CIBC Wood Gundy

Perspective

Compliments Of Voronoff Private Wealth Management

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Risk: That Four-Letter Word?

Risk. It's a four-letter word that many Canadians love to hate. But in today's world, being too risk averse can be a risk itself when it comes to investing and meeting future retirement goals.

For investors who still have the luxury of time before retirement, one of the keys to retirement planning is realizing that the investing landscape is much different than it was just twenty years ago. Back then, it was easy to achieve substantial returns by investing in low-risk fixed income instruments like guaranteed investment certificates (GICs) or government bonds.

Today, with interest rates at historically low levels, investors may overlook the fact that putting funds into low-risk fixed income investments can actually be risky. Any small gains made can be eroded when interest income is taxed when these investments are held in non-registered accounts. Although it doesn't appear to be a threat in the near term, inflation can also erase any gains made in low-yielding investments over time by reducing the purchasing power of your capital. This is further complicated by the challenge of planning for longer life expectancies because income requirements are higher. While interest rates are expected to increase, today's low-rate environment demonstrates how the risk profile of certain investments can easily change based on market conditions.

Assuming some risk has always been a normal part of investing and is necessary to build wealth over time. This doesn't mean that investors need to take excessive risks in an attempt to maximize their returns. Making intelligent decisions when it comes to managing risk is part of effective portfolio management.

As the investing world continues to evolve, one of the most important services that we provide is helping you to manage the changing risk environment appropriately over time so that risk never becomes that four-letter word.

Voronoff Private Wealth Management

Speaking Personally: At the time of writing, markets close to home continue to perform well. However, we expect periods of short-term volatility as the year progresses. Given that volatility is a normal part of the markets, it is worth repeating that staying invested is important. At the same time, don't forget that small market corrections can turn out to be great buying opportunities.

Enjoy the longer days ahead.

Financial Market Monitor

	Recent 03-06-14	*Six Months Ago (09-05)*	*One Year Ago (03-06)*
S&P/TSX Composite Index	14271.92	12845.06	12831.96
Dow Jones Industrial Average	16421.89	14937.48	14296.24
Canadian Interest Rates/Yields			
Canadian Prime Rate	3.00%	3.00%	3.00%
Treasury Bills* -3 month	0.83%	1.00%	0.95%
-6 month	0.87%	1.03%	0.99%
Gov't. of Canada Bonds* -5 year	1.71%	2.15%	1.30%
-10 year	2.50%	2.80%	1.84%

* Approximate annual rates.
Subject to transaction volumes, availability of specific issues, and other important factors.

In This Issue:

Page

Estate Planning: Gifting While Alive 2
Our Weakening Dollar 2
Winding Up Your RRSP 3
Why "Buy-and-Hold" Makes Sense 4

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Take Action Today

Estate Planning: Executing Plans While Alive

For many, the idea of estate planning means preparing for what happens *after* death. But executing your estate plan may be possible well before death. Outside of the satisfaction of seeing your beneficiaries enjoy the gifts during your lifetime, distributing assets while alive may provide additional benefits than waiting until a will is invoked.

Since Canada does not have a gift tax (unlike the U.S.), assets can be gifted by you and received by the beneficiary tax-free. However, if your gift is not in cash but in the form of assets that may have appreciated in value, such as real estate or marketable securities, you will be considered to have disposed of the assets at fair market value at the time of gifting which may result in a capital gains tax liability.

Minimize Taxes While Alive — If your adult child or grandchild beneficiary is in a lower tax bracket than you, it may be beneficial to transfer investable assets to them during your lifetime. Any annual investment income will be taxed at their lower marginal tax rate instead of at your higher marginal rate, reducing the overall family tax bill. Gifts to spouses or related minor children may result in negative tax consequences because any income generated from the gifted property or capital gains from gifts to your spouse can be attributed back to you.

Reduce Taxes at Death — Gifting assets during your lifetime can reduce the size of your estate and the potential capital gains taxes that arise upon death. In addition, reducing the size of your estate during your lifetime can generally help to reduce or avoid probate or estate administration tax in provinces where applicable.

Maximize Charitable Donation Credits — If part of your estate plan is to provide assets to a charitable organization, you may receive greater tax benefits by making gifts annually and using the charitable donation credits to reduce your tax liability during your lifetime as opposed to having a large donation credit at death which may not be fully utilized.

Seek Assistance

Many factors may impact your decision to make gifts during your lifetime, including the amount of assets needed to maintain a certain standard of living, the difference between your marginal tax rate and your beneficiary's current/future marginal tax rate and whether or not your will is subject to probate or estate administration tax.

