TFSA for Beginners: How You Can Easily Turn $10,000 Into $125,000

Description

If you are new to investing, you need to know about the Tax-Free Savings Account (TFSA). The TFSA is a registered account designed by the Canada Revenue Agency (CRA) to help Canadians build long-term savings.

TFSA 101

Here's how it works. Any cash put into the account can be invested into savings accounts, GICs, bonds, mutual funds, indexes, ETFS, or individual stocks.

Any profits earned (interest, dividends, or capital gains) over time are completely safe from any tax liability. You don't have to report your income and you don't have to pay any income tax on Canadian assets in the account. Likewise, when you withdraw your funds from the TFSA, there is no reporting or tax liability.

Don't be deceived by high-interest TFSAs promoted by the banks

Many banks will try and sell you on "high-interest" TFSAs. Generally, what this means is that the account will have a promotional high-interest rate for a short period (often noted in small print).

That high interest rate is normally between 1% and 3% (if you are lucky). The problem is, these accounts generally benefit the bank more than you. It secures funds that they can use to sell loans or other banking services.

In turn, you will basically earn a negative inflation-adjusted return. Over years, that could cost you a lot of wealth creation.

Buy a Canadian bank stock instead

You are likely much better off investing in one of those banks than buying one of their savings products. In fact, many Canadian banks have delivered steady long-term total returns to patient shareholders. **Toronto-Dominion Bank** (TSX:TD)(NYSE:TD) is an interesting blue-chip stock for beginner TFSA investors to consider.

With a market cap of $156 billion, TD Bank is one of Canada's largest banks and stocks. It is a dominant retail bank in Canada and the U.S. east coast. Its business is diversified by geography and service category. This has helped it deliver an attractive mix of stable dividend and capital returns over long periods of time.

Over the past decade, shareholders have earned a 10.9% average annual total return. Today, this TFSA stock earns a 4.15% annual dividend yield, which is an attractive tangible cash reward in the equation.

Despite its stock being down 10% this year, TD just delivered better-than-expected second-quarter results. Adjusted earnings per share came in at $2.09 per share, which was 2.5% above the market's expectations. It just added two large acquisitions in the U.S., which could provide attractive growth opportunities going forward.

How to turn $10,000 into $125,000 (or more)

Say you put $10,000 of TFSA capital to work in TD Bank stock today. Not only would you earn its attractive quarterly dividend, but chances are good that those dividends will grow annually by the mid- to high single digits.

Combine that with 5-7% average annual stock appreciation and you end up with an annual return close to its 10.9% historic rate of return. If you just buy and hold TD stock for the next 15 years, it could grow to as much as $46,500.

However, if you saved an additional $200 every month (around 5% of the average Canadian's monthly income), contributed it to your TFSA, and invested in more TD stock, your account could grow to over $127,800 in 15 years!

The Foolish bottom line

The point is, save regularly, contribute to your TFSA regularly, and invest regularly. By paying no tax, you keep *all* your income, and your TFSA portfolio can compound your capital into a small fortune over years and decades.

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