Canada Revenue Agency: Where Should You Invest Your 2020 Tax Return?

Description

If you're one of many Canadians who were fortunate enough to get a tax return from the Canada Revenue Agency this year, you're probably contemplating whether you should splurge with it, save it, or invest it.

I'm going to focus on the latter two options: saving versus investing. If you already have an emergency fund in place and aren't at risk of exhausting your liquidity reserves should you lose your employment should a second wave of coronavirus crisis cases hit the economy again, then it makes a tonne of sense to invest your return in high-quality dividend-paying stocks that can give you a lot more yield than those savings accounts that now offer absolutely abysmal interest rates.

A predictable dividend stock that's better than savings

You don't need to settle for nearly negligible interest, but you will need a long-term time horizon and a stomach for a bit of volatility, as you look to some of the promising defensive dividend stocks out there. Consider **Hydro One** (TSX:H) as a bond alternative at today's levels. The stock has a ridiculously low beta, which means shares have a lower correlation to the broader markets. Hydro One has a highly regulated operating cash flow stream, making the stock more likely to trade in its own world than trading alongside the broader market indices.

A low beta or correlation to the broader markets doesn't mean you'll be protected from downside if another market crash were to occur, though. In the world of high-return securities, there are no guarantees. But if you position your portfolio defensively, a low-beta strategy can help you dampen the inevitable bumps in the road.

Why is Hydro One a great bond proxy for new investors looking to invest their return from the Canada Revenue Agency?

It has a virtual monopoly over Ontario's transmission lines. And while such a monopolistic positioning can be to the detriment of growth due to regulatory hurdles, I think in times like these, where volatility reigns supreme, that exposure to lowly correlated defensive dividend stocks is a must, at least with a portion of your portfolio.

What you see is what you'll get from the electric utility. Hydro One sports a 3.8% dividend yield at the time of writing. And its dividend is in a position to grow at a decent annual rate, regardless of what ends up happening next to the economy or the broader markets. It certainly sounds like a better deal than savings accounts if you're sitting on a sizeable tax return from the Canada Revenue Agency.

The company is remarkably resilient in the face of the COVID-19 crisis, but it's not completely immune. Delays in capital investments are to be expected in conjunction with shutdowns, but I don't see such delays interrupting Hydro One's mid-single-digit bottom-line growth trajectory. COVID-19 had a minimal impact on Hydro One's first-quarter numbers. While a modest headwind is expected to pressure the firm's top line in the slightest, management is looking to offset any pressures with cost-saving efforts.

Foolish takeaway

Given Hydro One's high degree of cash flow predictability, its stock is a great addition to the defensive portion of a portfolio as an alternative to cash. The dividend may not be remarkable, but given its predictable growth potential over the long term, it becomes more apparent that the name is a buy, especially given how unrewarding savings account interest rates have become lately.

Just make sure you've got some dry powder on the sidelines and sufficient emergency fund, though. Because, as we witnessed during the cash-crunch coronavirus crash earlier this year, there are no true risk-free, high-return alternatives for cash.

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