TFSA Pension: How to Turn $6,000 Into $110,000 — and Pay No Tax to the CRA

Description

Canadians have traditionally relied on pension programs such as the Canada Pension Plan (CPP) and Old Age Security (OAS) to fund their expenses in retirement. These payouts can also be supported by RRSP withdrawals that can help you generate another stream of income.

However, each of these income sources is subject to tax by the Canada Revenue Agency. So, it makes sense to consider alternatives to increase your retirement income without paying additional taxes.

This is even more important for retirees who receive OAS pensions and might experience a clawback in case they earn over the minimum threshold amount each year. This is where retirees can leverage the Tax-Free Savings Account (TFSA).

Tax-Free Savings Account

Any withdrawal from the TFSA is exempt from Canada Revenue Agency taxes and the contribution limit for 2021 stands at $6,000. The maximum cumulative contribution limit in your TFSA increases to $75,500, which provides you enough room to hold a diversified portfolio of quality stocks.

You can use the TFSA to create a steady stream of recurring income that can grow each year. One popular investment strategy is to build wealth by purchasing quality dividend stocks and use the distributions to acquire additional shares. This strategy allows investors to benefit from the power of compounding where you can turn a small investment into a large pool of capital for your retirement.

Let’s take a look at one such **TSX** stock that has managed to reward long-term investors in the past and should continue to be a top bet for a TFSA pension fund.

Enbridge is one of the best dividend-paying companies

Enbridge is a diversified energy giant and one of the largest Canadian companies. If an investor would have bought $6,000 worth of Enbridge shares at the start of 1995, the investment would now be worth over $110,000 after accounting for dividend reinvestments. In case we exclude dividends, the $6,000 would still have ballooned to $60,800 in this period.

We can see that it's not advisable to ignore the power of dividends over the long-term. Since 1995, Enbridge has increased its dividends at an annual rate of 11% each year. Despite plummeting oil prices in the first half of 2020, Enbridge maintained its dividends with a payout ratio of less than 70% in Q3.

The energy heavyweight has a portfolio of cash-generating assets and continues to invest heavily in sectors such as renewable energy. Its contract-based business model has meant that Enbridge is relatively immune to volatile commodity prices, allowing it to generate predictable cash flows across business cycles.

The Foolish takeaway

Enbridge has a forward dividend yield of 8.2%, which means a $6,000 investment in the stock will help TFSA holders derive over $490 in annual dividend payments. The company expects distributable cash flow of around $4.65 per share in 2020 and expects this metric to rise at an annual rate of between 5% and 7% in the near-term.

In 2021, the DCF figure is projected between $4.7 and $5 per share. Given Enbridge's dividend growth history, strong balance sheet, and robust liquidity position, TFSA holders should look to invest in this blue-chip Canadian stock for outsized gains in 2021 and beyond.

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