How Millennials Can Retire Rich

Description

Millennials are navigating the second major economic crash in their young professional lives.

The Great Recession made it tough for new grads to secure solid full-time work. Once the economy got back on track and they built up some savings, young people started to feel better about their long-term prospects.

Now, the pandemic lockdown is creating a new recession, and young people are wondering if they will ever be able to retire. The situations appears bleak, but there might be a silver lining in the current crisis.

TFSA pension fund

Young investors have a unique opportunity to build a retirement portfolio.

The TFSA is a useful vehicle for millennial savers. Funds invested inside the TFSA can grow tax-free and if you decide to remove the money to cover an emergency the CRA doesn't take a slice of the profits. This isn't the case with RRSPs. A withholding tax is applied on RRSP funds removed before retirement.

Power of compounding

The secret to building long-term wealth lies in the power of compounding.

How does it work?

Contributions invested in quality dividend stocks generate distributions that are then used to buy new shares. This sets off a snowball effect. Each new dividend buys additional shares that generate more dividends.

Many companies offer discounts on new stock purchased with dividends, and most brokerage accounts with the big banks allow you to set up the process automatically. Ideally, the TFSA pension investments are left to grow for 20-30 years. In that time, top companies tend to raise their dividends each year, and their share prices normally appreciate in value.

Let’s take a look at two stocks that have delivered great returns and should continue to be solid picks for a TFSA pension fund.

Fortis

Fortis (TSX:FTS)(NYSE:FTS) owns power generation, electric transmission, and natural gas distribution assets in Canada, the United States, and the Caribbean.

The company gets most of its revenue from regulated businesses that serve essential needs in the economy. People have to turn on the lights and heat their homes, even when there is a recession. The cash flow stream should be predictable and reliable. This is one reason Fortis holds up well when the broader market takes a hit.

Fortis raised the dividend in each of the past 46 years and intends to boost the payout by an average of 6% per year through 2024. The existing distribution provides a yield of 3.75%.

A $10,000 investment in Fortis 25 years ago would be worth about $200,000 today with the dividends reinvested.

Royal Bank

Royal Bank of Canada (TSX:RY)(NYSE:RY) is one of the top 15 banks in the world by market capitalization. The Canadian financial giant is so large that it is part of the select club of global banks deemed too big to fail.

Fortunately, Royal Bank is in solid shape, and investors shouldn’t have to worry about a bailout. The company entered the current crisis with a CET1 ratio of 12%. That means Royal Bank has a strong capital position to help it ride out the challenging months ahead.

Loan defaults are expected to rise significantly in the next year, as government aid programs taper off and deferrals on mortgage payments expire. The result will be higher loan losses, and investors should prepare for a big increase in provisions for credit losses when Royal Bank and its peers release fiscal Q2 results later this month.

That said, the sell-off in the stock to date is significant and likely covers most of the anticipated hit. The dividend should be safe and investors who buy today can pick up a 5.25% yield.

A $10,000 investment in Royal Bank 25 years ago would be worth more than $250,000 today with the dividends reinvested.

The bottom line

Fortis and Royal Bank might not generate the same returns over the next 25 years, but they still appear attractive for a dividend-focused TFSA pension fund.

The strategy of buying top dividend stocks and investing the distributions in new shares is a proven one. Over time, young investors can turn small initial investments into substantial funds for retirement.

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