

# *Future Financial News*

Certified Financial Planners, Chartered Financial Consultants, Chartered Life Underwriters

SUMMER 2009 NEWSLETTER

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## **C**arl's Comments

I often wonder if our clients actually read our quarterly newsletters. Based on the behavior of some I believe they don't or they do but act on their own judgment, poor as it may be. There are many examples of this behavior. RRSP contributions are way down this year. Some clients insisted on investing contributions in GICs instead of buying stocks at a 50% discount. Some clients went as far as redeeming their mutual funds and investing the entire proceeds at 3% for the next three years, locking themselves out of any market recovery. Interestingly enough these are well-educated individuals, business men and women, professionals and consultants who, despite our best efforts and significant supporting data, still made terrible, costly decisions.

So what were we actually saying? Be greedy when others are fearful. Watch the behavior of the world's richest man, Warren Buffett. He had more acquisitions in 2008 than in the previous 10 years combined. CIBC world market economists were predicting an 11,000 mark for the TSX (which we are just shy of) and bear markets provide the best buying opportunities. When the market overreacts in one direction it's bound to swing back dramatically in the other. Investors generally get it wrong, according to Dunbar Market Research, because they're driven by fear. When money market funds are peaking out with cash and equity funds are bottoming out, these provide the greatest opportunities.

The good news is that, out of all the money we manage, the percentage of these mistakes was limited to less than 2%. So all in all the majority of our clients have stayed put and have enjoyed a great recovery.

Where are we now? Summer I hope. I just planted my flowers on June 13 somewhat confident that we're not likely to get another frost. However I have not yet required the use of my air-conditioning unit.

Oh! You mean my view on world markets? I feel the further we get away from October 2008 the better. The good news is that the sky did not fall when a very high percentage of individuals believed it would. Stimulus funds are flowing and little by little the economic news of the day is much more positive. The collapse of General Motors boosted the TSX 3% in one day. Had this occurred in October 2008 I believe the result would have been devastating to world markets. My bias is that we are on the road to recovery.

There are two camps out there; one says that the market will test March 2009 bottoms and the other says that the market will go down but then back up higher and that this pattern will continue into the future. I would say I'm cautiously optimistic and I'm maintaining my conservative posture that has served our clients well. We're proud to report that our average client, in the darkest days, was off 20% versus world markets being off 50%. This was equivalent to the pullback of a conservative pension fund.

Last fall taught me that there is no certainty out there. Either camp may be right. The camp that did the best during the downturn is predicting the market will test bottom. The camp that did the worst is predicting the worst is over. So a pull back from current levels should not be a great surprise to us.

## **T**ax Free Savings Account

When the TFSA first surfaced I noticed that the government blew its brains out on advertising like they had just invented sliced bread. But the fact is that years ago we were all allowed to earn \$1000 without paying any tax whatsoever. They're just giving us back what we once had. My question is why promote the TFSA so heavily when the majority of Canadians don't take advantage of maximizing their RRSP contributions. RRSP contributions will reduce your taxes immediately. The TFSA will not.

Another observation is that a number of clients have set up these TFSAs with their banks using savings or GIC accounts. So you have \$5,000 invested earning 3% or \$150 of interest at a 40% tax bracket. Wow! You've saved \$60 in tax. I invested mine in a very aggressive fund, have currently earned \$2,000 YTD and have saved \$800 in tax. So my take is that if you don't need the TFSA as a source of emergency funds perhaps an aggressive strategy provides the greatest opportunity. If you need it as a source of emergency funding, yes, be conservative. TFSAs definitely have a place in an investment portfolio but that place is behind an RRSP for the most part.

## **E**state Planning Tips

A number of clients have purchased term life insurance on a temporary basis to make up for their recent losses in their investment portfolio until things recover.

Another useful life insurance concept includes buying insurance to protect the loss of pension income to a spouse. The present value of this amount could be astronomical and life insurance can help preserve that loss and protect the spouse's income.

