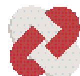
Investing
Your Dollars

A beginner's guide to investing



CANADIAN BANKERS ASSOCIATION
Building a Better Understanding

On behalf of the banking industry, the Canadian Bankers Association has embarked on a program called Building a Better Understanding. This is our commitment to communicate better and to provide useful financial information to Canadians.

As part of the program, we are offering a free series of publications, ranging from money management and interest rates to mortgages, starting a small business and saving for your children's education. To obtain copies, call toll-free 1-800-263 0231 or visit our web site at www.cba.ca. You can also order by writing to Building a Better Understanding, c/o Canadian Bankers Association, Box 348, Commerce Court West, 199 Bay St., 30th floor, Toronto, Ontario M5L 1G2.

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These publications are also available in alternative formats for people who are partially sighted or have limited vision.

La version française de cette brochure est disponible sur demande.

This booklet gives information of a general nature and is not intended to be relied on by readers as advice in any particular matter. Readers should consult their own advisors on how this information may apply to their own circumstances.

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Smart investing is not a matter of luck, but a result of deliberate planning.

Introduction

We all work hard for our money, so when it comes to investing we naturally want to make our money work for us.

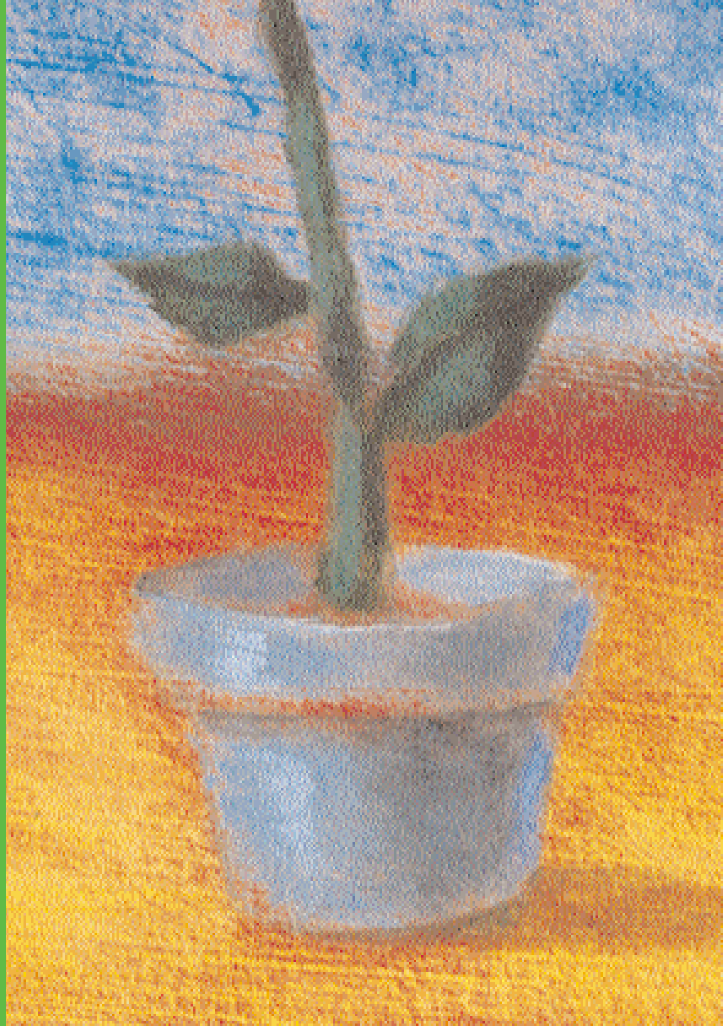
Whether we choose Guaranteed Investment Certificates (GICs) or alternative forms of investment like stocks, bonds and mutual funds, it all comes down to our individual goals, our tolerance for risk, and of course, our budget.

Today we have a multitude of options. Add to that different investment styles – simple and straightforward at one end of the spectrum to highly sophisticated at the other. Then there's the decision of whether to handle your finances yourself or use a financial advisor. The fact is, you're in a great position – you have money to invest and that's an exciting prospect. So where do you begin?

Investing Your Dollars, one of a series of booklets published by the Canadian Bankers Association, will give you a basic overview of this vast and complex topic. You'll learn about different types of investments, things to consider in selecting what's right for you and a few guidelines for successful investing. The booklet also offers a comprehensive glossary of terms and a list of sources that you can explore to become a more informed investor.

After all, being knowledgeable is the first step toward making wise investment decisions.

The Basics



Goals and Dreams

Most of us have goals for the future and realizing them likely depends on how smart we are with our money today. Chances are you aren't independently wealthy, so making your dreams a reality will take serious financial planning and smart investing. Investing is all about preserving your money and making it grow. An investment is simply a vehicle into which you put your money in order to earn a return or profit (i.e. investment income). Typical investments include stocks, mutual funds, bonds and GICs.

Whether your goal is a comfortable retirement, a good post-secondary education for your children, a new home, your own business or even a holiday, the sooner you begin planning, the better your chances of success. This means a smart investment strategy and overall financial plan that balances how much money you need today with what you'll need for the future, taking into account the effects of inflation. *(The CBA has three other publications – Planning For Retirement, Saving for Your Children's Education and Managing Money – that may also help you with your planning.)*

Just as inflation can erode your investment savings, "compounding" can help them grow even faster. Compounding simply refers to earning income on your income. You receive income not only on your starting amount, but also on any previous income accumulated in your investment. The chart on this page illustrates the effects of compounding at various rates of return. Note how a higher rate of return can significantly increase the size of your savings over time.

THE EFFECTS OF COMPOUNDING OVER TIME

$1,000 INVESTED AT VARIOUS RATES OF RETURN

YEAR	2%	5%	8%	11%
1	$1,020.00	$1,050.00	$1,080.00	$1,110.00
5	$1,104.08	$1,276.28	$1,469.33	$1,685.06
10	$1,218.99	$1,628.89	$2,158.92	$2,839.42
15	$1,345.87	$2,078.93	$3,172.17	$4,784.59
20	$1,485.95	$2,653.30	$4,660.96	$8,062.31
25	$1,640.61	$3,386.35	$6,848.48	$13,585.46
30	$1,811.36	$4,321.94	$10,062.66	$22,892.30
35	$1,999.89	$5,516.02	$14,785.34	$38,574.85

* This chart is for illustrative purposes only. The effects of inflation and taxation are not included and it is assumed that interest is compounded monthly and income is reinvested.

