



TFSA Investors: Why NOT to Invest \$6,000 Now

Description

When January 1 rolled around, investors got another \$6,000 of contribution room for their Tax-Free Savings Accounts (TFSAs). This is \$6,000 that you can invest for tax-free returns!

As time-elapses permits inflation to reduce the purchasing power of cash and invested capital to compound returns, some people think that it's best to be fully invested at all times. Naturally, these people would also contribute \$6,000 to their TFSAs as soon as they could.

However, it may not be the best idea to invest the \$6,000 as early as possible. What if there aren't any suitable investments right now?

Stocks you already own

Like me, you may find **Bank of Nova Scotia** ([TSX:BNS](#))([NYSE:BNS](#)) to be attractively priced, as it trades at a price-to-earnings ratio of about 10.2.

The international bank is building a top-tier local and cross-border Pacific Alliance business, growing its U.S. presence, and expanding its highly profitable Canadian franchise.

From fiscal 2017 to 2019, Scotiabank increased its Pacific Alliance countries' earnings by more than 38% to \$2.2 billion. In the same period, it increased its U.S. earnings by 41% while maintaining high returns on equity (ROE), especially at its Canadian Banking operations.

Last year, its Canadian business had an ROE of 18.8% versus its other businesses with an ROE of 13-14%.

Thanks to Scotiabank's consistent, durable, and growing profits, it has paid dividends for 186 years! Moreover, it was awarded Dividend Aristocrat status for having increased its dividend for more than five consecutive years. Currently, it provides a secure yield of close to 5% that's backed by a payout ratio of about 50%.

Despite Scotiabank's attractive valuation, prospects, and dividend, you might not invest any of your \$6,000 TFSA contribution room in the bank stock this year if your portfolio has a big allocation, say 7%, in it already.

High risk and high return stocks?

Your friend may find **Whitecap Resources** ([TSX:WCP](#)) to be [super attractive](#) because it trades at about 3.1 times this year's estimated cash flow (which is very cheap), offers high current income with a yield of 7.1%, and has about 40% upside potential over the next 12 months.

However, the stock may land outside your comfort zone due to its dependence on volatile energy prices. A five-dollar difference in the WTI price will meaningfully change its key metrics.

For example, assuming a West Texas Intermediate (WTI) oil price of US\$60 per barrel, Whitecap would generate \$680 million of funds flow and \$310 million of free funds flow as well as have a payout ratio of 75% and a net debt to funds flow ratio of 1.5 this year.

However, assuming WTI US\$55, Whitecap would generate \$602 million of funds flow (11% reduction) and \$232 million of free funds flow (25% reduction), with a payout ratio and net debt to funds flow ratio of 85% and 1.8, respectively, this year.

In summary, you'd bypass high-risk stocks, which you aren't comfortable with, even if they're cheap and can potentially deliver high returns.

Stocks you want are too expensive

There may be businesses you like whose stocks are too expensive to be purchased at the moment. In other words, their estimated returns are perceived to be too low for your standards and their downside potentials are too great for you to take risks.

You certainly wouldn't want to waste your TFSA contribution room in expensive stocks for low returns.

Investor takeaway

Your TFSA contribution room is invaluable. You should seek investments that can deliver your target returns (e.g., 12% per year) without taking on excessive risks, such as having too much capital allocated to one stock, going outside your comfort zone, or buying stocks that have substantial downside risk.

Who knows? A [market correction](#) may not be too far away — and the stocks you want may reach your buy zones sooner than you think.

CATEGORY

1. Bank Stocks
2. Dividend Stocks

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4. Investing
5. Stocks for Beginners

TICKERS GLOBAL

1. NYSE:BNS (The Bank of Nova Scotia)
2. TSX:BNS (Bank Of Nova Scotia)
3. TSX:WCP (Whitecap Resources Inc.)

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Date

2025/07/22

Date Created

2020/02/01

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