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C.E. VANDENBERG & ASSOCIATES INC.

Financial Planning— Insurance— Wealth Management

For more information

& contact details go to
www.careyvandenberg.com

Questions?

carey@careyvandenberg.com

604 541 2690

1 866 274 1222

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S Surrey / White Rock Office
13230—16th Avenue
South Surrey, B.C. V4A 1P3

Burnaby / Vancouver Office
4400 Dominion Street
Suite 410
Burnaby, B.C. V5G 4G3

More Pessimistic Than What The Facts Show

Templeton Growth Fund was created for Canadians in 1954 and, on average, has returned about 14.5% a year. An investment of $10,000 at that time would be worth nearly $5.8 million today, assuming all distributions were reinvested. One of Templeton's mantras was "invest worldwide." He took that to heart by investing in Japan before virtually anyone else, and making big financial gains there. He later applied his strategies in South Korea, among other foreign markets.

But Templeton's success didn't as much depend on investing in growing parts of the world as it did how he invested there. One of the financial guru's most famous quotes was, "The time of maximum pessimism is the best time to buy and the time of maximum optimism is the best time to sell." Despite the recent passing of Sir John Templeton, the philosophy of the investment firm which he started is still very applicable today, probably more so, as we just happen to be in one of those times of maximum pessimism.

Just ask any American how they think the economy is doing and you won’t get a middle of the road answer. Virtually all believe it’s downright awful. Consumer confidence is at its lowest level in almost 30 years and comparisons to the Great Depression are widespread. But frankly the reality is quite different. According to most broad measures of how the economy is doing, it's not nearly as grim as we perceive it to be.

Yes, the Red White & Blue economy is soft. Is the U.S. in a recession? It depends on who you ask. Although mortgage problems have been in the news and made us all nervous for several months now, so far the U.S. economy is holding up better than it did during the last two recessions (1990 and 2001). Companies aren’t laying off people as in times past and because of it the unemployment rate is still relatively low with productivity still rising. Yet, the last time U.S. consumers felt this bad was in May 1980, when unemployment was 7.5% and inflation was 14.4 %. Today in the U.S. those numbers are 5.5% and 4.2% respectively.

Why does it appear to be worse today? First is housing prices. Housing prices are falling across the U.S. and every home owner is feeling it. Reduce the value of a person’s house and spending habits ironically change dramatically. It has nothing to do with cash in versus cash going out, it’s simply a psychological reaction to feelings.

The second is gas prices. This too effect cuts across all economic status’ and unlike an increase in rent or mortgage payments, we see increased gas prices every single day, several times a day. Our car is filled up one, two, three times a week. We cringe every time we do and when we drive to go to buy our milk and bread we cringe again. When the news is turned on it’s all about those prices we just paid today.

So, despite an economy producing relatively good numbers in comparisons to previous economic slowdowns, the feeling among American consumers is not bad but terrible. This isn’t because it is so but simply because we have gotten so used to things being so good for so long. This makes these times seem bad more by feeling rather than by reality. The feelings permeate throughout the investment landscape as well and is reflected in investment prices which haven’t been this attractive in decades.

What to do with that information? Go out and apply some time tested advice from the highly successful investment manager, the late Sir John Templeton. "The time of maximum pessimism is the best time to buy….”

YOUR RRSP, RRIF, RESP ETC IS NOW CREDITOR PROOF

Protecting assets from creditors is a common concern among business owners and entrepreneurs, and until recently an investor's registered assets like an RRSP could not be taken by a creditors because of bankruptcy or legal action. This was completely different from the treatment of insurance investments like Segregated Funds and Registered Pension plan monies. These have never been able to be touched by creditors in a bankruptcy action.

That has changed with the passing into law of Bill C-12. As of July 7, 2008, all registered investments (RRSP, RRIF, RESP etc) will now enjoy the same creditor protection as insurance and pension investments. If you expect to be facing bankruptcy that doesn't mean you can take whatever money you have left and dump it into a Registered plan so as to intentionally keep your money of the hands of your creditors. Contributions made to an RRSP etc in the 12 months prior to bankruptcy will probably not be protected from creditors.

IMPROVE YOUR FINANCIAL LIFE BY WRITING IT DOWN

Can't seem to get control of your spending? Does it always seem you just get by, pay cheque to pay cheque, week after week, year after year? These two simple ideas may help you get on the right path, the one to financial freedom.

Training in all it's forms, whether it be to achieve Olympic medal performance or is as everyday as losing weight, writing down the steps you are taking along the way is the key to making your goals happen. To lose weight you need to write down in a log book what you ate during the day. This makes you aware of what is coming into your body and helps you determine how your habits can be modified to make your body goals happen.

It's no different with your money. It comes in because of your work efforts and goes out through various expenses, much of which can be of the "sand through the fingers" or "discretionary spending" variety. If you don't know where your money is going then how can you determine what habits you need to alter? The long term improvement of your financial position can only be done with writing down what is spent during a typical day. It is only then will you reveal where your expenses can be reduced.

