

ClientTel



*The central message of ClientTel is that I value my clients.
I'm as close as your telephone, and available
and delighted to serve you.*

David Chalmers BA, FLMI, CLU, CFP, RFP, ChFC

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Welcome to another issue of **ClientTel** – a newsletter for the clients of David Chalmers and Dylan Reece of Rogers Group Financial.

The purpose of this ClientTel is to discuss the following matters:

- **Market Volatility – *how is the financial crisis affecting me?***
- **Tax Free Savings Accounts – *when, where and how?***

STOCK MARKET VOLATILITY

The intention of this section of the newsletter is to provide a summary of what is transpiring in financial markets, and what we have done, as your Financial Advisors, to prepare your portfolios for market corrections such as this (and this financial crisis in particular).

Note that we are not recommending any material changes to our clients' portfolios at this time, as your long-term financial and investment objectives have not likely changed (please let us know if this is not the case). Note that it may *feel/like* your risk tolerance is decreasing during times like these, and we empathize with the uncertainty that you may be feeling at this time.

Before we begin, we want to state that our clients do not have any direct or significant holdings in banks, investment dealers, or insurance companies in the United States, and thus the following commentary regarding US bankruptcies (generally) does not apply to our clients. In fact, while stock markets have continued to be very volatile, our clients' portfolios are "weathering the storm" relatively well.

The Current Financial Crisis

As we write this newsletter (September 17, 2008) the “financial crisis” stemming from the United States continues unabated.

Over the weekend, Lehman Brothers, a 158 year old US investment bank, declared bankruptcy (the largest in US history) and Merrill Lynch agreed to be taken over by Bank of America in an effort to stave off its own bankruptcy. Just a few weeks prior the US Treasury bailed out Freddie Mac and Freddie Mac, two of the largest mortgage insurers, and yesterday the government made a move to take over 80% of the world’s largest insurance company, AIG, as they were all “too big to fail”.

The effective collapse of these large US financial institutions have caused investors to wonder when the bankruptcies will end and whether we are headed for a global recession; as a result stock markets have reacted negatively (the US market was down 4.5% on Monday and 4.7% today). What’s more, the front pages of the Canadian newspapers make it appear as if Financial Armageddon has finally descended (“A Day of Reckoning” according to Tuesday’s front page of the Globe & Mail’s Report on Business).

While these are not insignificant events, it is our opinion that these bankruptcies were somewhat inevitable given the inadequate regulation of banks and hedge funds, and the seemingly egregious behaviour of the management who ran these firms. These financial institutions borrowed too much money (30 to 1 in many cases) and either loaned the money to people they should not have (individuals with no jobs, assets and credit should not be receiving mortgages) and/or invested in seemingly “risk-free” mortgage investments which subsequently disintegrated due to falling US real estate values.

It is our opinion that these bankruptcies are in fact “healthy” for the financial system over the *long-term* (but certainly not the short-term). Banks will learn they cannot continue to borrow excessively or take unreasonable risks with their capital (just as an individual should not borrow beyond their means and spend carelessly).

Unfortunately, it is not just the shareholders of these US banks (and to lesser degree Canadian banks) that are being punished, but stock markets across the globe are falling as banks and hedge funds must sell their assets in a “fire sale” to cover bad loans, reduce their debt levels, and facilitate withdrawals.

In other words, the sell-off in global stock markets has been widespread, and even the good quality companies that continue to have solid business plans and generate stable profits have seen their share prices drop (in many cases for no good reason). In times of investor uncertainty (or even panic and fear), “the baby is thrown out with the bathwater”.

It is in these times that great long-term buying opportunities present themselves.

Be Greedy When Others are Fearful...

Warren Buffett, arguably the world's most successful investor, and the wealthiest individual in the US as a result, is famous for saying; "*a successful investor must be fearful when others are greedy and greedy when others are fearful*". In other words, "buy low and sell high".

Unfortunately, the human brain is not designed to think in a contrarian manner when it comes to investments, and historically the average investor does the wrong thing at the wrong time. Investors tend to rush into stocks and real estate when markets are hitting all-time highs (think technology bubble of 2000 and US real estate bubble of 2006...arguably the Vancouver real estate bubble of 2007 may be beginning to unwind as we speak). And almost without fail, they capitulate and sell when markets crash.

The timeless adage of "buy low and sell high" always seems to be swept aside in the wake of greed and fear.