Financial Goals Worksheet

Within five years, I'd like to:	**$$ Needed**
Goal #1:________________	$________
Goal #2:________________	$________
My savings now are:	$________
I need:	$________
Within 10 years, I'd like to:	
Goal #3:________________	$________
Goal #4:________________	$________
My savings now are:	$________
I need:	$________
Long term, beyond 10 years, I'd like to:	
Goal #5:________________	$________
Goal #6:________________	$________
My savings now are:	$________
I need:	$________

What to Do with Your Money

Before discussing the ins and outs of investment planning, it helps to have an understanding of the basics.

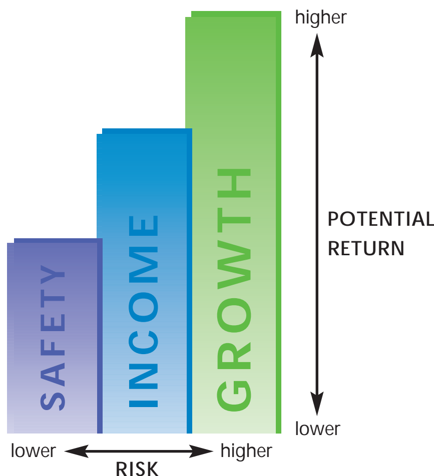
There are many investment instruments on the market. Each has a different level of risk and expected return. Certain types of investments tend to be "safer" than others, meaning you have a better chance of preserving your original investment, but the rate of return will be low. At the same time, other investments have the possibility of a higher rate of return, but will likely be less "safe."

Investors willing to accept a higher risk in their investments expect to be rewarded accordingly or they won't invest in a given opportunity. Those looking for "safety" or "income" in their investments know that their return won't potentially be as high, but they don't run the risk of losing some or all of their investment. Investments basically fall into three main categories, based on your investment needs:

- Cash and cash equivalents: These are assets which, at any time, can be made accessible ("liquid"). Examples are savings accounts, treasury bills, and money market mutual funds. This is generally the safest category of investment but produces the lowest returns.
- Fixed income investments: These generally offer higher returns than those in the cash/cash equivalent category. They provide a source of regular investment income which remains the same over time. Examples are term deposits/GICs, bonds and income mutual funds.
- Equity investments: These are assets which can grow in market value, but don't necessarily pay dividends to the holder. Examples are stocks and equity mutual funds. This is generally the riskiest category of investment, particularly over the short-term, but offers the greatest potential for the highest long-term returns.

The type or mix of investments you choose depends on your investor profile, your time-frame for investing and your appetite for risk. Risk and return are factors that you need to be aware of. How much risk are you comfortable with? And what return are you looking for? To help you determine this, see the Investor Profile on pages 18-19.

Risk and Return Trade-off



Investment Options

As an investor, you can choose to be a "lender" or an "owner." Lender or debt investments (Cash/Cash Equivalent or Income) pay interest. Owner or equity investments offer the potential to generate earnings or profits.

As a "lender" investor you are, in essence, lending your money to a borrower. This may be to a government, a financial institution or a corporation. Your "loan" might be in the form of a bond, GIC or Treasury Bill, and your income is the interest paid at a specific rate, in exchange for the borrower's use of your money. You are also promised the return of your original "loan," or investment, at a given point in the future. It should be noted that certain debt investments like bonds can be sold to others in the marketplace prior to maturity, which may result in capital gains or losses. However, this is not a primary motivator for income investors.

As an "owner" investor, you become a partial owner of the company in which you are investing. You own a share of the company and may be paid a portion of the company's earnings in the form of dividends. You expect to make your money from two sources – dividend income, if applicable (your share of the earnings that are paid to investors in the company), and capital appreciation (when you sell your ownership position for more than what you originally paid because the company has grown in value since you invested). Investors primarily buy equity investments like stocks with the expectation of capital appreciation.

"Owner" investments are usually classified as growth or equity and could also include such things as real estate, art works, collectibles, etc. Note that neither dividends nor capital appreciation are a sure thing with equity investments. Returns can vary widely from year to year and different equities have different risk levels. Penny stocks, for instance, are highly speculative.

The following chart provides a brief overview of common investment options and is not intended to be an exhaustive list (you can also refer to our glossary of terms). Mutual funds are a special type of investment option, discussed in the next section. For more detailed information and advice on such things as the pros and cons of each investment for your own needs, please see a financial advisor.

Investments can produce these types of returns:

- *interest*
- *dividends*
- *capital gains*

Investment Choices

(mutual funds are discussed on page 12)

DEBT INVESTMENTS

(Cash/Cash Equivalent and Income)

Savings Account

- An account held with a financial institution
- Safe vehicle for short-term savings of any amount
- High liquidity (easy to cash)

Canada Savings Bond (CSB)

- A special type of bond issued by federal gov't, purchased through financial institutions
- Available only at specific times
- Pay a fixed interest rate, subject to periodic adjustment by the gov't
- Safe, guaranteed by the gov't and highly liquid (although the new Canada Premium Bond is only cashable once a year on its anniversary date)
- Unlike other bonds, cannot be traded
- Available in various amounts and for as little as $100

Government Treasury Bill (T-Bill)

- Short-term investment: terms of one month to a year (considered a cash-equivalent)
- Safe, government-backed
- Don't pay a specified interest rate, rather T-Bills have a face value; you purchase it at a "discount" (less than the face value) and then redeem it at face value; the difference is your return (e.g. you may pay $90 for a $100 face value T-Bill – you receive the face value upon maturity)
- Investments of $1,000 and up; can be purchased from most financial institutions

Term Deposit/ Guaranteed Investment Certificate (GIC)

- You invest a sum of money with a financial institution for a set period
- Traditional GIC pays interest and your principal and return are guaranteed
- New "market-linked" GICs guarantee principal, but any returns you may earn are linked to some stock market index
- Terms range from less than 1 month to 10 years
- Available in various amounts

Bankers' Acceptance (BA)

- Short-term debt issued by corporations that is guaranteed by a bank
- Highly liquid (terms to maturity of less than a year)
- Considered safe, low-risk
- Purchased on a "discounted basis" to mature on a specific date; your return is fixed
- Usually $100,000+

Commercial Paper

- Similar to BAs, but without the guarantee of a bank
- Available through financial institutions

Investment Choices continued...

