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Money Wise!

CAQ Financial's Quarterly Newsletter

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Special points of interest:

- **Unlocking locked-in plans: how does it affect you?**
- **Infrastructure as an emerging asset class**
- **Recent rule changes protect all Registered accounts from seizure from creditors**

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Markets at a glance

The markets have continued their rocky ride year to date, with rising oil prices and the continued fall-out from the problems in the US sub-prime mortgage sector dominating investor concerns. While the overall situation may not be nearly as bad as the media would have you believe, the element of diversification is as important as ever to avoid being caught in the wrong sector at the wrong time.

In the first quarter of the year, financial stocks felt the full brunt of the credit crisis, with many good companies with little exposure to the affected areas being dragged down with the bad. Investor attention was dominated on high-flying commodity and energy stocks, leaving stocks of solid businesses in other sectors weak.

More recently, financials and other out-of-favour sectors have staged a rebound and we have seen considerable short-term weakness in energy and commodities. Whether this represents a temporary drop or the beginning of a change in leadership for the markets remains to be seen. Certainly, there are still valid reasons for higher commodity prices despite economic slowdowns in Asia and elsewhere. Financial history has shown, however, that periods of rapid appreciation, a high degree of speculation and a narrow investor focus in a particular sector tend to be followed by often-dramatic drops in that sector, even if the fundamentals are still favorable.

In any event, as of the end of July, the performance of global stock markets year to date was not a pretty picture. The US Market was down nearly 14% and the overseas markets (Europe, Asia & the Far East) were down 19%. Canada fared better, down less than 2% due to the support from rising energy & commodity prices.

From a global perspective, moderating oil prices should help relieve energy-related inflation concerns and strengthen the overall economic outlook. In Canada, the results should be mixed but largely favorable as declines in energy and commodity stocks should be offset by gains in areas affected by high oil prices.

In times like this, we need to remind ourselves that markets have endured similar concerns in the past and have always weathered the storm. As bad as it seems in the midst of a period of financial turmoil, the stage is already being set for the next positive upward cycle. Proper diversification cannot be underestimated in this environment, and a proper portfolio should be well-balanced to offset any large swings in any one area.

Opportunities in Infrastructure

You may have been hearing and reading a great deal about "infrastructure" lately. Infrastructure refers to physical assets or services (including transportation systems, water, gas and electricity distribution and telecommunications assets) which form the foundation of a modern economy.

While effective infrastructure is essential to economic prosperity, much of the developed world's infrastructure assets are outdated and in need of replacement. (Locally we are no exception.) In addition, world population and economic growth means many regions, including China and India will need to virtually start from scratch. As a result, global investment in infrastructure is set to skyrocket, creating an opportunity for investors. Certainly, large institutional investors such as the Canada Pension Plan have shown a great amount of interest in this area.

If you are interested in learning how an investment in infrastructure may benefit your portfolio, I would be more than happy to discuss

How much income will you need in retirement?

You've worked long and hard, you're healthy and active, eager to pursue new interests, learn new things, and keep doing what you love most.

But are you really ready to retire?

A secure, enjoyable retirement depends on having enough income to maintain your lifestyle, probably for much longer than you think.

An important step in retirement planning is to calculate your "income replacement rate" — the proportion of your pre-retirement income you will have to replace to maintain your lifestyle.

If you are like many Canadians, you spend your money in four basic ways:

- consumption (i.e. personal spending)
- taxes
- public benefit plans (such as employment insurance and Canada/Quebec Pension Plan)
- personal savings (such as contributions to an RRSP)

At retirement, this picture will change. You may reduce personal spending - on clothing and transportation, for example - and your tax bill may be less. Instead of contributing to a public pension, you will take benefits. Rather than being a saver, you will be a spender.

Financial planners have long believed you should aim at replacing 60% to 70% of your pre-retirement income. But people retiring today are likely to live longer and be more active. Based on their research, Fidelity believes that Canadians should plan on replacing 80% of their pre-retirement income. The exact amount will vary, depending on factors such as your plans, your living situation and what part of the country you live in. The bottom line is that you will need to assess your own personal situation in order to come up with a replacement rate value that is right for you.

A good place to start is Fidelity's Retirement Readiness Snapshot. This calculator will give you a better idea if you're on track to get the income you think you'll need in retirement. The more you know, the better prepared you will be to ensure that your retirement income matches your goals. I'd be more than happy to send you the link or walk you through this exercise the next time we get together. It's a conversation worth having!

Bankruptcy law changes regarding seizure of Registered assets

New law provides potential creditor protection for RRSPs & RRIFs

Having assets seized due to bankruptcy proceedings is a real concern for many investors, particularly small business owners who might see a significant part of their savings seized.

