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An Investment Update

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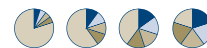

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What's News

By Neil McIver

I'm often asked by folks in social situations who know me by my professional reputation, "Neil, what should I do this year with my money?" It is a tricky question to answer for several reasons, not the least of which being that without specific knowledge of the individual's financial needs, I have no point of reference from which to base any suggestions. It is a little like asking a doctor, in that same social situation, what you need to do to finally 'get healthy' over the next year. The difficulty is that the depth of questioning may be more involved than either one of us really may wish to explore at that moment over the Brie cheese dip.

Perhaps an easy answer to such an off-the-cuff question would be to suggest that the individual follow our tactical calls on the market. Currently, these would be to lighten exposure to Canadian equities, lighten exposure to bonds in general, increase U.S equity exposure, and to consider real return bonds. In addition, I could even throw in a few of our favourite individual stocks to consider, such as Canadian Tire. (Please see our annual Special to the Vancouver Sun with our 2012 Market Predictions). These suggestions, however, are simply short-term tactical ideas.

What these suggestions do not provide is any information on the relative size of any recommended position or asset class, the inherent historical risk of one market versus another, or any sense of the timing one might need to consider in buying and owning these asset classes or securities. In short, no strategic plan is explained. There is just a list of short-term maneuvers, or tactics, and, therefore, zero sense of the over-all risk anyone would be taking by following these suggestions. In fact, if I had a single conversation with two investors at the same time, over the Brie cheese dip, and each investor went ahead and followed the tactical proposals I provided, but in different proportions and at slightly different times, the amount of risk that each might assume could be dramatically different and their respective results could vary greatly.

Investing on a tactical basis, without a strategic plan, does not seem like a very bright idea. Yet this is exactly how most portfolios are put together. They are a series of individual tactical decisions that are made without consideration for the relative size of each position or asset class and without any knowledge or understanding of how these positions move in the market on a relative basis to each other. In short, there is no understanding of the level of risk to which the portfolio is exposed. This is why most portfolios fail and why many investors become jaded.

Simply because a portfolio is 'diversified' does not mean it has a strategic plan. Nor does it mean that any work has been done to understand the level of inherent risk it may have. A good acid test for this is to ask the folks who manage a portfolio what the expected Standard Deviation (expected variance) of your portfolio is. If they do not know the answer, or say they need to get back to you, then no such work has ever likely been done, and the portfolio doesn't amount to much more than a dart throwing exercise.

Why do our portfolios outperform? The answer can be attributed to the fact that we have a strategic plan for each of your portfolios, designed not only to calculate the level of risk (expressed as the Standard Deviation from your expected rate of return) but also to ensure your portfolio has the best chance, mathematically, of enjoying the highest rate of return for your given level of risk. Each individual asset class, or position, is added to the portfolio in the most efficient proportion based upon 80 years of market history in our data bank. Only after the strategic asset allocation structure is determined, and the percentage of each asset class or position is set, does it make sense to use tactical information to maximize the return the market can provide. It is the combination of a stringent adherence to the strategic asset allocation structure with smaller tactical maneuvers that results in our outperformance on your behalf.

This common-sense yet sophisticated process is not new. It has been successful for more than 30 years for large institutional pools of capital and it has been peer-reviewed by the most prestigious academic organizations. It is just rarely used for private clients.

On the Mark

By Mark Jasayko

Greece III

The Grease movie franchise was never extended into a trilogy. However, the follies concerning Greece, the country, are entering their third year, with each year feeling like a new episode. The political and banking industry rhetoric has always suggested that a solution is just around the corner. But then, a new year dawns and we are subjected to a plot extension with an evolving cast of characters.

This year's installment begins with private holders of Greek debt trying to get the best deal possible in order to avoid maximum write downs. And, in the background, the European Central Bank suggests that it should not have to take a write down at all because it was only trying to help out when it acquired about $400 billion worth of Greek bonds over the last year and a half. What's good for the goose, is good for the gander? Not here.

Just as interesting as the players in this "movie" have been the reactions of the viewers watching the "movie." The Greek crisis has been able to produce seemingly contradictory headlines from one week to the next. One week everything is okay and investors are optimistic of the outcome. Then, the following week, negotiations breakdown or someone does the math again and finds that it still doesn't add up, causing investors to run for the hills. The next week, investors are back, seduced by some soothing political rhetoric emanating from the umpteenth summit organized to deal with the issue.

This back-and-forth has been so common that the industry has recently coined a couple of new phrases to describe it. "Risk On" is used to describe the situation where everything seems okay thanks to happy prognostications from the policymakers. Investors rush back into the markets in an attempt to take advantage of the potential economic recovery that should result. "Risk Off" is used to describe the opposite: maybe negotiations breakdown and a disorderly Greek default looks assured, causing investors to sell.

Surprisingly, it has been institutional investors including mutual fund and hedge fund managers who have been caught in this alternating tide.

