POSTED ON 24/01/07

Report on RRSPs: PORTFOLIO STRATEGY

A page from the pros' playbooks

Four financial advisers share their RRSP tactics with JEFF BUCKSTEIN

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SPECIAL TO THE GLOBE AND MAIL

Last year may have been another sizzler for the S&P/TSX Composite index -- which was up by 14.5 per cent over 2005 -- but professional financial managers know that good times never last and some are waiting nervously for the other shoe to drop in 2007.

The good news is that many financial experts who are not bullish expect only a moderation, rather than a precipitous drop-off, in equity markets. For this reason, and others, they feel little need to panic when it comes to holding steady with investment plans -- especially when it comes to their own RRSP portfolios.

Here, four financial experts discuss what they are doing with their own registered retirement savings plans in 2007, as well as the market conditions they expect will serve as their investment backdrop for the next 12 months.

They caution, however, that the decisions made for their portfolios are geared to their own personal circumstances, and might not be relevant to others.

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Report on RRSPs

On the hunt for a sure bet

A page from the pros' playbooks

Enlarge Image

David Phipps

Position: Senior financial adviser, Assante Capital Management Ltd., Ottawa

Age: 41

RRSP portfolio: Weighted approximately 60 per cent in equities and 40 per cent in fixed-income instruments.

Mr. Phipps, a certified financial planner, takes a consistent, steady-as-she-goes approach to his RRSP. It includes developing an optimized portfolio based on long-term returns from different classes of assets.

"It's based on the premise that we cannot accurately predict which asset class is going to outperform in the future," he explains, which is why he doesn't like to change the basic composition of his RRSP portfolio in a new direction "in any single year."

The asset allocation in his RRSP involves about 60 per cent equities, geographically split with 24 per cent from Canada, 21 per cent from the United States and 15 per cent international.

The fixed-income category consists of about 15 per cent income trusts, 15 per cent Canadian government bonds, 10 per cent corporate bonds, 10 per cent a mixture of income trusts and high-yield bonds and the remaining 5 per cent in global bonds.

Target rate of return: Mr. Phipps doesn't like to select a specific one-year target.

"Look at history, and there are so many years where events came out of nowhere and changed everything, so I really don't have a short-term target rate of return," he says.

Instead, Mr. Phipps prefers a long-term target of "around 8 per cent," which he believes is a strong return for a portfolio with only 60 per cent equities.

Basic strategy: Mr. Phipps, who expects to retire in about 20 years, describes himself as a conservative investor, especially within his RRSP: "My philosophy is that the RRSP should be designed to replicate a pension plan." He prefers to take investment risks outside the plan, and prefers to hold individual stocks outside the plan to have capital gains and dividends taxed on a preferential basis.

He likes to contribute as early in the year as possible to his RRSP, to get the maximum growth and compounding. He also reviews his RRSP portfolio on a quarterly basis and looks for "in-depth reporting," including quarterly statements for his investments. "You can have the best strategy in the world, but if you aren't getting a number to indicate the internal rate of return that your portfolio is generating, you don't have a clue what's going on in your account," he stresses.

Forecast: Mr. Phipps expects the good times to at least moderate in 2007. "My feeling is that we have had a bull market in equities in both Canada and internationally for quite a number of years now, and any time [there have been] three or four good years in the equity market, I start to get a little bit nervous." Consequently, he expects a "correction of some type is in order," particularly in North America. "I'm not especially bullish."

Rob Kerr

Position: Chairman and founder, Kerr Financial Corp., fee-only financial advisers, Montreal

Age: 62

RRSP portfolio: About 65 per cent equities, 35 per cent bonds.

Mr. Kerr doesn't subscribe to the theory that as you get older and closer to retirement you should increase the proportion of fixed-income investments in your RRSP.

But then the 62-year-old chartered accountant isn't looking to retire any time soon from the financial advisory firm he established in 1979. Moreover, he is so bullish on equities and their long-term growth potential, "I would probably hold 100 per cent equities if I had the time [to monitor them]," he admits.

