How to Turn Your $81,500 TFSA Into $1,000,000

Description

The Canada Revenue Agency (CRA) has maintained the annual Tax-Free Savings Account (TFSA) annual limit to $6,000 in the last four years. However, the total contribution room has accumulated from 2009 to 2022. Only Canadians who are eligible to contribute since the TFSA's inception but haven't done so would have an available contribution room of $81,500 effective January 1, 2022.

Assuming you're one of the lucky soon-to-be TFSA users, aiming for a $1,000,000 million balance in the tax-advantaged investment account is a long shot but possible. Even if you have $81,500 to invest, building wealth takes time. Besides the capital, the investment window is a crucial element in your journey to one million.

Furthermore, whether your time frame is 20, 25, or 30 years, the rate of return on your investment will make the difference. Also, you won't be touching the principal or making withdrawals at any point during the wealth-building process.

Sample estimates

If the target is $1,000,000 in 20 years, the rate of return or dividend yield of the stock must be 13.36%. In 25 years, a yield of 10.55% should do the trick. However, if you can go the distance or 30 years — a rate of return of 8.75% is good enough. While the power of compounding is at play when you reinvest the dividends, reaching the goal depends on the tenor and yield.

Enticing but risky option

Labrador Iron Ore Royalty Corporation (TSX:LIF), or LIORC, pays a ridiculously high 16.33% dividend for the share price of $33.68. The yield is perfect, if not higher than the required 13.36% yield in 20 years. Unfortunately, the mining stock is unique, as the yield is never constant. It spikes or dip depending on market conditions. Sometimes the payout is $0.

The $2.15 billion royalty corporation, through Hollinger-Hanna Limited, has a 15.10% equity interest in

Iron Ore Company of Canada (IOC). Labrador's subsidiary collects a 7% gross overriding royalty from all iron ore products of IOC (production, sale, delivery, and shipment).

IOC is North America's leading producer and exporter of premium iron ore pellets and high-grade concentrate. Labrador's dividend yield was only 10.72% in February 2022. In Q1 2022, royalty revenue declined 17.6% to $53.7 million versus Q1 2021. Moreover, equity earnings from IOC declined 29.12% year over year to $40.4 million.

The decreased demand for iron ore by steel producers brought down iron ore prices. Data from the World Steel Association shows that global crude steel production decreased 6% over Q1 2021. Because of lower royalty revenues, LIORC suspended dividend payments in Q1 2022.

LIORC's dividend yield is enticing, but the setup makes the mining stock a risky proposition. The point here is that TFSA users should choose the income-producing assets they hold in the account carefully. Not all dividend payers, especially stocks with juicy yields, are safe investments.

Stick to quality businesses

The advice to TFSA investors is to stick to quality businesses, even if the rate of return is significantly lower. LIORC's problem is that it's entirely dependent on the operations and performance of IOC. There could be no capital gains and no dividends if the downtrend continues.

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