

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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A Little "Shaking of The Tree"

Investors need to get used to market volatility again. What we saw in May, and it seems to be continuing, was a return to a more normal market environment, one that produces lots of ups and lots of downs. This is contrary to what we have experienced over the past couple of years, a continual "up". We needed this good "tree-shake" and it arrived rather swiftly. Things need to be purged occasionally so lower quality investors and investments are shaken from the tree. This is what has been happening which keeps the investment environment healthy.

Most investment managers like volatility because it creates opportunities, but only for the few who are poised to take full advantage of them. I am happy to say that many of the specialty investment managers I use as a Financial Planner for my clients had (and still have) a sizable amount in cash reserves to take advantage of buying "good companies at good prices". One investment manager I use for clients recently stated this about his the portfolios he manages, "I also love the "other part" of the portfolio that isn't invested in stocks. I would make three important points: 1) I have over \$2.2 billion in cash, 2) I have over \$2.2 billion in cash, 3) I have over \$2.2 billion in cash."

What We Have Seen Since 1973

If you believe history for the most part repeats itself I think you'll be very interested in these snapshots of history. It has been said that, "those who ignore history are doomed to repeat it". It is for this reason I think it's worth revisiting what we have gone through.

Let's start with the period of 1973-74: In 1973, Coca Cola shares were trading at \$3.01 and a PE (Price to Earnings) ratio of 45.31. By 1974 Coke was worth \$0.95 for a loss of 68% and it took over 12 years for its share price to recover. In that same era, oil was selling for \$4 a barrel and gold was worth \$180 per ounce. The vehicle of choice was the Pontiac Trans Am with a V8.

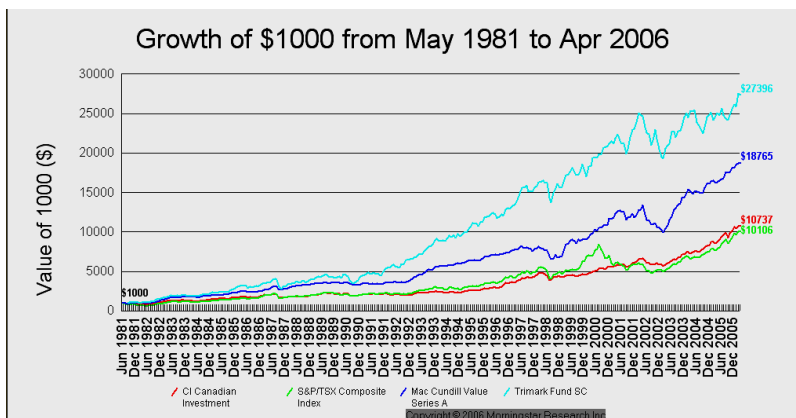
Moving ahead 6 years to 1979-80: The S&P 500 (U.S. stock index) had moved sideways for the previous 6 years. The TSE 300 (Canadian stock index) was on a tear as resource companies took off. A barrel of oil had jumped to \$39.50 (a 887% increase in 6 years) and an ounce of gold hit \$934 (a 400% increase). The vehicle of choice was the Chevy Chevette.

This era was followed by a severe recession.

Jump to 2000-02: Tech mania! In 2000 Nortel, the investment many felt they had to make or be left behind was trading at \$124.50. By 2002 it was worth \$0.67, a loss of over 99% from it's high. Oil was selling for \$34.40 per barrel in 2000. Gold was worth \$252 per ounce and the vehicle of choice was the Chevy Suburban with a V8 (of course).

Which brings us to today, 2006:

The S&P 500 has for the most part moved sideways for the past few years for a 3 year compounded annual rate of return of 3%. The TSX on the other hand is on a tear (again) and has compounded at 20% per year for the past 3 years. A barrel of oil has jumped to \$74 and an ounce of gold is around \$550. The vehicle of choice is the Toyota Prius Hybrid.



So where do we go from here? One has only to look at the interest rate increases over the past 18 to 20 months which has created an "inverted yield curve". This is when short term interest rates are higher than long term interest rates. In eight of the last ten times we've experienced inverted yield curves, recessions have followed.

No one knows what the future holds which is why it is important (correction... imperative) that your portfolio be well diversified so as to weather any economic scenario.

