Here’s How You Can Make an Extra $4,000/Year in Tax-Free Income

Description

If you have savings and are looking for some recurring income, dividend stocks are a great way to achieve that. And if you also invest in a dividend stock with some good growth prospects, then you could also benefit from some strong capital appreciation, giving you multiple ways to make money from the stock.

One stock that could offer you a great mix of both is **TransAlta Renewables Inc** (TSX:RNW). Currently paying investors a dividend of 6.3%, it’s one of the higher payouts that you can find on the **TSX**.

Not only does the stock pay a good dividend, but it’s also produced some strong returns for investors, rising by more than 40% year to date. While investors wouldn’t expect to see those types of returns every year, it’s still likely to produce good returns, especially given TransAlta’s growth opportunities.

The utility provider’s focus on renewable energy makes the stock a solid long-term buy, especially as consumers’ demand for environmentally friendly sources of energy continues to rise. TransAlta has 34 renewable energy facilities, 20 of which are wind facilities.

As renewable energy becomes more mainstream, the stock could see sales grow, which in turn will lead to an even stronger share price. In the meantime, however, TransAlta could still generate some modest returns while also adding a good dividend.

Is the dividend safe?

One of the concerns investors may have about TransAlta’s stock is whether the dividend is sustainable given it’s a fairly high yield at over 6% per year. But if we look at the company’s cash flow, we see that TransAlta is actually in a very strong position.

Over the trailing 12 months, the company has generated $319 million in free cash flow. During that time, TransAlta paid out $221 million in dividends, or about 69% of its free cash.

The company has been in a good enough position that it's been able to pay down debt as well, allocating $162 million for that purpose during the same period.

And with its free cash flow growing over the years, the company's cash position could get even stronger down the road as its operations continue to grow.

The dividend could generate significant cash for your portfolio

If you were to max out your tax-free savings account (TFSA) and invest the full $63,500 into TransAlta shares, you'd be in a position to earn $4,000 per year in tax-free income.

And as the funds would be inside of a TFSA, you wouldn't have to worry about the dividends being taxable. In addition, if the stock were to achieve returns of 10% per year, that would give you another $6,350 in capital gains, which also wouldn't be taxable.

It's not hard to see how you could make more than $10,000 a year in tax-free income by investing in a high-yield stock like TransAlta.

However, it's by no means a guarantee, and there is of course the risk that the stock could incur losses as well, chipping away at the income you may have earned in stronger years.

That's why TransAlta may be more appropriate for long-term investors, as in the short term there could be a lot more volatility as the company is still growing and it may not be a safe bet to generate strong returns year in and year out.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. TSX:RNW (TransAlta Renewables)

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1. Business Insider
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djagielski