

## Investment Markets

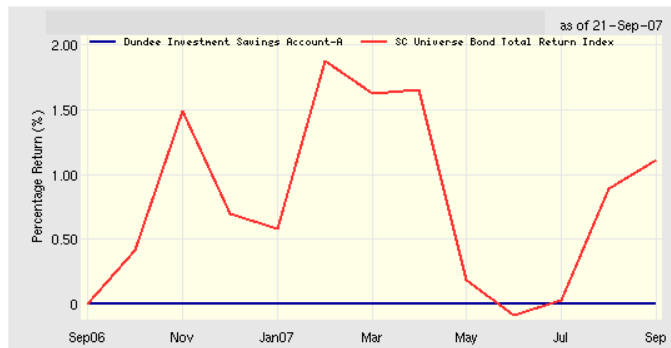
The summer of 2007 brought the most volatility we've seen in the stock and bond markets for some years. The graph below shows an indication of the past 12 months of market history.



At one point, the S&P/TSX index, which is an indicator of the overall Canadian stock market (upper line) had fallen back to levels last reached in January, erasing any gains made in 2007. But by the first day of fall, the market had recovered to a 10% gain since the first of the year.

Bond markets, as represented by an index fund (lower line), declined in the first half of the year as interest rates rose.

The increase in interest rates can be seen in market rates for GICs. January 2nd rates were 4.1% for both 1-Yr and 5-Yr GICs, but by September, best rates were over 5% for all terms for the first time since 2001.

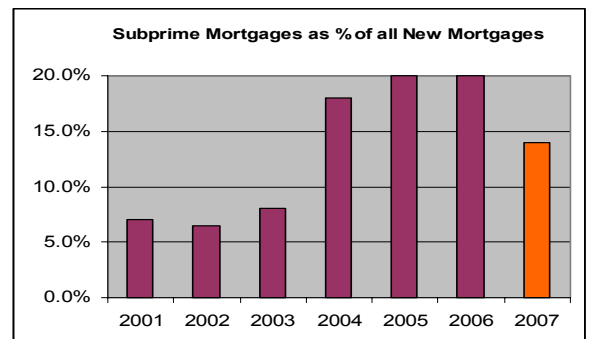
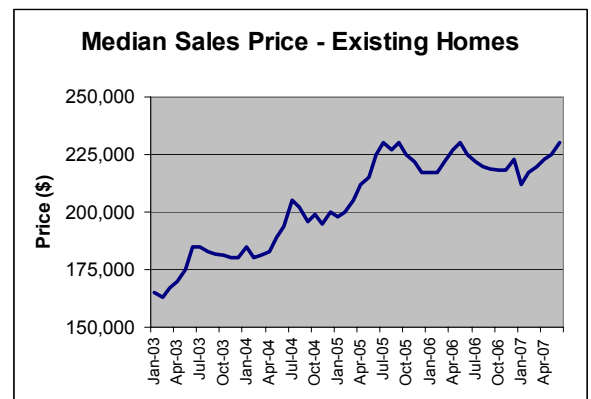


A closer look at the bond market in general (second graph from top) shows that even with interest payments included, the total return on bonds has been just over 1% in the past 12 months because of the market value of those bonds declining as interest rates have increased.

High quality government and corporate bonds are still paying regular interest payments, and will mature eventually at their full value, so long term investors needn't worry. But in the meantime, their value on paper is reduced, and someone needing to cash out will get the lower price.

What's going on? Much has been written lately about the United States housing and sub-prime mortgage 'crisis' which has been a key factor in much of the past quarter's market changes. This article will summarize the situation.

US house prices have grown 80% over the past 5 years, making it difficult for many people to buy a home. By 2004, many US mortgage lenders relaxed their criteria for extending mortgage loans to self-employed people and those with poor credit histories. As any lender would do, they considered the value of the houses being bought as good security on those loans in case the borrowers defaulted on their payments. The easy availability of mortgage loans increased demand for homes, and pushed prices even further upward. Two factors contributed to making this a very unstable mix: first, the debt ratios on these mortgages were very high, many at or approaching 100% of the purchase price, and with low or no principal repayment scheduled (ie interest only mortgages); second, the mortgages were issued with a low 'introductory' interest rates, which were scheduled to revert to fair market interest rates after (usually) two years. Sub-prime mortgages accounted for 18% of all US mortgages issued in 2004, and 20% in 2005 and 2006.



By 2006, the 2004 mortgages were passing their 2<sup>nd</sup> year, and it became clear that many sub-prime borrowers would not be able to keep up their interest payments when the interest rate was raised to market rates. The percentage of mortgages in default spiked upward, and house prices began to fall as foreclosing lenders tried to sell the properties on the market. Reduced market prices also reduce the incentive for borrowers to keep making their payments, especially when the house is worth less than the mortgage balance owing. This leads to even higher default rates, and more downward pressure on house prices.