Government Bond	• Issued by the federal gov't and provincial gov'ts and available through most financial institutions • Set at fixed interest rate, for a specified term • Safe (guaranteed to maturity by the issuing gov't) and liquid • Come in terms of one to 30 years • Can be sold in the bond market before maturity
Corporate Bond	• Issued by a corporation and available through a brokerage house • Set at fixed interest rate, for a specified term • Backed by specific assets of the issuing company • Come in terms of one to 30 years and in various types • Can be sold in the bond market before maturity
Debenture	• Type of corporate bond, but not secured by specific company assets. Simply based on the general reputation of the issuing company
Mortgage-Backed Securities	• Fixed rate investments that represent an ownership share in a pool of mortgages insured by the federal government's Canada Mortgage and Housing Corporation • Minimum investment of $5,000; terms range from one to 10 years • Receive a monthly payment that is a blend of principal and interest accruing from the pool of mortgages

EQUITY INVESTMENTS

Stocks - general comments	• Issued by corporations; investor becomes a partial owner in the corporation by buying shares (also called stocks) of the company • Two main categories of shares: "common" and "preferred" • Share prices and returns fluctuate, and there is no guarantee as to income • Traded on stock exchanges or over-the-counter markets
Common Shares/Stock	• With common shares, you typically have voting rights • Common shares are usually purchased for potential capital appreciation • If the company makes money you will share in the profits either by seeing the value of your shares rise, by being paid dividends, or both; if the company suffers a poor year or the markets decline, your share values may fall and dividends are unlikely (resulting in a potential capital loss)

Blue Chip Stock

- Typically stocks of large, stable and actively-traded companies with a record of regular dividend payments
- Tend to be conservative equity investments

Penny Stock

- Low-cost common shares (typically under $1), usually purchased for speculative purposes
- Issued by start-up or unproven corporations seeking capital for expansion

Small-, Mid- and Large-Cap Stock

- Corporations of all sizes issue common shares to raise money; generally, the smaller the corporation, the higher the risk

Preferred Shares/Stock

- Differ from common shares in several ways and in fact are regarded as bond-like investments
- Normally purchased by investors who want a steady stream of dividends, rather than capital appreciation
- Pay a dividend, which is higher-yielding than a common share
- Value and share price influenced more by interest rate trends than by company's earnings
- Don't typically give voting rights
- They are preferred because you get a preferential claim to the assets/profits ahead of common shareholders

Precious Metals

- Gold, silver and other precious metals
- Held in form of bullion (the actual metal) or certificates of ownership

Commodities

- Bulk goods such as grains, metals, oil and foods
- Traded on commodities exchanges
- Held in the form of a contract

Derivatives

- A security whose value depends on the market value of something else, such as a stock or commodity
- They are complex investments used by sophisticated investors for speculative purposes or to help manage risk (as a hedge against changing market conditions)
- "Options" and "futures" are examples of derivatives; an option gives the investor the right to buy or sell a specific security at a given price before a specified date; a futures contract obligates the investor to buy or sell a specified amount of an asset at a set price on a certain date

Other Investments

Some people put their money to work in areas outside of "mainstream" investments. Perhaps the most common is real-estate for rental purposes. In this form of investing owners may be able to earn rental income and see their capital investment appreciate over time, assuming real estate prices rise.

Mutual Funds

Mutual funds have become popular with Canadians in recent years. Today 40% of Canadians hold some $290 billion in more than 1,300 different mutual funds.

A mutual fund is an investment product in which your money is pooled with the money of many other investors. A professional fund manager invests this pool of money in a variety of securities, depending on the fund's specific objectives. The manager monitors each of the investments on an on-going basis.

If you're like many people, you don't have time to fully research and manage your investments, but you'd still like some say in where your money goes, and you'd like to be able to move it around from time to time. If this sounds like your style, you may want to consider mutual funds.

There are funds that invest in specific market or geographical sectors, while others invest in blue chip companies or small company stocks. There are also "green" funds that only invest in environmentally friendly companies.

Mutual funds have many advantages:

- You gain access to a wider range of investments that you otherwise may not be able to afford;
- You can have "instant diversification." If one company or investment in your mutual fund flounders, it will likely have little effect on the mutual fund's overall performance;
- They are readily available – most financial institutions offer a wide assortment of mutual funds;
- They are a simple way of investing, for instance, most financial institutions give you the option of buying mutual funds through regular account withdrawals; they also offer the benefits of professional management.

Types of Mutual Funds

The range of mutual funds is staggering and can be bewildering to a beginning investor. Keep in mind that companies offering mutual funds have similar types but with different names and objectives. Most mutual funds generally fall into five broad categories, as shown in the following chart.

Mutual Fund	What they invest in
MONEY MARKET	
Money Market Funds	• short-term debt instruments (less than one year) • T-bills, commercial paper
INCOME	
Mortgage Funds	• residential mortgages • some funds invest in commercial mortgages
Bond Funds	• government bonds • corporate bonds and debentures
Dividend Funds	• common or preferred shares that generate dividends
BALANCED	
Balanced Funds	• a broad mix of income, equity and money market investments
Asset Allocation Funds	• similar to balanced funds, however portfolio manager has wider discretionary powers to allocate assets to various sectors to allow maximum growth
EQUITY/GROWTH	
Equity/Growth Funds	• common shares of public corporations • portfolios can vary widely in stock selection, and can focus on specific company sizes (e.g. small-cap, large-cap, etc.)
Specialized Funds	• invest in specific industry sectors such as technology, health, energy and natural resources
INTERNATIONAL	
International/Global Funds	• common shares of foreign public corporations, foreign bonds • can invest broadly across the world, in specific countries or in specific areas (Europe, Asia, etc.)

