Don’t Believe the 3 Myths That Say Your RRSP Isn’t a Good Way to Save for Retirement

**Description**

Questions arise during the first 60 days of each calendar year when Canadians are encouraged to top up the Registered Retirement Savings Plan (RRSP). Many say the RRSP is not a good way to save for retirement. Here are three myths that confuse many users.



## Myth one: You pay back all savings in taxes anyway

The myth is popular although not entirely accurate. Yes, you pay tax on RRSP withdrawals, but you also get a tax deduction upon contribution. If your tax rate is the same in the contribution year as in the year you withdraw, you effectively get a tax-free rate of return on your net RRSP contribution.

More so, you get an even better after-tax rate of return on your RRSP investment if your tax rate is lower in the year of withdrawal.

## Myth two: The TFSA is the better tax shelter than the RRSP

The majority of Canadians believe that it’s better to invest in a TFSA than in an RRSP because all earnings are completely tax-free. Generally, if you expect a lower tax rate in retirement, the RRSP is a better choice. Baby boomers, for example, expect lower income when the working years are over.

The TFSA is the ideal choice of those expecting a higher tax rate upon withdrawal, or a clawback trigger is imminent. However, if you’ve maxed out your TFSA contribution room and still have money to invest, the RRSP can supplement your retirement income or pension.

## Myth three: You must have huge money to invest

It’s a mistake to think that you need to make considerable investments in an RRSP. With modest but regular contributions, you benefit from the long-term compounding of your investment in your RRSP.

It’s effectively tax-free and better than non-registered investments.

Suppose you were to invest $100 every month in an RRSP for 35 years and purchase an asset that yields 5% on the average. Within the period, you can grow your money to nearly $114,000 in your RRSP. You have extra money on top of your investment income, let’s say from your TFSA.

## Blue-chip investment in your RRSP

When you’re investing in your RRSP, you should be looking for assets that can stand the test of time and offer a steady income for years. **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM), or CIBC, for example, is the highest dividend payer in the banking industry.

This fifth-largest bank in Canada by market capitalization is currently paying a 5.16% dividend. Let us assume CIBC can sustain the dividend yield and maintain a 50% payout ratio for 35 years. Your $50,000 savings would be worth $290,897.65 at the end of the investment period.

I won’t have second thoughts about investing in the prominent retail bank if my gauge is dividend history. CIBC has been a dividend payer since 1868. Such a record is remarkable — not to mention the steady dividend payouts during the 2000 and 2008 financial crises.



Credit goes to CIBC for revolutionizing Canada’s banking industry. It was the first financial institution to offer a mobile banking app. Expect the bank to introduce more digital enhancements, as it continues to expand its global reach moving forward.

## Defer tax until retirement

Individuals with high income in particular can invest in blue-chip stocks like CIBC. You can defer tax from earnings until retirement when you fall in a lower tax rate. But you can also withdraw before retirement in case there is a financial need.

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