So, is there any merit to trying to time the headlines coming out of Greece? Not if last year's evidence involving mutual funds and hedge funds is any indication. US equity funds woefully underperformed the S&P 500 index in 2011. Only 17% of those funds that invest in larger companies were able to beat the S&P 500[1]. Even more astoundingly, all 12 of the major hedge fund strategies that comprise the main HFRX Index failed to beat the S&P 500[2]. Every single one of them.

Being overly active did not pay and, in general, led big investors to chase their tails. After all, if one has liquidated a number of positions the previous week because of bad headlines coming out of Europe, it is difficult to get back in when those headlines become more positive. It was a common occurrence in 2011 for stock markets to jump over 1% at the open in response to positive news that was reported from Europe overnight. There isn't any chance to get back into a position at a good price if the market gaps upward at the start of trading.

Although the first few weeks of 2012 have been positive for the markets, this year is likely to be more of the same with respect to "headline whiplash." Greece is still a prominent source of anxiety. Optimistic rhetoric is still being uttered. But the math still does not add up. Unless the other European countries (and countries elsewhere through the International Monetary Fund) feel like giving Greece a big free pass on what they owe, the debt burden will still be too high to ever be paid down to a sustainable level (even if negotiators get a great deal on concessions from the private holders of Greek bonds).

Eventually, the endgame will be an inflationary episode as money is printed to pay off the debts of Greece and the other profligate Euro-currency members. However, until we get there, the tug-o-war between fantasy and reality will persist, leading to a continuation of seesawing headlines and to this environment characterized by "Risk On" and "Risk Off" days.

By focusing on our Asset Allocation process, we avoid the seduction of good headlines and the fear from bad headlines. By resisting the temptation to become too active, we allow the allocation of our selected asset classes and underlying investments contribute their full potential to portfolio returns while minimizing risk. Bring on "Greece IV". We're prepared.

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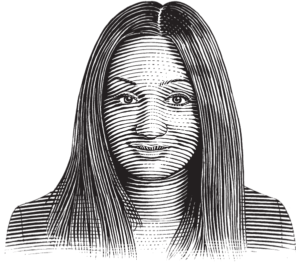
[1] Morningstar Research Inc.

[2] SeekingAlpha.com & Hedge Fund Research Inc.

Good Karma

By Karm Bhatti



Investment Policy Statement (IPS)

As all of you are aware, the Investment Policy Statement (IPS), which outlines and details your portfolio's structure and risk, was signed when you originally set up your Asset Allocated Managed Portfolios. However, in order to keep all accounts up-to-date we are required to have you sign a new IPS on an annual basis.

RRSP – Deadline and Limit

It's RRSP season again and the contribution deadline of Wednesday February 29, 2012 is fast approaching. The maximum contribution limit for 2011 is $22,450. There are two ways to ensure that you make your contribution in time:

Cheque, by mail

Send in your contribution by cheque in the mail. Please notify us that you have mailed a cheque so we know your contribution is on its way. Ensure that the cheque is made payable to "Richardson GMP" and on the memo line of the cheque please write "2011 RRSP Contribution". Lastly, please ensure you mail the cheque leaving ample time for it to reach us through the mail.

Transfer from your non-registered investment account

Your RRSP contribution may be made by a transfer of cash or securities from your non-registered investment account to your RRSP account. Please call me directly at 604-678-6563 with the details of the amount you would like to have transferred and I will arrange this for you.

Preserve and Protect

By Mike George

RRSP season is always a good time to review the fundamentals of tax-advantaged investing. Here are some of the easy basics:

Tax Efficient Investing

- Tax-Free Savings Account (TFSA) - If you are a Canadian resident over 18 years of age, you may contribute $5,000 per year to a TFSA. Amounts withdrawn are not added to your contribution room until the year following the date of withdrawal. While contributions are not tax deductible, the income earned is tax-free and there are no taxes on withdrawals. Attribution rules are not applicable to investments made by a spouse in a TFSA.

- **Registered Retirement Plans**

  Contribute to an RRSP in the current year and claim the deduction in future years – Depending on your contribution room, it is possible to contribute to your RRSP without claiming the tax deduction. So if you are in a low tax bracket now you may want to consider contributing to an RRSP to take advantage of tax-deferred growth, however, consider waiting to claim the deduction until you are in a higher tax bracket.

  Consider contributing to a spousal RRSP – Depending on your contribution room, it is possible to contribute to a spousal RRSP. The spousal RRSP allows the contributing spouse to take a tax deduction as long as the funds remain in the plan for 3 calendar years. Providing your spouse is in a lower tax bracket you will realize tax savings for your family. Despite the pension income splitting measures, you may still want to contribute to a spousal RRSP.

  Make an advanced contribution – If you turn 71 during the year, you are required to wind up your RRSP by the end of the year. However, if you have earned income during the year in which you turned 71 you will have RRSP contribution room in the following year. Because you cannot contribute to your RRSP in the following year, you may consider contributing in December. While you'll be subject to a 1% penalty for the month, you will get a tax deduction and the funds will accumulate tax-deferred until withdrawn. Alternatively, if your spouse or common law partner is under 71, you may want to contribute to a spousal RRSP if you still have RRSP contribution room.