When do you need your money?

When investing, consider how long you plan to leave your money invested. Shorter periods tend to mean relatively conservative, low-risk investments (i.e. savings accounts, T-Bills and GICs). A longer term allows for more aggressive, "risky" positions (i.e. stocks and equity mutual funds) – you have time to ride out cycles of highs and lows in the market.

As with any type of investment, there is an element of risk with mutual funds. Although the fund is diversified, it will still reflect the performance of the securities in that fund. And depending on the mutual fund, it can vary from very low to very high risk. Mutual funds are generally intended to be held as long-term investments. With mutual funds, you can potentially earn money in two ways; through distributions (profits of the funds that are passed on to you) or through a rise in the unit or share price.

Be aware of the fees involved with mutual funds. In many cases, there are no acquisition or disposal fees (these are called "no-load" funds). However, some funds may charge either an initial fee, called a "front-end load", or a fee when you sell the mutual fund, called a "back-end load". With these fees, you pay a percentage of the purchase price that may or may not be waived if you hold the fund long enough. All mutual funds have a fee known as the Management Expense Ratio (MER), which is the annual cost of managing and operating the fund.

Where Do You Go To Invest?

It depends on the investment. While most financial institutions offer a variety of investment choices, only certain institutions like investment dealers can actually engage in the trading of securities. Debt investments like savings accounts, GICs/term deposits, Treasury Bills, Canada Savings Bonds and other government savings bonds are available through many financial institutions like banks, trust companies, credit unions and investment firms.

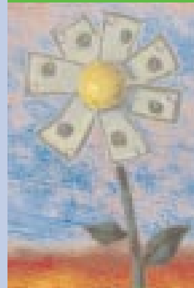
With specific investments that you wish to trade (buy and sell), like stocks and corporate bonds for instance, you do so through an investment firm registered with a securities commission. Investment firms and their registered employees are licensed to trade securities, which is done through financial markets – stock, bond and money markets. A full discussion about the role of financial markets is beyond the scope of this booklet, but suffice to say they are simply the places where investments are bought and sold (for more information, the Canadian Securities Institute has

a useful series of pamphlets on financial markets - see page 31 for contacts). Mutual fund units can be ordered directly from the company offering the mutual fund (ranging from insurance companies to mutual fund dealers) or through an investment firm.

How We Invest

- *40% of Canadians have mutual funds*
- *20% have Canada Savings Bonds*
- *18% have individual stocks*
- *17% have GICs (terms of more than one year)*
- *15% have GICs (one year or less)*
- *11% have provincial savings bonds*
- *8% have other bonds issued by government or corporations*
- *7% have off-shore investments*
- *6% have T-Bills*
- *4% have index-linked GICs*

Source: Compas Inc./CIBC Financial Health Poll, 1998



Know Your Investment Objectives

What is Your Investor Profile?

Before you can start to make investment decisions, find out what kind of investor you are. What are your investment objectives? Are you looking for income, growth through capital appreciation, safety, a fair amount of liquidity? When you think about risk, is your preference slanted towards high-, medium- or low-risk investments?

Most financial institutions have worksheets and self-administered tests to help you figure out your investment style and how much risk you can handle. Your financial advisor can also walk you through a similar test. Your answers will help you or your financial advisor determine a suggested portfolio mix – which investments might best suit your investment style. There is a sample questionnaire on pages 18-19 to get you started.

Where Do You Fit On the Investment Time-Line?

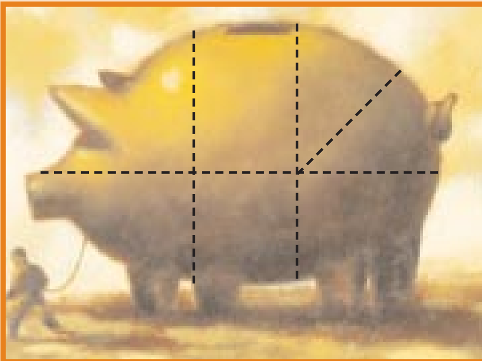
Another way of looking at investor profiles, and the resulting "portfolio mix" is to consider where you stand on the investment time-line cycle (see pages 20-21).

Put briefly, there are four very different stages almost all of us pass through during our earning years, and our financial goals change accordingly. And as these goals change, so too will your approach to investing money.

Portfolio Mix

Your portfolio is made up of various securities and investments. You and your financial advisor should determine which mix of investments is right for you.

A portfolio mix is based on many factors, such as your investor profile (see pages 18-19) and where you are on the investment time-line (see pages 20-21).



TIP

If you are saving for a short-term goal like a home, computer or trip, stay away from risky investments in which you may lose some or all of your money.

What Kind of Investor Are You?

1. How would you define your investment objectives?

A) Safety - I definitely need to preserve my capital	**2 points**
B) Safety plus income - I need regular income	**4 points**
C) Income plus long-term growth - I need some income, but I'd also like to see some growth in my investments	**6 points**
D) Capital appreciation - I want to see my investments grow much faster than the inflation rate	**7 points**

Your Score

2. When will you need to start withdrawing money from your investments?

A) Under 2 years (short-term)	**2 points**
B) 2 to 5 years (medium-term)	**3 points**
C) 5 to 10 years (medium to long-term)	**5 points**
D) More than 10 years (long-term)	**6 points**

Your Score

3. How would you define your current level of investment knowledge?

A) I have little or no knowledge about investing	**0 points**
B) I have some knowledge and am reasonably familiar with basic types of investments, including mutual funds	**1 point**
C) I am both knowledgeable and experienced in investing	**2 points**

Your Score

4. How much risk are you comfortable with? Recognize that generally speaking, the higher the risk, the higher the potential for gains and losses.

