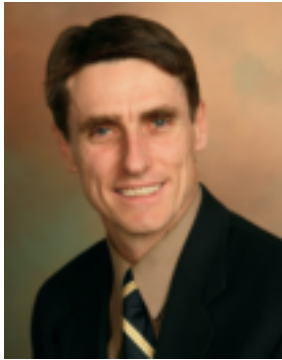


# Portfolio advisor

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Summer 2009



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## Taking positive action in negative times



During negative economic times, people naturally become more cautious about their money. But despite all the doom and gloom making headlines, there are several positive steps you can take now to help rebuild and protect your family's financial security.

**In this issue of *Portfolio Advisor*, we highlight proactive steps you can take to:**

- Ensure your investments are properly positioned for a market recovery
- Build long-term wealth in smarter ways than stashing money under the mattress (or in money market funds)
- Take advantage of new opportunities to reduce your single biggest expense – taxes
- Overcome today's historically low interest rates to enhance your retirement income
- Create a new financial plan for your new financial realities

## Get ready for recovery

**If history is any guide, both the economy and the markets will eventually recover – despite all the negative headlines. As an investor, it's important to be properly positioned for the recovery well in advance.**

No one can say exactly when we'll see a recovery. What looks like the beginning of a new long-term bull market today could turn out to be a short-lived “bear market rally” months from now – or vice versa.

The key thing for investors to know is that the markets have always recovered strongly, even after a major economic crisis that, at the time, had many people doubting they ever would. There have been other downturns as severe as the current one – The Oil Crisis (1973-75), The Early '80s Recession (1980-82), Black Monday (1987) and the Technology Bubble (2000-2001), to name a few. Each time, after suffering a major setback, the markets recovered and continued their long-term upward advance, typically making up losses within two years.

### History lessons: The market always comes back

	Decline	One-year returns from end	Two-year returns from end
The Oil Crisis	-48.2%	32.0%	65.6%
The Early '80s Recession	-27.1%	51.8%	50.2%
Black Monday	-33.5%	18.8%	37.7%
The Technology Bubble	-49.1%	22.2%	17.7%

S&P 500 Index Bear Markets (RBC Asset Management)

### STOCKS GENERALLY RECOVER BEFORE THE ECONOMY

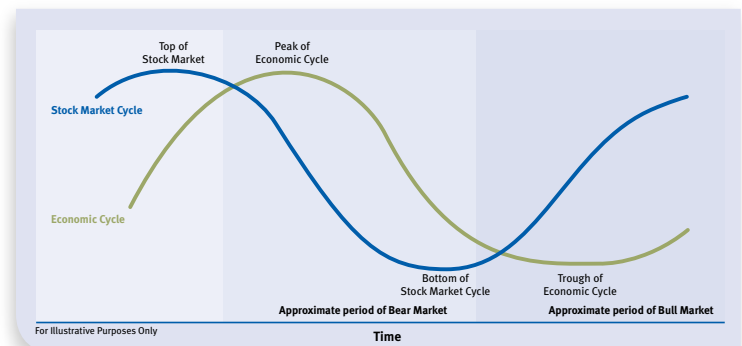
History tells us that the markets will recover – but it doesn't tell us exactly when. However, it does give us some clues. Most importantly for investors, history shows that the stock markets are a “leading indicator” of economic recovery – that is, they tend to recover before the economy as a whole.

Since the Second World War, the longest recession has lasted about 16 months. If the current recession lasts as long, then we should start to see signs of an economic recovery later this year. As a leading indicator, stock markets should recover even earlier.

For investors who have been sitting on cash, waiting for the economy to pick up before getting back into the markets, this is a crucial point. Waiting for actual signs of economic recovery could mean missing out on all or part of the stock market recovery, as the following chart illustrates.

### Stock market cycles historically lead economic cycles

A bear market typically starts before a recession. Similarly, a bull market usually begins before the recession ends. That means if you're waiting for the economy to perk up before investing, you may miss out on the market recovery.



Source: RBC Asset Management

### BLINK AND YOU COULD MISS IT

Not only could a recovery happen sooner than many think – it could happen faster too. Often, recoveries are concentrated in just a few trading days, making it virtually impossible to accurately “time” when you should be in or out of the markets. As the following table shows, even missing just the 10 best trading days over 16 years on the Dow Jones would have cut your returns in half.

### It's time in the market – not market timing – that counts

Amount invested in 1990	\$100,000
Value after 16 years	\$453,000
Value if missing the 10 best trading days	\$281,000
Value if missing the 100 best days	\$38,000

Dow Jones Index, 1990-2006

What's more, there's currently a record amount of money on the sidelines earning next to nothing, waiting to come back into the markets. In Canada, investors now have \$74.9 billion socked away in money market funds – up from \$46.3 billion just two years ago. In the U.S. it's nearly \$4 trillion – a truly staggering amount. As investors regain confidence, much of this money will come back into the markets, and could propel them upwards very quickly.

Please contact us for our current outlook on the global markets and economy.

## Getting ready: What you can do now

Using history as our guide, we know that despite all the negative news, the markets will probably recover, that they will likely do so before the negative news stops making headlines, and that the recovery could be over before we know it. So what should you do to get ready?

### 1. Start looking at your statements again

Like many investors, you may have decided to simply tune out what's happening in the markets and wait for it all to end. Now's the time to take a look at where you stand and determine if you should make some changes to reposition your portfolio for the coming days.

