The Sean Fahy Group
PROFESSIONAL WEALTH MANAGEMENT

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FINANCIAL *Perspectives*

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Uneventful First Quarter

After the market roller coaster of 2008 and 2009, the first quarter of 2010 has been uneventful by comparison - the markets ended the first quarter about where they started the year, although up almost 60% from their lows of a year ago.

That being said, there is still a cloud of uncertainty that is making many investors nervous. Even with the stabilization of the global economy, there's no shortage of short term causes of concern:

- Continued questions on the direction and timing of the economic recovery in the United States and Europe
- US housing prices that are staying stubbornly low and unemployment levels in North America and Europe that are stubbornly high
- In late March the deputy director of the International Monetary Fund made headlines as he talked about the need for advanced economies to cut spending in order to reduce deficits.

The good news is that there are offsetting positives:

- On Monday March 22, the Wall Street Journal ran a story about dividend hikes as a result of rising profits by US companies. The article also mentioned that cash on hand on US corporate balance sheets was at the highest level since 2007.
- The Financial Times also ran a similar story about dividend increases in Europe.
- There is growing attention to the impact that Germany's emphasis on manufacturing productivity had in sheltering it from the worst of the economic downturn - and questions about whether this might be a model for other countries. In March the Economist ran a 14- page feature on how Germany positioned itself for success.

Forecasting the Future

Whether you choose to focus on the positives or the negatives, there's broad agreement that the steps taken by governments stabilized the financial crisis that we were facing a year ago - and there is almost no talk today of a global depression. So the issue is not whether the economy will recover, but when and at what rate -and whether there might be another stumble along the way.

If you look for investing advice in the newspaper or on television, the discussion tends to revolve around what stocks will do well in the immediate period ahead ... this week, this month, this quarter. When it comes to short-term predictions, whether about the economy or the stock market, there's one thing we can say with virtual certainty: Most of them will be wrong. Quite simply, no one has a consistent track record of successfully forecasting short term movements in the economy and markets.

Which is why in uncertain times such as today, one of the people I look to for guidance is Warren Buffett.

Advice from Warren Buffett

In an investment industry poll a couple of years ago, Warren Buffett was voted the greatest investor of all time; among the runners up were Peter Lynch, John Templeton and George Soros. Buffett's returns are a testimony to the power of compounding. Warren Buffett has said that it only takes two things to invest successfully - having a sound plan and sticking to it and it's the "sticking to it" part that investors struggle with the most.

I apply this approach as well - putting a plan in place for each client that will meet their long term needs and modifying it as circumstances warrant, without walking away from the plan itself. Boom times such as we saw in the late 90's and scary conditions such as we've seen in the past two years can make that difficult - but those conditions can also represent opportunity.

Stick to Your Plan

Many of the positives that drove market optimism two years ago are still in place, among these the continued emergence of a global middle class in developing countries like Brazil, China, India and Turkey. This educated middle class will fuel global growth that will make us all better off.

Stick to your plan - In the face of economic and market uncertainty, the key to success is having a diversified plan appropriate to your risk tolerance - and then sticking to it. It can be hard to ignore the short-term distractions, but that's the only way to achieve your long term goals with a manageable amount of stress along the way.

Investing Your Tax Return

Every year at the end of February there is a mad scramble to make RRSP contributions. People take out loans, use their credit lines and many need time stamps just to prove they got it in on time.

Because you made an RRSP contribution you likely have a return. Why not take at least part of this tax return to make an early RRSP contribution? Not only will your reduce your stress for next year, but you also will increase the odds of better long term returns.

The Role of Insurance in Tax Planning

Insurance has typically been used to protect against the risk of future financial loss. However, more and more, innovative insurance solutions are being used to safeguard the value of investors' assets in a tax efficient manner.

Creating a Tax-Free Wealth Transfer

Once you have a financial plan that ensures your capital will generate sufficient income and address needs, you may want to consider shifting a portion of your assets to a tax-exempt environment. With a tax-exempt insurance policy, you can maximize the value of your estate and the value of your assets at death since the assets accumulate within the contract, free annual accrual taxation. Part of the policy premium will pay for the cost of the insurance and the rest will be invested, allowing the policy's ultimate benefit to grow through the years. Tax-exempt life insurance shares certain characteristics with other types of investments, however no other asset allows for the following:

- tax-deferred growth, much like within your registered pool of assets
- potential tax-free income during retirement
- tax-free distribution on death

Protecting Assets against Taxation

If you have worked hard to build your investment portfolio, it is worth protecting it from the eroding effects of taxation. This is especially critical for registered investments like RRSPs and RRIFs that become fully taxable on the death of the surviving spouse. Taxation concerns extend beyond your retirement assets to other investments or valuables such as a family cottage that may be subject to capital gains tax.

Tax-free insurance proceeds are immediately available on death and provide funds to pay taxes at the time. In the absence of using tax-free insurance, beneficiaries may have to consider either selling the estate assets or borrowing funds to pay taxes owing on the estate.

Generating Tax-Preferred Income

An insured retirement strategy can help you meet the need for both supplemental retirement income and estate liquidity in a tax effective way. By allocating excess capital or income into a tax-exempt insurance structure a number of years ahead of retirement, you allow the investment component to grow over time into a large pool of capital, better known as the policy's cash value. At retirement, up to 90% of this cash value can be pledged to a bank for a series of loans. As loans, the corresponding retirement income is not considered taxable income.

This approach is also a consideration for small corporations. Shareholders can use the tax-free loan proceeds against the cash value of a corporate-owned policy to supplement their retirement income.

Securing a Guaranteed Income Stream

Life annuities can be very useful in providing a guaranteed, lifetime, tax-preferred income. An annuity is the opposite of life insurance: instead of paying an insurer small annual amounts in return for a large amount at death, you give the insurer a large amount up front and receive small annual amounts every year until death. Each payment is a blend of interest and a return of your original capital, of which only the interest portion is taxable.

If guaranteed income is a requirement as well as maintaining your estate, this can be accomplished by insuring your original annuity deposit. The net income from this strategy is often much higher than the net income from a GIC or bond, even with the cost of insurance.