**De Thomas Financial Corp**

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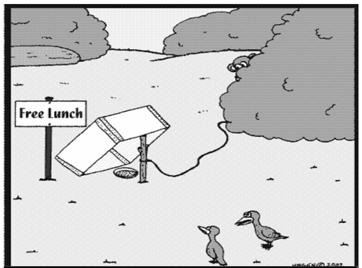
### Capitalism and Failure

Capitalism without failure (or bankruptcy) is like Christianity without hell - it loses its ability to motivate people to be prudent and act properly.



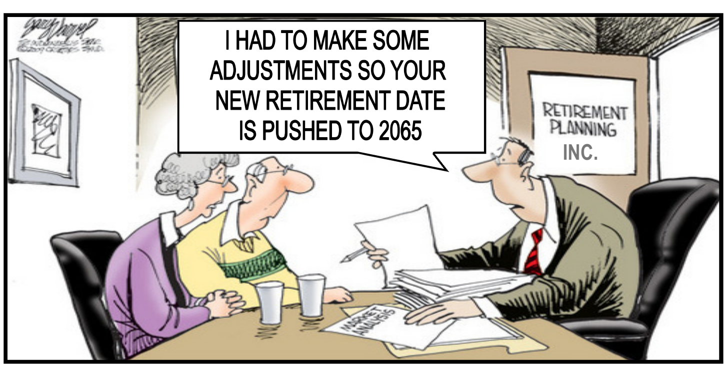

"I am a bit suspicious...in my experience, there is no such thing as a free lunch!"

Just think of the hedge-fund fraudster Bernard Madoff, who may have cheated his well-healed clients of well over $50 billion. One investor Allan Goldstein said he trusted Madoff because he trusted the government. "*We conducted our affairs in good faith in the belief that the SEC (Securities Exchange Commission) would never allow this sort of scheme to be con-*

### DOWNSIZED RETIREMENT DREAMS

Many workers of all ages are coming to terms with a daunting realization - they may never be able to *fully* retire. The idea of retiring one day to enjoy life is a relatively modern invention. In 1889 German chancellor Otto von Bismarck crafted the world's first government-supported pension for workers at age 70 (later reduced to age 65). This was not such a big deal back then as the average life expectancy was only 40. He was a brilliant general and a very clever actuary. He knew only a few would ever get the pension so it was not a very expensive benefit to give away. Since, then, retirement has morphed into a "very long vacation that is not sustainable with today's average retirement span at over age 85 (and increasing).

Many experts now think there is no getting around the fact the 30-year retirement dream has become unsustainable. Some provinces like BC and Ontario have abolished mandatory retirement age. Going forward, CPP will reward those that stick around and work until age 70.




So perhaps it is a good sign that more workers plan to keep working in some fashion after they retire. Besides, maybe working longer is not such a bad idea after all. Researchers at the University of Maryland found that retirees who take on temporary or part-time jobs related to their fields suffer from fewer diseases and mental health problems than those who opt for full-time retirement.

(by W Larson (North America)

**Worker to Retiree Ratio (2002 survey)**

| AGE | 1941 | 2000 | 2010 | 2020 | 2030 | 2040 |
|---|---|---|---|---|---|---|
| 62 | 4.5 | 2.9 | 2.6 | 2.1 | 1.7 | 1.7 |
| 65 | 6.1 | 3.5 | 3.4 | 2.7 | 2.1 | 2.0 |
| 70 | 10.7 | 5.0 | 5.3 | 4.0 | 3.3 | 2.9 |

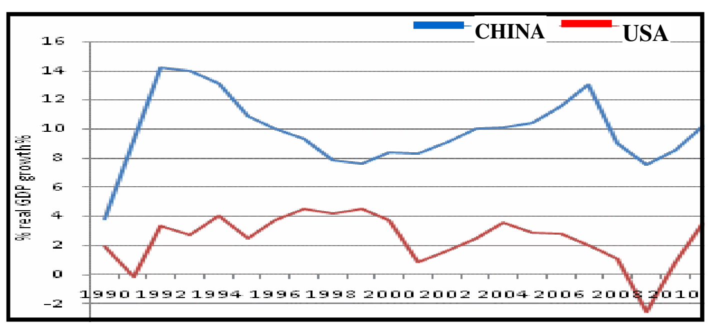
### The Nature of Real Wealth

Buttonwood, Oct 8th 2009, *The Economist*

Investors confused "paper assets like fancy derivatives" with real assets. At the heart of the 2008 crisis was a fundamental confusion about what is real wealth. If your financial assets rise in price, does that not mean your aggregate wealth has increased? Not always.

