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TFSA Users: Keep the Canada Revenue Agency at Bay With Your $6,000 in New 2020 Contribution Room

Description

If you're a TFSA account holder, you'll be getting an extra $6,000 in contribution room for 2020.

That's $6,000 worth of space that you can use to invest any way you like and watch the dividends and capital gains accumulate tax-free. Although $6,000 may not seem like a lot of room, TFSA contribution space is cumulative, so you can potentially deposit much more than that. This gives you a lot of flexibility to build a tax-free income stream that the CRA won't touch.

In fact, with high-yield dividend stocks, you could build a sizable tax-free, passive-income stream using nothing but a TFSA alone. I'll be exploring how to do that in just a minute. First, let's look at how much contribution space you have to play with.

The total is now up to $69,500

Last year, the total accumulated amount of TFSA room for account holders who were 18 or older in 2009 was $63,500.

Next year's $6,000 brings the total to $69,500. That's enough contribution room to earn $2,780 a year in dividends at an average portfolio yield of 4%. Not too shabby. By simply sticking $69,500 worth of cash in your TFSA and investing it in high-yield stocks, you could earn enough in dividends to pay your annual car insurance. But that's not even the whole story.

How much can your money grow over time?

In addition to the significant income potential of a TFSA, there's also the possibility of increasing your balance through capital gains.

While $69,500 might not seem like much at first glance, it could grow significantly over time.

How much could it grow?

To answer that question, we need to look at the Rule of 72 — a simple law that approximates how long an investment will take to double at a given rate of return. The formula is 72 divided by the average annual rate of return. Going with an average return of 10%, which is about what North American markets have returned annually since 1970, it would take 7.2 years to double your money. That means if you can get a 10% return, you could turn your $69,500 into $139,000 in just slightly over seven years.

So, you don't need to go investing in ultra-high risk stocks to double your TFSA money.

Instead, you could just stick your entire $69,500 into a low-risk index ETF like **iShares S&P/TSX 60 Index Fund** (TSX:XIU) and watch it grow over time.

XIU is a perfect TFSA index fund for a number of reasons.

First, it has a fairly high dividend yield of about 2.8%, enough to provide $1,946 a year in dividends with $69,500 invested.

Second, it has built-in diversification, as it's based off the TSX 60 index — an index made up of the 60-largest TSX stocks by market cap.

Third, it has low fees, so you don't need to worry about hidden costs eating away at your return.

Finally, as Canada's most popular index ETF, it's extremely liquid and easy to sell.

By simply investing your entire TFSA in XIU, you get all the diversification you could want (apart from exposure to foreign markets), and a solid income-producing portfolio that will pay you dividends for life. It's an excellent TFSA pick by any standard.

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