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mutual gains™

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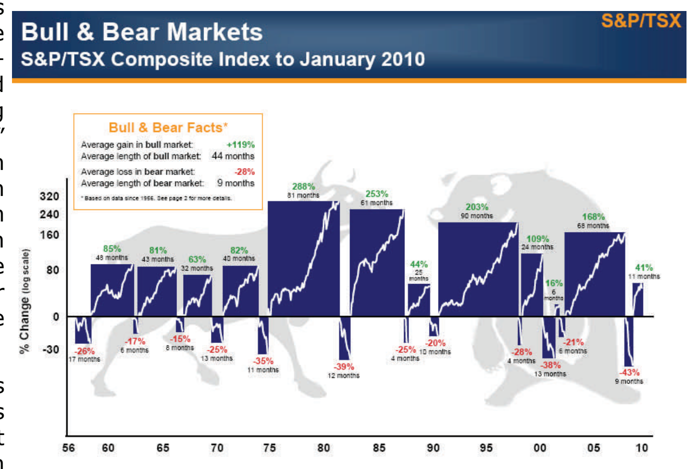
The Pause That Refreshes On Recovery Road

After a significant, virtually uninterrupted upward trajectory since last March it seems the positive market momentum is taking a breather. This is to be expected and normal and very healthy after a steady upward climb.

Frankly, I have been a little cynical about the short term strength of the economy, particularly since we have quickly gone from so many thinking we were going into another "Depression" less than a year ago. Now, it seems it's "Life In The Fast Lane" again. I never believed the Depression scenario back then. Today though, a lot of people are racking up debt again, both mortgages and consumer debt, throwing prudent caution to the wind. The banks have even expressed concern in this regard. But I digress.

Just how closely your own portfolio's performance has mirrored the rebound in the broader markets depends on several factors, including overall asset allocation, geographical diversification, and the decisions made by individual portfolio managers you may have working for you on your behalf.

However, the year's events underscore the importance of a structured, well-diversified portfolio, and of avoiding the temptation to "time" the markets by jumping in and out of investments in reaction to short-term conditions. Investors with the fortitude to stay the course over the past year have benefited from the turnaround.



Source: Mackenzie Financial (Datastream: month-end data points as at January 31, 2010; total return, local currency)

If your portfolio remains invested as it always has and you feel it hasn't seemed bounce back in line with the indexes (namely the TSX and the S&P 500) you may be feeling the itch or pressure to make some changes. Change for change's sake could work against you.

During this upswing it seems that companies that were subpar in terms of financial strength and sustainability of earnings were the ones whose share prices increased the most.

Case in point. Berkshire Hathaway Inc., the best long term performing investment portfolio in modern history, which Warren Buffett has so successfully led as chairman for more than four decades, advanced 2.7% on the New York Stock Exchange in 2009, less than the 23% return in the Standard & Poor's 500 Index. (Financial Post, Jan 2010)

In other words, quality, name brand, lower risk companies have actually lagged in terms of their share price appreciation. This is normal after a significant decline like we saw as the speculative, "in and out" investment money tends to try to make a quick buck from the off the bottom bounce. Don't fret. Your patience will be well rewarded in time.

Why Employing High Quality Investment Management Is Worth It

Among the many quantitative criteria of evaluating investments practiced by the majority of the portfolio managers I use for clients is valuation. That one criterion is the most important and is really the difference between long term success and failure. A thorough analysis of a company's other attributes can be quickly undermined if too much is paid for its shares.

By nature, these investment managers are cautious and frugal, wanting to know when the investment will be paid back. Seeking confidence that, if all doesn't go as planned for the company, probable downside is limited and manageable. Conversely, individual investors and many money managers alike routinely set aside the financial conservatism that guides purchases in other areas of their lives to acquire lavishly priced stocks in their investment portfolios.

This most often occurs when a company or industry captures the public imagination. Nobody seems to want to miss out on the "story's" opportunity. When that 'story' is so compelling the calculations used in determining a prudent price for the investment is ignored by so many. This has happened recently in the story of one of Canada's great new companies. It provides a lesson in what can happen when principals of value are overlooked in pursuit of a big gain or "home run".