A) Very High - I could tolerate a decline of 20% or more in the short-term value of my investments, in anticipation of a positive long-term return	**6 points**
B) High - I could tolerate a moderate decline, between 10-20%, in the value of my investments, in anticipation of a positive long-term return	**5 points**
C) Moderate - I could tolerate a modest decline, between 5-10%, in the value of my investments, provided I receive a positive long-term return	**3 points**

D) Low - I could tolerate a minor decline of less then 5% from time to time, but any drop in the value of my investments would make me uncomfortable **2 points**

E) Very Low - My primary concern is the security of my investment **0 points**

Your Score

5. Take a moment to consider your personal financial situation - income, payment of bills, net worth, etc. The more secure your finances, the more you can afford to take some risks in your investments.

   In a year or so, how secure do you feel your finances will be?

   Very secure = 0 points

   Somewhat secure = subtract 1 point

   Not sure = subtract 2

   Likely worse = subtract 4

Total Score

What Does Your Investor Profile Score Mean?

Your score on this questionnaire will give you an idea as to what kind of an investor you are. However, this will change according to your goals.

6 or less: a security-oriented investor. You might want to consider a relatively conservative portfolio with no fluctuations in value. You would likely place money in safer investments such as cash and cash-equivalent vehicles, along with income-focused investments.

7-10 points: a balanced-conservative investor. You will likely feel most comfortable with most of your money in cash/cash equivalent and income investments, with a small portion going to equity or growth investments.

11-15 points: a moderate-growth investor. You will tend to have as little as 5% of your money in cash/cash equivalent investments, and you will favour income and growth investments.

16+ points: a growth-oriented investor. You are comfortable with riskier investments, and have the time to see your money appreciate with the markets. Your portfolio mix will have 70% or more invested in equities, and the bulk of the remainder in income investments.

Recognize that this sample test, and the resulting score provide only an approximation of your investor profile in a particular situation or for particular goals. As you look for investment alternatives, take the opportunity to complete several similar tests with various financial institutions. Compare your scores and the resulting recommended portfolio mixes. You should be able to get a reasonably accurate picture of where to best invest your dollars.

Where are You on the Investment Timeline?

	Early Years up to mid-30s	Middle Years mid-30s to late 40s
Your goals	*Get started*	*Build and Invest*
Your investment life stage	• Early earning years • Heavy financial outlays (car, house, family) • Minimal investments • It's time to start investing • Short-term financial goals	• Usually more disposable income • Growing portfolio of investments • Set solid savings strategy/ objectives • Focus on short-, medium- and long-term financial goals
Your concerns	• You need to start saving, but when? • Overall shortage of cash • Savings need to be liquid to cover short-term obligations	• Family commitments • Saving some, but probably not enough • Managing investments • Minimizing taxes
Consider	• It's never too soon to start investing • Develop a plan • Start investing regularly to save for short-term needs and retirement • The more you put into RRSPs, the better your tax refund • Growth-oriented investments for longer term	• Maximize yearly RRSP contributions • Diversify investments to ensure suitable asset allocation for your goals • Larger proportion of growth/ equity investments – you have time to let them grow

This chart is for illustrative purposes only and the timelines are rough approximations. Everyone has different goals, circumstances, concerns and risk tolerance levels at different times in their life. Consider your own situation and consult a financial advisor to determine an investment portfolio based on your needs.

Leading to Retirement

late-40s to retirement

Consolidate for future

- Heavy spending times are past; fewer family commitments
- Now able to maximize investments
- Significant investment portfolios
- Goals tend to shift to medium-term

- Planning for retirement – now
- Managing existing investments to ensure maximum returns
- Typically more risk averse than at previous stages
- Minimizing taxes

- Maximize yearly RRSP contributions and consider catching up on excess contribution room
- Ensure diversification but re-evaluate your asset allocation mix – as time goes on, decrease the percentage of higher risk investments in your portfolio
- Begin to consolidate for future and plan your estate

Retirement Years

60+

Income and security

- Retirement is uppermost in mind or already retired
- Financial commitments typically light
- Rely on retirement savings for income, but also need to keep funds invested in order to generate a good enough return on which to live
- Focus on meeting short- to medium-term goals

- Is there enough income for retirement? How will inflation affect my savings?
- Planning can be difficult as retirement years can last up to 30 or even 40 years
- Portfolio must be able to maintain living standards while continuing to earn income
- Minimizing risk with your savings

- Wind down RRSPs and select retirement income options for your savings (e.g. Registered Retirement Income Fund, annuities)
- Continue investing but shift asset allocation mix towards more conservative instruments
- Focus on estate planning

Your Investment Strategy

Smart investing is not a matter of luck, but a result of deliberate planning. In this section we discuss ways to improve your success with investing and things to consider as you create your investment strategy. It is also important to remember that your investments should be viewed in the context of your overall financial plan.

Do your homework

The first rule of intelligent investing is “be informed.”

So how do you become an informed investor? By learning more – doing some homework, seeking out experts and listening – you can make investment decisions that are based on a good understanding of the market.

There are many ways to become a more educated investor. For your convenience, we have outlined some sources of information at the back of this booklet.

Investment Education Sources

- *Seminars and presentations*
- *Financial institutions and advisors*
- *Magazines, newspapers, television, videos and books*
- *Internet*
- *Courses*
- *Private investor newsletters (fee-based)*
- *Investment clubs*

Once you decide it's time to invest, look into the financial institution or brokerage firm you're thinking of using, read up on the different types of investments and consider which best suit your objectives.

Beware of "hot" tips – they can "burn" the uninformed investor. Rely on recommendations from trusted advisors or make investment decisions based on solid research and a knowledge of the market.

Invest Your Time

As with other aspects of financial planning, you'll need to spend time on your investments – whether it's researching your options, or choosing and monitoring your investments. This can vary from minimal to significant, depending on the types of investments you own and the type of investor you want to be (active versus passive). You can also have a professional advisor spend time on your behalf (discussed in next section), although you'll still need to be involved to a certain extent.

If you're an active investor in equities, you may need to devote several hours a week. Income and safety investments do not require such regular attention.

Fully involved investors, especially those heavily invested in equities, spend considerable time tracking their

TIP

Remember to re-examine your portfolio regularly, for instance, every three months, six months or at least yearly, to ensure that it is meeting your objectives.

investments – reviewing each investment's performance against their own preferred performance criteria. They'll sell the unproductive ones – selling off once they've reached a target price, rather than waiting for a peak that may never materialize – and then they'll use the funds from sales to acquire new investments. At this point the cycle begins again – more research and more time!

