Canadian Retirees: CPP Should Be 100% Solvent When You Retire

Description

Canadian retirees in general and baby boomers in particular, want to know if their Canada Pension Plan (CPP) money is secure and safe in the pandemic. Despite the huge pot of cash, the Canada Pension Plan Investment Board (CPPIB) is managing, will there be enough when retirees begin drawing their pensions?

The CPPIB is the fund manager of billions of dollars that come out from the paycheques of Canadians. The worry is that the government might use the funds for other purposes given the COVID-19 outbreak. CPP contributors, however, should understand the mechanics of the pension and discard the misconception.

Primary rule

The CPP contribution is kept entirely separate from government general accounts. In 1997, there was a rule created by the federal government. Pension benefits must be covered each year by the cash that comes from Canadian employers and workers.

Similarly, the level of contribution rates ensures there's extra to set aside in an investment fund. The allocation will cover the additional cost of benefits for baby boomers or those who will be retiring until about 2030 and could live for an extended period beyond that.

More important, the fund is arms' length from the federal government, namely, no party in power can dip its hands in the fund. Every three years, the chief actuary reviews the fund. The goal is that over the next 75 years, at least, there shouldn't be a shortfall.

Top investment

Some believe they can do better investing personal funds in stocks like **Canadian Natural Resources** (TSX:CNQ)(NYSE:CNQ). However, it would be difficult to match the high return of investment by the CPP. When the CPPIB invests, the fund is indexed to inflation, whereas your investment is at the mercy of how the market moves.

Nonetheless, CNQ is one of the CPPIB's top stocks, where the position size as of December 31, 2019, is $827.8 million. Everyone knows that the energy industry in Canada is in dire straits because of the coronavirus and plunging oil prices. CNQ is an oil and gas explorer and producer.

With the price dropping to $18.78 per share, as of April 3, 2020, from $39.64 (down 53.5%) on January 2, 2020, bargain hunters are catching a falling knife. Even the Mawer Canadian Equity Fund bought more shares of CNQ in the second half of 2019 to increase its position by 8.09%.

For regular investors, owning this dividend-paying energy stock is an advantage. Currently, the dividend yield is a high of 9.72%. Your $25,000 idle cash can produce $2,430 in passive income.

The CPP benefit is modest that it replaces only 30% of an average income. Hence, it makes sense not to rely on the CPP 100%. The pension serves as a base income for retirees such that it becomes important to have other income sources during retirement.

Fulfilling the mandate

The mandate of the CPPIB is crystal clear. This professionally managed investment group must optimize the return on investment and keep the risk profile low.

So far, its track record speaks for itself. Canadians today and the future generation should feel secure that the CPP would be solvent when it's time to retire.

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