RRSP 101: How to Turn $20,000 Into a $250,000 Pension Fund

Description

Canadian savers are getting ready for RRSP season.

The Registered Retirement Savings Plan is a useful tool for investors to set aside funds to help cover living expenses in their golden years. Not everyone has a company pension, and relying on CPP and OAS just doesn't cut it for many people.

The RRSP is particularly attractive for those who find themselves in the higher tax brackets. Contributions can be used to reduce taxable income, which effectively offsets the current net cost of making the investments. Income tax is paid on the funds when they are withdrawn, but planning can be done to ideally make sure this is at a lower tax rate.

Investments inside the RRSP grow tax-free. This means the full value of interest, dividends, or capital gains can be reinvested to expand the portfolio.

One popular RRSP investment strategy involves buying quality dividend stocks and using the distributions to acquire more shares. The compounding process can turn small initial investments into a large retirement fund over time.

Let's take a look at one stock that might be an interesting pick to get the RRSP snowball rolling.

Enbridge

Enbridge (TSX:ENB)(NYSE:ENB) is a giant in the North American energy infrastructure sector, with oil, gas liquids, and natural gas pipelines that transport a significant amount of production in Canada and the United States. The company also owns natural gas distribution businesses that supply homes and commercial clients with the fuel needed to keep buildings warm.

Finally, Enbridge is investing in renewable energy power assets, including wind, solar, hydroelectric, and geothermal facilities.

Growth comes from a combination of acquisitions and internal developments. For example, Enbridge spent $37 billion in 2017 to buy Spectra Energy in a deal that added key natural gas assets to complement the liquids pipeline business.

On the project side, the company will continue to work on its current $11 billion capital program. Additional opportunities should emerge across the asset base in the coming years.

Enbridge is pushing to change the revenue model on its Mainline pipeline network that carries 2.9 million barrels of oil per day from Canada to the United States. Under the new system, 90% of the capacity would be booked on long-term contracts, as opposed to the existing process where energy companies send in monthly bids to ship their production. Oil producers are complaining, but the transition should be a plus for Enbridge's investors.

The board just raised the dividend by nearly 10% for 2020, and ongoing increases should be in line with anticipated 5% to 7% growth in distributable cash flow. Investors who buy today can pick up a yield of 6.25%.

The stock has enjoyed a nice run since late August, rising from $43 to $52 per share. This is still well below the $65 it hit in 2015, so solid upside potential remains.

Long-term investors have done well with Enbridge. A $20,000 investment in the stock 20 years ago would be worth $250,000 today with the dividends reinvested.

The bottom line

Enbridge offers an above-average dividend yield and should continue to be a solid RRSP pick for a balanced buy-and-hold retirement fund.

The TSX Index is home to many top stocks that have generated similar returns. The strategy of owning high-quality dividend payers and investing the distributions in new shares is a proven one.

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