Mr. Kerr, who has a professional money manager looking after his RRSP portfolio, maintains about 65 per cent in equities and 35 per cent in bonds. The equities are split about evenly between Canadian and U.S. and other international stocks. Examples of Canadian equities held include Power Corp., Royal Bank of Canada, Manulife Financial, Loblaw Cos. Ltd. and Shaw Communications Inc. International holdings include Nestlé SA, Wachovia Corp., Wells Fargo, Sapporo Breweries Ltd. and Heineken NV.

Two-thirds of his bond portfolio is invested in "large companies with comfortable cash flows" such as PepsiCo Inc. and TransCanada PipeLines Ltd., with the remaining third invested in Government of Canada bonds.

Target rate of return: Given market conditions, Mr. Kerr expects to earn about 7 per cent or 8 per cent on his overall RRSP portfolio in 2007 -- slightly lower than the 10 per cent he normally expects.

Basic strategy: Mr. Kerr, who puts money into his RRSP twice a month, with each paycheque, describes his investment style as that of a "careful risk-taker." For instance, he says, while "I like being in the stock market, I hedge my bets a little by choosing to be in the larger capitalization companies with sustainable earnings growth."

He prefers to buy and hold stocks as opposed to selling when prices begin to fluctuate. "I'm patient. I don't mind standing still for periods of time, because I like to allow the professional managers' choices to show through. It's sort of an old-fashioned approach which I think is a more profitable way."

He says that's one of the key lessons he's learned -- that emotional responses and knee-jerk reactions to a market downturn can cancel the benefits attainable through disciplined investing with a long-term strategy in mind. "I know people get nervous or upset about something that's not working," he says, "but generally when they act on those nerves, they give up some good investment opportunities."

Forecast: Mr. Kerr expects North American equity markets to drop off slightly in 2007, and he says investors should look for average returns in the range of about 8 per cent to 10 per cent. Similar conditions might continue "for the next couple of years," he predicts, but "then we'll get back to brisker markets" with returns bouncing back to about 10 per cent to 12 per cent for the rest of the decade.

David Salloum

Position: Portfolio manager, RBC Dominion Securities, Edmonton

Age: 51

RRSP portfolio: 100 per cent in fixed-income vehicles.

Mr. Salloum, a certified financial planner, has stuck to the fixed-income policy for his RRSP since he began contributing to it in 1979. He sees no reason to change his strategy now or in the future. "I don't want to have interest income in a taxed account, so I try to take all that high-taxed interest income and put it into my RRSP," he explains.

His RRSP breakdown is 50 per cent Canadian bonds and 45 per cent Canadian GICs. The other 5 per cent is invested in preferred securities, which are debt instruments with features that make them a cross between long-term corporate bonds and preferred shares.

Target rate of return: Mr. Salloum does not establish either a short- or long-term target rate of return for his plan, mainly because it is fully invested in low-risk fixed income assets. "If I said I wanted to get an 8-per-cent return on my fixed income, then I'd have to start taking on some pretty high levels of risk, and I'm not prepared to do that."

Basic strategy: Because Mr. Salloum's RRSP portfolio is limited to fixed-income assets, he does not worry about dollar-cost averaging (putting in a fixed amount on a monthly basis to take advantage of fluctuating prices). Instead, he tries to contribute the full amount as early in the year as possible to take advantage of maximum compounding over time. He also staggers the bonds' maturity dates so money comes due consistently over a five-year period.

Mr. Salloum is flexible on his eventual retirement -- he expects to start "cutting back some time around age 70" -- and defines his investment style as conservative. He says he has always preferred to hold his RRSP bonds to maturity because that provides a guaranteed value, regardless of any interim price increase or decrease. Bonds held include those of blue-chip organizations such as Sun Life Capital Trust, Great West Life Capital Trust, Canadian Imperial Bank of Commerce and Business Development Bank of Canada, among others. He holds guaranteed investment certificates from several major banks, including Bank of Nova Scotia, Bank of Montreal, HSBC and National Bank.

