

Financially Speaking

RRSPs – The Basics

Registered Retirement Savings Plans, commonly known as RRSPs, were introduced in 1957 to assist self-employed individuals and employees who were not members of a registered pension plan (RPP) to help save for their own retirement. Quite simply, an RRSP is an investment plan registered with the Canada Revenue Agency (CRA) which hold investments for your benefit. That is not to say that RRSPs are only for those who do not already contribute to some other method of retirement savings; like a pension plan. They too may be able to take advantage of the significant benefits that come from contributing to an RRSP.

Advantages of Contributing to an RRSP

The first significant benefit is the immediate tax savings. Contributions to an RRSP made during the year or the first 60 days of the following year can be used as a deduction from income when your tax return is filed. This deduction will result in immediate tax savings equal to your marginal tax rate.

What is your marginal tax rate?

Marginal Tax Rate is the amount of tax that you'll pay on your last dollar of income.

The second significant benefit from contributing to your RRSP is the tax-deferred savings. The investments made inside the RRSP may earn income such as interest, dividends, or capital gains. These earnings inside the RRSP will remain tax-sheltered until they are withdrawn from the plan at which time they will be taxable as income. Since these earnings are not taxed inside the plan, your investments continue to accumulate tax-free, compounding tax-free, over a long period of time.

Many investors are new to the market and do not know what return they should expect on their investments. Advertisements may try to persuade you that you shouldn't accept anything less than 20%. If you are a long-term investor (more than five years) do not expect huge double-digit returns to continue indefinitely. The 40-year history of the TSE shows that the simple average one year return for the TSE 300 is 11.15%, the five-year return is 10.20%, and the ten-year return is 10.2%.

In 2004, the Toronto Stock Exchange index registered a rate of return of 12.48 %; in 2003 that figure was 26.7 %. If you pulled your money out in 2002, which was a bear market year, you would have missed out on the gains of the past two years. The lesson: ***stay invested and don't worry about the fluctuations of the market particularly if you have 10 or more years before you retire.***

Defensive Strategies for Long Term Investing

These are helpful points to consider to help minimize the effects of a falling market and will help keep you focused during turbulent times:

1. **Think long term.** The stock market is like any other store: prices increase when demand is high and prices drop when the demand is low. But unlike other stores, no one can predict exactly what the stock market will do and when. The key is to stick to a long-term plan. Only investors who need their money today should be concerned about short-term fluctuations. Short-term market fluctuations should not be a concern for investors with an appropriate time horizon and a diversified portfolio matched to financial goals and objectives.
2. **Remember the benefits of diversification.** A diversified portfolio made up of equities, bonds, and interest-bearing investments will cushion investors in a market correction and should be weighted to suit individual risk tolerance and reflect investment objectives.
3. **Invest regularly.** The best approach is to continue investing regularly. Maintaining the discipline of regular contributions is important and awards you with the benefit of dollar-cost averaging. This strategy allows a person to spread out the average cost per unit of buying mutual funds, reducing the risk of buying at the wrong time, and increases the number of units you buy. What's important is your time in the market, not timing the market.
4. **Rebalance your portfolio.** Once you've established your tolerance to risk you should periodically review your portfolio with your advisor and make sure that your risk tolerance matches the types and proportion of investments your portfolio holds. If economic or personal circumstances change, review your portfolio and, if necessary, adjust your portfolio to your level of risk tolerance.
5. **Establish and maintain a financial plan.** If you have not established goals, how can you evaluate the performance of your portfolio relative to what you need it to do? Like anything else in life, you need to establish a plan to reach financial objectives. Be sure to ask yourself what your objectives are, how much risk you can tolerate, and when and for what purpose will you need your money. Remember to fine-tune your plan as personal or economic circumstances unfold.
6. **Consider buying.** Down markets are a prime buying opportunity. There is no better time to make a purchase than when you discover a "sale." Remember to always "buy low, sell high."

The mutual fund industry, and some media articles, takes great efforts to educate investors on the benefits of mutual funds and what questions they should ask before investing. However, sensationalized media coverage of market declines may exaggerate bear markets, corrections, and crashes. Remember: sharp drops get more attention than steady climbs, so don't let headlines cause your emotions to downplay reason as you make financial decisions.

Call me if you have questions about your investment portfolio. Give me the courtesy of a phone call before you make any decisions about the funds you entrusted me to manage for you. That phone call may save you a lot of money. And you may have friends and family members who may benefit from a second opinion or a sounding board; as a service to you, I can give them a call and visit with them if they wish. Either I will validate what they already have, or suggest changes to their existing portfolios

*My aim is to help people make better financial decisions and help them realize their dreams. Thank you for the opportunity to do this for you. **Richard Navarro, CFP***



RICHARD NAVARRO



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