Quarterly Exchange

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Through the *Quarterly Exchange,* we'll keep you up-to-date on current investment trends and strategies. We are committed to working one to one with you to help you achieve your financial goals. Please contact us if you have any questions or wish to discuss any of the articles in this newsletter.

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Tell Me Something Good

Benjamin Tal, Managing Director, Wholesale Banking

It is well known that financial markets overreact to macro-economic data, and that, in normal times, they overreact to bad news more than they overreact to good news. But these are not normal times. In today's environment, good news has the upper hand.

In Europe, Greece-fatigue makes European developments secondary in affecting the mood in the market with investors growing increasingly indifferent to news from the zone—probably with the realization that any turn to the worse will be dealt with effectively by the ECB.

In China, there is seemingly no such thing as bad news. When the January "semi-official" PMI reading topped expectations, the market took it as a welcome sign that the manufacturing sector there is still expanding. For the opposite reason, markets also reacted positively to the worse-than-expected 4th quarter GDP print, taking the two-tick miss as a sign that policy will be eased further.

In the U.S., the 12% rally in the S&P 500 since mid-December is largely attributed to the better-than-expected economic data during that period. But on average, the market has also been reacting positively to negative data surprises. No less than one-third of all major economic data released over the past three months outpaced expectations. And those positive surprises were immediately translated into gains in the equity market. After all, with the Fed committed to remain in neutral until 2014, the market can enjoy the full benefit of stronger-than-expected macro data without worrying about the usual spoiler of increased policy-tightening expectations.

In Canada, negative surprises dominated the economic scene over the past three months. Still, the market managed to advance by 9% — dancing to the tune of international and U.S. markets, while largely ignoring domestic data. And the likelihood is that investors will have plenty to ignore in the coming months, mainly in the manufacturing sector where the impact of the strong dollar is still clearly evident.

How long this win-win trading environment will last is anybody's guess, but the likelihood is that this process has not been exhausted yet. The U.S. economy is fully capable of upside surprises in the coming quarters, its way back into the economy, while the Fed, in all likelihood, will keep the QE3 option alive as long as possible. This euphoric trading could continue until the market wakes up to the realization that whatever it gets now will be taken away by the big fiscal drag of 2013.

Blinded By The Refund

Jamie Golombek, Managing Director, Tax & Estate Planning, CIBC Private Wealth Management

With the introduction of the Tax-Free Savings Account (TFSA) in 2009, some Canadians may find that they now have a better option when saving for retirement. However, a lack of understanding and appreciation of how TFSAs work may have some missing out on the benefits of this powerful new retirement savings tool. Since its launch only 20 percent of eligible Canadians have opened an account investing some $19 billion tax-free, which suggests that Canadians are not embracing the TFSA as a means to funding a comfortable retirement.

It goes without saying that Canadians that can afford to maximize both RRSP and TFSA contributions would be well advised to do so, but the reality is that most Canadians simply cannot afford to do both.

To help explain the tax mechanics behind both an RRSP and TFSA contribution let's compare the after-tax net cash over 20 years. Remember, unlike an RRSP on which tax is deferred until the funds are withdrawn from the plan, taxes on assets held within a TFSA are "pre-paid."

Chart 1 – After-tax cash in TFSA & RRSP

	TFSA	RRSP
Pre-tax income	$5,000	$5,000
Tax (40%)	(2,000)	
Net contribution	3,000	
Growth at 5% / 20 years	7,960	13,266
Tax upon withdrawal (40%)	--	(5,306)
Net cash	$7,960	$7,960

So the question is what savings vehicle should take priority? It's only when your tax rate upon withdrawal is either lower or higher than your current tax rate that the TFSA or RRSP wins out. By taking the time to look at three retirement scenarios – unchanged tax rate, high to low tax rate, and finally low to high tax rate – we come to conclusions that favour one savings vehicle over the other.

As we can see in the chart at the bottom of the page, when the tax rate stays the same during retirement the TFSA and RRSP provide the same net cash results. However, in looking at the second scenario, when the tax rate is reduced in retirement we see the RRSP will produce the better result. Conversely, in the final scenario, when tax rates increase during retirement, the tax benefits of the TFSA win out.

One advantage the TFSA provides over RRSPs in all scenarios, is accessibility. The ability to withdraw funds from the TFSA, at any time, tax-free, may be an important consideration for some Canadians. In addition, funds withdrawn from a TFSA can be re-contributed unlike an RRSP.

This provides a simple overview of the benefits both the RRSP and TFSA can provide, however there are a number of other considerations that should be taken into account before contributing to either plan such as income-tested government benefits and credits such as the Old Age Security (OAS) benefit and Age Credit.

Working with your Investment Advisor can help you understand the solutions that are right for you – whether a TFSA, RRSP or both.

For a full copy of this report or to discuss this information further, please contact my office.

