Warning: Most Canadians Are Using the TFSA Incorrectly

Description

The average Canadian saver is making a big mistake with their Tax-Free Savings Account (TFSA). They're leaving the account in cash. Here's why that's such a bad idea and what savers should be doing instead.

TFSA awareness

The TFSA is a wildly popular and remarkably effective program. According to a survey conducted by Pollara Strategic Insights, 53% of Canadians deployed some cash in their TFSA this year. Last year, the rate was 58%.

However, less than half of TFSA users said they knew the account could be used for investments besides cash. In fact, 38% of the total national TFSA amount is held in cash. That's a mistake for two reasons: taxes and interest rates.

Interest rates have been low since the financial crisis erupted more than a decade ago. This year, rates plunged to historic lows. Even the best high-interest savings accounts only offer 1.5% to 2%. That rate is simply too low to help you generate wealth over time.

Another reason keeping cash in the TFSA is a mistake is the lack of tax benefits. Any return earned in the TFSA is tax-free. This means your 2% interest payment is completely shielded from the Canada Revenue Agency. However, you could be earning much higher returns with the same tax benefits.

By leaving cash in the account, you miss out on the TFSA's true potential.

Better alternatives

Rather than considering the TFSA a savings account, consider it an investment vehicle. Deploy the majority of your cash in investment opportunities that offer you either passive income or the potential for capital gains.

A robust dividend stock like **Telus Corporation** (TSX:T)(NYSE:TU) could be an example of the former. Telus offers a stunning 4.8% dividend yield. That's already twice as high as any high-interest savings account. Meanwhile, the business of selling wireless data and phone services is as robust and essential as any other utility now.

Telus stock price has tripled in the past decade, which makes this a dividend-growth stock — the perfect fit for any TFSA.

However, if you're looking for capital gains and don't need tax-free passive income right away, **Kinaxis** (TSX:KXS) is a better option. Kinaxis stock is up 1,221% since it listed in 2014. That means a $6,000 investment in the stock six years ago would be worth $132,100 by now. Bear in mind, that's *completely tax-free.*

There's still plenty of room for the company to grow further. Kinaxis offers supply-chain management software, which will be essential as global trade rebounds in 2021. If you're looking to accumulate immense wealth in your TFSA, this one should be on your radar.

Bottom line

Keeping cash in your TFSA is a tragic waste of opportunity. Canada's taxes on income and consumption are some of the highest in the world. The TFSA offers a tax shield for savings and investments. Deploying this tax-protected cash into a robust growth stock like Kinaxis should be the obvious choice.

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