# Outlook on Business

*Money matters*

## Investing after Black Monday

By J. BRUCE MOORE
Herald Special

Since Black Monday, October 19, 1987 the financial markets and the factors affecting them continue to attract major media attention.

The investment marketplace as Canadians have historically known it, was a matter of knowing what effect U.S. policies and procedures would bring to bear on Canada.

This perception is no longer accurate as indicated by media reports. The marketplace is now global. Activities in Washington have an immediate and sometimes, calamitous effect in London, Tokyo and Toronto.

What should you do with your investment funds, with the current environment of conflicting forecasts for interest rates, the dollar and recessions?

One suggestion: Invest in your home!

—Prepay your mortgage
—through an annual lump sum payment
—monthly principal reduction payments
—higher monthly mortgage payments.

Every homeowner with a mortgage can save money in interest costs. This can be used for more useful purposes such as investment for your retirement.

To illustrate: Savings from mortgage prepayments.

A $100,000 semi-annual mortgage with 12 per cent interest compounded semi-annually, can be discharged over 25 years with monthly payments of $1,031.90. You would end up paying $309,570 - or more than twice the amount borrowed, in interest payments.

Consider the first year's payment of $12,382.80 (12 x $1,031.90); only $700 is applied towards reducing the $100,000 principal amount. $11,682.80 has been used for interest charges.

Look at it another way. If the $96,000 you saved over the 15 year term ($533.33 per month), was invested in a self directed retirement plan earning 8 per cent interest compounded semi-annually. Your accumulation upon retirement would be $179,470.

Isn't this better than paying $96,000.

Canadians cannot deduct interest on money borrowed to buy a house, so home ownership is very expensive.

If your mortgage rate is 12 per cent and you are in a 50 per cent tax bracket, you must earn double the amount of 24 per cent on your money to meet your payments.

Quite a burden!

It would be beneficial to discharge this after tax expense, as early as you can.

Increase your monthly payment by just $150 more each month and you will save, in our example above, $96,000 in interest costs. What's more, you will own your home 10 years earlier.

The interest you save ($96,000) can be utilized for more beneficial purposes

You could invest in a self-directed RRSP where your contributed funds are pre-tax dollars and your funds grow tax free.

Taxes and inflation always ravage our savings. Assuming inflation of 5 per cent and assuming your present income is $45,000, in 20 years you will need to earn $119,398 just to preserve your purchasing power.

Because funds grow tax-free within a RRSP, your before tax and after tax rate of return are identical.

For example, you purchased $10,000 worth of Canada Savings Bonds this year, your return is $900 for the first year.

If, however, you are in a 50 per cent tax bracket and the CSBs are *held outside a RRSP, (and ignoring* the $1,000 interest expense deduction), your return is $450. If you deduct inflation of say 5 per cent, your rate of return is negative and your principal is being eroded.

It makes sense to always consider ways to reduce your interest charges by prepaying your mortgage and to determine how one can continue to reduce taxes and keep ahead of inflation.

Despite the uncertainty and volatility of today's market, personal asset planning and management cannot be ignored.

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**For more information on this article or for virtually risk free investments to protect your capital, please call (416) 897-3207 and ask for Bruce, John or Cap.**

## Take aim on financial independence

**By Mark Serbinski, CA**

(NC) — Financial independence is a goal more of us would achieve if we had a proper plan and the necessary pool of money to take advantage of opportunities.

Start by setting your goals. Figure out what you really have to have, and what you merely want — because achieving financial independence means giving up something today to have the money you need tomorrow. Set medium-term (3-5 years) and long-term (from now till you retire) goals. Assign them a priority.

Next, construct a budget. It's the only way to build that pool of money you need to reach your financial goals. And be realistic: don't cut yourself too short or build in too much budget fat — both are prescriptions for failure.

Your next job is to set a path to reach your goals. For example, if you want to buy a house in two years, determine the downpayment you'll need and how much you must save each month to have that amount in two years. Then check your progress regularly, to see if you are on track. If you are not, calculate what is required to get back on track, then take the corrective action. Be tough on yourself.

Once you have your pool of money, you can begin investing for financial independence. Let's review some possibilities:

**RRSP's:** If you are going to invest, choose tax-deferred investments — like RRSP's — first. There are two reasons: you can't count on the Canada Pension Plan to keep you in your old age; and contributions to an RRSP give you an important tax saving.

**Stocks and Bonds:** Unless you know a lot about stocks and bonds and have time to study the markets carefully on a continuing basis, avoid them. For most, the risks of losing outweigh the chances of big gains.

**Mutual Funds:** A better bet. Your risk is less because your money, pooled with the money of others, buys into hundreds of different stocks. A caution — past performance is no guarantee of future performance.

**A House:** One of the best investments. To get one you'll need a plan to save the downpayment. Remember, you don't have to start with your dream house. Buy a house you can afford — which will help protect you against housing inflation — and trade up as your income rises.

Work at paying off your mortgage, a risk-free return on your money, and when you're done, you can turn to other investments.

**Moneycare is general financial advice by Canada's chartered accountants.**

## DOLLAR SENSE

**By Sheldon Buchalter, CA**

Because of widespread opposition, Finance Minister Michael Wilson's $500,000 lifetime capital gains exemption for individuals might not be long-lived, so taxpayers should take advantage while they can.