  Base your annual minimum RRIF withdrawals on the age of the younger spouse – When transferring your RRSP to a RRIF, your mandatory minimum RRIF withdrawals may be based on the age of your spouse. Therefore, if your spouse is younger, this option may minimize your minimum RRIF withdrawals.

Contribute to a Registered Education Savings Plan (RESP) – With increasing costs of post-secondary education, an RESP can assist you by providing tax deferral, income splitting opportunities and government assistance. The lifetime maximum contribution is $50,000. For each dollar contributed to an RESP the Canadian government will contribute 20% (Canada Education Savings Grant) to a maximum of $7,200 (maximum of $1,000 per year). The funds within the RESP accumulate on a tax-deferred basis and the grant and the income earned in the plan are taxable to the beneficiary when withdrawn for educational purposes. Certain provinces also offer additional governmental programs. This is the case in Québec, where the Quebec Education Savings Incentive (QESI) pro¬vides a grant on contributions made to the RESP.

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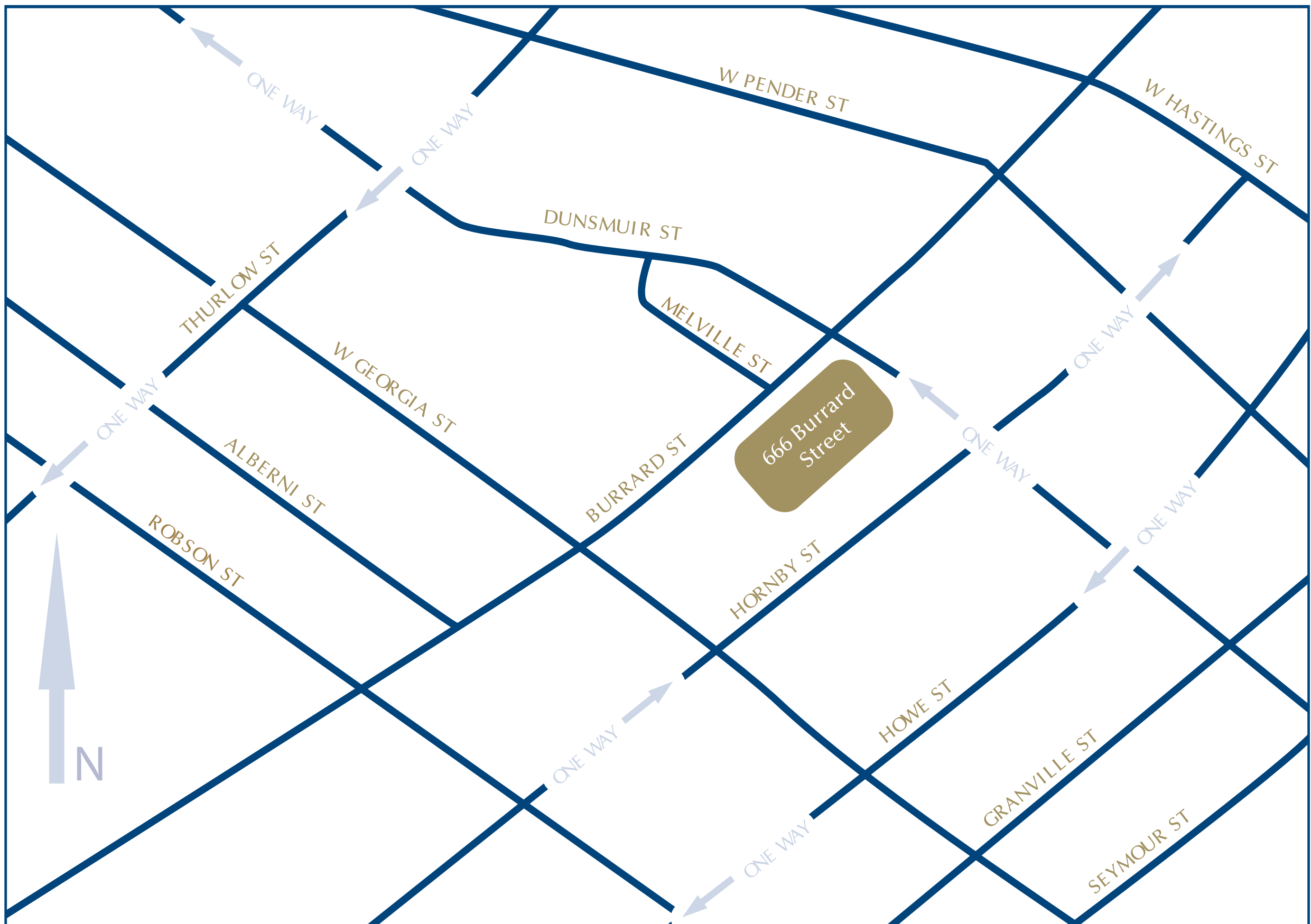

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