First Timer's Guide to Retirement

It might seem like just yesterday you got your first job, which means the concept of retirement is a distant and abstract idea at best. "There's plenty of time between now and then to save and plan," you might say to yourself. And while that's true, time also has a way of passing a lot faster than you think, especially the older you get.

Planning and saving for your eventual retirement is the ultimate long game. A little bit of strategy now can lead to a more winning future. And we're here to help you get there.

What is retirement?

Picture this: After getting up and going to work every day for most of your life, there comes a day where you get up and can do whatever you want—and that day is not a Saturday, Sunday, holiday, or vacation day. Retirement is a time to enjoy the efforts of your hard work and focus a little bit more on you, while leaving the workforce behind. Your passions, hobbies, family, friends, or whatever else it is you'd like to do with your time, become the focus of your days rather than your job. But only if you make, and stick to, a solid plan to get there.

In Canada, the age most often associated with retirement is 65, but that's not a mandatory requirement. Human rights laws prevent your employer from forcing you to retire once there's a certain amount of candles on your birthday cake. The age of 65 is more of a milestone marker in that it's the age you become eligible to collect pension benefits from the federal government, and possibly your employer, depending on your benefits package—but we'll get into all that a little further along.

WHAT ARE REGISTERED SAVINGS?

If you're wondering how you'll afford to buy groceries or travel once you're no longer holding down a 9–5, registered savings are a big part of that. But what exactly are registered savings?

By definition, registered savings are a savings plan that is registered with the Canada Revenue Agency (CRA) designed to help build money for retirement. Money that is put into an RRSP, along with any income it earns, grows tax free until it is withdrawn.

Tax-Free Savings Accounts (TFSAs) are also registered savings plans which, by definition, means that they are a savings plan that is registered with the Canada Revenue Agency (CRA) that allows you to hold cash or other investments (ex. GICs, mutual funds). You can only put a certain amount of money into a TFSA each year and this limit is determined annually by the government. Any money held inside of a TFSA grows tax free and the growth is never taxed, even once it's taken out.

TAX TALK

There's a lot of talk about taxes when it comes to savings. Confused? Want to learn more? Check out our Your Two Cents segment Gimme Credit: Talking Taxes to get the lowdown.

HOW MUCH DO I NEED TO RETIRE?

How much you need to retire depends on your current income, lifestyle, and expenses. The general advice is that you should aim to replace 70% to 90% of your annual pre-retirement income through savings for retirement.

For example, say you earn an average of $63,000 per year before retirement. That means you should try to budget for $44,000 to $57,000 per year in retirement. If you're curious how much you should aim for, check out our Retirement Savings Calculator.

The basics of registered savings

When it comes to retirement, there are two main types of registered savings we'll be talking about—Registered Retirement Savings Plans (RRSPs) and Tax-Free Savings Accounts (TFSAs).

WHAT IS A REGISTERED RETIREMENT SAVINGS PLAN (RRSP)?

A Registered Retirement Savings Plan (or RRSP for short) is a savings plan that is designed to help you set aside money for retirement. Money contributed into an RRSP is tax deductible and any tax on earnings generated within an RRSP is deferred until the funds are redeemed. Until redemption, earnings grow without any tax implications.

Money that goes into an RRSP can be held in a variety of ways. Eligible products that can be held in an RRSP are term deposits (aka a guaranteed investment certificate or GIC), mutual funds, stocks, bonds, and real estate.

Term Deposits

Term deposits provide a low risk, fixed rate of return and are insured, up to a certain limit, by the Canadian government or provincially in the case of a credit union. In other words, when you deposit money in a term deposit via your RRSP, you earn interest on that money. The catch? The money has to stay in there for a certain period of time (options typically range from one-to-five years).

Term deposits are considered safe investments because the financial institution who issues you the term deposit is legally obligated to return your principal (your initial investment plus earnings).

Stock

A stock is a share in the ownership of a company. If the company does well, shares increase in value (capital gain) and, in some cases, companies will also pay out a portion of their profits to their shareholders (called dividends). If the company does not perform well, the value of its shares may decrease. Unlike other forms of investments, stocks are not guaranteed. When held in an RRSP, the capital gains and/or dividends generated are not taxed until withdrawn or de-registered.

In terms of retirement savings, investing in stocks can offer high returns—but come with bigger risks. It's best to work with a licensed investment professional who can fill you in on the potential risks and rewards of playing the market.

Mutual Fund

A mutual fund combines the benefits of diversification and professional management with being affordable to the average investor. It is a professionally managed collective investment that pools money from many investors to purchase many different kinds of securities like bonds, stocks, etc. The original amount you invest is not guaranteed and, depending on the mutual fund, the potential for returns and potential risks can vary greatly from one mutual fund to another.

Want to learn more about saving and investing? Check out our First Timer's Guide to Saving and Investing.