Immersed In Buffettology

As you may know Warren Buffett is one of the richest individuals in the world, whose wealth was simply created by buying good businesses at good prices and holding them for the long term. He has done that successfully for 50 years through the holding company- a mutual fund of sorts- Berkshire Hathaway (BH).

You would think at the age of 75 he would be winding down, retiring and using the days for golfing, travelling and taking in his favourite spectator sport, baseball, while licking a Dairy Queen treat or munching on See's candy while sipping a Coke. So far he continues at full steam. Speculation has been rife on when he will turn over the BH leadership. It is for this reason I thought it important to make the trip to Omaha Nebraska to attend the Annual General Meeting of Berkshire Hathaway (open only to shareholders).

Mr. Buffett along with his senior side-kick Charlie Munger, have created the world's best long term investment results: 21.5% average annual returns, more than two times the S&P 500 index including dividends. I believe the pilgrimage to Omaha was the way to better understanding and insight into what makes BH's investment process so successful. This I achieved by:

- 1) Attending all of the AGM: This included a presentation on BH's most recent acquisition, 80% of Iscar Metalworking Companies, an Israeli tool business for which they paid \$5 billion. I also spent a few hours absorbing the questions posed by shareholders and the responses to them by Warren and Charlie. This included several concerning the financial picture of the U.S. as a whole. Several hours of wisdom and common sense.
- 2) Visiting the numerous booths of the various BH owned companies. These included; GEICO (insurance), American Express (financial services), Johns Mansville (insulation & building products), Benjamin Moore (paint & coatings), Shaw Industries (carpet & floor coverings), Fruit of The Loom (apparel), Campbell Hausfeld (industrial products), Clayton Homes (manufactured homes), Dairy Queen, Coca Cola, and the Pampered Chef (a direct seller of kitchen tools).
- 3) Reading the 2005 Berkshire Annual Report cover to cover, an interesting read. From it you can't help but gain much appreciation for all that it means to be an excellent investor, which is being a business person buying pieces of businesses. Excellent management from the bottom all the way to the top is the key ingredient, diametrical to the unfortunately common approach of; "I bought this investment because I heard it was supposed to be good (or, will make me a lot of money)". Instead, choose the right companies by paying attention to their quality of product and branding, and a management team that thinks and works like an owner of the business. Buy that package at a good price and you can't help but make smart investments.

Most of the investment managers I use for managing client portfolios share Warren Buffett's investment philosophy, which is all derived from Benjamin Graham, the father of what is called "value investing.", In times of

investment euphoria or of chasing rising investment prices in a particular sector (ie energy or gold) this kind of investing can seem to lag but it provides superior returns in the long term and is the lowest-risk way to invest. It's simple but it's often not easy. It takes patience and discipline, something we humans often lack.

I'll leave you with Warren Buffett's addition to Sir Isaac Newton's Three Laws of Motion. This is what Warren calls the Fourth Law of Motion for investors; "Returns decrease as motion increases".

It is Time That Makes Your Money Grow

The following is an illustration that was shown to me 20 years ago. It all about the power of time and consistency:

"Early Erin" invested \$100 each month for 10 years starting with her first part time job at the age of 15. After turning 25 she stopped and never invested another cent. On average, Erin's investment earned 8% per year. Even though Erin only invested \$12,000 and let it sit in her investment account for years, her investment grew to \$422,616 by the time she reached 65.

"Late Liam" took a totally different road. He didn't start investing until the age of 25. When he finally did start , Liam put away \$100 per month until he was 65, a total of \$49,200. He put his money into the same investment as Erin but when Liam turned 66, his investment account was only worth \$349,120. How is that possible? Well, Einstein was right: the length of time your investment grows could have a greater impact than the amount of money you've invested.

Do you want to do some calculations or play with some numbers? You will find lots of calculators here: <http://careyvandenberg.com/calculators.php>

Give 10% of your Income To Charity Get 9.5% Back

The most recent Federal budget on May 7th has given you a gift and it relates to charitable gifting of publicly traded investments. These include stocks, mutual funds and flow through shares the latter of which we will be exploring particularly closely because it is by far the most attractive investment for you to give.

