Retirement Wealth: How to Turn a $20,000 TFSA into $226,000

Description

Canadian investors are working hard to save enough money to live comfortably in retirement.

In the past, most people could rely on a generous company pension, as well as CPP and OAS payments, to cover the bulk of their retirement costs. Today, however, the way people work is changing, and that requires more planning for the future.

What's up?

The rise of the gig economy has created new and creative jobs, giving people the flexibility to work from home or during hours that are compatible with their lifestyles. The freedom is great, but there is a downside; most contract work doesn't come with pension or health benefits.

Canadians also change jobs and careers more often than in previous decades, with stints as business owners or contract workers often mixed in with blocks of traditional full-time work. Again, the freedom to do what we love is great, but the impact on pension income can be negative.

As a result, most Canadians are using their RRSPs and TFSAs to put aside extra funds to ensure they have enough cash in the golden years.

The TFSA, in particular, is becoming more popular as a retirement-planning tool, now that the contribution space is getting to the point where people can build a substantial investment fund.

The attraction of the TFSA is that all earnings are not only tax-free when generated inside the fund, they are also not taxed when cashed out and spent. This is different from RRSP withdrawals, which are subject to income tax.

One way to take advantage of the tax-free status of the TFSA is to buy dividend stocks and invest the distributions in new shares. This sets off a compounding process that can grow the portfolio significantly over an extended timeframe.

Let’s take a look at two top TSX index stocks to see how the process works.

TD

Toronto Dominion Bank (TSX:TD)(NYSE:TD) is a leader in the Canadian banking sector with operations providing loans, investment products, insurance, and advice to people and companies across the country. TD is also a major player in the U.S., where it now has more branches than in Canada.

TD is broadly viewed as the safest pick among the Canadian banks due to its heavy focus on retail banking. The company is very profitable and has a great track record of dividend growth. The current payout provides a yield of 3.9%.

A $10,000 investment in TD just 20 years ago would be worth about $88,000 today with the dividends reinvested.

Fortis

Fortis (TSX:FTS)(NYSE:FTS) is a Canadian utility company with $52 billion in assets located in Canada, the U.S., and the Caribbean.

The company has grown significantly through strategic acquisitions and organic projects. Large deals south of the border in recent years provided better balance to the revenue stream and diversified the company’s geographic exposure.

Fortis is currently working through a five-year $18.3 billion capital program that should drive cash flow growth and support ongoing dividend hikes of 6% per year. The board has raised the payout annually for more than four decades and the existing distribution provides a yield of 3.5%.

A $10,000 investment in Fortis 20 years ago would be worth $138,000 today with the dividends reinvested.

The bottom line

A $20,000 portfolio split between the two stocks two decades ago would be worth $226,000 today with the dividends reinvested.

While TD and Fortis should continue to be solid buy-and-hold picks for dividend investors, a balanced portfolio is always recommended and the TSX index is home to many top stocks that have generated similar returns.

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aswalker