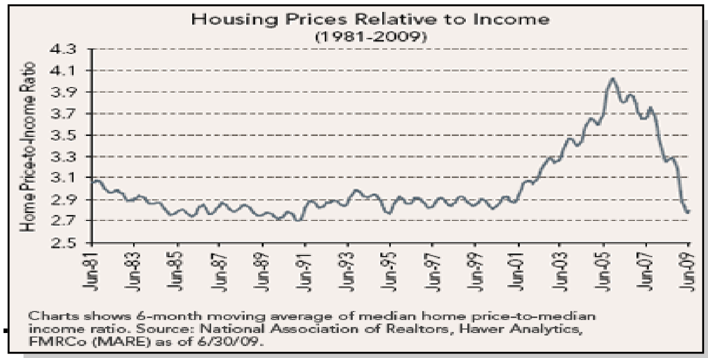
- Think of a pizza as your assets. If everyone sitting at the table is given a pizza slice and the share price rises from $1 to $2, is your pizza meal any bigger or is your meal the same size?

The fundamental reason why wealth increases over time is because the economy is linked to better economic productivity (making more pizzas at less cost). As productivity grows so does net revenue. Profits will rise and dividends (your meal) to shareholders will increase. Look at the chart below. Compared to China, the average U.S. family income as a percentage of the GDP (gross domestic product) has been steadily declining since 2003.




This is what the real estate buyers (and derivative sellers) forgot. Selling homes at a higher price, while not improving productivity is a recipe for disaster.

Real estate: rising prices did not make people richer in aggregate, unless that re-pricing represented an accurate prediction about improvement in productivity and income. People were using rising prices as a barometer of wealth The chart below shows historical housing prices relative to income.




**TRADING (Houses or Stocks) Does Not Create Wealth**
Stock trading, like real estate flipping, does not create real wealth. **CNBC,** the world's top business television channel, broadcasting around the globe, devoted 16 hours of live coverage every day and analyzed every detail of the credit crunch but its ratings slumped. Why? Despite devoting its entire show to business, the channel failed to put up any warning flags before the credit crunch. Investors stopped watching because they were not getting any richer.

> *Don't try to time the market. It's very, very difficult to do. There may be a couple of people in the world who can do it, but if there are they're not telling you."*
>
> *Ben Bernanke, July 2009*

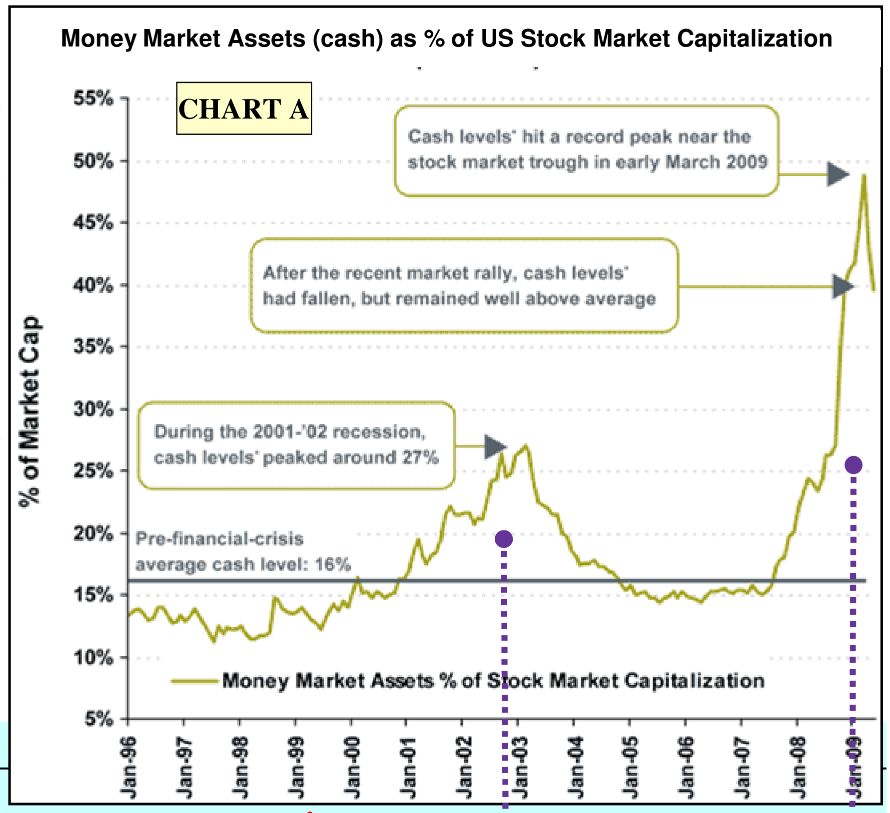
**$ CASH HOARD** *Financial Post Sept. 29, 2009*
A record **trillion** dollars of cash was sitting on the sidelines in Canada (Sept 2009), and 10 times that much in the United States. Derek Holt, vice-president of Scotia Capital Economics, and colleague Karen Cordes revealed .