In the summer of 2008, shares of Research in Motion (the maker of the Blackberry) traded at a Price to Earnings (PE) multiple of nearly 50 times. This meant that, if the company didn't grow from that point forward, it would have taken 50 years for the earnings of the company to pay back one's investment in the company. Of course, at that time, many implored in unison that such a line of analysis shouldn't be looked at. RIM was different. RIM had a first mover advantage in the fast growing smartphone arena. Their head start would allow it to maintain its healthy market share and hefty profit margins as far as the eye could see. In other words, earnings would be climbing so fast that considering any other scenario was pointless.

Since that time, Apple's I Phone has emerged as a serious competitive threat to RIM's Blackberry and, along with its groundbreaking technological advances. The I Phone has become the undisputed embodiment of cell phone "cool" which has started to make the Blackberry appear to have become "your father's smartphone".

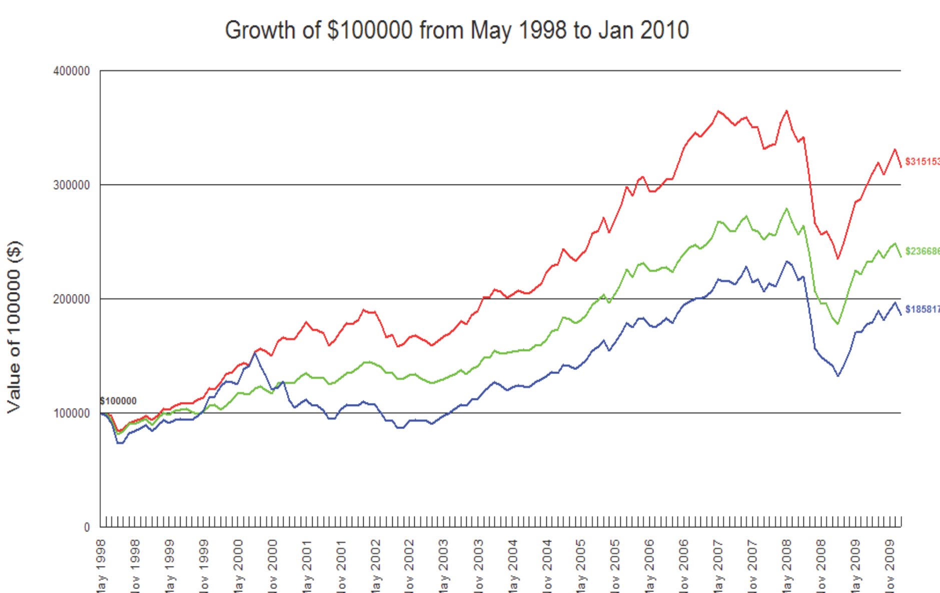
Other entrants to the smartphone arena, such as the highly regarded Palm Pre and the recently released Motorola Android are also taking sizeable bites out of RIM's prior dominance, helping to crowd a space that was recently unpopulated. In response, RIM shares have been losing their luster very quickly. Many are realizing that the company can't grow like it has in the past.

Since the summer of 2008, the PE multiple on RIM has receded to just 17 times. Instead of this ratio falling due to RIM's earnings exploding upward, it has resulted from a plunge in share price. RIM shares traded at $140 in June 2008, at $92 this past September, and now resides in the $70 range.

RIM makes a fantastic product and is one of Canada's few non-resource global stars. Its stock, however, was priced for perfection under the assumption that the company would continue to grow at a stellar rate and RIM's competitors wouldn't work feverishly to eat at it's market dominance.

Going forward, RIM will have to continue to innovate to maintain its position and may even be required to compete on price. These are characteristics of a maturing firm, one whose shares are likely to trade at a valuation more in line with the rest or "average" of the market.

I give you that RIM example to show why disciplined investment management is crucial to reduce the risk and in time, give you superior investment portfolio performance.



You will see a chart comparing 2, of many portfolio managers I have used for several years (one since 1987). This shows their portfolios against the benchmark that they are measured against, namely the S&P / TSX Composite Index (the **Red** Line). You will see that, despite the internal costs of using a investment manager to run different parts of your portfolio, benefits in both performance and reduction in risk far outweigh the costs. If you had invested in the S&P / TSX Index in the summer of June 2000 when everyone thought investing was easy) it would have taken 5 years to recoup your investment). It may not show in the short term, but the benefits of high quality investment management, coupled with the coaching of your own, personal Financial Planner, will definitely become evident and very clear over time. (Read Disclaimer, bottom of page 5)

Source: Dixon Mitchell Investment Counsel, Morningstar Research Inc.; Morningstar Research

IPP—The Super Sized RRSP

If you are a business owner, senior executive or incorporated professional, you may be constantly disgruntled and dismayed at having to shell out hefty tax dollars to the government year after year. The RRSP contribution has often been the first line of defence against that. You can however ease your income tax pain even more by using an Individual Pension Plans (IPP) instead of an RRSP.