Preparing Client Portfolios

If you read our newsletters over the last three years (both the "ClienTel" and "Andex Letter" – all available on www.rogersgroup.com), which were written when stock markets were hitting all-time highs and thus before this financial crisis really took hold, we discussed the possibility of a pending market correction, and one that could be worse than normal (such as the financial crisis we are experiencing today).

In preparation of this market correction (as we know that markets will, on average, suffer losses three years in every 10), we reviewed the risk tolerance and investment objectives of our clients, and the "asset class allocation" of their portfolios (i.e. the percentage of the portfolio that is in Fixed Income investments such as GICs and Bonds, and the percentage in Equity investments), and made changes as required.

In addition, we have been recommending for over three years that clients hold at least 5% of their portfolio in Precious Metals (gold, silver and platinum bullion) as a possible "hedge" against a falling US dollar, rising inflation, and/or a widespread lack of confidence in the financial system (all of which have come to fruition). Since that time, the price of Precious Metals has risen significantly.

Given the increased financial risks in the global economy, we now recommend a weighting of 10% in Precious Metals holdings (e.g. BMG Bullion Fund or Central Fund of Canada stock).

Again, we are not speculating on the price of gold or silver, but rather using it as an insurance policy against further losses in stock markets (gold tends to rise when markets fall...for example, gold rose 9% today while the Canadian stock

market fell by 2.8% and the US market dropped by 4.7%). Of course, the price of gold and silver may not always rise if stock markets fall, and the movement in the price of Precious Metals can be extremely volatile on a day-to-day basis.

In addition, when we choose portfolio managers to pick individual stocks on our behalf (in the form of a mutual fund), we are looking for conservative managers who have a proven history of generating reasonable returns when stock markets are good, and most importantly, protecting capital when markets were falling (again, markets tend to produce negative returns three years in every 10).

The portfolio managers that we have recommended on your behalf have indeed protected capital relatively well, as most have produced better returns than stock market indices (i.e. they have lost less than the market as a whole).

Finally, we have diversified the Equity holdings among a number of portfolio managers, countries, industry sectors and market capitalization (i.e. large, medium and small companies) in an attempt to “spread our eggs in many baskets” (and thus reduce the risk of significant losses).

For our retired clients, we have ensured that we have enough cash and Fixed Income investments (GICs and Bonds) in the portfolio in which to create the required retirement income for at least three to 10 years without having to sell any equity investments (thus avoiding having to sell when equity markets are down).

To summarize, we have been preparing your portfolios to weather this market uncertainty by:

- Ensuring you have the appropriate amount of “safe” investments (GICs and Bonds)
- Holding Precious Metals as a “hedge” against financial disorder
- Diversifying your Equity holdings

In hindsight, we are very pleased with results of the preparation.

Moving Forward

So what should our clients be doing for the remainder of this market correction, the duration of which no one knows? (This could be one day, six months, or two years)

Assuming your risk tolerance and investment objectives have not changed, then we recommend that we adhere to our long-term investment strategy and make no material changes.

As discussed above, we are recommending an increase in Precious Metals holdings to 10% to increase our “insurance” position.

For clients who are retired, we will continue to create your income via Money Market Funds, Bond Funds and/or maturing GICs. We may also want to “rebalance” your portfolio to our long-term asset allocation target buy adding a small amount to your equity positions (buy low).

For our clients who have not yet retired, then this financial crisis, touted as “the worst since the Great Depression”, will likely create the single greatest buying opportunity since the 1920’s. In other words, now is a reasonable time to be adding to your equity positions in order to (hopefully) reap gains over the long-term.

The challenge is trying to determine when markets will “bottom”, as one is naturally hesitant to buy Equity investments when stock markets may continue to fall.

Given that timing the market is virtually impossible, we recommend clients “dollar cost average” into the markets. By this we mean making automatic monthly contributions to your investment portfolios (which many of you are doing already). For those who are sitting on larger cash positions (e.g. from the receipt of an inheritance or the sale of a real estate property), then we recommend slowly adding to your equity positions over a series of months (similar to making automatic monthly contributions).

Of course, the amount you invest in Equities versus Fixed Income investments will depend on your age, risk tolerance, objectives and overall financial position. We will discuss an appropriate strategy with you based on your unique position.

