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RRSP CRUNCH

By Gordon Pape, Publisher and Editor

This may come as a bit of a surprise, but more Canadians say they are saving for retirement this year than in 2022.

It's a small difference: 75% of the 1,521 respondents said they are putting money aside for retirement compared to 72% a year ago. But it's significant that the percentage is up in the face of a range of headwinds that include high inflation, rising interest rates, the worst bond market in 40 years, and falling stock prices.

The poll was conducted in November by Leger on behalf of Questrade. It found that 75% of Canadians are saving for retirement in one form or another, up from 72% last year. RRSPs remain the most popular way to do this, at 42%, but Tax-Free Savings Accounts are a close second, at 40%.

Most of the people surveyed said they plan to invest about the same amount in their retirement plan as last year (67% for RRSPs, 69% for TFSAs). But almost one in five expect to invest less in RRSPs, while 16% said the same about TFSAs.

It's surprising those numbers aren't higher. It costs more to fill the gas tank, service the mortgage, keep the heat on, and put food on the table. People are being squeezed but the retirement saving commitment remains high, despite the fact that 35% of respondents said inflation has impacted their ability to save.

Where's the money going? This was a bit of a shocker. Despite the sharp drop in the markets last year, the most popular choice among RRSP investors was exchange-traded funds (ETFs). The report found that 41% planned to invest directly in stocks while 39% named mutual funds. (Respondents were allowed to select more than one option.) Conservative choices ranked at the bottom of the list with 38% naming Guaranteed Investment Certificates (GICs) and 33% preferring high interest savings accounts.

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These results suggest a deemphasis on safety that could spell trouble down the road for some retirement plans. The first rule of investing according to Warren Buffett is "Don't lose money". Even if your assets underperform the market, the fact RRSPs and TFSAs are tax-sheltered for decades can push the value of a plan into six- or even seven-figure territory.

The final take-away from the report is that 41% of retirement savers use the services of a bank financial advisor. That's not always bad but it's important to be aware that these folks are incented to push the bank's own products, which may not always be the best choice for the client.

The study found that 32% of respondents were do-it-yourself investors or used robo-advisors. That could be good or bad, depending on your knowledge level and your sources of input. Just remember Buffett's cardinal rule: "Don't lose money." A retirement plan isn't a roulette wheel. Choose securities that will almost certainly profit over time and stick with them.

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THREE STOCKS FOR YOUR RETIREMENT PLAN

By Gordon Pape

As mentioned above, the primary rule for retirement plans is to conserve assets. Whether you use an RRSP or a TFSA for your savings, it's essential to protect your principal. Growth is important, of course, but if you suffer heavy losses you may never recover them.

Consider this hypothetical example. Suppose you invest $5,000 in an RRSP this year and the plan loses 50%. By year-end, you're left with $2,500. The next year, your plan grows by 50%. You're back to breakeven, right? No. A 50% increase from $2,500 takes you up to $3,750**.** You're still down $1,250 from your original stake.

This is a simplistic way of looking at retirement savings management, but some people never seem to grasp it. Whenever you're faced with an investment decision, the first question to ask is: "What's the risk?" Once you understand that, you can proceed with the decision-making process.

This is a different approach from the one you might use investing in a non-registered account. If you lose money in that situation, you can at least claim a capital loss, which mitigates the impact. In an RRSP or TFSA, there's no such relief valve.

This is not to say that you won't experience short-term losses in a specific investment. Nothing goes up forever. But ask yourself this question: "Is this security likely to be worth more five or ten years from now than it is today?" If the answer is yes, it's a candidate for your plan. Remember, you're investing for the long term. Time is on your side.

Here are three securities to get you started. I would be astonished if they are not more expensive in five years than you'd pay now. Plus, they all offer dividends, thereby adding cash flow to your plan.

Fortis Inc. (TSX, NYSE: FTS)

Utility stocks are the perfect security for retirement plans. Most of their income is regulated, which means a steady increase in cash flow to keep up with expenses and ensure the company is viable. A failed utility is unimaginable. Consider the reaction if all the lights went out in your city because the hydro company couldn't pay its bills. It won't happen.

We have several good utilities from which to choose in this country including Hydro One, Emera, and Canadian Utilities. But I keep returning to Fortis as my number one choice because of its stability, international exposure, and its long history (approaching 50 years) of annual dividend increases.

The company is based in St. John's, Newfoundland and Labrador. It's a regulated electric and gas utility with 2021 revenue of $9.4 billion and total assets of $64 billion as of Sept. 30, 2022. It has 9,100 employees and serves customers in five Canadian provinces, nine US states and three Caribbean countries.

Fortis will release final 2022 results on Feb. 10. For

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the first nine months of the fiscal year, the company reported adjusted net earnings of $982 million ($2.06 per share) compared to $919 million ($1.96 per share) in the prior year.

At the same time, the company increased its dividend for the 49th consecutive year. Shareholders received an additional 6% for a quarterly payment of $0.565 ($2.26 a year). The shares yield 4.1% at the current price. Fortis says to expect annual dividend increases of between 4% and 6% for the next few years.

Royal Bank (TSX, NYSE: RY)

People complain about bankers being too rich. If you're one of them, do what they do. Buy the stock and let the profits roll into your retirement plan.

That's not to say that banks don't fail. The collapse of Lehman Brothers in 2008 triggered a massive stock market plunge that contributed to the depth of the Great Recession.