In reviewing portfolios and beneficiary concerns, I've noticed that many second marriage clients plan to leave their RRSPs to their children rather than their new spouse. This would be fully taxable to their children on their demise. These clients could set up an

arrangement to buy insurance for an equal amount, leave that amount to their children tax-free and leave the RRSP in-tact, tax-deferred to their new spouse and vice versa.

Another idea involves taking a single life pension without survivorship benefits. This provides substantially more monthly income than a joint pension and then using the difference in income to acquire life insurance. This has multiple advantages. Should your spouse predecease you the policy can be cancelled or there could be a change of beneficiary. Should you predecease your spouse, he or she would receive a tax free amount of capital which could be invested and the residual could pass on to future generations. Life insurance can be a powerful estate planning tool when used appropriately.

## **P**otential RRSP Pitfalls

The RRSP remains one of the best tax planning tools available to Canadians. Help make the most of it by avoiding these potential pitfalls.

- **Starting late.** A common regret among those approaching retirement is that they didn't start saving sooner. A person contributing \$5,000 annually starting at age 25 would have \$998,176 at age 65, compared to just \$204,977 for someone starting at age 45 (assuming a 7% annual compound return).
- **Withdrawing early.** Taking money out of your RRSP prior to retirement should be your very last resort. First, the withdrawal will be fully taxed as income. Second, you'll be giving up tax-free compounding on your contribution, and it's impossible to get that contribution room back.
- **Borrowing carelessly.** The interest on an RRSP loan is not tax-deductible. So unless you're sure you can repay the loan quickly and minimize borrowing costs, it might make more sense to take that monthly loan payment and use it to make automatic monthly RRSP contributions instead.

## Profiting from the rebound

History shows that the first few years after a market downturn offer the best opportunities for growth. For example, the three-month return on the S&P 500 Index was -30% following "Black Monday" in 1987. However, as the table below shows, the markets rebounded strongly, providing a cumulative 87% return over the next five years.

**Worst three-month period of each decade has typically been followed by periods of growth**

Month-end of worst 3-month return	Main driver of decline	3-month return (%)	S&P 500 Index cumulative return (%)			
			1-year	3-year	5-year	10-year
November 30, 2008	Credit crisis	-30	?	?	?	?
October 31, 1990	Persian gulf war	-15	29	54	91	370
November 30, 1987	Black Monday	-30	19	40	87	315
August 30, 1974	Watergate scandal	-26	32	52	72	161
June 29, 1962	Cuban Missile Crisis	-21	27	54	66	96
October 31, 1957	Civil rights movement	-14	25	30	38	129
October 31, 1940	Blitzkrieg – WWII	-24	1	30	62	103
May 31, 1932	Great Depression	-46	116	114	264	82

Source: Bloomberg, as at March 31, 2009; returns in US\$

## Recovery time: Cash vs. equities

Unexpected volatility can make many people nervous. The question is what to do after a sharp drop in the market. Some people will decide to take a slower route to achieving their financial goals and move their savings to a money market fund or GIC. Others simply ride out the storm. The table below shows different scenarios for how long it will take for an investment to recover its worth. For example, if a fund declines by 25% and the investment is left in the fund to grow, and assuming an 8% annual return, it will take less than four years to recover. However, it's a different story if the investment is sold and the proceeds placed in a GIC or money market fund paying only 3% a year. In that case, it will take almost 10 years to recoup the loss.

### Years to recoup your loss

Initial decline (%)	Annual returns (%)							
	3	4	5	6	7	8	9	10
-5	1.74 years	1.31 years	1.05 years	0.88 years	0.76 years	0.67 years	0.60 years	0.54 years
-10	3.56 years	2.69 years	2.16 years	1.81 years	1.56 years	1.37 years	1.23 years	1.11 years
-15	5.50 years	4.14 years	3.33 years	2.79 years	2.40 years	2.11 years	1.89 years	1.71 years
-25	9.73 years	7.33 years	5.90 years	4.94 years	4.25 years	3.74 years	3.34 years	3.02 years
-30	12.07 years	9.09 years	7.31 years	6.12 years	5.27 years	4.63 years	4.14 years	3.74 years
-40	17.28 years	13.02 years	10.47 years	8.77 years	7.55 years	6.64 years	5.93 years	5.36 years
-75	46.90 years	35.35 years	28.41 years	23.79 years	20.49 years	18.01 years	16.09 years	14.55 years

## Locked in? Or locked out?

While money market funds are highly flexible, some GICs and savings accounts may require you to lock in your savings for a set period of time. To discourage you from making an early withdrawal, you may be required to pay a penalty if you redeem before this date. This may leave you effectively locked out of investing in the equity markets – sometimes for several years.



