

Canada Savings Bonds are Coming

By George Perdue, B. Sc. P. Eng.

It's just like the election. One competing against the other. All making promises. None telling all.

The banks and trust companies are introducing their products to go against the CSBs and they are setting interest rates just over 4 percent. They have their CSB special on giving cashable GICs to compete against the liquidity of the CSBs.

All the institutions want your money. So what's in it for them? Better returns, that's what. They invest the money you loan them. That's right, they view your money as a low interest rate loan. They invest it in higher return securities. They pay you and keep the rest. Then, in the case of the banks, they report record profits.

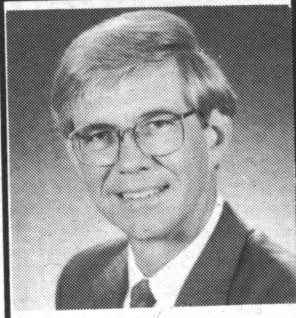
Now, of course, even the smallest investor can short-circuit the institutions and make direct investments in those higher income securities and keep it all.

So what are the pros and cons?

CSBs are convenient and they are liquid. Although Brian Costello has unkind words for them, they do have some appeal. They are as secure as the government who prints them. They help finance the debt. The yield is low and the income is taxed 100 percent at your marginal tax rate.

The first alternative to CSBs are GICs. They are

Money Talk with George Perdue



almost as convenient and secure. They finance institutional investments. The yield is low and the income is taxed 100 percent at your marginal tax rate. In contrast to most GICs the GICs issued at this time are arranged to be liquid. All of the other alternatives discussed are also very liquid.

Another alternative is the money market. This is also convenient. The rate of return fluctuates with the bank rate. Security is also tied to the government which issues treasury bills to finance its debt. The yield is low and the income is taxed 100 percent at your marginal tax rate.

Traditionally, mortgage funds have been an alternative to CSBs and GICs. These securities have been performing with lower rates (around 5 percent annualized) as interest rates have declined. Interest income is 100 percent taxed at your personal marginal tax rate.

Next is an alternative that is more aggressive and has a higher yield. This security also has a fluctuating yield. These are mortgage backed securities. The yield in recent years has been 11 percent to 14 percent. If taken as interest income you are taxed 100 percent at your marginal

tax rate. This option also can be turned into a capital gain which attracts no taxes if you have not used up your capital gains allowance.

Dividend producing securities are also an alternative. They too have a fluctuating yield and a reduced tax burden. Since they are securities from companies trading on the stock exchange they have more volatility in their performance. The yield here has fluctuated between 9 percent and 15 percent in recent years.

Balanced funds provide an attractive alternative today. There is no guaranteed rate of return. Since the returns are often a combination of interest, dividends and capital gain, there is a tax advantage.

The final alternative is equities. These have the highest returns, the most volatility, and the least taxes.

Of course you can also provide diversification by combining several alternatives that meet your objectives.

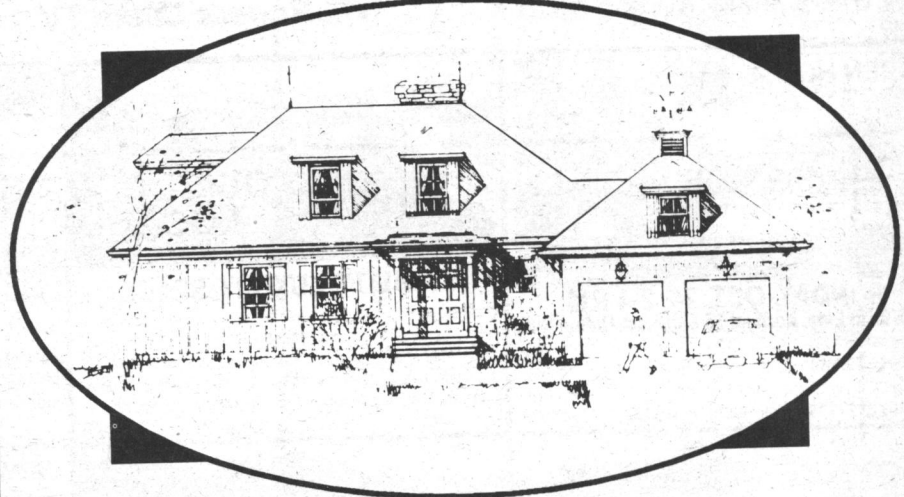
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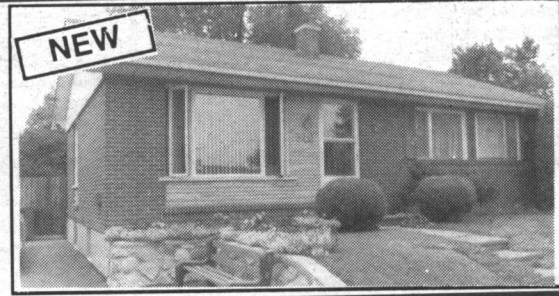
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