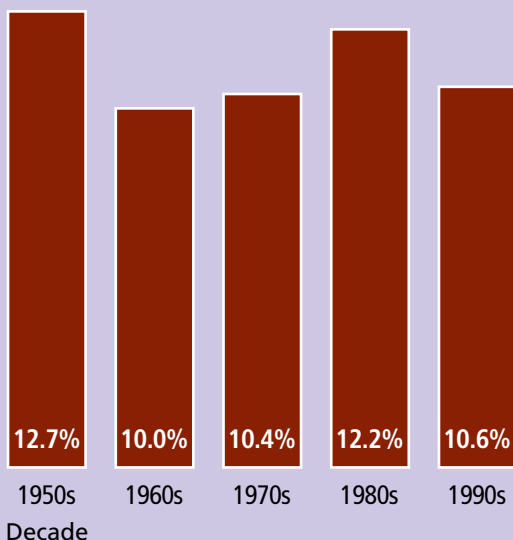


Why you should look beyond market ups and downs

Every time the stock markets stumble, the media leaps into action. Just think back to “Black Monday” in October of 1987, the Asian market chaos 10 years later, or the “Tech Meltdown” in the early 2000s. The headlines were full of doom and gloom, with references to the stock market crash of 1929 and subsequent depression.

Over a 50-year period, long-term returns from Canadian equities have been remarkably consistent.

S&P/TSX Composite Index
 Compound annual return



Source: 2007 Andex Chart

In today's wired world, these messages arrive via multiple channels – television, radio, newspapers, and the Internet. It can be difficult to stay focused on your investment objectives when you're surrounded by all of these distractions.

Lessons from the past

In times like these, it can be helpful to recall the wisdom of industry veterans who have seen many market cycles. Nick Murray, for instance, has 40 years of industry experience, is widely recognized speaker, and the author of *Simple Wealth, Inevitable Wealth*.

He likens stock market activity to a child riding up an escalator while playing with a yo-yo. Focus on the yo-yo, and all you see are ups and downs. Focus on the escalator, and the longer-term, upward movement becomes clear.

Historical market activity supports his observation. From 1950 to 1999, stock markets have been buffeted by 9 recessions, 13 bear markets, wars, acts of terror, and natural disasters. Yet 10-year compound annual returns of the S&P/TSX Composite Index have ranged only from 10.0% to 12.7% – a difference of less than three percentage points (see chart to the left).

Volatility equals opportunity

For pro-active investors, who recognize the value of a long-term approach, temporary downturns actually represent a valuable opportunity. When you purchase shares or mutual fund units during a market-decline, you may pay less for them than you would if the markets were rising.

Purchases made during market declines help to bring down your average price per share or unit. And since the long-term market trend has historically always been upward (think back to our escalator example, above), declines may actually enhance your overall returns.

Since no one can accurately predict when the markets will go up or down, one of the best ways to take advantage of the upward trend is to commit to a pre-authorized purchase plan, where you automatically invest a regular amount on a regular basis. This also helps eliminate the impulse to try and time the market.

Your Scotia advisor wants you to be comfortable with your portfolio. If you're ever concerned or have a question about the markets or your investments, contact your advisor.

Scotia® solutions

One of the main benefits of working with a Scotia® advisor is that your financial plan has been developed based on your short-and-long term financial goals. Your portfolio includes the types of assets and specific investments that reflect your financial objectives, time horizon, and risk comfort level.

Your advisor can help you see market events in their proper perspective, answer your questions, and listen to your concerns.

One solution your advisor may suggest to help you manage market volatility is a Scotia Partners Portfolio®. With one investment decision, you get a professionally managed, diversified portfolio of mutual funds from some of Canada's top fund managers.

Once you've selected the portfolio that matches your investment profile, you can focus on your life and let the professionals focus on your investments.

Received a tax refund? Put it to work!

If you received (or are expecting) an income tax refund, you have a valuable opportunity to give your financial plan a boost. Best uses to consider include:

Reinvest your refund in your Registered Retirement Savings Plan (RRSP). It can begin earning tax-deferred income right away, and you can get a tax deduction for the 2008 tax year (assuming you have sufficient room).