Chart 2 – Working vs retirement tax rate scenarios

	Same Tax Rate		High To Low		Low To High	
	TFSA	RRSP	TFSA	RRSP	TFSA	RRSP
Pre-tax income	$5,000	$5,000	$5,000	$5,000	$5,000	$5,000
Tax rate – contribution	40%		40%		20%	
Tax	(2,000)	-	(2,000)		(1,000)	-
Net Contribution	3,000	5,000	3,000	5,000	4,000	5,000
Growth at 5% / 20 years	7,960	13,266	7,960	13,266	10,613	13,266
Tax rate – withdrawal		40%		20%		40%
Tax	-	(5,306)		(2,653)	-	(5,306)
Net Cash	$7,960	$7,960	$7,960	$10,613	$10,613	$7,960

Benefit From The Multi-Disciplined Approach Of The CIBC Investment Strategy Committee Model Portfolios

"To invest successfully over a lifetime… what is needed is a sound intellectual framework for making decisions and the ability to keep emotions from corroding that framework." — Warren Buffet

We are pleased to announce the availability of a new investment service available exclusively to CIBC Wood Gundy clients. The **CIBC Investment Strategy Committee Model Portfolios** are expertly crafted model portfolios, designed and managed by leading investment professionals from across the CIBC group of companies.

A model portfolio allows you to directly own a concentrated portfolio of equities, fixed income and cash that is recommended by a team of experts at CIBC. These portfolios are continuously monitored and updated so your portfolio is always positioned to take advantage of current market conditions.

Two model portfolios are available: the **Canadian Core Model Portfolio,** which seeks to achieve long-term growth of capital and income by investing primarily in proven Canadian companies, and the **North American Yield Model Portfolio,** the objective of which is to provide sustainable yield and capital appreciation by investing in a diversified portfolio of Canadian and U.S. companies.

The CIBC Investment Strategy Committee Model Portfolios are led by Peter Gibson, Head of Portfolio Strategy & Quantitative Research at CIBC World Markets Inc. Brendan Wood International has ranked Peter as the TopGun™ Analyst in Quantitative Analysis for the last 10 years and the TopGun™ Analyst in Portfolio Strategy for 8 of the last 10 years. Mr. Gibson and the Investment Strategy Committee use a multi-disciplined approach to stock selection, combining the strength of fundamental, quantitative and technical analysis. Such an approach aims to overcome the weaknesses associated with a single-style approach.

I believe these model portfolios can make an excellent addition to your current investment plan. For more information on the CIBC Investment Strategy Committee Model Portfolios, or to discuss whether one of the portfolios is right for you, please contact my office.

Why Are A Majority Of Business Owners Not Planning For Their Exit?

Sean Foran, Managing Director, Business Transition Planning and Trust Services

For many years now it's been common knowledge that a majority of small business owners are not planning for the succession of their business. But, why?

I believe that behind a reluctance to let go of their business is a lack of a framework to approach this potentially emotional decision. To increase the likelihood of a successful transition of your business, it is important to have a framework that isolates the critical success factors in the decision to keep or sell their business.

When speaking with clients, I offer the following four points to consider.

1. **Consider the future leadership needs of the business.**

   There are essentially three forces at play in Business Transition Planning – the family involvement in the transition, the desires of the shareholders around successor ownership and leadership and the needs of the business itself. Asking what the business itself needs from successor leadership can provide the objective criteria for the successor selection or best exit strategy for the owner of the business.

2. **Identify a capable successor and prepare them to take over.**

   The research on family business tells us that in order to truly let go, a business owner must trust in a willing and able successor. Successors don't become willing and able overnight. They need adequate preparation and need to see that the owner will begin to let go of increasingly important decisions. That's a key driver of successful succession. Ask your successor if he or she feels prepared to take over your role. You may be surprised at the answer.

3. **Understand where the business sits in the competitive landscape and your available resources to keep it growing.**

   Business owners should regularly analyze their business to determine its place in the competitive landscape. Knowing where the business sits and how well resourced it is in terms of the financial and managerial resources of the business and the emotional resources of the business owner are critical factors in deciding whether to keep or sell the business.

   Emotional resources are about the commitment of the owner and family to continue to invest or re-invest in the business after the owner is no longer actively running the business.

   If you are not confident about your emotional, financial and managerial resources to keep the business in the family, maybe it's time to let someone else take the business to the next level.

4. **Leave at the top of your game.**

   Many business owners leave their succession and transition planning too late, curtailing their exit options. Investing in strong tier two management is really an investment and not an expense. Teaching others to do what the owner has historically contributed to the business is an investment in the owner's future freedom and is a critical success factor in a successful transition whether the business is to transition to a successor within the family or to a third party.

   As small and medium sized businesses represent $600 million of GDP, understanding these critical success factors and a framework for deciding on the appropriate exit strategy are key to ensuring stable transitions both for small and medium sized businesses and the economy as a whole.