# FUND REPORT

Compounded to May 31, 2009



Fund	RRSP Eligible	Volatility	1 yr %	3 yr %	5 yr %	10 yr %	Globe's Rating
<b>CANADIAN EQUITY</b>							
Trimark Cdn First Class	Y	M-H	-30.05	-9.95	1.70	6.42	★★★
BMO Dividend	Y	M	-22.61	-4.06	3.73	8.03	★★★★★
Dynamic Power Cdn Growth	Y	H	-42.30	-4.15	8.03	9.53	★★★★★
Fidelity Canadian Growth Company	Y	M-H	-31.15	-6.25	1.63	4.94	★★
Fidelity Cdn Disciplined Equity A	Y	M-H	-29.44	-1.69	6.36	8.68	★★★★
Front Street Growth	Y	H	-41.87	-9.87	8.38	15.04	★★★★
BMO Monthly High Income	Y	M-H	-26.97	-7.00	5.28	10.34	★
IA Canadian Conservative Equity	Y	M-H	-21.86	-4.10	4.32	7.07	★★
IA Clarington Cdn Leaders	Y	M	-20.50	4.52	7.21	4.84	★★★★★
IA Clarington Cdn SmCap	Y	H	-26.36	-8.75	3.46	10.42	★★★★
IA Clarington Dividend Inc-T4	Y	M	-25.47	-6.87	1.53	5.65	★★★
Sprott Canadian Equity	Y	H	-43.18	-5.41	7.95	22.17	★★★★★
<b>INTERNATIONAL EQUITY</b>							
AGF European Equity Class	Y	M-H	-28.11	-9.26	-2.77	0.58	★★★★★
Dynamic Global Value Class	Y	M-H	-31.00	-7.91	0.10		★★★★
Fidelity NorthStar A	Y	H	-28.91	-9.18	-2.29		★★★
Mackenzie Cundill Value A	Y	L-M	-22.99	-7.84	-0.65	5.45	★★
Trimark Europlus	Y	M	-38.32	-11.86	-3.00	2.68	★★★★★
<b>BALANCED FUNDS</b>							
Acuity Canadian Balanced	Y	M	-16.10	-2.11	2.91	5.88	★★★★
AGF Canadian Balanced	Y	L-M	-7.09	3.47	6.23		★★★★★
Dynamic Value Balanced	Y	M	-13.24	0.46	7.49	7.84	★★★★
Fidelity Canadian Asset Alloc A	Y	M	-13.43	2.23	6.09	5.67	★★★★
Renaissance Cdn Value Balanced	Y	L-M	-12.76	-2.48	2.27	5.05	★★★
Fidelity Cdn Balanced	Y	L-M	-12.79	2.67	5.72	7.27	★★★
Dynamic Power Balanced	Y	M-H	-18.98	2.49	8.26	8.16	★★★
<b>OTHER FUNDS</b>							
Vertex	Y	H	-24.60	-2.01	8.23	15.82	★★★
Arrow Multi-Strategy	Y	L	-9.89	-2.30	3.06		★★★
BluMont Hirsch Performance	Y	H	-26.33	-6.42	1.79	12.70	★★★
Hillsdale Cdn Long/Short	Y	H	-19.06	-4.91	5.15		★★
Hillsdale Cdn Performance Equity A	Y	H	-42.05	-13.28	-1.30	9.64	★★★
Sprott Opportunities Hedge Fund LP	Y	H	-6.37	7.35	21.20		★★★★

**All Mutual Funds Sold by Prospectus Only & Hedge Funds Sold by Offering Memorandum**

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