in just one dividend stock.

The safe route

If you're looking for a good dividend-payer to buy and hold for decades, a stock like **Royal Bank of Canada** (TSX:RY)(NYSE:RY) certainly stands out. It's the biggest stock on the **TSX** and it provides a lot of stability. The bank has routinely increased its dividend payments over the years and there's a lot of incentive for holding onto the stock for decades.

As long as the economy doesn't do a complete nosedive, investors should expect to see RBC continue to chug along and produce solid results. And even if there are tough times ahead, it'll be a good bet to recover and come out strong afterwards. Overall, there are plenty of reasons to like RBC as a long-term investment.

In terms of using it to achieve $5,000 in dividend income, however, that's another story. Currently, it's yielding around 3.9%, and that's with the markets being down on bank stocks this year. Normally, the dividend rate isn't that high. But even at 3.9%, you would need to invest about $128,000 in order to generate $5,000 in dividends each year.

That's a hefty amount, and even if you and your significant other maxed out both your TFSAs you'd still fall short of putting the entire investment in the accounts, meaning that some of that investment would inevitably be exposed to taxation, albeit not a whole lot.

Looking outside of bank stocks

One alternative to bank stocks is investing in food stocks. Restaurants never go out of style, and while people may cut back during a recession, there's generally still a lot of people that will go out to eat.

That's where a stock like **Boston Pizza Royalties Income Fund** (TSX:BPF.UN) becomes an attractive option. Investors are likely familiar with the restaurant brands, and while it's not nearly as safe an investment as RBC, it's not high risk either.

The fund is pretty consistent in generating revenues, with sales normally above $40 million a year. As more restaurants get added to the pool, there's room for the fund to grow. However, the reason investors will like the stock is that it pays a very significant dividend yield of 8% per year.

To generate $5,000 in dividends, it would require an investment of about $62,500, which would be just under the cumulative limit for a single TFSA – $63,500.

Should investors be concerned about the yield?

With a yield this high, there will always be questions about whether the company can maintain such a high payout. But as long as the fund continues producing strong results, it shouldn't be a big issue. That's because the fund isn't going to have need for capital expenditures and can distribute all of its cash flow as dividends. In each of the past four periods, cash flows from operations have been sufficient to handle the stock's dividend payments.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. TSX:BPF.UN (Boston Pizza Royalties Income Fund)
3. TSX:RY (Royal Bank of Canada)

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