3 TFSA Mistakes Millions of Canadians Are Still Making

Description

Do you have a TFSA? If you do, you're already doing better than the two-thirds of Canadians who haven't set one up yet.

But having a TFSA is only the first step. After creating a TFSA, millions of Canadians still leave money on the table by making a few classic mistakes.

If you want to make the most of your TFSA and boost your odds of retiring rich, be sure to avoid the self-imposed mistakes outlined below.

Investing in cash

For some reason, a tonne of TFSA assets are invested in cash. This is perhaps the worst mistake you can make. You don't necessarily have to have 100% of your money in stocks, but there are certainly better options than cash.

For example, several short-term bond funds are delivering annual income streams of around 3%. Because these funds only invest in short duration bonds, they're largely insulated from swings in interest rates. Plus, because they're stashed in a TFSA, they're completely protected from taxes.

If you have a multi-year time horizon, your best bet is still to invest in a diversified portfolio, complete with a sizable equity allocation. But if you have near-term needs or just want to remain conservative, choose low-risk bond funds instead of cash. After all, even a 3% interest rate is better than a 2% interest rate.

Not catching up

Few Canadians are able to meet their annual maximum contribution limit, which this year is set at $6,000. Even fewer Canadians ever meet their *cumulative* contribution maximum.

If you put $6,000 into your TFSA this year, that’s incredible, but you should know that you likely have even more room to invest. That’s because any unused contribution room from previous years *rolls forward*. This is a huge lesson to learn: you can’t lose your TFSA contribution room!

In total, you’re allowed to contribute $63,500 to your TFSA. That’s the sum of every year’s contribution limit since the TFSA was created. If you ever withdrew money from a TFSA, that also opens additional contribution space. Work hard to meet your annual contribution max, but never forget that your real maximum is much higher.

Mixing priorities

A TFSA is technically a “savings account,” but you can invest in anything you’d like. Due to its tax-free status, many investors are urged to invest in dividend stocks. These stocks pay monthly or quarterly cash to shareholders simply for owning the stock. Often, you can earn a 3%, 5%, or even a 7% dividend every year.

Owning dividend stocks certainly isn’t a poor choice, but it often prevents you from owning high-growth companies. These companies prefer to keep the cash for themselves in order to reinvest it back into the business at an attractive rate. The capital gains you can earn from these stocks can often outpace the income that dividend stocks produce.

It doesn’t matter if you make your money with dividends or capital gains: both are tax free. If you have a long-term time horizon, don’t be persuaded into dividend stocks purely for the tax benefits. Stocks that don’t pay dividends have just as much upside, if not more, and are similarly protected from taxes.

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