Except with a family farm, the exemption is being phased in, so you can claim the exemption against capital gains of $50,000 in '86, $100,000 in '87, $200,000 in '88, $300,000 in '89 and the full $500,000 in 1990 and subsequent years. On the sale of a family farm, the whole $500,000 can be claimed, starting in 1985.

The gains for a particular year are reported on line 127 of the tax return ("Taxable capital gains/Allowable capital losses"). A form called T657, available from the tax office, is used to calculate the exemption. You must also fill in Schedule 3 (Summary of Dispositions of Capital Property in 1986).

## Yes — you can move your RRSP to get more

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**IT'S YOUR MONEY**
**Paul J. Rockel**

(NC) — Is your RRSP earning 11%, or less?

Today, many many people are receiving 11% or less rate of return on their RRSP investments. Oh, sure, in many cases they are "locked up" in "guaranteed rates" for a specific period (usually five years or less) but on average, even 5-year GIC's have only "averaged" 10.89% over the past 10 years, despite the fact there were a few months in 1982 where you could get as high as 17% or 18%. But, overall, those high rates were available only for a short while, as they soon fell rapidly to the more "normal" rates available today (and still falling).

But, what if you can get more return for your RRSP's? Are you forced to stay with the RRSP you currently have, that may be paying less than others have proven to do? The answer is "No, you are not forced to stay where you are." You can transfer your RRSP to another institution, (the industry word for this transfer is "rollover") by simply using a Government transfer form, called a T-2033. They can and will be provided by the new institution you wish to take over your existing RRSP.

Or, you can have two or more RRSP's, with different institutions. No matter where you use your RRSP, the tax-deductions will always be the same, fully related to your taxable income.

Why would you want to move to another institution? Well, if it is indeed only giving you a rate of return of 11% or less, and you feel comfortable that another RRSP could return 15%, wouldn't it be wise to change?

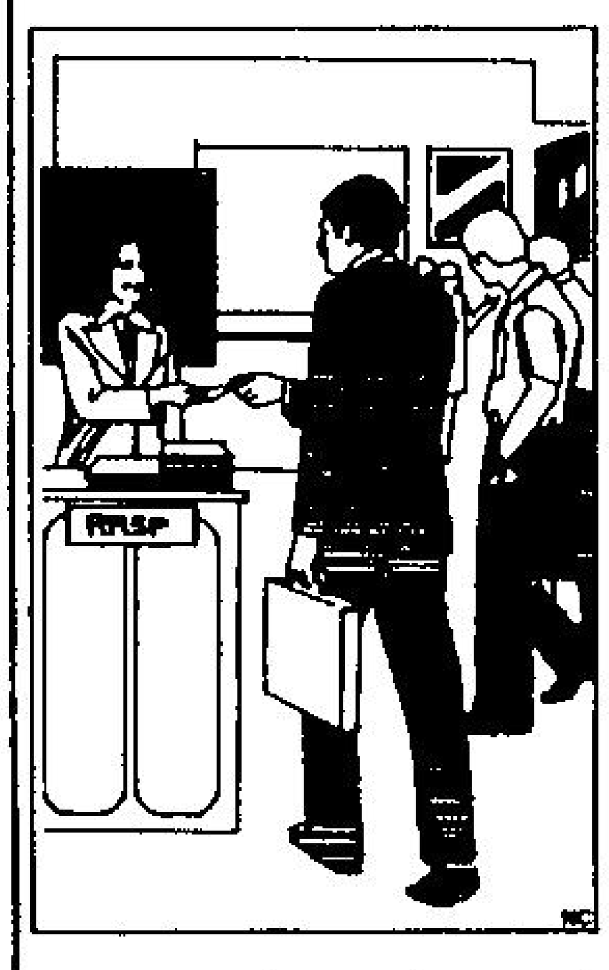
The mathematics say you should change. If you are 35 years old, and put $3,000 per year into an RRSP, chances are you'll save at least *$1,000 in taxes each year (or more,* depending on your tax bracket). In effect, it makes the "true cost" of that RRSP to be $2,000 (or less) rather than the actual $3,000 you invested.

But, from age 35 to age 65, a period of 30 years, the person receiving 11% rate of return would have a value of $662,739, whereas the person receiving a 15% rate of return would be worth $1,499,870. It's a mathematical fact. That's $837,000 more dollars.

The question arises: Which amount would you rather have for your retirement, $662,739 or $1,499,870? I guess the answer is obvious, isn't it!

Can you get 15% **average** rate of return? Well, the past has certainly proven so. There are many good equity mutual funds that have long-term records of achieving 15% and better over the past 10 and 15-year periods. (Some have 10-year records of 20%). Admittedly, some years those funds achieved 25% and better, and other years only a small, or negative return. But the **average** of 15% is real.

If you are getting 11% or less now on your RRSP, maybe a transfer (rollover) should be considered?




**Your comments and questions are welcomed. Simply write: Paul J. Rockel, Regal Financial Centre, 153 Union St. E., Waterloo, Ontario, N2J 1C4 and/or for a copy of his book "Why I Invest in Mutual Funds" forward payment of $8.95 (retail $12.95).**
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