Age	IPP	RRSP	IPP Advantage
40	$82,000	$21,000	+$61,000
50	$169,100	$21,000	+$148,100
60	$274,300	$21,000	+$253,300
Based on $118,000 Income Source: Canadian Western Trust 07 2009			

Let's use a scenario of a professional earning upward of $300,000 a year. Even if he were to max out his RRSP room of $21,000, it would still represent just 7% of his total income. An IPP contribution could be topped off at a little more than 30% depending on age and the amount being transferred into the IPP from an existing RRSP. The older you are, the higher your allowable contribution amount. In an actuarial best case scenario up to $3 million could be contributed to an IPP.

There are 3 main variables that will determine if an IPP makes sense for you. The first and most important is your age. The IPP numbers can start to work as early as age 40 but it looks more and more attractive the older you are. The second is your income. $75,000 is the benchmark. Again, like age, more is better. Thirdly, it's the years you have been employed by your company.

An IPP is designed to provide retirement income. It is the very much a pension plan. Like with any kind of pension plan, the idea is to average 7.5% growth performance over a 3 year period. If the IPP is underperforming, the actuarial firm you choose to administer the plan will require your IPP be topped so as to provide you sufficient income when you retire.

Having to add extra money isn't necessarily a bad thing. If your IPP is underperforming you will be able to take out a bunch of retained earnings from your company and get more in tax deductions, something you can't do with an RRSP.

Why RRSP Contributions Make So Much Sense

The limit for RRSP contributions is $21,000 for the 2009 tax year or 18% of earned income, whichever is less. Many people don't use near the amount they have available to them. That is understandable. Socking away 18% of one's income for "retirement" can be quite the financial cash flow sacrifice for many however it's much less costly than it appears. That cost advantage one of the key things that makes RRSP contributions quite lucrative in building your net worth substantially over time.

2009 B.C. Total Tax Rates	
first $35,716	20.06%
over $35,716 up to $38,832	22.70%
over $38,832 up to $71,433	29.70%
over $71,433 up to $77,664	32.50%
over $77,664 up to $82,014	36.50%
over $82,014 up to $99,588	38.29%
over $99,588 up to $126,264	40.70%
Over $126,264	43.70%

I'm sure you know that an RRSP contribution will reduce your taxes. Most people experience that when they get a tax refund. That tax savings is the key reason that annual RRSP contributions are much more advantageous than the alternatives. Let me show you why I am convinced of that.

For every $1,000 in RRSP contributions the government pays you back a percentage of the tax they've taken from you throughout the year. If, as an example, you earned $92,000 in 2009 you will be given back $38.30 for every $100 you put into an RRSP. In other words, if you put $10,000 into your RRSP you are getting back $3,830 from the government. You are now $3,830 richer. That $10,000 has turned into $13,830. Your RRSP contribution has given you a 38.3% return the minute you made the contribution.

Probably the most common question I've been asked during my past 23 years as a Financial Planner is, "should I contribute to my RRSP or paydown my mortgage?" (I'm 46 now so I'm sure I'll be asked this still for many more years to come). Although a mortgage pay down may feel more comfortable; the RRSP contribution in most cases puts you farther ahead financially. It gives you more money to work with,

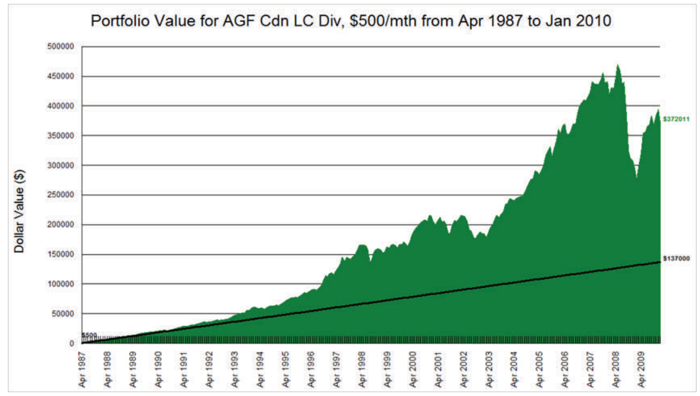
Do you want to do some of your own calculations on that? You can find a very nice Mortgage Paydown versus RRSP Contribution calculator on our calculator page.

