

MUTUAL GAINS™



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Without money, possibilities are limited..... without personal relationships, life is barren...
without balance, happiness and fulfillment are just a dream.



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Foreign Versus Canadian Assets

In February's Federal Budget it was proposed that the 30% foreign content limit would be removed. With the Gomery inquiry uncovering more and more corruption within the Liberal government it appears for the time being at least, that the 30% foreign content limit will remain in place.

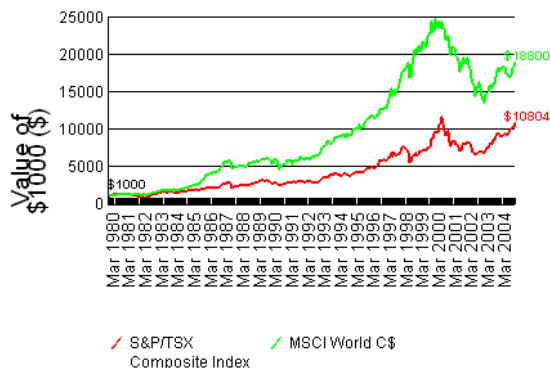
I do believe that if the Liberals are defeated in a forced election the 30% foreign content limit will, sooner rather than later, be eliminated. Pension plans and RRSP issuers will again be able move in the direction of much more foreign content within their portfolios.

If you look over a long periods of time you will see that foreign investments perform much better than Canadian investments. In the short term however Canadian assets do have their times in the sun, as has been the case since 2000. However, it is after utopian periods such as these that you need to revisit the historic averages and either rebalance or allocate new assets to areas that have done very well historically but may have lagged over the past few years.

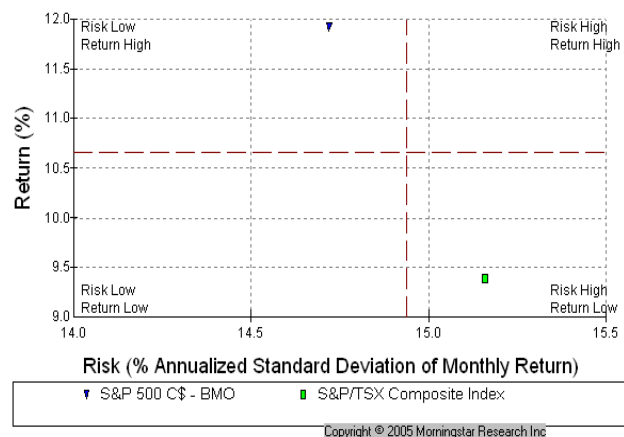
"IF FOREIGN INVESTMENTS PERFORM BETTER THAN WHY HAVE ANY CANADIAN ASSETS AT ALL?"

The biggest risk of have a large part of your portfolio allocated to foreign investments is the short-term currency risk. Your investments are quoted in Canadian dollars on your statements so as an example, if your U.S. investments increase by 9% but the Canadian dollar goes from \$0.73 to

Value of \$1000 from Mar 1980 to Feb 2005



20 Year Risk/Return Report at March 31, 2005



\$0.81 per \$1 U.S. dollar your portfolio will show a 2% decline in value. Like all things however, these issues tend to fall back to historical averages. It's just a short-term risk that will be evident on your portfolio statement.

Aside from the currency issues, foreign investment markets,

over a long-term basis, fluctuate less than the Canadian market (see 20 year graph above). So for your portfolio, on one end of the spectrum, you can invest 100% in foreign investments and be subject to short-term currency changes or just invest in Canadian assets but have less money in your nest egg at the end of the day.

The alternative to having either / or is to have a mix of the 2. This in fact has shown to produce a smoother performing portfolio than either 100% foreign content or 100% Canadian. For most people smoother is better. The ideal mix is 60 - 70% foreign with the balance in Canadian investments, something I apply to virtually every portfolio under my administration.

Today, it may seem much more advantageous and feel better to own or invest more money in Canadian assets. You should however be much better off allocating additional monies into International investments. Today this is particularly relevant as international investments offer better value than Canada has to offer.

How Foreign Content Elimination Will Effect Canadian Markets

With foreign content being lifted Canadian companies will be compared more directly, in every respect, to similar foreign companies.

Take the largest home improvement chain in Canada and compare it to the largest home improvement chain in the U.S. For many years a portfolio manager has been restricted to making Canadian investments and this Canadian company would attract the investment dollars simply by default. When the foreign content limits are inevitably eliminated Canadian companies, with their International alternatives IN ALL RESPECTS. Because Canadian pension and RRSP dollars won't have to stay in Canada these dollars will be able to be invested where the best value is, without limits.

