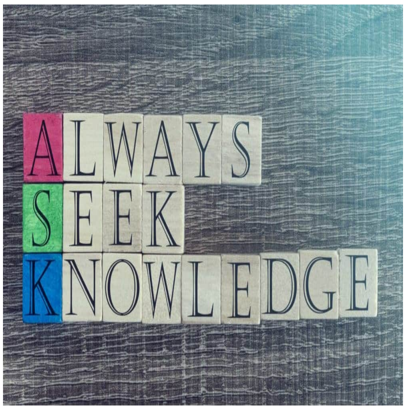

Retirees: How to Earn an Extra $336 Per Month and Avoid OAS Clawbacks by the Canada Revenue Agency

Description

Canadian retirees are searching for ways to squeeze extra income out of their savings while protecting their Old Age Security (OAS) pensions.

The CRA imposes a pension recovery tax of 15% on every dollar of net world income that is earned above a set threshold for each tax year. In 2020, the minimum income level is $79,054. The maximum level, where all of the OAS payments would be clawed back, is $128,137.

Now, you might think that $79,054 is a high income for a retiree, but hitting that amount is quite easy for someone who collects a decent work pension, CPP, and OAS. These are all taxable income streams and are added to the net world income calculation.

In addition, retirees pull funds from RRSPs or receive payments from an RRIF. Finally, some people have other taxable investment income that would add to the pot.

One way to generate additional cash flow while protecting OAS is to earn it inside a TFSA.

The TFSA contribution limit increased by $6,000 in 2020, bringing the total cumulative space to $69,500. This would give a retired couple as much as $139,000 in investment capacity that could generate tax-free income.

Where should you invest the funds?

Let’s take a look at two Canadian dividend stocks that might be interesting TFSA picks today.

Enbridge

Enbridge (TSX:ENB)(NYSE:ENB) plays a critical role in the oil and gas industry as a major transporter of the commodities. Enbridge also owns natural gas distribution businesses that supply the fuel to companies and homes. Renewable energy assets, which include solar, wind, and geothermal operations round out the portfolio.

Enbridge gets the majority of its revenue from regulated businesses. This means the cash flow should be predictable and reliable over a long period of time. That's an important feature for income investors who are seeking out top dividend stocks that have solid track records of dividend growth.

Enbridge raised the payout by nearly 10% for 2020, and investors should see annual hikes over the medium term in the range of 5-7%, based on the company's anticipated growth in distributable free cash flow.

The current dividend provides a yield of 6.3%.

CIBC

Canadian Imperial Bank of Commerce (TSX:CM)(NYSE:CM) often sits in the shadows of its larger peers, and many investors simply skip the stock when evaluating financial companies for a new investment.

The knock against CIBC is that it has a history of making bad decisions that have cost the company and its shareholders dearly. For example, CIBC had to write down roughly $10 billion in bad subprime mortgage bets during the Great Recession. A few years earlier, it agreed to pay US$2.4 billion to settle a lawsuit related to its relationship with Enron.

Today, the main concern is exposure to the Canadian housing market. CIBC has a large residential mortgage portfolio relative to its size, and that could pose a problem in the event the housing market crashes.

The concern is evident in the share price, as CIBC trades at just 9.6 times trailing 12-month earnings.

Why buy?

The stock appears oversold, and the dividend, which should be very safe and continues to grow, provides a robust 5.3% yield.

The bank is well capitalized, and its diversification into the United States in the past couple of years is providing more balance to the income stream. CIBC now generates about 17% of profits south of the border.

A housing meltdown is unlikely, and CIBC is capable of riding out an economic downturn.

The bottom line

A TFSA investment split between Enbridge and CIBC would provide an average dividend yield of 5.8%. That would generate $4,031 in tax-free income per year, or about $336 per month.

All of the gains can go straight into your pocket, and retirees don't have to worry about the extra income triggering a clawback on their OAS pensions.

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Date
2025/07/30
Date Created
2020/01/02
Author
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