Why the impact on global bond and stock markets? Today, few lenders actually continue to hold the mortgages the issue until the maturity date. Often, the loans are bundled together and sold in the financial market as a mortgage-backed security (MBS). A pool of mortgages sold in such a bundle could include both prime and riskier subprime mortgages. A particular MBS would receive a quality rating, based on the percentage of prime versus subprime debt in the bundle – the higher the amount of subprime debt, the higher the risk, therefore the lower the rating, and the higher the interest rate on the bundle.

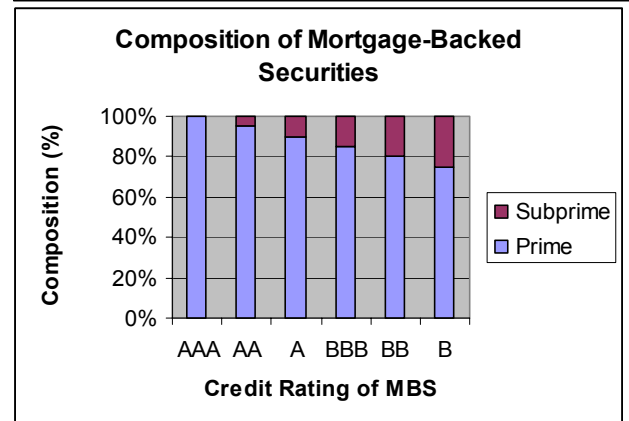
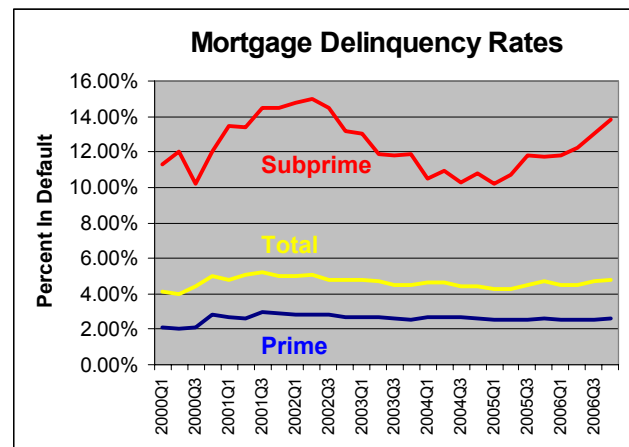
A number of investors and investment managers around the world saw opportunity in these higher-yielding MBSs. They could borrow money at lower rates to buy the higher-yielding MBSs and earn the difference between the two rates. The MBSs are now held in many portfolios belonging to corporations, governments, banks, and investment funds. Rising default rates on the subprime components of the MBSs

could turn such borrow-to-buy-loans approaches into money-losing propositions. The first such problems became apparent in July 2007 with the failure of two hedge funds which had used this strategy. Several European banks and municipal governments are also facing this problem. Because it can be difficult to know exactly what the subprime exposure of a particular MBS is, or of financial companies and investment vehicles that may or may not hold them, buyers simply stopped buying MBSs and any other investments that may be exposed to them. New investment dollars instead went to top quality government bonds and caused bond prices to increase (and bond interest rates to drop). At the same time, interest rates on any debt instrument with even a small degree of risk have gone up.

During late August and early September, financial firms were issuing statements to confirm their exposure or non-exposure to MBS securities, and related securities called Collateralized Debt Obligations (CDOs) or Asset-Backed Commercial Paper (ABCP). Even those with zero exposure to these investments have seen the value of their portfolios drop because the market is not offering as high a price for any debt instruments below the safest grade. Commercial US real estate has also suffered a significant drawdown along with the residential housing price slump.

What's next? Investment funds confirming low or no exposure to the problem loans should recover some value. Meanwhile, US consumer spending could drop as people 'feel poorer' because of reduced market values of their homes. Some fear a recession in the US could occur as a result, with some impact on Canada because much of our exports go to the US. Canada is already feeling some pain because of the higher value of our dollar vs. the US\$. Steep cuts to short term interest rates in the US may well stave off a consumer recession, and many US companies who sell their products globally will have increased US\$ revenues as the US\$ declines with the interest rate cuts. There will be continued volatility in both stock and bond markets globally as analysts sort through the implications. While investors don't like volatility, volatility provides opportunity for skilled portfolio managers, backed by a team of competent analysts. There has never been a better time to have your portfolio managed by a team of the world's top managers, as many of our clients do.

Having a long-term view is important in these times. A solid well-designed portfolio does not need to be taken apart and rebuilt each time there are changes in the market. A strategic long-term asset allocation and regular rebalancing will see you through. Please let us know if you would like to discuss your particular situation in more detail with us.



