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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Deceptively Attractive

Now that the Income Trust issue has stabilized it is important to look at business valuations. It is calculating a business' value that determines if a company as a whole is cheap, expensive or at fair market value. In time, it is that determination which will give us an idea of what we can expect going forward.

Two fundamental areas that need to be looked at are:

Return on Equity (ROE) – this is a measure of profitability.

Price-Earnings Ratio (PE) – how much investors are willing to pay per dollar of earnings.

A value investor, one who is concerned with downside as much as with upside likes to own companies that have above average ROE's with below average PE's.

The Canadian economy, with the exception of a large part of Canada's traditional manufacturing sector is in a blissful place today. This is particularly evident in the "Energy and Materials" sector (anything commodities based). We only experience this every couple of decades.

The current Canadian market picture may be unsustainably rosy, driven by extraordinary results in the "Energy and Materials" sector. The ROE's and PE's for these kinds of companies are well outside their long term averages. The question that needs to be asked is whether this is sustainable. Can these deeply cyclical companies continue to defy history and generate earnings and returns so far above their long term averages? If you are convinced this current "commodity super-cycle" will continue indefinitely this existing nirvanic state may be of no concern to you. However, if you are equally concerned about preserving your capital and at the same time growing it over time then your portfolio should be reviewed now (if it hasn't already). One last question for the "commodity super-cycle believer", what if you are wrong?

Note: The current cycle of rising earnings in Canada is the longest since 1975 (Investment Executive Oct '06)

Income Trusts Are Out, Retirement Income Splitting Is In

Income Trusts are on the way out and frankly, they had to be. Prior to the Federal Government's announcement on October 31st, there was a big advantage for a company to convert to an Income Trust and the momentum for converting from a corporation to an income trust was quickening. The continual one by one conversion of Canadian companies to Income Trusts would have eroded the amount of tax revenue being paid by corporate Canada. It also would have slowly choked the ability and incentive for Canadian companies to grow and prosper and would have been devastating to the long term growth of the Canadian economy as a whole. If the government did not act as they did our children and their children would be paying for it dearly years from now.

What the Federal Government brought in at the same time on October 31st was the ability for retired couples to divide pension income between them. This is an enormously significant development, one that could reduce retirees income taxes by several thousand dollars. It will be particularly noticed by couples 65 or older where one partner was the substantial bread winner during their working lives and thus has a much higher taxable income than the other due to a healthy company pension plan income. This income splitting change will also be a huge tax saver for couples where one has a much larger RRIF value. This income splitting / tax minimization technique however can not be used with Old Age Security (OAS) or Canada Pension Plan (CPP) retirement benefits.

Note: there is now a very limited use or need for Spousal RRSP's however existing plans cannot be changed.

One of the Many Responsibilities of Your Financial Planner

Everything we deal with has a cost of some kind. In the investment world the costs are often wrapped into the investment and are seldom seen by you the investor. One of the responsibilities I have as a Financial Planner is ensuring you are getting good value from the investment managers who manage various parts of your portfolio.

An example of this is a conversation I had almost 2 years ago with one investment manager who runs a 245 million dollar regionally specific investment pool. I told her point blank that I couldn't have her investment team managing part of my client's portfolios because their internal costs were too high. Although her management expertise was very good I believed there were investment managers with equally good track records as well but their internal costs were much lower. The bottom line is my clients were paying (although again it's seldom noticed) and my fiduciary responsibility was that my clients were getting good value for their money.

> "Parents should give their children enough so they feel they can do anything but not enough so they feel they can do nothing."
> Warren Buffett

Jump forward 20 months to September 11th of this year. That night I was invited to an exclusive dinner with a couple of investment managers I use for my clients. Over a drink before dinner the investment manager who I challenged almost 2 years prior came over to me. She said that shortly after our previous conversation they had reduced the MER (Management Expense Ratio) on the investment pool her team managed. In other words, that previous conversation proved to a million dollar one as it is currently saving all existing clients of that pool (my clients and clients of other financial advisor's alike) approximately $1.4 million per year in internal management expenses.