Pay Yourself Like You Pay Everyone Else

In 1987 when I started in the Financial Services field I read "The Richest Man In Bablyon" which was originally published in 1926. You may be more familiar with the modern version, "The Wealthy Barber". That too I read many years ago.

Both of these books are simplistic yet powerful. The simplicity is that they talk about taking a part of every dollar you earn and investing it for the long term. Over the course of a month you pay the bank their mortgage payments, the government it's taxes, the phone company for various phones and internet use, the gas station for fuel, etc. What you pay yourself it seems is whatever is left over, if anything. The key is to turn that completely around by paying YOU first and paying everyone else with the other 90%. By doing so you are setting aside a portion of your lifetime income to create an investment pool that will give you an income for your future. A pool of money that can work for you so eventually you don't have to. In the Richest Man In Babylon it refers to your dollars creating offspring, and their offspring creating offspring, and so on and so on. If you are giving all of your offspring so to speak, to everyone else, you have nothing to work for you.

The point however I want to make is not to try and convince you of the power of this simple principle. I know you probably understand that already. What I has been very clear to me having gone through this downswing we have experienced over the past year and a half is that the clients I work with, those who have adopted and stuck to monthly and to a lesser degree, annual saving habit, have overall, produced the best investment returns over time.



It hasn't necessarily been due to picking the absolute best investments. It hasn't really had anything to do with financial prowess. The power has been in the simplicity of a habit. The habit and discipline of investing a fixed amount of money every month, year in and year out. Sticking with it, despite the news of the day and what is happening in the "markets". In fact, the volatility of the "market" has contributed to the success of this simple, historically proven wealth building strategy with the principle of "dollar cost averaging" where down is good.

Note: The chart on the right shows $500 per month in a portfolio managed by Connor Clark & Lunn, one of the investment managers I have used for a portion of my clients portfolios since 1987. The straight black, slowly ascending line is the amount of deposits invested over time. The green is the investment growth. The success has been in the habit and sticking to the habit. Have you started yours? Source: Morningstar Research (Read Disclaimer, bottom of page 5)

Mitigating Risk For The Single Person

According to Stats Canada, almost 52% of people aged 15 and over are unattached. Also, for the first time ever in Canada, there are more families without children than there are with. Also, 26% of families are headed by a single parent.

Mitigating risk is one of the pillars of holistic financial planning. Being single, not having he ability to rely on someone else has significant ramifications on the risk side of the ledger in a financial planning context. If you are single, the biggest risk is of potentially not having someone there who could assist you in your living requirements should you not be able to. That could apply in your old age but it also could prove to be the case should you be faced with a debilitating illness or disability.

There are many ways to protect yourself from those risks. Disability insurance can provide the income you need should you become disabled during your working years. A feature I've often added to that is what is called "Return of Premium". In that, you get 50% of your premiums back every 8 years if you haven't claimed on your policy (both my wife Cheryl and I are expecting 2 cheques as we will be soon reaching one of those 8 year benchmarks on our own disability insurance policies.

Critical illness is another risk that can be more financially upsetting if you are single. If you get cancer, have a stroke or heart attack to name just a few "critical illnesses" a Critical Illness (CI) policy will provide you a lump sum of cash so you can work at healing rather than having to earn an income.

Worried about not being able to get the care you may need in your old age? You can put your mind at ease knowing your costs are covered if, as you get older, you need care because of health conditions such as Alzheimer's or Dementia. Long Term Care (LTC) insurance offsets that risk and pays you a monthly amount as long as you need care.

Even if you have a group plan at work don't assume you are covered from all possible risks. I've seen on many occasions, after reviewing a new client's financial plan, large risk holes.

Use Your TFSA To Give You A Guaranteed, Tax Free Income For Life

Are you contributing to a TFSA? Is that TFSA sitting in a savings account? Will you most likely be adding to your TFSA annually? Will that money probably sit there for years? Would you like that money to potentially be able to give you a guaranteed, tax free income for life?