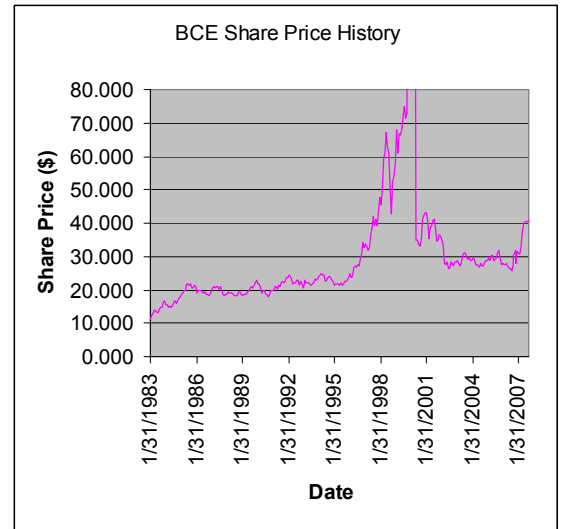
The strategies discussed in this newsletter are not for everyone. We would only recommend a particular strategy after fully understanding your unique situation, objectives, and values. We would be glad to offer a complimentary **'Initial Assessment and Evaluation'** meeting, and a written **'My Life – My Wealth'** report of the areas in which we believe we could help you achieve your financial goals. Please call us if you would like to discuss this opportunity.

## Do You Own Bell Canada Stock?

Many of our clients own shares in BCE, the parent company of Bell Canada. If you own BCE shares, you may soon have a significant tax bill to pay. A group of investors led by Teachers Private Equity has offered to buy all BCE shares for \$42.75 per share. Shareholders and the Competition Bureau have both approved the deal, which should close early 2008.

If you have held these shares since 1983, your 'cost basis' is about \$11 per share. When the takeover is concluded, you will automatically receive cash for your shares, and will have to declare as taxable income one half of the difference between your cost and the proceeds you receive. An investor in the top 45% tax bracket owning 2000 shares would pay over \$14,000 in income tax. (The shares have split 24-fold since 1949 so an original 100 shares would be 2400 shares now).

Date	Event	Per Share	2000 Shares	Gain
31 Jan 1983	Purchase	\$11.19	\$22,380	\$ 0
31 Feb 2008	Buyout	\$42.75	\$85,500	\$ 63,120
			Taxable Portion	\$ 31,560
			Tax at 45%	\$ 14,202
			Net Proceeds	\$ 71,398



Since you will get cash for the shares, at least you will have the money available to pay the tax, but there are a few planning opportunities which can help you reduce the impact:

1) If you don't need the proceeds from the sale of your BCE shares for your own financial security, consider giving the shares to charity before the buyout is effective. In this case you don't pay any of the tax on the capital gains, and still get a charitable donation credit for the full share value at the time of the donation. The difference between the net after-tax proceeds you would have had, and the donation tax credit you will receive, is the net cost of making the donation.

	Sell Shares	Sell Shares and Donate	Donate the actual Shares
Value of Shares	\$85,550	\$85,550	\$85,550
Cost Basis	\$22,380	\$22,380	\$22,380
Capital Gain	\$63,120	\$63,120	\$63,120
Tax Payable on Sale	\$14,202	\$14,202	\$ 0
<b>Net Proceeds of Sale</b>	<b>\$71,398</b>	<b>\$71,398</b>	<b>\$85,550</b>
Amount Donated	\$ 0	\$71,398	\$85,550
Donation Credit	\$ 0	\$28,673	\$34,357
<b>Net Cost of Donation</b>	<b>N/A</b>	<b>\$42,725</b>	<b>\$37,041</b>

More for the Charity.

Less out of your pocket.

If the total donation will exceed your donation limit (75% of income) you can carry the donation forward and use it up over 5 years. If you would like the total donated amount to benefit several charities over several years, a charitable foundation can be set up to minimize the administration – this can now be done very economically for amounts as low as \$25,000.

2) If you hold other securities, mutual funds, or real estate that is in a capital loss position, you can trigger a disposition of some of those assets to realize the paper loss and offset the BCE gains.

3) If you plan to reinvest the net proceeds, make sure that the amount needed to pay the remaining tax is set aside in a vehicle which can be cashed in before the tax is due in April 2009. Remit instalment payments to ensure you don't leave a significant amount owing at the end of 2008.

4) Rather than reinvesting the net proceeds into another single stock, consider establishing a diversified stock portfolio through a mutual fund or managed account. This approach is less risky than being invested in a single stock because the investment is spread across 20 or more stocks chosen by professional portfolio managers and analyst teams, without the need for you to make decisions each time a change to the holdings is warranted.