Until recently an investor's registered assets (RRSPs, RRIFs, DPSPs) were not subject to protection against the claims of creditors in a bankruptcy action. This was markedly different from the treatment of insurance investments such as Segregated Funds and Registered Pension monies which were generally exempt from the claims of creditors in a bankruptcy action. Segregated funds always enjoyed potential creditor protection whether or not they were held in an RRSP.

However, with the passing into law of Bill C-12, an amendment to the federal Bankruptcy and Insolvency Act, this situation has now been addressed. As of July 7, 2008, all registered investments will now enjoy similar potential creditor protection as insurance company-issued investment products (segregated funds) and pensions. The protection applies to all bankruptcy actions initiated on or after July 7, 2008. The bill does state that contributions made to registered plans in the 12 months prior to the bankruptcy action (or such longer period as a Court may order) may not be subject to that protection. This is designed to deal with the potential situation where a person intentionally attempts to place funds beyond the reach of a creditor.

Several provinces (Saskatchewan, Prince Edward Island, Manitoba, and Newfoundland) have already acted to provide potential creditor protection of registered assets in their jurisdictions. Those laws will remain in place and the new federal law will apply in other provinces and territories.

This new law will be of particular interest to the self-employed or business owners. Going forward, these individuals' registered investments will be accorded the same potential protection as insurance investments and pensions should they have to seek bankruptcy protection.

That being said, potential creditor protection is only one benefit of segregated funds, the insurance industry's version of mutual funds. Segregated funds also have the ability to bypass probate for non-registered accounts and in most cases offer principal protection if the assets are held for a minimum term (usually 10 years.)

A long-held criticism of these plans, however, has been the high costs associated with them and the limited choice and overly conservative nature of many of the products, all of which can potentially lead to diminished returns over time for investors.

Segregated funds have many valuable features, providing potential protection from most creditors, not just bankruptcy as well as no 12-month restriction. While it may be tempting for business owners to consider changing their investments away from segregated funds in light of the recent changes to the Bankruptcy Act, they should consider the other features segregated funds have.

Inflation: the erosion factor

For the past several years, the Canadian economy has enjoyed a period of strong economic growth. Increased demand for oil, metals and other commodities have led to record profits for Canadian companies, and higher wages for many Canadian workers. So much so, that many economists and analysts are starting to worry. Normally, economic growth would be considered a good thing. But when the economy is growing too strong too fast, it can lead to negative consequences, due to the damaging effects of inflation.

Inflation is the annual increase in the price of goods and services. An inflation rate of 5% means that the products and services you're buying today will cost-on average-5% more this time next year. Left unchecked, a hot economy can cause inflation to rise rapidly. But when prices rise too high, consumers spend less. As a result, the economy slows. To make matters worse, if your income isn't rising at the same rate of inflation, your overall purchasing power and standard of living may be affected.

To prevent this boom-bust pattern, the Bank of Canada tries to regulate inflation by raising interest rates. Interest rates are a measure of the "price" of money – how much it will cost you to borrow a given sum for a year. By making it more expensive for businesses and consumers to borrow, the central bank hopes to slow down (but not halt) economic expansion. Hopefully, a well-timed rate hike will keep prices from climbing too fast, and consumers will keep on buying. When the economy slows the drop will affect Canadian lifestyles a lot less.

What does all of this mean for the individual investor? Imagine you have a conservatively invested retirement portfolio of $500,000. Your portfolio consistently generates returns of about 6% a year, which would generate an income of about $30,000 per year. Let's assume that $30,000 is exactly the amount you need to live a comfortable lifestyle during retirement. On the surface, you have nothing to worry about – your withdrawals equal your annual growth. As long as your portfolio continues to generate $30,000 a year, you never have to touch your capital.

But what about inflation? Let's assume that inflation rises to 4% a year – well above current levels, but not unheard of historically. In order to maintain your standard of living, you will have to increase the amount you withdraw each year by 4%, which means that the 6% return on investments you were receiving will not be enough. You'll have to dip into your capital. In fact your nest egg would be reduced to zero after just 15 years. Not a pleasant prospect at all.

There are a lot of people who think that big inflation numbers are a thing of the past. It's true that, over the past several years, Canada has enjoyed a period of extremely low inflation. (Currently between 1% and 3% — within the Bank of Canada's official target range.) The problem is, your retirement will probably last a long time. In fact, if you're like many Canadians and retire at around age 61, the median retirement age in Canada today, your retirement could last 25 to 30 years or even longer. Inflation will inevitably fluctuate during that time, with even a low 2% inflation rate rapidly depleting your capital. While it's possible the long-term average will stay low, there's no way to know for sure.