Although investing in mutual funds can be easier than with other types of investments, there is still work involved. You'll need to do research before choosing a fund for your portfolio and you'll need to regularly track the performance of each of your funds.

Relying on Professional Advisors

You can use a financial advisor for investment guidance and advice. You may be charged a fee for this, depending on the type and amount of help you want. If you want less active personal involvement in your portfolio, or once your portfolio grows to a certain size, you may want to use a professional advisor, who for a fee, will manage your investments based on your objectives. If you rely on an advisor to handle your money, you'll spend far less time on your portfolio. But remember, you're paying someone else to spend the time.

Start Early and Invest Regularly

Begin early and invest regularly even if you can only afford small amounts. In fact, small amounts frequently invested can actually grow faster than large sums invested less often. That's due to the benefit of compounding over long periods of time. Compounding occurs when all income from an investment is reinvested, thereby earning additional income.

TIP: *When choosing a financial advisor, rely on the advice and recommendations of friends or associates you trust. Make sure you feel comfortable with the individual you are considering. Enquire about his or her credentials and any fees involved.*

"Dollar-cost averaging" is a strategy based on investing a fixed amount at regular intervals such as $100 or $200 monthly. This works best with mutual funds. You can automatically buy more of an investment when prices are low and less when prices are high. Although this strategy doesn't guarantee profit or protect you against loss, it reduces the risk of investing all of your money at a market peak.

Diversification and Balanced Investing

Some people hold only one or two types of investments and this may be all they're comfortable with.

However, a proven strategy for successful investing is diversification – in essence, spreading your investments around so that you don't have all your eggs in one basket. Diversification is an effective way of minimizing risk and protecting you from volatility in a particular asset class or industry. Using a diversification strategy, you would hold a variety of different investments within and between each of the three asset categories, producing a portfolio of highly secure investments, income producing investments, and growth-oriented investments. This way, if one area of your portfolio is underperforming, your investments in other areas will hopefully take up some of the slack.

Studies have shown that less than 20% of most portfolios' returns are attributable to the choice of individual investments and 80% due to choosing the right mix of investments (i.e. between asset categories, industry sectors and geographic regions.)

Generally, it's not a good idea to place all your money in what you hope will be one or two star performers. Any given sector can perform well for some time. But all it takes is a change in the factors that influence that sector to see the rate of return suddenly slow down or drop. Certain mutual funds – like balanced funds – provide you with instant diversification across asset classes.

Did You Know?

That 48% of Canadians say they use a financial advisor.

Source: Compas Inc./ CIBC Financial Health Poll, 1998

Some investment experts recommend you rebalance your investments. This means selling those that don't have a good outlook and investing the funds elsewhere to align them with your investment plan or recommended portfolio mix. Constantly rebalancing your portfolio is known as active investing. Taken to the extreme, it involves fund-hopping or investment-hopping, practices that can incur large fees.

On the other side is passive investing, where you buy and stay with a set of investments. Research has shown that passive investing can be just as effective over the long term, providing you have a well-diversified portfolio.

Understand Tax Treatment

Depending on the type of investment, the way it is taxed will differ. Let's look at how different investment income is treated from a tax standpoint:

- Interest Income: treated exactly the same as salary income and taxed on its full amount. If you earn $100 in interest income and are in a 40% tax bracket, you'd end up paying $40 in tax.
- Dividend Income: You get a more favourable tax treatment than you do for interest income. Dividends from Canadian corporations qualify for a dividend tax credit. To calculate the taxable amount, 25% is added to the dividend income. For instance, for $100 in dividend income, you would add on $25 to get $125 in taxable income. However, the government issues a tax credit equal to 13.33% of the $125 taxable amount. If you're in a 40% tax bracket, you would pay roughly $25 in tax.
- Capital Gains: When you sell certain equity investments like stocks for a profit, it is considered a "capital gain." With capital gains, you also get a tax break. Only 75% of capital gains are taxable at an individual's personal tax rate. If you bought a stock for $100 and sold it for $200, only $75 of your capital gain would be taxed. If you're in a 40% tax bracket, you'll end up paying $30 of tax. Note that capital gains aren't taxable until you actually sell your investment.
- Income from Foreign Companies: Whether interest or dividends, this is taxed as ordinary earned income.

Be aware that the above applies to investments held outside of a registered savings plan. Income from investments held in registered (tax-sheltered) plans like an RRSP is taxed only when it is withdrawn from the plan, at which time it is all treated as ordinary earned income.

Weathering a Volatile Stock Market

Stock markets can fluctuate very quickly, so it's easy to panic when they take a sudden dip as in late summer 1998. You may wonder whether to move your assets into cash or cash-equivalent investments. If it means you'll sleep better at night, this may be a good move.

Rather than beating a hasty retreat from the stock market, you may be wiser to stay your course. Even the experts can't always predict where the markets are headed. If you're looking for long-term gains:

- *Stay with your financial strategy;*
- *Keep a diversified portfolio;*
- *Don't overreact to market fluctuations;*
- *Concentrate on the long term.*

Registered Retirement Savings Plans (RRSPs)

So far we haven't talked about RRSPs and your investment strategy. An RRSP is simply a savings strategy for your retirement that allows you to invest on a tax deferred basis. Your contributions to the plan are allowed to accumulate, along with investment income on a tax-free basis until the funds are withdrawn during your retirement years. Although the funds will be fully taxable at that time, this will be during a period of lower income and your tax rate will likely be lower.

Depending on the plan you have, there is a wide range of investments that can be held in an RRSP. Various types of RRSPs are designed to meet different investing needs, including deposit RRSPs (your investment choices are generally limited to savings accounts and GICs) and mutual fund RRSPs. If you want a broader range of investment options you can opt for a self-directed RRSP in which you can hold everything from stocks to mutual funds to bonds to T-Bills.

Tax Tip:

Understand how tax rules affect your investments so you can maximize your after-tax returns. Seek assistance from your financial advisor or accountant.

