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Opportunities Abound Today Just Like The Late 90's

The U.S. economy is getting stronger with each passing day. Europe continues to recover, yet is a few years behind the U.S. on that path. China on the other hand continues to slow. Inflation is non-existent and thus interest rate expectations continue to be "lower for longer".

It is China's slowing economy that is causing the last several months of uncertainty. After many years of hyper growth China's slowing is having a negavive impact on commodities of all kinds including energy (oil) and the investment confidence people feel is shaky. Déjà vu from almost 20 years ago.

At the end of 1997, the U.S. economy was strengthening and interest rates were just starting to increase. The European economy was growing (as it is today) and Japan devalued it's currency (like 18 months ago). Commodity prices fell through the floor and oil reached $12 / barrel. The U.S. government hesitated on its interest rate increases and what followed was a speculative bubble in technology. There are hints of this happening again today in the technology sector, with people paying higher valuations (prices are what people pay, valuations are what companies are actually worth).

The investment managers I use for client portfolios have a very different discipline in what they buy and how much they will pay for something. Unlike many people who chase things without set investment parameters and research, discipline and patience will keep you out of trouble. Doing things any different puts money at risk of "permanent loss of capital".

Also, the investment managers I use will only hold a very limited number of businesses in a portfolio. They view themselves as business valuators buying pieces of businesses. When they find a business that 1) Is a leader in its field and 2) Is priced below what it is actually worth, they will buy it, only if it looks more compelling than their least attractive, existing investment.

Through 2015 this has created a lot of portfolio turnover as pieces of businesses they owned became expensive. It isn't prudent to continue to own a company that is over-priced thus, many holdings were sold (these included many medical companies). This process substantially reduces risk.

As we went through the fall and came into January this year, the cash that was created from selling over-priced businesses were re-allocated to buying businesses that could be bought at compelling valuations. These included many U.S. banks and insurance companies which had fallen dramatically for reasons that were seen as very temporary in nature.

It is through this kind of active management, one which buys and sells with discipline on an ongoing basis, that you can have confidence you continually have the best positioned portfolio no matter what kind of environment we are in and where we are headed. That is the kind of portfolio I have as well.

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These 3 Investment Sectors Are Ripe For The Picking

Whenever you go through a time of uncertainty like this, certain investment segments get particularly hard hit. This creates opportunity to cherry pick very healthy investments for cheap. These are:

High Yield Bonds— these are bonds that are considered to have more risk attached to them however mispriced gems can be found among them. In other words, on the surface, they appear to be higher risk than they actually are.

The high yield bond sector as a whole has fallen to levels we haven't seen in 4 years. This translates into an opportunity to be able to buy bonds below "par value"; what you would receive if you held the bond to maturity. The result is that high yield bonds are paying interest rates in the 9% / year range.

Preferred Shares— this investment sector declined more 2015 than it did during the global financial crisis in late 2008 / early 2009. Because of this, dividend yields in this investment sector are averaging approximately 6% / year, in what is considered to be the lowest risk equities that you can invest in. On top of the very healthy dividend yield, dividends are taxed very lightly in comparison to interest income.

Emerging Markets— With the worry of economic slowdown globally and the steep drop in oil prices, shares of even big, healthy businesses in countries like Brazil, Mexico, China, etc. have seen their share prices fall dramatically. It is cheaper to buy in these areas now than it has been in 10 years. Also, because these businesses are in areas of the globe where they can grow their market share much faster than in a developed country, their share prices should increase faster (ie A cell phone service provider or bank in Canada will grow much slower than a similar company in China because so many people in China don't have phones or a bank account).

Investment success is directly related to doing some detailed analysis of the merits of 1 investment over another. This is where a seasoned investment analyst picking and choosing specific investments for one's portfolio is critical.

3 Financial Planning Mistakes I Continually Come Across

I come to working as a Financial Planner for many, by people doing a Google search for a Financial Planner / Advisor. In reviewing the information that is given to me so I can prepare a "Financial Planning Recommendations Summary", there are a few mistakes that seem to be very common in how one's personal finances are structured:

Allocation of RRSP contributions — When you have 2 income earners in a family, most often they are in very different tax brackets. When RRSP contributions aren't maximized every year, the monthly RRSP contributions being made, are commonly split 50/50 (ie $500 / month to both spouse's RRSPs) The savings habit is definitely the right thing to do however, it should done a bit differently because, simply splitting RRSP contributions this way can leave lots of tax savings on the table.

A much better way can be to put as much as $1,000 / month in the higher income earner's RRSP. With these dollar amounts, making that adjustment can create as much as $1,600 / year in MORE tax savings. If one spouse doesn't like the that all the RRSP's are in 1 name then this is where a Spousal RRSP can work well. The "contributing spouse" (higher income earner) gets the tax deduction but the money is in the lower income spouse's name.

