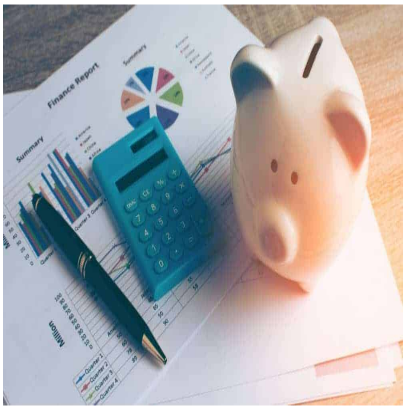

RRSP Investors: 2 Top TSX Stocks to Own for Decades

Description

RRSP investors just made their final contributions for the 2020 tax year. Now, it's time to decide which stocks deserve to be on the RRSP buy list.

RRSP investing strategy

Investors want RRSP investments to grow at a steady pace for 20-30 years. A popular and proven strategy for building RRSP wealth involves buying top dividend stocks and using the distributions to acquire additional shares. This triggers a compounding effect that acts like a snowball slowly rolling down a mountain. The process takes time but can deliver fantastic gains.

Sitting on stock positions through market volatility takes discipline. Dips provide opportunities, rather than reasons to panic and sell. We saw this last year as well as after the financial crisis. Investors should consider adding to quality positions when markets get oversold. Pullbacks also enable the dividends to buy more shares.

Dividends and capital gains accrue tax-free inside the RRSP. Investors pay tax when the funds are withdrawn. Ideally, this is at a lower marginal tax bracket than when the investor makes the original contribution.

Let's take a look at two top **TSX** stocks that might be interesting RRSP picks right now.

Why Royal Bank is a good RRSP stock

Royal Bank (TSX:RY)(NYSE:RY) just reported strong fiscal Q1 2021 results. Net income came in at $3.85 billion for the three months and return on equity is a solid 18.6%.

The bank navigated the worst of the pandemic in good shape and is now poised to benefit from the economic recovery.

Low interest rates continue to fuel strong housing demand. That bodes well for Royal Bank's mortgage business. Equity markets now trade near record highs and investor activity has increased with a wave of young people getting involved in stock trading over the past year. These situations support growth in the wealth management and capital markets divisions.

Royal Bank's CET1 ratio is 12.5%. This means it has excess capital built up to protect against significant losses. The worst-case pandemic scenario has not materialized due to extensive government support. As a result, investors could see a large dividend hike and share buybacks as soon as Royal Bank and its peers get the green light to deploy the surplus funds.

Long-term Royal Bank shareholders have enjoyed fantastic returns. A $10,000 RRSP investment in Royal Bank stock 25 years ago would be worth $320,000 today with the dividends reinvested.

Fortis stock appears cheap right now in an expensive market

Fortis trades close to $49 at the time of writing compared to the 12-month high near $59. The stock is down as investors worry that the recent surge in treasury yields could trigger an exodus from safe-haven dividend plays, including utilities.

At the same time, rising yields can be a headwind to Fortis. The company borrows money to fund part of its capital programs, so higher debt costs can put a pinch on cash available for distributions.

That said, the jump in bond yields appears premature. Inflation remains under control, and both the Bank of Canada and the U.S. Federal Reserve say they don't intend to raise rates until at least 2023.

Fortis has a $19.6 billion capital program in place that should boost the rate base from $30 billion to $40 billion through 2025. The board expects cash flow to grow enough to support average annual dividend hikes of 6% over that timeframe. This dividend growth should help offset any negative impact on the stock from rising treasury yields.

A $10,000 investment in Fortis 25 years ago would be worth about $190,000 today with the dividends reinvested.

The bottom line on RRSP investing

Royal Bank and Fortis are good examples of how RRSP investors can use the power of compounding to build retirement wealth. The stocks might not deliver the same returns over the next two decades, but they deserve to be part of a balanced RRSP portfolio.

CATEGORY

1. Bank Stocks
2. Investing

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1. Editor's Choice

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aswalker