### 2. Clean out the dead wood

During a market downturn, most stocks typically go down. But not all of them come back, as downturns can expose weaknesses in certain stocks previously buoyed up by the generally positive economic climate. Clean up your portfolio by identifying which stocks you own that may not bounce back as strongly as others, if they bounce back at all.

### 3. Seize new opportunities

Many of the greatest opportunities arise during times of turmoil. As an investor, you can find many blue-chip stocks priced well below their intrinsic value. You can also find high-quality corporate bonds offering higher yields than normal to attract investment in today's more risk-averse environment.

### 4. Regain your balance

The key to successful investing, like life, is balance. As an investor, you need the right balance between different types of investments to achieve your particular goals. For example, if you're looking for security and income, you would typically want more bonds in your portfolio. If you need long-term growth, you would favour stocks. With the recent market turmoil, your investments probably need to be rebalanced to align with your goals.

### 5. Get back in touch with your emotional side

How you balance your investments isn't just about your goals. It's also about how comfortable you are with investment risk. Investors often find their risk tolerance drifting upwards with the markets, without even really thinking about it. Then, when the markets come back down, they realize they weren't really prepared (emotionally or otherwise) to take so much risk. As an investor, it's important to take an honest look at your real comfort level with risk and adjust your investments accordingly.

## Taking positive action: New opportunities to reduce taxes

It may be harder to make money in today's challenging markets. But at least you can do something to protect the money you do make from taxes. Following are several strategies that can help you reduce your family's tax bill.

### A HISTORIC OPPORTUNITY RIGHT NOW: THE SPOUSAL LOAN STRATEGY

If you pay taxes at the highest rate, you know just how punishing Canada's marginal tax system can be. But if your spouse earns little or no taxable income, you currently have a historic opportunity to reduce your family's overall tax bill using the Spousal Loan Strategy.

Here's how it works. First, you make a loan to your spouse, which is backed by a simple promissory note setting out the terms of the loan. Then your spouse invests the entire loan amount in their own name. This way, the investment income is taxed at your spouse's lower marginal rate – reducing your family's overall taxes.

To ensure the income is taxed in your spouse's hands – and not yours – your spouse must pay you interest at a certain rate, which is set by the Canada Revenue Agency (CRA). However, between April 1, 2009 and September 30, 2009, the CRA-prescribed interest rate on spousal loans dropped to a historic low of 1%, creating an unprecedented opportunity to maximize this proven, yet often overlooked strategy.

Bear in mind the rate may be different after September 30, so consult with a professional advisor for the latest rate.

### HELPING YOUR FAMILY WHILE REDUCING TAXES: THE FAMILY TRUST

You could be looking at some large capital gains over the next few years as the stock markets recover. While this is welcome news, capital gains are of course taxable outside a non-taxable account. One way you can reduce these taxes is through the new RBC Dominion Securities Family Trust.

With the RBC Dominion Securities Family Trust, you can effectively transfer the tax-reporting obligation for the taxable income generated in the trust to your children or grandchildren. Because of the basic personal amount they can claim on their tax returns, they can each earn up to approximately \$50,000 in tax-free income, depending on the income mix generated in the trust (varies by province of residence).

*continued on page 4*

To qualify for the tax break, the income generated in the trust must be used for the benefit of, or allocated to, the beneficiaries of your RBC Dominion Securities Family Trust. If you are currently paying for things like your children's education costs from your after-tax income, the Family Trust can make a lot of sense. When properly structured, you don't pay taxes on the capital gains earned within the trust, so your dollar goes a lot further in covering this sort of cost.

### EARN TAX-FREE INVESTMENT INCOME

The new Tax-Free Savings Account (TFSA) is a no-brainer for anyone looking to reduce taxes. With the TFSA, you can earn tax-free investment income and make tax-free withdrawals any time you want for any reason. You can contribute up to \$5,000 annually and, while this may seem like a small amount now, over time it can make a big difference, especially with the effect of tax-free compound growth.

### ENHANCE YOUR AFTER-RETIREMENT INCOME WITH LIFE INSURANCE (WE'RE NOT KIDDING)

Many people are surprised to learn that life insurance can be used in other ways than simply providing a death benefit for loved ones. There are two things about a life insurance policy that may be news to you:

1. You can hold investments within the policy.
2. The income you earn from these investments is free from annual taxes, resulting in greater tax-deferred growth (similar to an RSP).

Plus, your beneficiaries still receive a tax-free benefit when your estate is settled.

Insurance can be used in other ways too. For example, an "insured annuity" combines an annuity that provides a guaranteed income for life and life insurance that replaces the annuity capital.

Please contact us for more information about these, and other, tax-reducing strategies.



## Improve your financial picture with the Family Snapshot

**The Family Snapshot is different from other financial planning tools in two very important ways:**

1. It takes into account your family's overall financial situation, which helps you identify powerful tax-saving opportunities only available to families.
2. It takes just minutes to complete, but gives you a valuable Wealth Management Report with specific, detailed recommendations customized to your situation.

**The unique Family Snapshot Wealth Management Report details opportunities and strategies that you can use to:**

- Reduce your family's high tax burden with proven, yet often overlooked strategies – including strategies that can reduce a family of four's taxes by \$45,000 annually
- Ensure you will realistically have enough for retirement
- Protect your purchasing power from taxes and inflation – even if you live to age 100
- Take care of your family if something unexpected happens

For more information about the complimentary Family Snapshot, please contact us.

In today's uncertain investment climate, strategies to reduce taxes and enhance your after-tax returns are more important than ever. To find out how you can benefit from any of the strategies discussed in this newsletter, please contact us today.



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