One investment strategy is to contribute as much as you can to your RRSP each year. Check your latest income tax notice of assessment (issued by Revenue Canada) to find out your maximum contribution for the coming year. Only after making your maximum RRSP contribution, should you consider other "non-registered" investments. These can offer additional income and also provide an emergency backup reserve. However, if you need access to your money now or in the immediate term, invest it outside of an RRSP.

Other advisors suggest holding growth and equity investments outside of an RRSP because of the preferred tax treatment of such things as dividends and capital appreciation.

TIP

Decrease the income tax you pay by contributing to an RRSP.

Virtually all investments are RRSP-eligible with one important proviso. Those that are deemed "foreign content" can make up no more than 20% of the book value of your RRSP portfolio. Foreign content is a key issue for investors since there are so many investment opportunities outside of Canada. It can make good sense to maximize your foreign content, and using mutual funds, you can do this in two ways:

- Purchase international mutual funds up to the 20% maximum for RRSP purposes;
- Purchase Canadian funds that invest up to 20% of their assets in foreign holdings; this can push your total foreign content up to 36% (assuming you are already taking advantage of the first 20% allowance).

Protect Your Interests

When investing in stocks and other equity securities, keep in mind the following tips:

- Do your homework to make sure you understand the investment and its risks.
- Make sure the investment you're considering is right for your objectives and investor profile.
- Select financial advisors carefully. Ensure they have the qualifications and experience required. Be comfortable with them, ask questions and make sure they take the time to explain things.

- Don’t be pressured into making a decision. Watch out for high-pressure sales tactics that urge you to act quickly.
- Keep records of all transactions you enter into.
- Be wary of schemes which guarantee a quick profit.
- Don’t invest on the basis of “hot” tips and rumours.
- Diversify your investments.

Investment Checklist

When deciding upon an investment, ask yourself the following:

✔ *Does it meet your investment needs and objectives?*

✔ *How does it fit into your overall portfolio?*

✔ *Do you understand its features? What are the risks? What is the earnings potential?*

✔ *Have you compared returns on similar or other investments? For debt investments, have you considered the direction of interest rates? For instance, should you lock in for the long-term if interest rates are high but expected to fall?*

✔ *To what extent is the success of the investment (like a stock or mutual fund) dependent on something like interest rates, market conditions or a company’s success?*

✔ *When will you need your money – short-term, medium-term, long term?*

✔ *In the event of an emergency, will you require this money to be liquid or easy to access?*

✔ *What type of income will the investment generate – interest, dividends, capital gains?*

✔ *Will you hold the investment in your RRSP?*

✔ *If investing in stocks or mutual funds, have you considered past performance and future prospects?*

✔ *Are there any fees/costs involved?*

In Closing

The world of investing doesn't have to be complex and confusing. In fact, it can be an exciting one full of challenges and rewards.

Maybe the best way to look at investing is to consider it a lifelong pursuit. As a novice investor, you'll find that there will be a learning curve. But you'll be surprised at how quickly you can get up to speed once you decide to spend a little time learning about the many possibilities of investing your dollars.

There's plenty of information out there and we hope that this booklet launches you on the road to investment success.

SOURCES OF INFORMATION

There are numerous sources of information, assistance and advice available to help both novice and seasoned investors learn about investment options and strategies. We've provided a listing of some of these below.

Financial Institutions

Banks, insurance companies, credit unions, trust companies, brokerage firms, and mutual fund companies all offer a variety of investment products and services.

You'll find helpful information through brochures, seminars, newsletters and on their web sites. Accredited financial advisors are also available to assist you.

Associations and Institutes

- Investor Learning Centre of Canada (1-888-452-5566, 416-364-6666, www.investorlearning.ca): Not-for-profit organization dedicated to helping Canadians learn more about investing through seminars, books, the Internet and free Resource Centres.
- The Institute of Canadian Bankers (1-800-361-4636, 514-282-9480, www.icb.org): Educational institute that offers a variety of courses and programs including the popular Investment Funds in Canada course.
- Canadian Securities Institute (1-800-274-8355, www.csi.ca): Offers the Canadian Securities Course and other investment learning programs.
- Investment Funds Institute of Canada (1-888-865-4232, 416-363-2158, www.ific.ca): National association that administers mutual fund courses and broadens public awareness of the investment funds industry.
- Canadian Shareowners' Association (416-595-9600, www.shareowner.ca): Not-for-profit organization for investors. Its benefits include information, research, and assistance in starting investment clubs.

Canadian Exchanges

The following exchanges offer a variety of investor services and useful information to novice and experienced investors alike.

- Alberta Stock Exchange (403-974-7400, www.ase.ca)
- Montreal Exchange (514-871-2424, www.me.org)
- The Toronto Stock Exchange (416-947-4700, www.tse.com)
- Vancouver Stock Exchange (604-689-3334, www.vse.ca)
- The Winnipeg Stock Exchange (204-987-7070, www.wse.ca)
- Winnipeg Commodities Exchange (204-925-5000, www.wce.mb.ca)

Newspapers, Magazines, and Other Publications

Newspapers and magazines provide the latest news on market conditions and a wealth of other information including investment tips. Examples of helpful, timely publications are *I.E. Money, Investor's Digest of Canada, Canadian Moneysaver, The Fund Counsel, The Investment Reporter* and *Canadian Mutual Fund Advisor*. Numerous books geared for all ages and investor types exist on topics such as investment strategies, stock markets, bonds, and the pros and cons of different products. Check out your local library or bookstore.

The Internet

There are many web sites offering information about investing. Some even have helpful interactive tools and worksheets. Below we have noted just a few. Conduct your own Internet search to explore the many resources out there.

Helpful Sites

British Columbia Securities Commission: www.bcsc.bc.ca

Ontario Securities Commission: www.osc.gov.on.ca

Quebec Securities Commission: www.cvmq.com

Canadian Online Explorer: www.canoe.ca/MoneyNews

i-money: www.imoney.com

The Fund Library: www.fundlibrary.com

Quicken: www.quicken.ca

sympatico: www1.sympatico.ca/Contents/Finance

Chartered Banks

Bank of Montreal: www.bmo.com

The Bank of Nova Scotia: www.scotiabank.ca

Canadian Imperial Bank of Commerce: www.cibc.com

Canadian Western Bank: www.cwbank.com

Hongkong Bank of Canada: www.hkbc.com

Laurentian Bank of Canada: www.laurentianbank.com

National Bank of Canada: www.nbc.ca

Royal Bank of Canada: www.royalbank.com

Toronto Dominion Bank: www.tdbank.ca

GLOSSARY OF TERMS

Assets: Things that you own which have value in financial terms.