Another way to do this, one which is particularly helpful for those whose strength is not in administration, is to use the envelope system. This means simply taking a fixed amount of money every day or week from your bank account and putting it in an envelope which you carry with you.

When that money is gone your spending stops. Do this for a few days or weeks and you will soon see where it's all going. It is from here where you can determine what habits need to be changed. And you will. Don't and you won't. Do and you will. It is this simple discipline that is the most important and powerful in determining your life's financial stability and escalating success. It is the small things that will be the difference between financial peace and life that runs on a treadmill of continuously digging one's self out of financial holes.

INVEST AS MUCH AS YOU CAN EARLY ON

That may seem like obvious wisdom however many of who have been there know that when we are younger our need for income is at it's highest yet our income is at the bottom of it's potential growth curve. As our life progresses the part of our income that we have saved tends to grow as does the amount that we can save thus creating a snowball effect of wealth building.

A paper written by two Yale University profs (Ian Iyres and Barry Nalebuff) and published by the U.S. National Bureau of Economic Research has shown that people understand and do diversification across different investments and geographies but they don't diversify by time period. In other words, most people don't have enough invested early on in their lives to use the time they have to it's maximum advantage.

The ability to get as much invested as possible early on in our working lives is difficult. The first substantial investment is usually the purchase of a home, but this too is usually done in the 30 something age bracket. The big reasons for this delay is two fold. The first is we often simply don't recognize the power of time on our side. The other is that usually a home purchase comes with a minimum level of debt we must incur. Often that amount is ominous.

However, the point here is in the power of the concept of getting as much as you can invested early on in life. People who have owned homes for much of their working lives have generally faired very will financially because an often enormous amount of debt has been taken on relatively early on in life to purchase an asset that has shown to appreciate over the long term.

The irony here is that we are often encouraged to buy a house using a significant amount of borrowed money, we are often discouraged and often prohibited from purchasing an equity portfolio using borrowed money, as it is viewed as short term speculation. Thus, younger people have little exposure to equities when the historical data proves that the cost to not being invested for the full amount of their lives is very costly.

Their report is based on back tested U.S. data from 1871 to 2007 and assumes 44 years of investing, starting at age 21 and retiring at 65. Using the study's model of applying a fixed amount of leverage when a person is young and slowly "deleveraging" or paying off that loan over a period of time shows that those who would have done that would be able to actually have less risk in their portfolio later in life.

This "deleveraging" concept is what most people do through the course of their lives. We borrow heavily for a home early on and pay it off over time and because of it, wealth is created. The research suggests the controversial, that investors should leverage their portfolios while they are young, to apply the same home leverage concept to one's investment portfolio or "retirement plan".

So how would this idea look like in practical terms? Take someone who has 10 or more working years ahead of them and either has a small, or no mortgage on their principal residence. Or maybe someone who has been and most likely will always be renting. In either of those cases, putting some leverage into a financial plan gives additional tax savings as the interest on the loan is tax deductible. The tax advantage of this increases with your income, with the maximum benefit enjoyed by those with over $123, 000 of taxable income.

One modified version of this concept which I have applied in some clients cases, particularly those who don't own their own home, is to borrow an amount of money that would be paid off over a period of several years. The amount of money that would be borrowed is determined by how much can be saved each month (on top of their RRSP contributions) along with when they expect to use this money. If the money is to increase a down payment on a first home the amount of mortgage financing needed will be much less which in the end reduces risk. Between now and then though, the person is using a customized amount of leverage, one that fits comfortably, earlier than they normally would.

Historically equities have returned about 9% while the cost of borrowing has averaged 5%. Add the benefit of tax deductible interest and you have a proven long term way of using the banks money, in an amount that is comfortable for your situation, to increase your wealth over and above what it would be if you hadn't. (Read leverage disclosure here - PIP Leverage Disclosure)

Save Tax By Converting Your RRSP To A RRIF Before Age 72

Conventional wisdom recommends you delay converting your RRSP to a RRIF as long as possible which is the year in which you turn 71. There is however an approximate $2,800 reason to move that conversion to an earlier date. It's all related to the pension credit which has been increased from $1,000 to $2,000.

The pension credit is only available starting in the year you turn 65 so if you aren't there yet you might just want to file this idea in your mind when you reach that age. If you are there and only get OAS and CPP benefits from the government then you may want to convert your RRSP to a RRIF now. That could save you approximately $400 in taxes each year.

Your modified plan would have you convert enough of your RRSP to a RRIF that will give you no more than the minimum RRIF payment of $2,000 per year. If you are 65 then $50,000 of RRSP should be converted to a RRIF (yes, you can have both a RRSP and a RRIF at the same time). The $2,000 of income you will be taking out will be offset by the $2,000 Pension Income Tax Credit. Don't need want to take that $2,000 out of your RRSP and pay as little tax as possible? You can do that but you will need to do one more step. Put the $2,000 per year back into your RRSP. You will need RRSP room of course to do this. At the end of the day you will have received a total of $2,800 in tax savings for the full amount of years in which this can be done (age 65 to 72).

