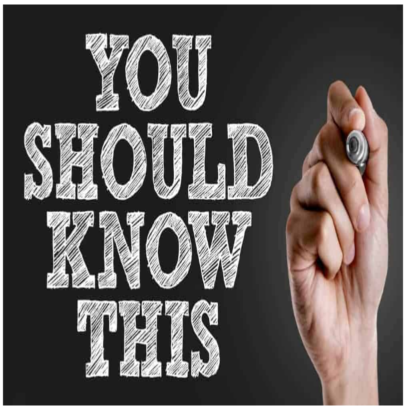

CRA: New TFSA Limit Announced!

Description

The Canada Revenue Agency (CRA) has just announced an update to the nation's most popular tax-saving scheme. The Tax-Free Savings Account (TFSA) contribution limit for 2021 has just been declared. Investors can now use this extra room to generate returns on stocks that the CRA can't touch.

Here's what you need to know about this recent update and what it could mean for your financial future.

CRA policy

The CRA has a clear mandate with regard to updating any of the investment or pension schemes offered to Canadians. For instance, the Registered Retirement Savings Plan (RRSP) and the Canada Pension Plan (CPP) contribution limits were just updated based on a mandated formula that takes wage growth and inflation into account.

Similarly, the TFSA is updated based on how much money the average Canadian is making and how much the government can afford to offer in tax incentives for investors. With this in mind, the CRA publishes an "indexation factor" every year to adjust the TFSA contribution room. This is the amount the room *should increase* to keep up with inflation.

However, the actual limit is rounded up to the nearest $500. This is done so that the dollar amount is easy to remember for everyone. For instance, the TFSA contribution limit was $6,000 this year, $5,500 in 2018 and $5,000 in 2012.

TFSA limit 2021

The CRA's indexation increase for 2021 is 1.0%. That increase is too tiny to allow the CRA to bump up the total figure. So, the TFSA contribution room for 2021 is $6,000 – the same as 2020 and 2019.

While the amount is unchanged, it's still highly consequential. This bump means that a taxpayer who has been maximizing-out her TFSA since it was introduced in 2009 and intends to max it out again in

2021 will accumulate $75,500 in total TFSA savings. That's enough for a downpayment on a house anywhere in the country.

Of course, investing that amount in the Canadian stock market would significantly accelerate wealth creation.

Where to invest your TFSA

It's perfectly reasonable to invest your TFSA in a safe index fund that tracks the total market. These index funds can deliver between 4% to 6% a year in annual returns. Similarly, a robust dividend stock in the telecom or energy sector could also deliver 6% to 8% annual returns.

But I prefer to focus my TFSA investments in reliable growth stocks. Growth stocks like **Constellation Software** (TSX:CSU) have delivered returns that far outweigh the stock market index or high-yield dividend stocks

A $1,000 investment in Constellation Software in December, 2010, would be worth $34,000 today. That's a compounded annual return of 42.3%. Imagine compounding a maxed-out TFSA ($75,500) over 10 years at that rate!

There's a good chance that Constellation can deliver similar returns over the next ten years. The business model is based on growth via acquisitions and there's an infinite supply of small software companies to acquire. Meanwhile, more than half of Constellation's software subscribers are government entities spread across the world.

This means Constellation is a low-risk, high growth stock that is ideal for your next batch of TFSA contributions in 2021. Keep an eye on it.

CATEGORY

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vraisinghani