The gift in the budget is the ability to give publicly traded investments and not have to pay tax on the capital gain. Rather than give you a whole lot of details in this article I thought I would go straight to the numbers as it relates to one particular flow through share offering (based on highest personal tax bracket):

Your investment in a flow through share offering	-\$10,000
Net tax savings you receive from investment (deductions & credits)	+\$ 5,991
You donate the shares to a charity and, to be conservative, we will assume that the investment has fallen in value by 20%	\$8,000
Tax savings to your for donating the shares	+\$3,496
Your Out of Pocket Cost	-\$513

You will see from this table that the effect of your charitable giving can cost you just pennies on the dollar assuming even a pessimistic outcome for the investment.

If you are giving money to one or more charities currently I strongly suggest you do it this way. The benefit to the charity is virtually the same as if you gave cash (they can sell the investment almost immediately upon it being given to them) but you on the other hand are much better off. It's very simple, there is nothing fancy about it and the tax numbers are quite sweet. Also, all

the tax benefits are written into the Income Tax Act and thus undisputable. I'm definitely making flow-through investments for the purpose of my family's future charitable giving, at least until the government changes the rules- (Always a possibility). Do you want to see how this will work in your situation? Call or e-mail me and I'd be happy to work out some numbers for you and answer all your questions.

The "Additional Grant" For RESP's

You may already know that for every dollar you contribute to an RESP the government will add \$0.20 (Canadian Education Savings Grant) to a maximum of \$400 per year coming from Ottawa. There is an additional grant available which is based on your family income. The additional grant amount can change over time as your family income changes.

Depending on your family income, your child could receive additional grant on RESP savings that you make after 2004 on behalf of a child:

- If your net family income is below \$35,595*, the grant will be 40 cents for every dollar on the first \$500 you save in your child's RESP each year (an additional grant of \$200 per year).
- If your net family income is between \$35,595* and \$71,190*, the grant will be 30 cents for every dollar on the first \$500 you save in your child's RESP each year (additional grant of \$150 per year).

Your net family income is reported on your Canada Child Tax Benefit statement (commonly known as "baby bonus", or "family allowance") that you receive from Canada Revenue Agency each July.

HHHhhhmmmm.....

Only 28 per cent of professional money managers are bullish on Canadian equities, down from 48 per cent only three months ago, said Russell Investment Group in an April 3 report.

The loonie is at its highest level since Jan. 26, 1978. It's been one of the world's top-performing currencies against the U.S. dollar. In the past month, the loonie has posted the second-largest monthly increase in 55 years.

Most Canadian's portfolios are loaded with some of the highest priced assets in the world valued by one of the highest priced currencies in the world. Sell high buy low?

A portfolio of 40% Canadian equities, 30% U.S. equities and 30% International equities has produced the highest return with the least amount of risk (fluctuations). AGF Fund Analytics, Nov. 30th 1985 to Nov. 30th 2005.

Tokyo house prices have continued to slide and are now 40% below what they were in 1991. Since 1997 house prices in Hong Kong have fallen by 43%. (The Economist, Dec. 10th 2005)

Australia has the most overvalued housing market with prices 52% above their "correct" level. Next in line is Britain where prices are 33% overvalued. (The Economist, Dec. 10th 2005)

In the past 20 years housing in Canada was least affordable in 1989. All provinces in Canada have housing that is significantly more affordable today than in 1989. This is measured by the percentage of the average income it takes to finance a mortgage. B.C. is the exception and is pushing the affordability limit where, after making a 25% down-payment, 65% of the average income is needed to pay for mortgage payments, property taxes and utilities (RBC Economics).

About 88 percent of people refinancing or renewing the mortgages on their homes took out loans for at least 5 percent more than their original balances, according to the latest quarterly review of loans by Freddie Mac a U.S. government-backed home mortgage company.

Crude-oil prices are about 40 per cent higher than a year ago. Accounting for inflation however, prices are still about 20 per cent below the records reached in 1981, when supplies became tight after a revolution in Iran and a war between Iraq and Iran.

Petroleum inventories and oil prices typically move in opposite directions. Since 2003, this has not been the case.

For those 65 or older, the government starts "clawing back" your Old Age Security payments when your income is over \$62,000. All of it is clawed back when your income is over \$101,000.



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