That is one of the many responsibilities and ongoing tasks of being a Finacial Planner on behalf of hundreds of clients just like you.

Note: The above mentioned investment manager currently has the number 1 performance record against all her peers over the past 1, 2 and 3 years with lower than average internal costs. NOW that is good value for clients.

Get Upside With Your Principal Guaranteed By A Canadian Bank

With interest rates still very low despite coming up a little bit from their ultra lows, interest rates are in a territory which is historically normal. So if you are investing in bank deposits / GIC's with 3 to 5 year terms, and have been for some time it's probably a good time to look at alternatives because interest rates aren't going anywhere.

The biggest reason for depositing money with a bank is the security offered on your money. Sure it's untouchable for a few years but when you get to the end of that term you know exactly how much money you will have.

An alternative to a bank deposit, one which also offers security of your money is a Principal Protected Note (PPN). The advantage PPN's have over a bank deposit / GIC is you can sell a PPN at anytime and you will pay half the income tax you would pay on the interest of a bank deposit.

Example 1: 3 year term – up to 10% per year return – principal guaranteed by a big Canadian bank – can be sold at anytime for market value.

Example 2: 4 year term – interest at maturity will be equal to the average of the 8 underlying global equity investments. Again, the principal is guaranteed by a big Canadian bank.

Principal Protected Notes have been around for several years now. I get a few e-mails each and every day notifying me of a new one of these PPN's however I use only use a select few. A PPN that came across my desk a couple of months ago offered a rate of return tied with the legendary Oracle of Omaha and the famous Berkshire Hathaway, one of the best performing investments over the past 44 years.

PPN's are an excellent choice if you normally look at investing in a bank deposit for a fixed term (ie. cash you have on hand which is to be used for a future home purchase or other large, future plan or if you just like security).

Note: The guarantee offered directly by the bank on a PPN is different than the deposit insurance offered by CDIC, a federal government agency.

Buy A Good Used Car In The U.S. for up to 35% Off Vancouver Prices

Since the success of your Financial Plan deals with spending almost as much as investing I thought this information would be of value to you. A penny saved is a penny earned, right?

If you are in the market for a modestly used car you may want to look across the border. I've done a bit of research myself on this topic after an associate of mine recently bought a good used car out of Phoenix on Ebay. Although he ended up flying to Phoenix and driving back (he had never been to Phoenix anyway) you can find similarly good deals within a few hours drive south of the border.

My research example: 2003 Pontiac Vibe / Toyota Matrix. Average price in the Lower Mainland is approximately $16,000. Average sale price on Ebay…… $9,500 (Canadian dollars).

Yes, it takes a bit of finger and leg work and it is much easier to peruse the local car lots however, if you consider a $6,000 gross saving in my example and you are in a 40% tax bracket, you would have to earn an extra $10,000 this year to pay for a good used car bought locally.

A penny saved is a penny earned? Not exactly correct. It should be "$6,000 saved is $10,000 earned" if you earn over $77,000 per year. If your income is $36,000 - $66,000 it is "$6,000 saved is $8,800 earned".

Trying To Avoid Probate Fees Can Be Costly To A Family's Peace

With the rising values of people's wealth there has been an increased tide to avoid paying probate fees however people are making some rather costly mistakes in trying to save a few loons.

Probate fees are costs a province charges on settling an estate. "Letters Probate" are simple a certification that a Will is valid. Probate fees are essentially a tax on the gross value of a person's estate that passes through the will.

Province of B.C. Probate Fee Schedule

$0 for estates under $10,000

$208 for estates between $10,001 and $25,000

$6 for every $1,000 exceeding $25,000 but is not more than $50,000

An additional $14 for every $1,000 the value of the estate exceeds $50,000

Here is an example of a probate fee avoidance situation gone wrong thanks to a poorly drafted will:

A financial planner's client had 3 daughters. After their Dad died 1 of them owed the estate $150,000 because "Dad" had given her some money to buy a house. He also fed money to her sporadically, money which the other 2 kids didn't get. The Dad recognized this inequity and his intention was for the scale to be rebalanced through his will, after he died.