So clearly inflation represents a considerable threat to millions of Canadians who are currently retired or are soon to be retired. Given the gravity of the risk it poses, it is important to factor inflation into your retirement income plan.

CAQ Financial: Business Update

The past year has certainly been an eventful one for my family business. The transfer of accounts from Manulife to Quadrus Investment Services Ltd., the change of ownership of the mutual fund business from my father to me and the move to a new office all were big challenges…even more so when they happened all at the same time!

Happily, the majority of this work is now behind me and I can renew my focus on one-on-one contact with my clients. I want to take this opportunity to thank all of you for your patience during this time of transition and to highlight a few of the changes currently underway.

First, I am pleased to announce that work is progressing on the launch of the new web site. Currently, there is just a static page with our basic contact information and the link for you to reach your account information on line. By early October, I hope to have the new site up and running which will incorporate a fresh new look as well as useful calculators, links, and regular commentary from the investment professionals managing your money.

Lastly, some of you may had contact with Alison O'Brien who was with the company for a term position to help assist with all the paperwork associated with the transferring of accounts. That position is now over and Alison is returning to school in September and I wish her well in all her future endeavors.

I plan on hiring a third person early in the New Year to further enhance the customer service I can provide to my clients. I will be sure to keep you abreast of any other changes as they come!

-Rick

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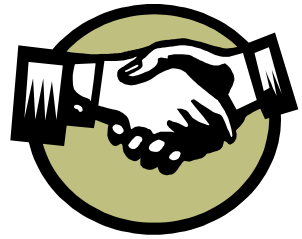

A referral is the best compliment that a client can give. Many thanks to all our clients who have referred us over the past year!

New options for your (Federally Regulated) Locked In Retirement Accounts

If you have a locked-in Registered Retirement Savings Plan or locked in Life Income Fund (LIF) you may be interested in the new rules that apply to **Federally regulated plans only.** Typically, locked-in accounts originate when an employee leaves an employer-sponsored pension plan with accrued benefits.

Because the withdrawal rules are so stringent, many times the assets are put away and forgotten about. Several new measures introduced recently, though, give you more flexibility and more options for repositioning your retirement assets and making use of this money under certain circumstances.

If you're 55 years of age or older, for example, you can legitimately unlock up to 50% of your locked-in assets, or convert them to another tax-advantaged registered account, with no withdrawal limits. There are also new provisions available for small, locked-in account balances, if you have significant medical expenses or if your annual income is likely to be very low in any given year.

Please note: These changes apply to locked-in assets from federally-regulated pension plans. According to Office of the Superintendent of Financial Institutions Canada, federally-regulated plans include pension plans for some federal Crown corporations, banks, companies involved in interprovincial and/or international transportation and communications companies, among others. For other pension plans, the locked-in rules outlined by individual provinces will likely apply. Although provinces may decide to follow suit and amend their legislation accordingly, such changes are not automatic or guaranteed. Before you attempt to access locked in funds you should confirm what jurisdiction governs your particular plan.

Specifically, there are three new options available for federally-regulated locked-in plans established after May 8, 2008:

One-time, 50% unlocking

Once you turn 55, you may transfer your locked-in assets to a new Restricted Life Income Fund (RLIF) account and then transfer up to 50% of the balance to any registered account within 60 days of the RLIF creation. After 60 days, the account is subject to existing withdrawal rules.

Small balance unlocking

If you're 55 years of age or older and your locked-in account assets are less than 50% of yearly maximum pensionable earnings (YMPE) — $22,450 in 2008 — you may be able to wind up your Life Income Funds (LIFs), RLIFs or the new Restricted Locked-in Savings Plans (RLSPs), and withdraw the cash, or convert them to an unlocked tax-deferred savings vehicle.

Financial hardship unlocking

Finally, under the new rules, anyone, regardless of age, may be able to withdraw cash, up to 50% of YMPE, from any combination of locked-in accounts (all withdrawals need to be made within 30 days), if they meet one or both of the following conditions:

Medical or disability

Those who expect to spend more than 20% of their income in any given calendar year for medical treatment, assistive technology or other expenses related to disability can make use of the provision if a licensed Canadian physician certifies that the treatment or technology is needed.

Low income

Those with low income, i.e. anyone who expects to earn less than 75% of YMPE — $33,675 in 2008 — will be allowed to withdraw an annual amount based on their expected income, to a maximum of 50% of YMPE.

Under the older set of rules, these accounts can also be unlocked if your life expectancy is reduced or if you plan to leave Canada permanently.

If you would like more information about locked-in accounts in general, or the new rules specifically, or if any of the above circumstances apply to you, please don't hesitate to call my office and let me know.

As always, if there are significant life changes affecting your situation, there are planning measures we can discuss and put in place, hopefully to make things better and keep your financial plans on track.