TFSA Users: Avoid the Same Massive Mistake as 43% of Canadians

Description

If you're like most Canadians, you have a Tax-Free Savings Account (TFSA). Today, 57% of Canadians have opened a TFSA.

A recent survey done by **RBC** shows some shocking numbers: 43% of users are using the TFSA wrong. 43% of Canadians think of the TFSA as a savings account only — and not for investments.

With a name like Tax-Free Savings Account, it's not hard to see how this mistake is made. It should be called the Tax-Free Investment Account, in my opinion.

Here are a few simple reasons why using your TFSA as just a savings account should be avoided.

Inflation will overwhelm you

Inflation is the sworn enemy of your savings, so you should do everything in your power to defeat it. In 2018, inflation in Canada was 2.2%. Inflation is not high right now by any means. But do you know what's an even lower number? The interest rate you can earn on your TFSA in one of the big four banks.

Let's take RBC's TFSA savings rate as an example. If you hold cash in your TFSA in an RBC TFSA, you will only be earning a meagre 1% per year.

If you're earning 1% interest, and inflation is 2.2%, you're losing 1.2% of the real value of your savings every year you hold money in your RBC TFSA. In the short term, this doesn't mean anything. But in the long run, this can add up.

Even worse, you aren't growing your purchasing power when you need it in retirement.

Investments are where the TFSA shines

The true power of your TFSA is unleashed by holding investments inside of it. The compounding effect of saving on the interest, dividends, and capital gains of a stock investment can work wonders for your retirement fund.

Take, for example, a company such as **Enbridge** (TSX:ENB)(NYSE:ENB). With a market capitalization of $105 billion, this oil and gas pipeline and midstream services company is a Canadian blue-chip stock. Enbridge also boasts an excellent dividend-growth track record. Over the last 24 years, the company was able to sustain dividend increases at a rate of 11% CAGR. The three-year dividend CAGR outlook for 2018-2020 is 10%.

Enbridge just announced an increase of 9.8% for its dividends effective March 1, 2020, which is more fantastic news from a tremendous company. The current dividend yield is 6.15%.

TFSA investment vs. savings

If you'd invested $10,000 in Enbridge 20 years ago and reinvested the dividends, it would be worth $147,421 today. This equals an average return of 14.39%.

If you'd instead held only $10,000 in a savings account at a 1% interest rate 20 years ago, it would be worth $12,201 today. That is a massive difference of over $125,000!

Conclusion

Enbridge has strong returns that aren't guaranteed in the future. This is just an example to highlight how much of a difference investing can make versus a simple interest only account. The amount of money could be vastly different when it is time for retirement. With interest rates so low, be smart and don't just save in your TFSA; invest also.

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