Investing in mutual funds can offer high returns—but can come with big risks as well. A financial expert can help you understand the pros and cons of investing a portion of your retirement savings in mutual funds.

OTHER WAYS YOUR RRSP CAN BE USED

In addition to being a great place to park your money for the long haul, RRSPs can be used in a few other ways throughout your life as well.

The Homebuyers Plan

The Homebuyers Plan lets you make a one-time withdrawal of up to $25,000 to put toward buying your first home. To qualify, you need to be a Canadian citizen and a first-time homebuyer or someone that hasn't owned a home for five years. There are also some rules around the kind of home you can buy or build.

The deal is, you can withdraw money from your RRSP with no tax penalties, as long as you pay back the money in scheduled payments over a maximum 15-year period. If you're struggling to save extra money to purchase a home, but have money sitting in an RRSP, the Homebuyers Plan could be the perfect solution.

The Lifelong Learning Plan

Going back to school can be a big decision, not to mention an expensive one. If you're heading back to class full time and have been saving in an RRSP, the Lifelong Learning Plan might be a better option than taking out a loan.

Funds can be withdrawn for either the account holder or the spouse of the account holder without tax implications, provided that funds are repaid to the RRSP within the required timelines. The plan lets you withdraw $10,000 in one calendar year and up to $20,000 in total to help cover the cost of going back to school.

WHAT IS A TFSA?

A Tax-Free Savings Account (TFSA) is a registered plan that can be used to save toward your short-, medium-, or long-term goals. While the money you put into your TFSA is not tax deductible, your contributions inside of the plan grow tax free, meaning any interest or returns earned are not taxed, even when they're taken out.

When it comes to TFSAs and RRSPs, it's helpful to think about them in terms of a mixture of the two, not an either/or kind of situation. You can find more information on the difference between the two here.

OTHER LONG-TERM SAVINGS OPTIONS

RRSP Loans

An RRSP loan allows you to borrow money to contribute to your RRSP even if you are short on cash. It works like any other loan, where you borrow a lump sum of money you agree to directly deposit into your RRSP account. You then have to make principal and interest repayments regularly over a period of time—typically within a year.

Real Estate Investments

Investing in real estate can be another option when it comes to your long-term retirement savings plan. The way it works is you buy income generating properties with the plan to liquidate or sell your real estate investments just before, or once you do, retire. You could also consider hanging on to your investment properties indefinitely and use the rental income generated from those investments. This option takes careful planning and it can be costly, so it might not be for everyone, but it is another option to consider.

Your approach to retirement savings

Like most things in life, there's no one set way to save for your retirement. It's more about understanding what your options are and picking the right combination or approach for you. And when it comes to financing your retirement, there are basically three sources of income that you can draw from: government benefits, workplace/ employer benefits, and personal savings. Knowledge is power—understanding your options will mean a more secure future.

Government benefits

In Canada, there are two primary sources of government benefits designed to help support those who are of retirement age.

The Canada Pension Plan

The Canada Pension Plan (aka CPP) is a monthly, taxable benefit that you are eligible to receive when you retire. The amount you receive each month is based on a combination of your average earnings throughout your working life, your contributions to the CPP, and the age you decide to start your CPP retirement pension. How much you contribute to the CPP is based on your earnings and there is a cap on how much you can contribute each year. People who earn a higher salary may reach their contribution maximum before the calendar year is over. This means what you can expect to receive once you retire might not be based on your full income.

CPP payments are not automatic—you need to apply to receive them. To be eligible, you must be at least 60 years old and have made at least one valid contribution to the CPP over the course of your working life.

For higher earners, or for those who have more expenses, CPP alone might not be enough to sustain your lifestyle once you retire. It's important to understand the full picture and to crunch the numbers so you know what can work for you.

Old Age Security

The Old Age Security (aka OAS) pension, by comparison, is a taxable monthly payment you can receive once you're 65 and older. Depending on where you live, you might not even need to apply to receive it—Service Canada will automatically begin payments. How much you're eligible to receive each month depends on how long you've lived in Canada (or certain other countries) after the age of 18.

For those who are in a lower income bracket, you might also qualify for additional funds under the Guaranteed Income Supplement which is available to low-income recipients of the Old Age Security pension. Once you reach retirement age, it's a good idea to check out federal government programs you may qualify for.

WHAT DOES TAXABLE MEAN?

A taxable payment/benefit means you have to pay income tax on the money you receive.

Workplace benefits

If you're going to retire, you've gotta work first. And depending on where you work, your employer might offer programs or incentives to enhance your retirement income. This can be via group RRSP or a workplace pension.

Every employer is different, so it's important to understand what's available to you when you start. Some companies or organizations might offer a defined benefit pension plan—that means you pay into a company-sponsored pension plan that comes with terms and conditions when it comes to how much you'll get, and when.