Are you between 65 and 72 and unsure if this makes sense or are totally confused I'm happy to give you some direction. Call or email me directly. Who knows? That tax savings might have just bought you that nice little vacation you've wanted.

Your Will May Not Be "Your Will"

Just because you put your wishes in a Will doesn't mean your wishes are going to be followed through on. This is particularly true when it comes to your desire to leave one of your family members with much less than the others upon your death.

In B.C., the Will Variation Act gives your spouse and children the right to apply to court to increase their share in your estate. This doesn't mean that the court will intervene and change the distribution of your estate. The court does have the discretion to vary your Will based on certain conditions and if your child or spouse can show that you didn't make adequate provisions for them. The court will look at your family member's standard of living and financial need and what the court sees as fair under the circumstances will in the end determine what your family members, or others who rely on you financially, will get.

You can however make your Will more firm by putting your wishes and the reasoning behind the directions in your Will by way of a detailed written statement. In it you can explain that they have given that family member X amount of dollars already, that they owe you a large sum of money already and that their inheritance is a forgiveness of that debt or that you haven't talked in 10 years and thus the relationship has been severed. That is a much firmer way to ensure that "your will be done".

Like any financial arrangements or plans it is always recommended that the proper professional be consulted. With a Will it is normally a lawyer. Should you require a suggestion on who to call in that regard I would be happy to give you the name of a lawyer who might be able to help.

Web Gems

VOLWEB— This is the place to go to for finding a place to volunteer www.volweb.ca/volweb/. Simply put in what kind of areas you want to help in and in what capacity, your skills etc and all kinds of opportunities will present themselves for you to help out in. You will even get emails when events fit your strengths, skills and preferred criteria. You can accept or reject these offers to volunteer. Get out and get involved. Meet new people.

EDMUNDS—Get other people's opinions and experiences on the kind of car you are looking at getting. This site will help steer you in the right direction and help you avoid an avalanche of repair bills on your used car purchase. You can simply go to www.edmunds.com then click on "Car Reviews" and then "Consumer Ratings".

SEAT GURU— If you fly regularly www.seatguru.com is a great resource to determine what seats are the best for any given aircraft, and more importantly, which ones to avoid. You can click on the airline you are looking at flying with, click on the plane for that particular flight and you will have a complete floor map of the plan. It isn't a big deal when you can't recline your seat on a flight from Vancouver to Calgary but to Europe, Australia or Hong Kong?

Hhhhhmmmmm……

"Spending on fuel as a share of wage income has shot above 6%. That exceeds the percentage seen during the 1974-75 and 1990-91 oil-price shocks and approaches the 7% to 8% seen during the 1979-81 price surge." Sherry Cooper, BMO Capital Market's Chief Economist, June 2008

Russia is the world's biggest producer of both oil (10 million barrels / day) and natural gas in terms of annual production. 2nd is Saudi Arabia (8.2 million barrels / day). The U.S. is 3rd (7.8 million barrels / day). (International Energy Agency)

Japan's Nikkei average fell 1.3 per cent as worries about the global economy hit exporters such as Canon Inc. The loss marked its 10th straight negative day, its longest losing streak since February-March 1965. (Globe & Mail, July 2008)

The majority of investment managers who run large pools of investment assets see the U.S. as the offering the most attractive investment opportunities. The average investor on the other hand views the U.S. as the worst place to invest.

"Someone who wasn't buying BMO two weeks ago, and wants to buy it now, but it has moved up 20%, ask them why? What was the mindset two weeks ago when you wouldn't buy it, but you want it now?"
Garey Aitken, CIO Bissett Investment Management

Since 1969, 43 financial institutions in Canada have shut down, putting 25 billion deposits at risk, including accounts at the Security Home Mortgage Corporation in 1996 and the Confederation Trust Company in 1994. These banks didn't fail because of some freak-ish accident or major fraud; they closed their doors due to the same events happening in the markets right now. Advisor.ca July 2008

The Canadian economy lost 55,000 jobs net in July, the largest los of jobs we've seen in 17 years (StatsCan, Augus 2008)

Late in June, shares of GM hit $11.21 which is what they were worth in 1955. This factors in stock splits, spinoffs and other dilutions, the $107 share price of 1955 is worth precisely the same as the $11 in 2008. Richard C. Young, Intelligence Report

"There are two kinds of people using premium gas: Those who have a car that requires it, and the other kind is a person who likes to waste money," Jake Fisher, Senior Engineer *Consumer Reports.*

Carey

Chartered Financial Planner

PS. It has on occasion been requested that I put specific investment opportunities / recommendations in my bulletins and in the pages of "mutual gains". "Promoting" specific investments in communications that may go to those who are not clients of Partners In Planning Financial Services requires much time in adhering to our firm's compliance rules as well as the rules and regulations of the various regulatory bodies. This creates long delays in getting timely information to you. The first priority remains to my clients and the responsibility I have to them. Also, investments that fit for one person may not necessarily be appropriate for another. This can only be really determined if an active client—financial planner / advisor relationship exists. Thanks for your understanding. It's very much appreciated.