Is $100,000 in Passive Income Enough?

Description

Most investors wonder about ways to *create* passive income. Some overlook an important question: *how much is enough?* Simply put, $100,000 in annual, recurring cash flow would be adequate for some investors, but negligible for others.

With that in mind, here's a closer look at all of the other factors that determine whether a stream of passive income is enough to deliver financial freedom.

Taxes

In Canada, there's a good chance that your passive income streams are taxable. That means a $100,000 annual flow could be drastically reduced after taxes. The tax rate on dividends depends on your tax bracket, but if you're in the highest tax bracket, the rate could be roughly 29%. So your after-tax passive income is reduced to just $71,000.

You could mitigate some of this liability by using your Tax-Free Savings Account (TFSA), but the cumulative contribution room in a TFSA is $75,500 if you're eligible for the program since inception in 2009. In other words, it's highly unlikely that you can generate $100,000 in passive income from your TFSA alone.

Passive income growth

While the impact of taxes is clear-cut, the impact of inflation isn't. That's why inflation is often compared to an invisible tax on your wealth. The annual inflation rate hit 3.6% in April and some experts believe it could increase further in the months ahead. That means the purchasing power of your $71,000 after-tax passive income stream is steadily being reduced.

The solution

To mitigate the impact of taxes and inflation, your passive income strategy needs two elements: a margin of safety and steady growth.

A margin of safety ensures that your passive income *exceeds* your cost of living. So if you need $80,000 every year to meet living expenses, you may want to aim for a passive income amount that is 15% to 20% higher.

To beat inflation, you may also need to aim for growth in your passive income stream. Investing in **Fortis** (TSX:FTS)(NYSE:FTS) stock could be an excellent strategy. Not only does the company offer a respectable dividend yield of 3.6%, but it also promises dividend growth every year.

Fortis's dividend has been expanding annually for the past 46 years. The management team is now aiming for annual growth of roughly 6% until 2025 at least. That means passive income from Fortis stock could outpace inflation by a hefty margin.

Put simply, $100,000 in cash flow generated from Fortis stock, held in a tax-shielded account, could provide the security most investors need.

Bottom line

Well, 100k in passive income sounds great. It's higher than the average household income and a decent living salary in most cities across Canada. However, this six-figure stream of recurring cash flow could quickly fall short when you account for taxes and inflation.

To secure your future, you need a source of cash flow that is reliably expanding. Fortis stock is a top bet.

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