Some organizations might offer an RRSP matching program—that means for every dollar you contribute to your own RRSP, you organization will match it, usually up to a certain dollar amount or per percentage. Other organizations might offer preferred interest rates or group RRSP programs that could give you a better interest rate than you might be able to access on your own. Some companies also offer bonuses, which might come with an option to transfer those funds directly into an RRSP so you can delay paying the tax until the funds are withdrawn.

Every organization is different, so it's important to speak with your manager, HR department, or to review your onboarding materials closely to understand what may be available for you to take advantage of. When it comes to retirement savings, every little bit really does add up over time to make sure you're taking advantage of programs that might be offered.

Personal savings

This guide is focused on helping you understand all the ways you can contribute to your retirement. But personal savings are only one piece of the pie, so it's important to review them in context with other programs and options that might be available to you. Don't hesitate to contact your local credit union to help you with this.

Why you should start saving now

How much you're able to put aside each month toward retirement savings depends entirely on your budget. There is no set amount or magic number you "should" save each month. That being said, a common amount to aim to save is between 5–10% of your monthly earnings. Regardless of what you are able to contribute, the best advice is to start early and make saving for retirement a habit.

One of the easiest ways to do this is to set up regular preauthorized payments from your primary bank account to your retirement savings account. This can be done with investments such as mutual funds and direct stock purchases, which can really reap benefits when sheltered in a TFSA or RRSP. If you're purchasing stocks and the company pays you a dividend, it's considered taxable income. If you're able to place that income into a TFSA or an RRSP you can avoid paying some of those taxes, which is why dividend reinvestment and capital gains can be huge!

Like any good habit, the earlier you get into it, the more likely you are to stick with it. Saving for retirement really is about the long game. So, the earlier you're able to make your money work harder for you, the better the outcome once you're ready to put your feet up.

MEET YOUR NEW BFF: COMPOUND INTEREST

Unlike other big purchases (like a car or even a home), you're going to need to save a lot for retirement. That's not meant to sound daunting—but you can realistically expect to need to save enough to live comfortably for at least 20 years, which probably isn't something you're going to be able to afford to do in a year or two. The more you're able to save now, the more that money will work for you in the future thanks to something called compound interest. Simply put, compound interest is basically earning interest on your interest.

Here's what we mean:

COMPOUND INTEREST IN ACTION

	PERSON A	PERSON B
Current age	25	25
Current income	$40,000	$40,000
Wants to retire at	60	60
Current savings	$5,000	$0
Current monthly contributions	$200	$300
Estimated rate of return	4%	4%
Projected savings at age 60	$250,200	$344,957
	Kudos to Person A for kickstarting their savings, however, their lower monthly contributions compared to Person B leave them with almost $100k less at age 60.	Person B may not have a saving nest egg but by increasing their monthly contributions by only $100 more a month compared to Person A they will have almost $100,000 more at retirement.

Want to see how much you'll need to save to retire? Check out our registered savings calculator.

This illustration is for education purposes only. Connect with your credit union expert to determine an appropriate retirement savings plan for you.

IT'S A MARATHON, NOT A SPRINT

Depending on how old you are when you both enter and exit the workforce, you could be looking at a period of upwards of 40–50 (or more) years from your first day of work to your last. That's an actual lifetime, which is why it's important to approach retirement savings like a marathon and not a sprint.

Especially when you're first starting out in your job, thinking about a work-free future might seem next to impossible to imagine. Not only that, it might feel next to impossible to pay for, too. Between paying back student loans, saving for a down payment on a house, purchasing a vehicle, and the general cost of living, it might not seem like you have a whole lot left at the end of the day to dedicate to your future self.

Here's the thing—your income will grow over time, but so will your expenses. That's where the idea of every little bit counts starts to come into play. Maybe you can only save $20/week in your first few years of your career. Over time, as you begin to grow and progress and make more money, you'll be able to contribute more to your savings, too. Plus, as outlined above, compound interest really is your BFF, so let it do some of the work for you.

Planning for anything that's 40 years in the future can be challenging, and when it comes to something as ever-changing as your financial situation, it's pretty much impossible to expect that what's working for you right now is going to work for you forever. Flexibility is key.

However, just as you might make more money the longer you progress in your career, it's reasonable to expect your expenses are going to increase, too. Cheap rent and a house full of roommates (or your old bedroom at your parents' house) won't always be appealing, so there's a mortgage payment to think about. And then don't forget property taxes, maintenance, furniture, etc. Or maybe you want to add to your family. Kiddos—of the human or fur variety—can be expensive. Whatever your long-term plan is, it's going to cost money to make it happen.

Be honest with your goals and with your budget and keep in mind that there are bound to be lots of ups and downs before it's finally time to enter your golden years.

Conclusion

Like anything, knowledge is power. Learning about retirement savings might be a bit of a snooze now, but there's nothing sleepy about being empowered to take on your future.

Your money can work harder for you—it's just about knowing how to make that happen.

And remember, when in doubt, your local credit union is here to help.