Finally, as this crisis and market correction could last months or even years, we ask that you stay patient with your investment strategy and know that we, as your financial stewards, have your best interests at heart. Your continued financial independence is our top priority.

Please do not hesitate to contact us if you have any questions regarding this article, or if you would like to arrange for a meeting to discuss your portfolio.

TAX FREE SAVINGS ACCOUNTS

Now for some good news!

The last Federal Budget announced the creation of the “Tax Free Savings Account” (TFSA). David Chalmers wrote about this new savings account in the last edition of the “Financialist” newsletter, and this article can be found on our website.

www.rogersgroup.com/Content/Newsletters/articles/DC_IND_TaxFreeSavingsAccounts.pdf

The purpose of this section is to briefly summarize the key benefits of the TSFA and our recommendations for setting up these new accounts in January 2009.

Starting in 2009, all Canadians over 18 years of age will be allowed to deposit up to \$5,000 a year (adjusted for inflation to the nearest \$500) to a TFSA. If you don't make your maximum contribution, you can carry it forward and make it in a subsequent year (similar to an RRSP).

Contributions are not tax-deductible; however, all investment earnings within a TFSA will be tax-sheltered and all withdrawals will be tax-free (and will not count as income when determining the Old Age Security clawback).

When you make a withdrawal, you are allowed to re-deposit the amount of the withdrawal to your TFSA at anytime (in addition to your regular deposit allowance).

This is the first completely TAX FREE savings account in Canada, and its importance in your overall financial and tax planning cannot be understated. While the \$5,000 annual limit may make this strategy appear to be of nominal value, let us illustrate the following comparison.

Assuming you are in the 31% marginal tax bracket, and you make annual deposits of \$5,000 to an RRSP, regular (taxable) non-registered account, and a TFSA over a 15 year period. Let us further assume that you also reinvest the \$1,550 tax refund generated by the \$5,000 RRSP deposit, that the investment income in the regular (taxable) non-registered account is taxed annually, and you earn a 7% investment return in all three accounts. At the end of the 15-year savings period, you liquidate the accounts and pay any necessary taxes.

The amount of capital that you would have accumulated is summarized as follows:

Account:	RRSP	Taxable Non-Registered Account	Tax Free Savings Account
Pre-Tax Amount	\$176,116	\$111,667	\$134,440
Tax Upon Withdrawal	(54,596)	\$0	\$0
After-Tax Amount	\$121,520	\$111,667	\$134,440

Therefore, the TSFA provides 10.6% more after-tax income than the RRSP and 20.4% more than the traditional taxable non-registered account!

If you are not yet retired, you might ask if you should contribute to a TSFA *instead* of an RRSP. Our answer is yes if your taxable income is less than \$38,000 per year, but a definite no if your income exceeds this threshold.

Assuming your income is greater than \$38,000, we continue to recommend that you maximize your RRSP Deduction Limit, and allocate any additional savings to the TFSA (up to the \$5,000 annual limit).

For those of you whom are retired, we would almost certainly recommend you open a TFSA.

For anyone with short-term savings (say in an ING Bank account), we first recommend allocating your short-term cash savings to a high yield TSFA.

ING Bank will be offering these plans in January 2009, and we can open these accounts on your behalf.

For example, if you already have a (taxable) ING Bank savings account then you should immediately transfer \$5,000 from this old ING account to the new ING Bank TFSA.

Once you have built up this ING Bank TFSA to a reasonable level (amount will depend on your unique cash needs) then we would recommend opening a second TFSA in which to hold other investments, such as GICs, Bonds, Mutual Funds and stocks etc.

If you have an existing non-registered account with these investments, then we can commence the transfer of these investments to the new TFSA (up to \$5,000 per year). Eventually (over a number of years) we will be able to transition part or all of your investments from the taxable account to the TFSA, and you will no longer pay tax on this investment income!

Not only will you pay no tax, but also filing your tax returns will become much simpler! (Your accountant will thank us)

We will discuss these accounts with you in greater detail in our periodic financial reviews.

Thank you for reading this edition of the Clientel. And thank you for your continued business and trust, both of which are greatly appreciated.

Sincerely,

Dylan Reece, DipIT CFP CLU
Financial Advisor
Direct Tel: (604)737-6744
dreece@rogersgroup.com

David Chalmers, CLU CFP RFP CHFC
Financial Advisor
Direct Tel: (604)737-6736
dchalmers@rogersgroup.com

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