Asset (or portfolio) mix: The combination of different investments within a portfolio. The asset mix is geared to an individual's investment goals and risk tolerance.

Bankers' Acceptance (BA): A short-term obligation of a major corporation that is accepted by a major chartered bank.

Bear Market: A market in which securities prices are declining (opposite of a bull market).

Blue Chip: Typically stocks of large, reputable and actively-traded companies with a record of regular dividend payments.

Bonds: Offered by governments and corporations, bonds are investments in which a sum of money is lent to the issuer for a set amount of time. Bonds are offered to the public at a particular price which may or may not be equal to the bond's "face value" (the amount of the loan to be repaid). The issuer of the bond agrees to pay interest regularly, and to pay back the principal or face value of the bond at maturity (the end of the bond's life when you receive your "loan" back). You can hold a bond to maturity for a predetermined return or sell it beforehand,
as most bonds can be traded. If sold prior to maturity, you'll receive the market value of the bond based on prevailing interest rates for similar bonds, which could result in a capital gain or loss (after a bond is issued, it can gain in value if interest rates fall or fall in value if interest rates rise).

Bull Market: A market in which securities prices are rising over a prolonged period of time.

Canada Savings Bonds: Investments issued to the public by the federal government each fall. Specific terms vary and they can be cashed for full face value plus any accrued interest any time before maturity. (The new Canada Premium Bond can only be cashed once a year.) Unlike other bonds, these cannot be traded.

Capital Gain or Loss: The difference between the price you paid for an investment and the price at which you sell (in other words, the profit or loss you make).

Commercial Paper: A short-term obligation of a major corporation.

Compounding: Refers to earning income on your income. For example, on fixed income investments that pay interest over time at periodic intervals, compounding means receiving interest on your

initial investment and also on the interest previously paid.

Corporate Bonds: Companies sell (or issue) bonds when they want to borrow money. Unsecured bonds are usually referred to as debentures. Bonds pay a fixed rate of interest known as the coupon rate. At the bond's maturity, the company repays the principal or the face value of the bond back to the investor.

Derivatives: A security whose value is determined by the market price of some underlying asset, such as a stock or a commodity. Examples of derivatives include warrants, futures and options.

Dividends: Company earnings that may be paid to shareholders according to the number of shares or stocks they hold.

Futures: Futures are contractual agreements that derive their value from an underlying asset. They are an obligation to buy or sell a specific asset like coffee, corn, oil or stock, on a set date for a predetermined price.

Government Bonds: Issued by governments when they need to borrow. The face value of the bond is returned to you at its maturity date and you receive interest in the interim. They are sold in increments of $1,000 and maturities of one to 30 years. The interest rate – or coupon – is usually paid in two semi-annual payments.

Guaranteed Investment Certificate (GIC): A debt investment with a fixed term and a set rate of interest. Today, there are many variations of GICs, including "market-linked" GICs which guarantee your principal, but any returns you may earn are tied to a stock market index.

Inflation: A rise in the average level of prices in the economy.

Interest: From a saver's standpoint, interest is a type of income you earn from an investment. It is money others pay you for the use of your money. You place an amount of money (called the principal) into an interest bearing investment and in return, the institution, government or corporation offering the investment generally pays you a specified percentage of interest in exchange for the use of your money. Interest income is earned on bank accounts, GICs, bonds, term deposits and money market funds.

Investment Income: This is income earned on investments you make. Investment income includes interest, dividends and capital gains.

Liquidity: Refers to the ease with which you can get your money back from an investment.

Mutual Fund: An investment in which your money is pooled with the money of many other investors. There are many varieties of mutual funds, each with specific objectives. When investing in a

mutual fund, you purchase units or shares of that fund. The value of your units can go up or down depending on the type and performance of investments held within the mutual fund.

Non-Registered Investments: Investments which are not held in a tax-sheltered or tax-deferred account such as an RRSP.

Options: These are contracts that let you buy or sell a security like a stock at a set price between now and a certain date.

Penny Stock: A low-priced, speculative security. Penny stocks typically trade for less than a dollar a share and are often those of "unproven" companies.

Portfolio: A collection of investments.

Preferred Shares: This is a special type of stock that regularly pays you a set amount of money from the company's profits (dividends). The reason they are called "preferred" is that you get preferential claim to the profits ahead of common shareholders.

Registered Investments: Investments held within a registered plan (eg., RRSP, RRIF, RESP) recognized by Revenue Canada. Investments in such plans allow you to defer paying taxes on principal and earnings until they are withdrawn from the plan.

Registered Retirement Savings Plan (RRSP): A deferred tax savings account where contributions accumulate with earnings on a tax-deferred basis. When the money is taken out of the RRSP it is taxed as income.

Return: Income earned and/or capital gain realized on an investment (often expressed as a percentage of the initial value of the investment).

Safety: In investment terms, this refers to preservation of your original investment.

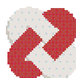
Stocks: Often traded on a stock exchange, they represent ownership of a portion of a company.

Stock Exchange: A place where stocks are bought and sold.

Term Deposit: A short-term fixed rate investment. Today, these are usually called Guaranteed Investment Certificates (GICs).

Treasury Bill: A short-term debt instrument issued by the federal or provincial government and sold in amounts of $1,000 or higher. T-Bills do not pay interest but are sold at a discount and mature at par (or face value). The difference between the purchase price and par at maturity is your income, which is treated as interest for tax purposes.

The Canadian Bankers Association, established in 1891, is a professional industry association that provides its members – the chartered banks of Canada – with information, research and operational support, and contributes to the development of public policy on issues that affect financial services. The CBA also provides information to the public on industry and financial issues.



CANADIAN BANKERS ASSOCIATION

Building a Better Understanding