When the foreign content limits are inevitably removed some Canadian sectors will be negatively affected. According to various investment managers I use, the most vulnerable are larger Canadian technology, biotech and healthcare companies. There are numerous and far superior international companies in these sectors. The average Canadian investor holds a very large proportion in Canadian banks and insurance companies. A part of these monies could find their way to cheaper U.S. and European companies. There are a number of Canadian companies that sell directly to the Canadian consumer. These are expensive when compared to their International counterparts. Money invested in these Canadian companies may flow over to similar but much better investments in other countries.

Canadian companies with sub par financials, ones that have had a captive investment audience and yet have attracted investment capital only because of foreign content limit constraints, will soon see much more pressure to compete and perform. Once foreign content limits are finally eliminated these Canadian companies will suffer.

Strong Loonie = Low Interest Rates = Buoyant Real Estate

The soaring Canadian dollar may be a drag on the economy as a whole, but it has been the propellant behind Canada's residential real estate market.

The rising loonie over the past two years has meant the Bank of Canada has been able to keep interest rates very low, almost artificially so. Cheap credit is the lifeblood for a healthy housing market.

What if the Canadian dollar wasn't so strong? In a recent report CIBC says that 5-year mortgage rates would be 1% higher. If that had been the case this CIBC report says that real estate would have only increased marginally countrywide.

Canadian Residential Real Estate Statistics and Compounding

There seems to be a perception that real estate is the best investment on a long-term basis. This is in fact more perception than reality. 1 reason for this widely held perception (or misconception?) is that real estate can be leveraged (borrowed against) to enhance its actual return, thus increasing the return on the money YOU invested (your down payment, not the banks mortgage portion). Take away the leverage in real estate or apply leverage to a portfolio of company ownership (ie. "equity investment") and you will have a much fairer comparison.

Over the past 25 years, the value of a house in Toronto has appreciated by 5.75% per year. Inflation has averaged 3.1%.

I can hear the statement now, as I have heard it many times before... "Vancouver real estate has done much better". The numbers for Vancouver show that over that same 25 years Vancouver real estate has increased by 3.68% per year however it's also seen it's prices go up and down much more (these numbers are from the Canadian Real Estate Association and the Multiple Listing Service). Add the rental income MINUS the maintenance expenses, insurances and property taxes and you can add another 4% to that return. A total average annual return of 7.68%, unleveraged.

As a comparison, the TSE / TSX Index, a measure of a blue chip Canadian equity portfolio returned 8.64% including dividends. That is approximately 1% per year more, albeit with more price variability than real estate. The S&P Index (U.S. equities) has done even better producing results 13.85% per year over the past 25 years.

It's not the investment per se. It's the compounding. Compounding can only materialize if you leave your investment in place. If you hold an investment that historically has proven to perform well OVER TIME (real estate, equities etc.) and stick with it, you will do well. With equity investments, many people just don't hold their investment long enough to see the long-term benefits.

No More Company Pension Means You May Have A Case Of PAR

Before you start thinking that PAR has a negative sound to it let me ease your mind. PAR stands for "Pension Adjustment Reversal". It's a 1-time boost in your RRSP contribution room when you leave a pensions plan before retirement. This usually happens when you change jobs.

While you are at a job that has a "Defined Benefit Pension Plan", your RRSP contribution room is reduced based on how much income you will get from that pension plan when you retire. If you leave your company and transfer the pension credits into a "Locked In RRSP", the "transfer value" is often less than the amount of RRSP room you lost while you were a member of the pension plan. PAR corrects this inequity by boosting your RRSP contribution room the year you leave the pension.

Your previous employer is the one responsible to calculate and report the PAR amount to both CCRA and to you.

Is Your RRSP Beneficiary "Estate"? It May Be Time To Change It

Naming a beneficiary on any Registered Plan (RRSP, RRIF etc.) lets you say where your money will go should you pass on prematurely. If you have a "spouse" it is best from a tax perspective to name your spouse as beneficiary. This way the monies in the plan would be transferred directly into a Registered plan for your spouse with no tax implications.

If you don't have a spouse I have usually suggested having your "estate" named as beneficiary and all your assets divvied up according to your Will's instructions. It's much easier that way, as only 1 document (your Will) has to be changed. It's much easier to determine who will get what, especially if you have assets all over the place.

