TFSA Income: A High-Yield ETF Yielding 7% That Can Pay You $5,000 a Month

Description

There's no question that extremely high-yielding securities get a bad rap.

Many income investors subscribe to the "4% rule" and see 7%-yielders as risky (even dangerous) bets that could result in dividend reductions alongside capital losses.

However, there are many instances that don't require one to risk their shirt on the stocks of distressed companies to get that big income raise.

BMO to the rescue

Consider the **Bank of Montreal**'s line of covered call ETFs, which don't just allow Canadian investors the opportunity to nab an outsized and sustainable distribution, but also allows one to lower the degree of volatility and downside risk.

Of course, there is a catch!

As you may know, apart from proper portfolio diversification, there are no free lunches on Wall or Bay Street. With covered call ETFs, you're essentially capping your upside potential, not to mention that you'll also pay a slightly higher management expense ratio (MER) for the labour involved in selling call options for premium income that will be added to the dividends and distributions paid from the ETF's long positions.

As a bond proxy, however, it's tough to match BMO's covered call ETFs. So, if you're on the hunt for handsome, but safe yields, consider the **BMO High Dividend Covered Call ETF** (TSX:ZWC), a 7%-yielding basket of stocks that incorporates the covered call strategy.

As you may have guessed from the name, the ZWC holds some of the higher-yielding Canadian stocks and REITs on the **TSX Index**.

The holdings aren't just screened for high yields, though; the managers running the ETF emphasize the ownership of high-quality dividend payers with sustainable payouts and dividend growth potential.

While some of the ZWC's constituents like **Enbridge** may be under some pressure, you won't find extremely distressed companies that are at high risk of slashing their dividends within the intermediate-term.

Watch out for foreign dividend withholding taxes!

Within your TFSA, foreign withholding taxes are lost for good, so Canadians should insist on all-Canadian dividends (or distributions) and gravitate from foreign dividend payers! With the ZWC, you'll get all-Canadian dividends (and distributions.)

While there are other attractive, more geographically diversified covered call ETFs in BMO's roster, the ZWC should be considered as a top income option for a TFSA because it's 100% focused on Canadian securities.

So, investors will not be subject to foreign withholding taxes like with other ETFs that own long positions in foreign dividend payers.

Foolish takeaway

A new year means another $6,000 that you'll be able to contribute to your TFSA, bringing the grand cumulative TFSA limit to $69,500.

If your contributions have been sitting around in a "high interest" savings account, it's time for you to put it to work by transforming it into a tax-free income stream that can add $5,000 to your annual income.

The ZWC is a safe way for income investors to give themselves a big raise without increasing one's risk profile significantly. Moreover, the covered call options strategy implemented by the ETF allows one to enjoy lower the degree of volatility, but at the cost of upside potential.

There's no guarantee that the ZWC will outperform the TSX Index. Still, for those seeking low volatility and higher income, the name will allow one to meet their income needs without requiring one to chase after distressed, but high-yielding securities.

Stay hungry. Stay Foolish.

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Date
2025/08/26
Date Created
2019/12/31
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