Invest for success

I finally have a bit of money left over at the end of the month and I'd like to invest in an RRSP, but I just don't know where to begin. What is the best way to get started?

When a client starts a registered retirement savings plan (RRSP), I make sure that she understands one key concept: an RRSP is not an investment in itself. Rather, it's a tax shelter where you can hold investments such as stocks, bonds, mutual funds and even savings accounts. Therefore, you never have to rush an investment decision; if you are unsure, contribute cash now and invest it later. You will not pay tax on the money you contribute, and if you later withdraw it when your income is lower (because you are returning to school or are unemployed for an extended period of time, for example), you'll be taxed at a lower rate. In the meantime, the slice that the taxman would otherwise claim each year will continue to earn investment returns – all for you!

Financial expert Lori Bamber has spent more than 16 years helping Canadians take care of their money

Step 1: build a solid foundation

Begin by accumulating the equivalent of six months' worth of living expenses in the RRSP version of a high-interest savings account (currently paying interest in the range of two per cent or more). The returns may be ho-hum, but those funds will always be there for you if your employment income is suddenly interrupted.

Check last year's Canada Revenue Agency tax assessment to find out your maximum allowable contribution, then set up an automated plan that transfers money from your chequing account on a monthly basis (you won't even miss the money, I promise). Many employers offer automatic-withdrawal RRSP programs that not only match employee contributions but also provide access to top money managers at a fraction of the cost that retail investors pay.

Step 2: be a couch potato

Once you've accumulated that comfortable cash cushion, it's time to broaden your investment scope. The most effective way to reduce the possibility of loss is through diversification: divide your savings between safe investments, such as government bonds and guaranteed investment certificates (GICs), and a broad selection of riskier but often higher-yielding investments, such as stocks. By buying both bonds (which tend to go up in value under conditions that depress the stock market) and stocks (which allow you to participate in the profits of businesses), you're much more likely to thrive no matter what happens to the economy. Consider buying a simple mix of low-cost bond and equity (stock) index funds, often referred to as a "couch potato" portfolio. This is a simple, inexpensive and effective strategy that regularly outperforms the erratic stock market and most professional money managers.

Step 3: consider the costs

Keep a close eye on what you pay in fees and commissions. Mutual-fund management fees can cost thousands of dollars over time and rarely correlate to higher returns. Consider index funds or low-fee managed funds for a similar performance at a fraction of the cost. (Index funds keep costs low by not paying for money managers, sales commissions or advertising; low-fee managed funds employ money managers but don't advertise or pay commissions and, in some cases, minimize administrative costs by requiring a high initial investment.)

Step 4: review and relax

Once your plan is set up, spend some time each year reviewing and rebalancing your portfolio (that is, buying and selling to return to your original mix of investments). Then sit back and relax – don't try to second-guess the market or let a salesperson talk you into more fee-laden programs. Save diligently, review annually and watch as your future grows brighter and brighter. ▷

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