TFSA Investors: How to Turn $69,500 Into $1.5 Million and Pay Zero Taxes to the CRA

Description

The contribution limit for Tax-Free Savings Accounts (TFSAs) for 2020 stands at $6,000. This means any Canadian who turned 18 at the start of 2009 and has never invested in the TFSA can now contribute $69,500 by the end of 2020.

The TFSA was first introduced in 2009 and has been one of the most popular investment vehicles for Canadians. In fact, around 70% of Canadians have a TFSA as withdrawals from the account are tax exempt.

An investor with a 20-year horizon can create significant wealth by leveraging the benefits of the TFSA. It is never too early to allocate funds to your TFSA that can help in long-term financial planning and wealth creation.

Since the TFSA is tax exempt, this account should be used to generate maximum returns. This makes the account an ideal choice for equity investors. But how do you identify stocks that will increase investor wealth for the next 20 years?

Canadian National Railway

The safest way to create long-term wealth is to allocate the majority of funds to large-cap securities such as **Canadian National Railway** (TSX:CNR)(NYSE:CNI). This company is a critical part of the domestic economy.

With a network of 20,000 route miles across North America, it connects three coasts and carries over 300 million tons of cargo, serving a large number of exporters, farmers, importers, manufacturers, and retailers, transporting about $250 billion worth of goods annually.

The company transports intermodal, grain & fertilizers, petroleum & chemicals, forest products, metals & minerals, and automotive among others. It generates 67% of sales from Canada and the rest from the U.S.

Due to its vast network, CNR has a distinct competitive advantage, and the company continues to invest heavily in capital expenditures. In 2019, CNR spent close to $4 billion on network upgrades, additional rail cars, and locomotives.

In the fourth quarter of 2019, CNR reported sales of $3.58 billion, compared to $3.81 billion in the prior-year period. The week-long strike in November coupled with lower-than-expected freight demand impacted company sales in Q4.

However, Canadian National Railway has managed to double revenue in the last 10 years. The company has created massive wealth for investors. An investment of $69,500 in the stock 20 years back would have grown to $1.6 million after accounting for dividend reinvestments.

Last year, CNR returned 80% of net income to shareholders via dividends and share buybacks. The board of directors also approved a 7% dividend increase for 2020, which means it has a forward dividend yield of 1.83%. CNR has increased dividend payments by an annual rate of 16% in the last 20 years, and with a payout ratio of just 37%, it has enough room to keep increasing these payments.

CNR stock is trading at a forward price-to-earnings ratio of 18.4. Analysts expect the company to increase sales by 4.7% in 2020 and 6.2% in 2021. Its earnings are expected to grow 6.2% this year, 12.1% in 2021, and by an annual rate of 7.1% in the next five years.

The verdict

While an investment in Canadian National Railway 20 years back would have increased substantially, it would not be prudent to invest your entire TFSA amount in a single stock. Instead, investors need to look at companies similar to CNR that have a huge market presence, robust cash flows, and strong fundamentals.

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