Holding money in a TFSA when you have a mortgage also— It very seldom makes sense to have money in a TFSA if you have a mortgage. I'll leave that statement stand as it is because as I type this I can think of scenarios where it does make sense but they are very specialized cases and for most people, these don't apply. If you would say that you use it as an emergency reserve, then I'd suggest, as I've written about before, that there are better ways to deal with a financial emergency and the most efficient is a Line Of Credit. See previous issue of Mutual Gains, bottom of page 2 "6... Myths".

Owing money on a mortgage and having investments outside an RRSP — In this case, investments are held outside a "registered" plan (ie RRSP) yet there is a mortgage on a principal residence. Because the interest on money borrowed for investment purposes is tax deductible, a swapping of debt should be done to make this situation much better. This simply means, selling the investment, using the cash to pay down the mortgage and borrowing money to buy back the investment. On $100,000, you enjoy as much as $1600 / year of tax savings when you make this change.

TFSA vs RRSP – Which Is Better?

I don't think any of us are happy that JT kept his promise about bringing the annual TFSA limit back down to $5,500. Despite that though, the TFSA is still a very attractive savings vehicle as its sister savings vehicle, the RRSP. So which is better to contribute to, a TFSA or a RRSP? Here are the key features:

Ease of Access— TFSA wins. You can withdraw money from your TFSA at anytime and if you do, you don't lose the contribution room. That comes back to you the following year. Money can go in and out relatively pain free because of this. Convenience though is also its danger. If you take the money out, what is to compel you to put it back in again? "Hhhmmmm... money in my TFSA or realizing the feel of falling asleep in the sun on the beach at that all inclusive resort..."

Discipline— RRSP wins in this department. The RRSP have an invisible barrier to protect you from yourself. Money goes in and if you withdraw it 20—50% goes to the government. A $10,000 withdrawal can become as little as $5,000 of cash in your hand. This is to pay back the income tax refund you got from contributing to it in the first place.

Tax Savings— On a long term basis, when used strategically, the RRSP wins by a landslide. Contribute $10,000 to an RRSP and the government will pay back to you up to, almost $5,000 in income tax you paid them. $10,000 turns instantly into almost $15,000. That is an up to 50% return in 1 year, guaranteed. So with the RRSP you now have $15,000 in your name. The TFSA contribution is still at $10,000. Add in the tax free compounding on both and in the end the RRSP value will be significantly higher than the TFSA.

If you are using money as a long term investment vehicle and you need more than $17,000 / year of retirement income if you're single ($23,000 / year if you are a couple), then the RRSP should be where you put money first. Having said that though, there are a lot of parts to consider in financial planning. Because of that, it is highly recommended to work with a Financial Planner on planning your retirement income to minimize tax and maximize your lifetime income.

You Know You Are Ready To Fully Retire When…

Here is a checklist to determine if you are ready to retire (the more you tick the more ready you are):

1) Your home is paid for. If you still have a mortgage then I'd suggest you should probably downsize to something you won't have debt on (or debt on anything else for that matter that you have to pay for on a monthly basis).
2) You have a pension plan that is fully funded; you will get the maximum income that the pension plan will pay. If you don't, your RRSP, CPP, OAS and other income producing assets should be able to meet all of your living and lifestyle expenses, and do that assuming you live well into your 90's.
3) Your children are financially independent. If you are continually shelling out money to your kids or plan on helping them with buying a home, you may want to hold off on retirement or pull away their crutch.
4) Your portfolio can weather negative market effects.
5) You have more than 1 income leg on your "retirement income stool".
6) Most of your friends are retired. If you're the only one of your closest friends to stop working, it may be too soon.
7) Your job is affecting your health. This is very subjective however only you can truly know this.
8) You have a purpose for the next stage of your life. You can picture and write down in detail how your week days and weekends will be used.

A Better Way To Pay Your Medical Expenses

I've used this idea for years however, to use it you must be self employed. If you aren't, you may want to pass this info on to that family member or good friend who is. They could very well say, "Wow, I didn't know that" and with that, you could be saving them thousands of dollars in tax every year.

As an individual you do get a small tax credit for claiming medical expenses, optical costs, dental work, etc. however the tax savings are relatively small. If you are self employed you can run your medical expenses through a Private Health Services Plan (PHSP), also known as a "Health Spending Account". Through it, you reduce your medical expenses by whatever your marginal tax rate is (ie if you earn between $140,000—$200,000 you are saving $437 per $1,000 of expenses). Comparatively, if you only have a $2,000 or so of medical expenses to claim on your tax return, your tax savings are virtually nil.

Applying for this is really easy. Simply go to www.careyvandenberg.com/paperwork.php and scroll down to one of the "Health Spending Account" links. If you want to travel outside of the province or country, I'd suggest clicking on the one with travel insurance included.

Does Contributing to CPP After Age 65 Make Sense?