Pay down debt. If you're carrying a balance on any credit cards, a line of credit, or personal loan, use your refund to reduce the amount owing and reduce your cost of borrowing.

Make a principal prepayment on your mortgage. Some mortgages allow lump-sum payments towards the principal. Your payment will reduce your total interest cost and help you be mortgage-free sooner.

Contribute to a Registered Education Savings Plan (RESP). The first qualifying \$2,500

contributed annually to your child's RESP will trigger a Canada Education Savings Grant (CESG) from the federal government equal to at least 20% of the amount contributed (depending on your net family income, subject to the CESG lifetime limit, and assuming all CESG eligibility requirements have been satisfied).

Top up your non-registered investment account. While investment earnings outside a registered plan are taxable, you can reduce the tax on investment income by focusing on investments that generate primarily dividends and capital gains, which are taxed less heavily than interest income.

Remember that it's okay to reward yourself, too. If you want to direct 100% of your tax refund to any or all of the objectives above, that's an excellent, forward-thinking decision. However, you may prefer to spend a portion on yourself or your family and enjoy it today.

3 ways to split income and reduce your family's tax bill

Are you paying more tax than you need to? If you have a spouse and/or children who currently pay tax at a lower rate than you, the answer may be yes.

By implementing a few fairly simple income-splitting strategies, you may be able to shift some of your taxable income into their hands, where it will be taxed at a lower rate. Result: a lower tax bill for the family as a whole.

Below, three frequently used strategies are outlined. To make sure they're appropriate for you, it's best to seek professional tax advice before implementing any of them.

a. Have the higher-income spouse pay all the household expenses and use the lower-income spouse's earnings to invest.

When the lower-income spouse invests, the interest, dividends, and capital gains generated are taxed in his or her hands.

Example: Jean is a top lawyer earning more than \$100,000 a year. Her federal and provincial combined marginal tax rate is 43%. Her husband, Dan, is a massage therapist and makes about \$30,000 a year at a marginal tax rate of 21% (less than half Jean's marginal tax rate). Jean pays all the household expenses – the mortgage, car payments, property taxes, food, and clothing – so they can use Dan's earnings to invest.

Last year, he reported interest earnings of \$8,000 and paid tax of \$1,680 on them. If Jean had reported the interest, the income tax payable would have been \$3,440, or more than twice as much.

b. Lend money to a lower-income spouse to invest.

Dan was a stay-at-home parent and didn't have any earnings to invest. Jean can't simply give him money to invest, because in that situation the investment income would be attributed back to her and taxed at her combined marginal tax rate.

However, she can lend Dan the money to invest – provided she charges interest at the Canada Revenue Agency's prescribed rate (4% for the second quarter of 2008). Dan must actually pay the interest to Jean within 30 days after the end of the year and Jean must report the loan interest as income. They should formally document the loan with a signed agreement and maintain separate accounts so that their arrangement is clear.

Example: Jean lends Dan \$30,000 on March 1, 2008, charging him 4% interest. Dan invests the money. As long as he pays the \$1,000 in interest to Jean by January 30, 2009, the investment income is taxable to him.

c. Hire a family member.

People who are self-employed can hire their spouse or child to work in their business and pay them a reasonable salary. The salary is deductible for the business owner as a business expense and reported as taxable income by the spouse or child.

Example: A massage therapist, Dan, could hire his 17-year-old daughter, Chloe, to maintain his client records for him. She might put in 10-hours a week and earn about \$6000 over the course of the year. This amount would be a tax deduction for Dan and would be taxable to Chloe at a much lower tax rate, a net benefit to the family's tax bill.



How to participate in uptrends and avoid market downturns

If you would like to be able to earn the potential returns that stock markets provide but aren't willing to accept the volatility, you may want to consider a market-linked GIC.



These are GICs with a difference — the return they pay is based on the returns of an underlying equity investment or market index. That investment might be a stock index (like the S&P/TSX60), a basket of stocks, or one or more equity mutual funds. In all cases, the principal is 100% guaranteed, just like a traditional GIC.

Market-linked GICs are available in different terms (typically three to five years) and with a variety of features. Some may guarantee a minimum return as well as guaranteeing the principal.

Scotiabank currently offers five market-linked GICs. If you'd like to know more about any of these investments, please ask your *Scotia* advisor.

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