We can work with you and your tax advisor to develop strategies that relate to your particular situation.

Consider The Impact

The Weakening Canadian Dollar

The Canadian dollar continues to trade at some of the lowest levels experienced in years. For most of 2011 and 2012, the dollar traded higher than the U.S. greenback and many of us became accustomed to its strength. Yet, it is easy to forget that until September 2007, the Canadian dollar had been valued lower than the U.S. dollar for almost 30 years.

What does this mean for investors?

A weaker Canadian dollar may help to boost Canada's economic recovery. Since our goods become less expensive to foreign purchasers like the U.S., our largest export market, the weaker dollar can help to stimulate an increase in exports. This can help to reduce excess capacity and potentially increase competition for production inputs, which can help to increase the prices of goods and services. This, in turn, could put upward pressure on inflation, which has been under the Bank of Canada's target of two percent for most of the past six years, and may help to stave off disinflation or deflation.

Don't underestimate the effect of currency risk when it comes to foreign investments. As the Canadian dollar weakens, investments denominated in foreign currencies experience currency exchange gains. Conversely, as our dollar strengthens, it takes a greater investment gain to make up for the loss in currency exchange. As such, we continue to stress the merits of diversification, including currency diversification, within a portfolio.

As we contemplate a weaker dollar, here are some interesting historical facts about our currency:

- **1858:** First Canadian government coins are issued, including a 20-cent coin (changed to a 25-cent coin in 1870).
- **1866:** First Canadian government-issued paper currency is released. Before this, notes issued by chartered banks were used.
- **1962 – 1970:** Canadian currency is pegged to the U.S. dollar.
- **1970:** Canada returns to a floating currency due to inflationary issues.
- **1986 (Feb. 4):** Commodity prices fall; Dollar hits a low of US$0.6913.
- **2002 (Jan. 21):** Dollar hits modern-day all-time low, reaching US$0.6179.
- **2007 (Nov. 7):** Dollar hits modern-day all-time high of US$1.10, eventually closing at US$1.0775.

What Happens Next?

Winding Up Your RRSP

The Registered Retirement Savings Plan (RRSP) continues to be one of the best savings tools for Canadians when it comes to retirement planning. If you have been making contributions but are not near retirement age, you probably haven't considered the options for when the RRSP eventually needs to be wound up. Of course, the funds in your RRSP can be accessed at any time prior to and during retirement, but we continue to support the practice of maintaining your RRSP for as long as possible for its tax-deferral benefits.

Your RRSP must be wound up in the calendar year in which you reach 71 years of age. What happens at that time? There are currently three maturity options available, which can be used exclusively or in combination:

1. Distribute funds as income. The RRSP is closed and RRSP assets are distributed to you and included in your taxable income in the year you receive the assets. This may create a significant tax liability. As well, any investment income earned on the after-tax value of the assets withdrawn from the RRSP in the future is also subject to tax. As such, this is likely not the most effective alternative for most investors.

2. Purchase an annuity. A lump sum amount is transferred from an RRSP to an insurance company, entering into an annuity contract. The annuity provides annual payments for the rest of your life. There are many different types of annuities, including annuities with guaranteed payout periods or those indexed to inflation.

While the benefit of this option is that an income stream is guaranteed for the remainder of the holder's life, there are potential disadvantages. Once a lump-sum payment is made to purchase the annuity, the contract cannot be reversed and access to the original capital is lost. Also, the annual payments associated with an annuity may be lower if it is acquired during a period of low interest rates compared to an annuity purchased during a period of higher interest rates.

3. Transfer to a Registered Retirement Income Fund (RRIF). The RRIF acts as an extension of your RRSP because capital continues to be invested on a tax-deferred basis and assets can transfer "in kind" (as is) from the RRSP. The main difference is that an RRIF is subject to an annual minimum withdrawal requirement, which creates taxable income for the holder.

The first withdrawal from the plan is required in the year following the year of conversion and the amount is determined by the holder's age and the amount of assets in the plan on Dec. 31st. However, for holders with a younger spouse, the minimum withdrawal calculation may be based on the spouse's age to lower the annual taxable payments.