To boost your CPP income, you can voluntarily contribute to CPP from age 65 to 70. It is a CPP sweetener that can increase the CPP income coming to you by 2.5% per year, to a maximum increase of 12.5%. If you are an employee, it can make sense if you are likely to live past age 75. Being self employed though, because you have to make contributions as the employee and as the employer, you don't reach a break even point until you live until age 81. Those are simple rules of thumb but of course, like any other financial decision, there are a lot of other things that can come into play.

Tech Gems— REW.CA

It's hard to tell what this is from the URL but this is Real Estate Weekly. We bought a house about 6 weeks ago that Cheryl found on this site. You would think that every site is equal however, we found that REW.ca had listings on it faster than Realtor.ca which ironically is controlled by the Canadian Real Estate Association. In our case, it was 2 days faster. We found the same time advantage (or delay, depending on what site you go to) when we listed our house for sale 2 weeks ago. Some sites simply don't have info up that fast and again, ironically, Realtor.ca was one of the laggards. In this environment of multiple offers, over asking price, every bit of extra time you have to determine what something is worth to you and the price it will probably fetch, is to your advantage.

Hhhhhmmm......

Say your grandfather had bought a DOW index fund (a “passive” portfolio rather than “actively managed”) at the market peak in 1929. Significant declines would have been experienced for 3 years and it would have taken another 25 years for him to break even. AdviceForInvestors.com

Even though China’s growth rate has been shrinking, the dollar value of its contribution to the world economy has actually remained fairly constant because their economic base is much larger. In 2009 China’s GDP was $5.1 Trillion vs almost $11 Trillion today (in other words, the market worries about China slowing is an overreaction) Dixon Mitchell Investment Counsel, Jan. 2016

Emerging Market companies as a group are at the cheapest valuations we have seen in over 10 years. They are selling at a 26% discount to developed world companies in aggregate. Because not a lot of people analyze companies in Emerging Market countries, there are a lot of investment opportunities to be found. Trimark Blog, March 2016

253 of the companies in the S&P 500 reported lower net income in 2014 than they did in 2013. For some companies, the drop in income has been going on for several years. (If you have a portfolio of passive investments you probably own all of the “good, bad and the ugly”) USAToday, March 2016

Most Canadian bank executives compensation is tied to profit as well as share price, so it's in their best interest to say that the negative impacts (to the bank) of low energy prices (and the bank's exposure to it) are contained. This implies that bank shares have not reached their bottom. Advisor's Edge Report, Feb. 2016

Since 1825, the U.S. equity markets only went down 30% or more in 3 separate years, 1931, 1937 and 2008. That is 3 in 187 years (1.6% of the time). Bloomberg & Ibbotson & Associates, as of Dec. 31st 2012

Canadians have increased personal debt by more than double over the past 15 years, making us more in debt that the Brits, Aussies, American's and virtually all other people in developed countries. This could mean a slow economy for several years which will be detrimental to Canadian banks and other companies that derive most of their business from Canadian consumers. Edgepoint, March 2016

If a tax prep service offers to do you tax return and fills in fraudulent information (they would do this to boost your tax savings motivated by being paid a percentage of your tax return), CRA will hold you personally liable for the fraudulent filing. Advisor's Edge Report, Jan. 2016

Average cost to own a dog is ~$2,000 / year. Dogster.com, March 2016 (my brother Daryl, who has had a few dogs and keeps meticulous records on all costs, disputes this number despite his situation being a very small sample size and having Boxers, a breed that is prone to health issues).

In the UK, where travel and auto insurance policies have been sold online for almost 15 years, 15% of policies have been declared void when a person makes a claim because the application wasn't completed properly. The client finds out they aren't insured only when they file a claim (which is too late). Insurance & Investment Journal, March 2016

The best built car brands are 1) Audi, 2) Subaru, 3) Lexus, 4) Porsche Consumer Reports Auto Issue, March 2016 (I own a Subaru WRX. Because they don’t make it in a 5 door anymore and I want AWD, my next car could very well be an Audi).

Swiss water decaffeinating process is done in Vancouver for all of North America. Told to Cheryl and me by a coffee roaster when I was in Maui, March 2016.

The US Postal Service has dropped mailing prices for the first time in 100 years. USAToday, April 2016

Since the 80’s over 200,000 Asian immigrants have come to Vancouver through investor programs. After 5 years only 39% of these people showed any annual income, averaging $21,000. After 15 years the average was $25,000 for that same group. Refugees on the other hand averaged $30,000 in earnings after 5 years. TheWalrus.ca

If you look at where the terrorists have been striking, it’s the London Underground and the trains in Madrid yet, you don’t see the government confiscating lipsticks and gel-filled bras (there). It’s simply a way of politicians making it look like they are doing something. Michael O’Leary, A Life In Full Flight (The Story of the Man Who Made Ryanair Take Off)

Spain, Germany and the UK’s attempts to create “green” electricity grid with wind and solar power failed miserably. Ontarians recently learned they paid $37 billion more than they had to for power. Alberta is going down the same path (they don’t seem to get that if you do the same thing others are doing you will get the same result). Investment Executive, Jan. 2016