But Canada's banking system is very different from that of the US, UK, or almost anywhere else in the Western world. Where else would you find an oligopoly of five banks that basically control the whole system? Yes, there are some bit players, but none has any real clout.

That puts the Big Five in the "too big to fail" category. Royal tops the list with a market cap of more than $190 billion and is about to get even bigger if its bid to acquire HSBC's Canadian assets is approved.

Bank stocks didn't fare very well in 2022. The rapid rise in interest rates, falling equity and bond markets, and recession fears drove investors elsewhere. The S&P Capped Financials Index fell 12.68% for the year.

And what was Royal doing while all this was happening? Posting a profit of $15.8 billion for the year ended Oct. 31, 2022. That was down $243 million or 2% from the prior year but diluted earnings per share remained unchanged at $11.06.

Meanwhile, Royal announced two dividend increases during the year and now pays $1.32 per quarter ($5.28 per year) to yield 3.8%.

Investors have discovered banks were oversold and are buying back in. The S&P/TSX Capped Financials Index was up 9% for 2023 as of Feb. 3. But you can still buy shares in Royal Bank for less than they were a year ago at this time and receive a higher yield as well. What more could you want for your retirement plan?

CN Rail (TSX: CNR, NYSE: CNI)

Telegraph lines. Iceboxes. Kerosene lamps. Scrub boards.

What do they have in common? All were commonly used in the 19th century. Today they're museum pieces.

But here's one 19th century business that's still producing big profits: railroads. There have been many technological upgrades over time, of course, but it still comes down to an engine pulling a line of cars along a steel track. And doing so very profitably.

Renowned investor Warren Buffett likes railroads so much that be bought Burlington Northern and Santa Fe for Berkshire Hathaway. Canadian Pacific is about to assume control of Kansas City Southern. If another railroad said it would consider bids, the line-up of potential buyers would extend for blocks.

Which brings me to Canadian National Railroad. It has been a recommendation of this newsletter since May 2002 when we advised buying it at what now seems the absurdly low price of $12.98 (split-adjusted). The shares closed on Feb. 3 at $160.66 for a gain of 1,138% over that time, not including dividends.

While there are occasional dips along the way, a look at CN's stock chart shows a long, steady upward climb. So it should: this is a company that churns out growing profits year after year.

Despite all the economic headwinds, 2022 was no exception. The company reported annual revenue of $17.1 billion, up 18% from $14.5 billion the previous year. Net income was $5.1 billion ($7.44 per diluted share) compared to $4.9 billion ($6.90 per share) in 2021.

The company is not a big dividend payer in terms of

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yield. The current quarterly rate is $0.79 ($3.16 a year) for a 2% yield. But the company has a history of annual dividend hikes, so consider them a small bonus to the capital gains potential.

There you have it.

With Fortis, Royal Bank, and CN Rail as the core of your retirement savings plan, you're unlikely to go wrong.

GORDON PAPE'S UPDATES

Procter & Gamble Co. (NYSE: PG)

Type: US common stock
Current price: $142.61 (figures as of Feb. 3 in US dollars)
Originally recommended: Jan. 28/21 at $132.24
Annual payout: $3.6532
Yield: 2.6%
Risk: Lower risk
Website: www.pg.com

Comments: P&G is an industry leader in the cleaning products business as well as personal health care and grooming.

P&G has a long list of brands, including Tide, Bounce, Pampers, Downy, Bounty, Charmin, Always, Tampax, Gillette, Head & Shoulders, Herbal Essences, Old Spice, Pantene, Cascade, Febreze, Oral-B, Mr. Clean, Crest, Scope, Vicks, Ivory, and Secret.

The company recently reported second quarter 2023 financial results. Sales were down marginally (1%) from the prior year to $20.8 billion. It would have been worse, but the company implemented across-the-board price increases averaging 10% which almost offset a volume decline of 6%.

Net income attributable to shareholders for the quarter was $3.9 billion ($1.59 per diluted share). That was down from $4.2 billion ($1.66 a share) the year before.

The company reaffirmed previous guidance of earnings per share growth this year of 0-4%. It raised its revenue guidance slightly, although it is still projected to be flat to slightly down.

Action now: Hold. There's nothing much to get excited about here but the yield is acceptable and the share price is holding steady after a pull-back at the start of the year.

YOUR QUESTIONS

RRIF withdrawal

Q – Is it always better to use the younger spouse's age for a RRIF? My wife turns 71 this year, but I'm turning 67. I've been told varying things. – ***A.M.***

A – Using the age of the younger spouse means the minimum withdrawals are less, which extends the life of the RRIF. The reduced income will also lower her tax bill and allow the RRIF savings more time for tax-sheltered compounding.

If you don't need the extra money, I would certainly choose that option. It offers more flexibility, reduced tax liability, and she can always withdraw more than the minimum if needed. – ***G.P.***

HOUSEKEEPING

The following securities have been removed from our on-line recommended list. Sell advisories were published some time ago so this notice is for record-keeping purposes only.

Air Boss of America. Recommended by Gavin Graham on Jan. 26/17 @ $12.92. Sold May 27/21 @ $34.03.

Vodafone Group plc. Recommended by Gavin Graham on Sept. 19/16 @ $28.99. Sold July 29/19 @ $18.25.

Sienna Senior Living. Recommended by Gordon Pape on April 17/14 @ $11.93. Sold April 23/20 @ $12.23.

Extendicare. Recommended by Gordon Pape on Aug. 30/18 @ $8.30. Sold April 23/20 @ $6.08.