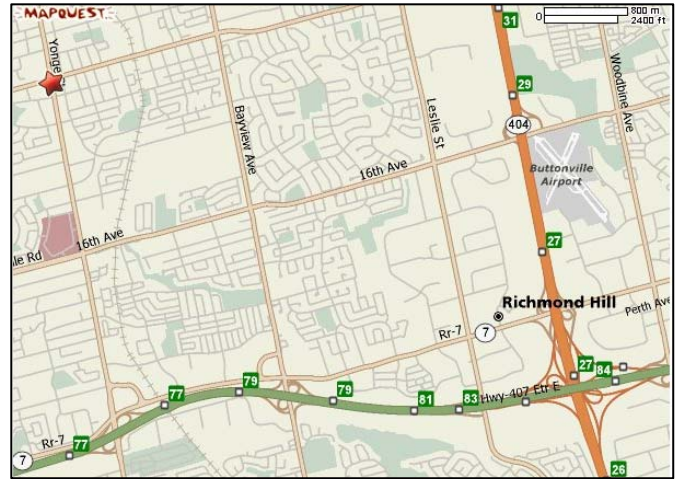
***If you would like to discuss your situation with us in confidence, please call us to arrange your own Initial Assessment and Evaluation meeting.***

Financial Planning services provided by Page and Associates Ltd. This is not an offer to sell any product.

## A World of Change

Change is constant. For the past 10 years, our firm has operated at the four corners of downtown Richmond Hill. Before that, Kenneth Brown Investment Services operated for many years just north of our current location. We are presently considering whether to move our office location once again.

As our business has grown, Richmond Hill has become steadily busier. The traffic congestion and property crime on our intersection has become worse each year. At the same time, the building we are in is showing its age more and more. It is over 100 years old, and has two furnaces and air conditioning systems. The heating, ventilation and energy efficiency of the building is very poor, and this has become more noticeable with the hotter summers and increasing energy costs. Since it is actually two separate small houses joined by an annex, the space is poorly laid out for collaborative work teams, and there is a great deal of under-used space. We often hear comments from our clients that our building doesn't reflect the sophistication of our service offerings, and there is a limited amount of change we can make to this building to allow it to reflect our positioning better. Finally, many of our clients live outside of the immediate area, and get to us via highways 404, 7 or 407. Since our location is about 10 minutes from any of these arteries, we have had many requests to move to a location closer to a major highway so that our clients can quickly and easily get to us while they are en route to or from work or social functions.



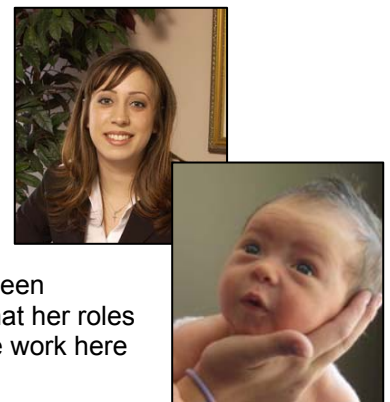
Naturally, we are sensitive to the fact that many of our long-time local clients like the convenience of having an office location here in the town. We have spoken with a number of our clients in this area, and have found that most would not mind a location closer to a highway because they also need to use the highway on occasion. We have also heard that because of changes in our processes over the past few years, most routine transactions are easily handled by telephone, mail or email, so in-person meetings at the office are usually limited to a quarterly or semi-annual review of financial plan updates and portfolio performance. Of course, we will make house calls if getting to our office is too difficult.

As we make these decisions, if you have any thoughts you'd like to share with us about how a location change would affect you, please call and let us know. We do want to make sure we continue to provide you with the service you expect.

## An Addition to the Family

This was a busy year for Karissa Smith. Even if you don't work directly with Karissa, you've benefited from her work here at Page and Associates because of her role as Alternate Branch Manager for Worldsource Financial Management Inc., and her contribution to the development of financial plans for many of our clients who deal with other advisors in our firm.

In July, Karissa began a maternity leave, and her first child was born on his due date July 21<sup>st</sup>. Baby Ryder was 7 pounds 12 ounces and is a healthy happy guy. Karissa has been enjoying her time off with Ryder, but is still in touch with us on a regular basis to ensure that her roles within the firm are being fulfilled by the rest of the team. Karissa plans to return to full-time work here in May of 2008.



## Feedback

We hope you've enjoyed this newsletter. Your comments are important, and they are very valuable to us. Please let us know any ideas you may have for improving the newsletter, or topics you'd like to see in future issues!

**Did you know?** – you can receive this newsletter by email? We'd gladly give our environment a break by sending you the next newsletter electronically. Please email [contact@askpage.com](mailto:contact@askpage.com) with your full name, and we'll switch you to the email version next time. *Thanks!*