Mr. Salloum frequently reviews his basic RRSP strategy, which he says mainly involves ensuring that the "rolling five-year time horizon" is in place and provides a consistent flow of income. As for determining where to put his money, whether in bonds, GICs or preferred securities, "I just look at all those areas and ask, 'Which is paying the best?' and that's the way I go. I just buy whatever is paying the highest return."

Forecast: Mr. Salloum doesn't expect Toronto's S&P/TSX index to continue at the torrid pace it has kept over the past three years, but he anticipates another solid year and continued growth of about 9 per cent to 12 per cent.

In particular, he anticipates "a tougher year" for the energy and materials sectors, which have been major drivers of the TSX. He also thinks that technology might have an improved year, and that some industrials may do well because of the global infrastructure build-up, particularly in China and India.

Paul Taylor

Position: Senior vice-president and chief investment officer, BMO Harris Investment Management Inc., Toronto

Age: 46

RRSP portfolio: Approximately 60 per cent equities; 40 per cent in a combination of bonds and cash.

Although Mr. Taylor, a chartered financial analyst, likes to keep "the lion's share" of his assets outside his RRSP account, he still makes it a point to diversify his plan as much as possible.

Most of his RRSP assets are managed through a BMO Harris account, the company at which he serves as senior vice-president and chief investment officer, and is roughly split into 60 per cent equities, 35 per cent bonds, with the remaining 5 per cent in cash. That 5 per cent is held to invest in equities or funds "when better opportunities present themselves."

In the equity portion, about three-quarters (or 45 per cent of his overall RRSP) consists of Canadian stocks such as Manulife Financial, Canadian Imperial Bank of Commerce, TD Bank Financial Group, Shoppers Drug Mart Inc. and Canadian National Railway Co. The remaining one-quarter (15 per cent of the total portfolio) is invested in U.S. and other international stocks.

Mr. Taylor prefers "safe and secure" corporate equity holdings inside the RRSP plan "to offset the more aggressive investing I do outside of my RRSP." This year, in response to market conditions, he expects to trim back "modestly" on the Canadian equity to bring it down to about 43 per cent of his RRSP, with a corresponding rise in non-U.S. international stocks.

On the fixed-income side, about 25 per cent of his RRSP bonds are federal or provincial government instruments, with the remaining 10 per cent being corporate bonds.

Target rate of return: Mr. Taylor does not target either a short- or long-term rate of return for his own RRSP, mainly because most of his risk-taking is outside the plan.

Basic strategy: Mr. Taylor, who has about 15 to 20 years to go before his expected retirement, characterizes his RRSP portfolio as one with "bedrock core assets that I want to ensure grow," but for which "capital preservation is also an important consideration."

He set up his RRSP about 20 years ago, and prefers to buy and hold, rather than sell, investments in his retirement portfolio. "Once I make my decision to put my money into the appropriate vehicle, I will leave it there as long as I feel it is being well tended."

Mr. Taylor reviews his entire portfolio, including RRSPs, at least quarterly, preparing a "personal financial statement, which shows me where my wealth level is" and determining if changes are required. He also conducts a more "comprehensive review" on an annual basis. "I know what I am trying to achieve and I know where I'm going."

Forecast: Mr. Taylor expects the Canadian and U.S. economies to "soft-land" and avoid recession in 2007. "Both the Canadian and U.S. equity markets will perform relatively well" with possible "high single-digit or low double-digit returns," he predicts. But he also says the "risk-return trade-off" is most acute in North America, so he is more optimistic about international opportunities.

RRSP facts

18%

Amount of your earnings that can be put in an RRSP (less pension adjustment, plus carry forward of unused room), up to $18,000

31%

Percentage of tax filers who made RRSP contributions for the 2005 tax year

40%

Number of Canadians who have made an average of three withdrawals from their RRSPs

$18,000

Average amount withdrawn by Canadians who have taken money out of their RRSPs

46%

Number of baby boomers who say their retirement savings are off track