The Dad had a RRIF and life insurance and names his 3 kids equally as beneficiaries these. This helped to reduce probate fees as these assets, because of their beneficiary designations didn't pass through the estate. The problem however was that there wasn't enough money left over to equalize the monies going to his kids because his house had a mortgage on it from the money he lent to his prodigal daughter. When all was said and done there was an extra $30,000 for the other 2 daughters to split. The prodigal daughter still owes the other two $120,000 ($60,000 each) if the estate was to truly be divided equally. Again, that was the Dad's intention.

What is the likelihood of the prodigal daughter paying the other 2 what is rightfully owed to them? If not, is the rift between the daughters worth a couple thousand dollars?

How To Plan to Give In The New Year

Giving is a part of our DNA however unless we are intentional about our giving it just doesn't happen. To make it intentional many people give a specific percentage of their income each and every month. For others it's a one time "charitable donation" at the end of the year. In each case it's intentional in the act and intentional in where the money is going.

The Income Tax Act makes it very favourable to give, and give you can for very little cost:

$10,000 invested in "Super" Flow Through LP	$6,000 tax savings
Flow Through Investment converts to a mutual fund and the mutual fund is donated	$4,000 tax savings
Net Cost of Charitable Donation	$0

If you want your giving to be more tax effective AND / OR more intentional e-mail carey@careyvandenberg.com

HHHhhhhmmmmm.........

The price of existing homes in the U.S experienced the largest monthly price decline since the Realtors began monitoring monthly prices monthly 40 years ago. (Washington Post, Oct 2006)

If you buy a 30 year strip bond and long term interest rates rise by 1% the value of your bond falls by 30%.

Interest rates have dropped since 1981, a typical "bond bull market". Such positive bond markets occur 2 to 3 times every one hundred years.

Valuation on a country's currency has a lot to do with whether it is running a trade surplus or trade deficit. Canada runs a surplus on trade only with the U.S. (mostly because of oil exports to the U.S.); Canada runs a deficit with most other regions. The US also runs a trade deficit with just about everybody except Australia. The U.S. and Canadian dollars are overvalued against most currencies in the world. Dr. Martin Murenbeeld, Chief Economist Goodman and Company Investment Counsel.

Investment Banking firm JP Morgan expects the Canadian dollar to fall to $0.82 against the U.S. dollar in 2007.

Canadian pension funds have been heavy buyers of foreign equity investments (Investment Executive Oct. 2006)

Mexico has displaced Canada as the largest supplier of auto parts to the U.S. market in 2000 and has widened its lead almost every year since then. (U.S. Census Bureau)

71% of investors burned by a fraud didn't get back any of their money. 98% of people stung by fraud were told of the investment from a source other than their Financial Advisor. (Advisors Edge, Oct. 2006)

The loss of truly "independent" financial advice is being lost. The following is one example. Saxon Financial was the top selling mutual fund family by the MD Financial Group's sales force. The Canadian Medical Association is Saxon's major shareholder. MD Financial is a subsidiary of the Canadian Medical Association.

In a recent survey on how 'account managers' at various financial institutions rated their firms, Coast Capital Savings Credit Union had the lowest rating in the category "Freedom To Make Objective (Financial / Investment) Product Choices (Recommendations)" (Investment Executive, July 2006)

Vancity Savings Credit Union offers rewards to their financial advisors from movie passes to dinner cruises during mutual fund sales campaigns or sales blitzes. National Bank offers their staff trips, CD players and Mastercard Reward Points. (Investment Executive, July 2006)

2006 limit for RRSP contributions is $18,000 or 18% of earned income whichever is less.

The most generous city in Canada for charitable donations is Abbotsford, B.C., with a median donation of $560 per person, followed by Toronto with a median of $350 per person. (Advisor.ca)

A common error people make is to judge the wisdom of a decision by its short-term outcome, an outcome of which most likely occurred by chance.

A money problem can't be solved with money.

Carey

Chartered Financial Planner