Investors: Turn a $10,000 Initial Investment Into $1,000/Month. Here's How!

Description

Passive income is a wonderful thing, but many investors balk at how long it takes to really get the snowball rolling. It can take the better part of a decade to go from $0 to $1,000 per month in dividend income by doing it the old fashioned way.

At a 5% yield, you'd need a nest egg of $240,000 to generate $12,000 per year in passive income.

The good news is that if you're willing to take some risks and borrow some significant sums of money, you can really supercharge the process. In fact, it's possible to turn just $10,000 of your own capital into a serious passive income stream today.

Let's take a closer look at how even an average Canadian investor can make this a reality.

Leverage – a double-edged sword

The process of turning a small amount of money into a large investing sum is relatively simple. First you borrow and then you borrow again.

Step one is to borrow against your house. Doing so will get you advantageous interest rates and if you use a home equity line of credit (HELOC), you'll also get flexible repayment terms.

Borrowing against your house is easiest if you don't owe anything against it, of course. Most people looking to implement this strategy will already have a mortgage, which means most lenders will only consider a total loan-to-value ratio of up to 80% of your property. That would include the original mortgage and the HELOC.

Folks with significant equity in their homes living in Toronto or Vancouver shouldn't have much problem securing this type of loan, assuming they have good credit.

The next step is to leverage this loan into a margin loan. You'd take $100,000 of original capital ($90,000 borrowed and the original $10,000 as a down payment) and then borrow an additional

$50,000 to up your total investible assets to $150,000.

Although we could use the $100,000 to borrow as much as $233,333 more (since the TSX only requires 30% margin on most blue-chip stocks), the last thing an investor wants in this situation is the dreaded margin call, which forces a sale at the worst possible time.

One note of caution before we go any further. Adding debt to your portfolio carries additional risk. If the stocks you pick go down, you could lose much more than you contributed. Yes, real estate investors commonly use large amounts of leverage, but that doesn't mean folks who use debt to buy stocks will see the same kind of success.

Choosing safe dividend payers

You'll need to find an 8% dividend to turn $150,000 into $1,000 per month in passive income.

One of my favourite high-yield stocks on the Toronto Stock Exchange today is **BTB REIT** (TSX:BTB.UN), a Montreal-based owner of 66 retail, office, and industrial properties in Eastern Canada, primarily in Quebec. The portfolio spans a little over 5.6 million square feet of gross leasable space and has a fair value of just under $900 million.

One thing BTB brings to the table compared to other REITs is it has a fully internalized management team. Some of its competitors are managed by outside management companies, which then charge the REIT excessive fees to do so. BTB's internal manager should mean more of its income is available for distribution, not for paying managers.

Recent results have been solid, primarily due to Quebec's hot economy. Rental income increased by close to 4% with the all-important funds from operations metric up nearly 12%. Occupancy also crept up and the fund sold a property to help bring its debt down. Investors should also note BTB's stock trades at a healthy discount to its book value; it's like getting some assets for free.

Although BTB's payout ratio on its 8.5% yield is close to 100% of funds from operations, increases in rents should be able to help bring the payout ratio lower over time. The company should also be able to increase its occupancy, which would also flow to the bottom line. In other words, the distribution should be more stable than a 100% payout ratio would suggest.

The bottom line

Borrowing to create an instant passive income stream can be an effective way to really supercharge your savings. But keep in mind some of the downfalls of the strategy, which include taking on additional risk and having to pay several thousand each year in net borrowing costs. If you're willing to accept these trade-offs, this strategy can be an effective wealth builder.

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nelsonpsmith