If you said, Yes, Yes, Yes and YES, then you could be setting yourself up with exactly that, a guaranteed 5% income paid to you every year for your entire retirement starting at age 65. Every year you don't take that annual withdrawal, your guaranteed income amount increases every year by 5%. No matter which of the respective life insurance company's investments you choose and how poorly they do, that 5% income amount is guaranteed. Also, because it is inside your TFSA the income and the entire portfolio's interest dividends or capital gains are all TAX FREE... for the rest of your life.

Think it's too late to do start this? Consider this. If you are 54 years of age and you contribute $5,000 into a TFSA every year for the next 10 years, you will have a guaranteed, tax free income of at the very least, $3,187.50 per year. It could be higher but you have peace of mind knowing exactly what you will get that income even if you live well past 100.

Web Gems

Canada's Olympic Team— Click on the "Vancouver 2010" on the top bar of the www.Olympic.ca site and you will see all the details of our 206 member team. This includes every member of both our hockey teams. You can see their pics, personal and competitive stats, what they have done in the past and if you like, leave a message for any of Canada's team members.

Hhhmmmmmmm......

Ontario Teachers Pension Plan (OTPP) is buying Simmons Co. the soon to be largest mattress maker in North America. The OTPP already owns Serta Intl., the 3rd largest mattress maker. Report On Business, Dec 2009

Colorado announced this week it will become the first state to lower its minimum wage since the federal minimum wage law was passed in 1938. The state will cut its rate by 4 cents to $7.24 an hour Jan. 1, to reflect a drop in the consumer price index. USA Today, Oct 2009

Manufacturers of computer printers sell their printers at a loss and recoup the money from the sales of their ink. That seems to work for HP which has the largest market share but unbeknownst to many consumers has some of the most expensive per page in print costs. A complete replacement of your ink cartridges could cost you more than the printer. USA Today, Nov 2009

In the mid-1980s, the average car accelerated from zero to 60 mph in 14 seconds. Today, it's 9 seconds with average gas mileage during the period not changing much. Many car companies are now only offering 4 cylinder engines in some of their cars for improved fuel economy. Some are adding turbo chargers to boost performance. Mazda's goal is to raise fuel efficiency 30% worldwide by 2015 and will do that with things like auto shut off at lights. It is expected that by 2020 only 10% of cars will be electric. USA Today

On the last Wednesday of October, North American stock markets slumped 2% on the news that new home sales in the U.S. fell 3.6 per cent in September. The following day, markets rose a similar amount, thanks to a report that showed the economy expanded 3.5 per cent from July through September. Globe & Mail, Nov 2009

In 1945, the U.S. debt was 121.7% of GDP, vs. an estimated 70% today, according to the Economic Report to the President. As the nation's debt became a smaller part of GDP, the debt became much less burdensome, much as a fixed mortgage payment becomes more affordable as your income grows.

The Congressional Budget Office estimates the U.S. federal government will owe more than $6 trillion (U.S.) by the end of its current fiscal year. That would be equal to about 54% of GDP, the highest ratio since 1955. Toronto Star, Dec 2009

Fighting a war is one of the most reliable ways to create a big debt. The British, for example, finished repaying their World War II debt to the U.S. in 2007. Germany will finish repaying its World War I reparations in 2010. Every Allied nation except Finland defaulted on its World War I debt to the U.S. USA Today, January 2010

The debt-to-income ratio among households hit a record this year. The latest Statscan report showed that for every $100 of personal disposable income, Canadians are carrying $145 in debt, up sharply from $88.60 in 1990. The ballooning debt comes at a time when the Bank of Canada is warning of higher interest rates. This is the first recession in which real credit, the amount of debt that people are taking on adjusted for inflation, has risen. While U.S. consumers are de-leveraging, Canadians continue to rack up debt. Globe & Mail, Feb 2010

In the 12 months ended August 2009, residential mortgage debt grew by 7.1%. That is despite many people having much more of their mortgage payments going toward principal because of the ultra low interest rates. (Investment Executive, Dec 2009)

The percentage of the population that owns their own home is at an almost 40-year high. Globe & Mail, Feb 2010

Ideally, you're supposed to keep a surplus in good times and deficits in the bad times. That's the advice Joseph gave to Pharaoh 3,000 years ago. He was the last politician to take that advice." USA Today, January 2010

Cows, sheep and other cud-chewing animals are the worst polluters responsible for about 50% more greenhouse gas than the entire transportation sector. (Mackenzie Financial Corp)

Carey

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