How a $10,000 TFSA or RRSP Investment Can Become $193,000

Description

If you want to maximize your stock market investing returns over a lifetime, you have to use your TFSA (Tax-Free Savings Account) and your RRSP (Registered Retirement Savings Account).

While you can only contribute a maximum of $81,500 to the TFSA (depending on your age), all investment income (including capital gains, interest, and dividends) earned is completely sheltered from tax.

The RRSP is attractive, because you can contribute cash into the account and then defer the tax liability to a later date (likely when you retire) when you withdraw. When you contribute to the account, you get a tax credit that can be deducted against your income tax that year.

You could be giving up 10-20% of your wealth by not using the TFSA or RRSP

If you are investing completely in a non-registered investing account, you could be losing as much as 10-20% of your total investment returns by paying tax. Over a long period of time, that can cost you a significant amount of wealth.

When you utilize the TFSA and RRSP in tandem, you have a much better chance of growing your retirement wealth. Another way you can maximize retirement wealth is by picking smart investments in top TSX stocks. Here at the Motley Fool, we take a long-term approach to investing, and here's one stock to consider holding in a TFSA or RRSP for many years ahead.

Constellation Software: A perfect TFSA or RRSP stock

Constellation Software (TSX:CSU) is a wonderful stock to hold in a TFSA or RRSP. You don't want to be paying capital gains tax on a long-term compounding stock like this. Over the past 10 years, it has earned shareholders a 1,840% total return. To put this in context, a $10,000 investment in

Constellation stock in 2012 would be worth $193,670 if held until today.

The secret to its success has been its acquisitions strategy of very niche software businesses around the world. The company has a decentralized operating model, so even its various operating divisions can efficiently acquire businesses. This helps it to rapidly grow and scale, even despite its already large $41 billion market cap.

For the past five years, Constellation has grown revenues and earnings per share by a +20% compounded annual rate. The company generates a lot of recurring spare cash, which has helped it support a very strong balance sheet. It can very effectively deploy its capital (cash or debt) at very consistent high rates of return.

Constellation has accelerated its acquisition spending over the past two years. Last year, it acquired over $1.5 billion of software businesses. Given that the world may be entering a recession, it could have significant opportunities to acquire more companies at discounted valuations for elevated long-term returns.

While these investments may take some time to accrete earnings growth, Constellation is a long-term owner. It has proven its success in the past, and there are good reasons it will continue to deliver strong returns in the future. That is why it is an ideal stock to buy and hold in an TFSA or RRSP for years to come.

The Foolish takeaway

If you want a tax-advantaged wealth-creation strategy, maximize the use of your TFSA and RRSP. Combine those two investment vehicles with great TSX stocks like Constellation Software, and it is possible to build generational, life-transforming wealth for (or before) retirement.

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Date
2025/09/20
Date Created
2022/09/25
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