Although the minimum withdrawal has no tax withheld, it may be taxable depending on total income. Amounts above the minimum can be withdrawn, but tax will be withheld. Finally, the full amount of the RRIF will generally be subject to tax in the terminal tax return of the holder at death, unless a spouse has been named as the plan's beneficiary or successor annuitant, or a qualifying financially dependent child or grandchild is named as a beneficiary.* As a plan beneficiary, a spouse can transfer funds on a tax-deferred basis to an RRSP or RRIF in their own name. As a successor annuitant, the surviving spouse can continue the plan under their name.

As you near the age where the RRSP needs to be wound up, proper planning can help to ensure that the best decision is made. Many factors will impact which option is most beneficial, including income needs, future capital requirements, current interest rates, level of inflation and size of the estate that you wish to leave for your beneficiaries.

*In Quebec, a beneficiary cannot be designated in certain RRSP/RRIF contracts. The designation has to be made in the will for these types of contracts.

Please note that comments included in this publication are not intended to be a definitive analysis of tax law. The comments contained herein are general in nature and professional advice regarding an individual's particular tax position should be obtained in respect of any person's specific circumstances.

Cash Flow Is King

Don't Forget Dividends

In today's low rate environment, cash is no longer "king". However, cash flow remains important and investing in dividend-paying equities continues to be one way of generating returns.

Solid companies that have strong balance sheets and perform well typically pay dividends in both good and bad market conditions, boosting performance in favourable markets and potentially cushioning against the impact of market declines.

Over the past 20 years, dividends have accounted for almost 30 percent of the total return of the S&P/TSX Composite Index, so their significance should not be overlooked.

Here's how dividends have contributed to the S&P/TSX Composite Index over this period:

S&P/TSX Composite Index Annualized Total Return

	5 Years	10 Years	20 Years
With Dividends	11.88%	7.92%	8.21%
Without Dividends	8.67%	5.18%	5.90%
Difference	3.21%	2.74%	2.31%
Dividends as % of Total Return	27.02%	34.59%	28.14%

Source: Bloomberg. All periods ending December 31, 2013.

Why “Buy-and-Hold” Still Makes Sense

Stick to your long-term investment plan. Here are some reasons why patience can add value.

While some investors may have dreams of becoming active day traders, most investors will benefit from a longer-term view to maximize their portfolio value over time.

Whenever we experience market volatility, it may be tempting to question our current ways and consider abandoning aspects of our long-term plan. But sticking to that plan and riding out periods of short-term volatility often does have its benefits.

Here are some reasons why the buy-and-hold strategy still makes sense:

Minimize taxes — Higher turnover in your non-registered investment portfolio can lead to higher capital gains taxes.

Let’s take a simple example: if an investor held an investment over a 10-year period that appreciated at a rate of 5 percent per year, the after-tax return (assuming a capital gain) would be 50.3 percent based on a marginal tax rate of 40 percent.

If all factors remained the same, but instead the investment was sold at the end of each year, giving rise to a capital gain, and both the principal and gain were reinvested, the after-tax return would only be 48.0 percent. This difference increases with higher trading volumes and over longer time periods. The example does not include trading costs which would further reduce the overall return of the higher-turnover investment.

Take advantage of dividends — With frequent trades, an investor may miss the opportunity to take advantage of dividend payments. In order to receive a dividend payment, an investor must be on the dividend-paying company’s books as a shareholder. When a company declares a dividend, it sets what is termed a “record date”.

Stock exchanges will fix an “ex-dividend date”, usually two business days before the record date. If a share is purchased on its ex-dividend date or after, the next dividend payment will not be received by that purchaser and the seller will receive the payment.

Don’t underestimate the effect of dividends on your portfolio’s return. Over the past 10 years, dividends have accounted for 35 percent of the Toronto Stock Exchange (TSX) total returns (as we show on page 3 of this newsletter), which is a very significant contribution.

Reduce transaction costs — The potential for higher transaction costs may also increase with more frequent trades. As such, an investment would have to achieve a higher rate of return to make up for the greater costs associated with frequent trading.

Avoid missing upswings in the market — Predicting when the markets will have significant gains, or timing the market, is difficult if not impossible. As renowned investor Warren Buffett has said: *“The only value of stock forecasters is to make fortune tellers look good.”*

Various studies have shown that some of the most significant investment gains have been made over a handful of one-day gains. Staying invested over the long term is the best way to avoid missing out on these gains.

Parting Thoughts

Of course, none of these reasons should be the primary decision-making factor when it comes to holding on to a particular security. Evaluating the long-term prospects and performance of an investment should always remain a priority. However, these considerations should be part of an overall investment strategy and are a good reminder to investors that having patience when it comes to your portfolio can add value.

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