That was my suggestion until now. A recent Supreme Court of Canada (SCC) decision has taken creditor proofing of RRSPs a step closer, provided you name someone as beneficiary. If you haven't named a beneficiary, creditors of your estate can grab your RRSP to pay any outstanding debt owed by your estate.

If You Have Debt, Critical Illness Insurance is Critical

We may be living longer, but that also means many more years when we are at risk of a serious illness or disability. We're all vulnerable whether we like to think so or not, and most of us have no idea how quickly chaos can happen. One day you're fine and the next day you have cancer or suffer a stroke and your whole life changes.

1 in 3 of us will be diagnosed with life-threatening cancer. Heart disease is on the rise. Today, 95% of heart attack victims survive their first attack. More than 70% survive their initial bout with cancer. 75% survive their first stroke. Today, if you get an illness you will probably survive but not be in any condition to work, at least initially. If you have any kind of debt, are self-employed, single or live in a 1-income family your financial risk is particularly high.

Unlike life insurance, which pays beneficiaries upon your death, critical illness is a "living benefit". It allows for a tax-free lump sum payment on diagnosis of a condition such as heart attack, stroke, cancer, multiple sclerosis, Alzheimer's disease, burns, organ transplants, blindness or paralysis. The funds can be used for any purpose. A \$100,000 payout could allow you to seek alternative health care outside Canada, pay for childcare or private nursing care, or renovate a home to accommodate a handicap. Alternatively you could take the trip of a lifetime before time runs out.

It is financially advantageous to apply for these types of insurance while you are healthy and relatively young. Your age, sex, health and habits affect the costs of insurance.

As is the case with any solid financial plan, risk of all kinds need to be addressed. Have you assessed yours?

Before Coming To Canada an Immigration Trust Is A Must

When you become a resident of Canada, your world income is automatically subject to Canadian tax. That is of course unless you have set up an Immigration Trust set up. Then you don't have to pay on your worldwide income for 5 years**.

An Immigration Trust is simply a "non-resident trust", established in a non-Canadian tax jurisdiction, which holds foreign investments and property. For 5 years, assets within this trust can accumulate tax-free in the trust. Example: \$1 million earning 7% per year for 5 years would be accumulate to \$1.4 million within the trust. If tax

had to be declared in each of those 5 years (no Immigration Trust) the portfolio would be worth \$1.2 million. Also, while assets are in an Immigration Trust they are creditor protected.

Many tax shelters and tax saving ideas have disappeared over the past several years. The Immigration Trust still stands, waiting to be used by Immigrants and non-resident company executives moving to Canada.

** You can set up an Immigration Trust at anytime within 60 months of becoming a Canadian resident however the 5 year tax deferral clock starts ticking the day you become a Canadian resident.

Filing a U.S. Tax Return Doesn't Mean You Pay Tax Twice

If you hold a U.S. investment and live and pay tax in Canada most likely you are filing a U.S. tax return. This may give the appearance that you are paying tax twice but that is not really the case.

Your U.S. investment gives the U.S. government the 1st right to tax the income related to that investment. The other country (i.e. Canada) has a residual right to tax the income and would grant a "foreign tax credit" for tax paid in the U.S. When the 2 countries tax laws conflict, the Canada-U.S. Income Tax Convention would come into play to determine which country has the 1st right. At the end of the day, you would be paying tax at the rate you normally pay where you live. That is unless you are filing your tax return late, in which case you would be paying penalties and interest on income tax owing.

HHHhhhhmmmm.....

At age 65, 73% of Canadians will have income lower than \$25,600 per year (Statistics Canada).

90% of all marriage break-ups are related to money issues.

The term "hedge fund" was coined in a 1949 Fortune Magazine article.

The 2nd richest man in the world, Warren Buffett, still lives in the same, modest house he bought when he was first married.

Warren Buffett's son was embarrassed to be driven to high school in the family's old VW. The Buffett's at that time were already extremely wealthy.

The strong Canadian dollar has made U.S. investments that much cheaper.

Dividend income is only 66% taxed. The vast majority of Income Trust distributions are 100% taxed.

Canadians are sitting on a substantial amount of cash currently totally \$40 billion in bank deposits, chequing accounts etc. (Source: Bank of Canada)

If you are an Ontario resident and have a medical issue outside of the country you are covered up to \$400 per day of expenses incurred by your provinces health plan. B.C. residents are covered up to \$75 per day. The average hospital room in the U.S. costs \$1,500 per day (in U.S. dollars of course).



Chartered Financial Planner

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