Should You Take CPP Benefits Early Because of COVID-19?

Description

In the wake of COVID-19, many retirement-age Canadians are considering taking CPP early. The pandemic has sent stocks lower and closed off many other income streams that retirees depend on, such as part-time jobs. In light of this, taking CPP earlier than planned can seem wise.

However, that's not necessarily the case. The economic downturn we're dealing with is temporary in nature. Investors are already bidding up stocks in anticipation of the coming recovery. If you have investments you can live off of, then taking CPP early to cope with a temporary downturn isn't wise. Let's explore that in a little more detail.

Need for income

Retirees need income more than any other class of investors. It's the reason why financial advisors often push retirees into bond funds and dividend stocks instead of growth stocks. When you're not working, you need a steady stream of cash coming in. That's the reason programs like CPP exist in the first place. However, the earlier you take CPP, the lower your annual payments will be. That provides a strong incentive to defer taking benefits.

Now, if you're retired, you may object to the fact that you have literally zero income coming in. That may be the case. However, if you have some savings, you can generate tax-free income by holding dividend stocks or bonds in a TFSA. Dividend stocks generate significant sums of cash income every quarter, and those dividends are tax sheltered inside a TFSA.

Consider **Fortis**, for example. Fortis is a Canadian dividend stock that yields 3.5%. "Yield" means the percentage of a stock's value that's paid out in dividends. So, with a $1,000,000 position in Fortis, you'll earn about $35,000 a year in dividends.

Of course, you can't fit a $1,000,000 position into a TFSA. The maximum amount you can contribute to one is $69,500. However, you could spread positions in Fortis out across taxable and tax-free accounts and earn $35,000 a year, with a portion of it being tax-free.

That's not to say that you should hold your entire portfolio in a stock like Fortis. As a retiree, you should be diversified across several stocks, bonds, and fixed incomes. However, the above example illustrates how much income it's possible to generate with a portfolio yielding 3.5%.

Survivor benefits

Another factor to keep in mind when taking CPP early is survivor benefits. If you or your spouse dies, the surviving partner gets a certain amount of benefits from the deceased's CPP.

If you're both getting maximum CPP, then it's just a one-time $2,500 cash transfer. If one partner gets max CPP and the other gets none, then the survivor can get up to 60% of their partner's CPP for life. If both partners are getting CPP but not the maximum amount, then the survivor gets additional benefits that "top up" their current CPP.

Basically, for most Canadian households, there is less CPP coming in when one partner dies. That can be offset to an extent by waiting longer to take CPP. The greater your CPP payments are, the higher the amount your surviving spouse can get. That's another reason to buy investments rather than take CPP early, if possible.

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