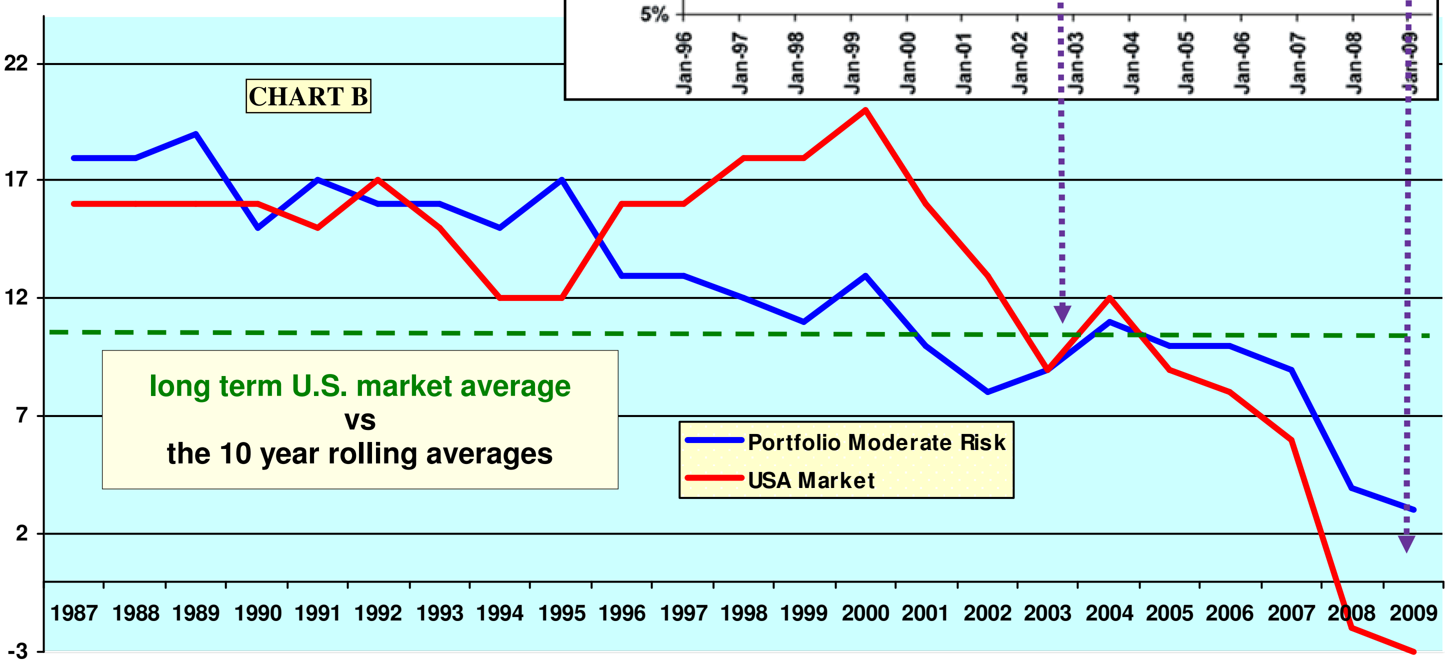
**CHART A:** Notice how the investors have more in money market or cash (Chart A) when the markets are cheap but have less in cash when markets are expensive (selling low, buying high).

**CHART B:** Chart B shows the ten year rolling averages for the US stock market (red line) and a moderate risk portfolio (blue line).

**Sample 10 Year Rolling Periods - Chart B**

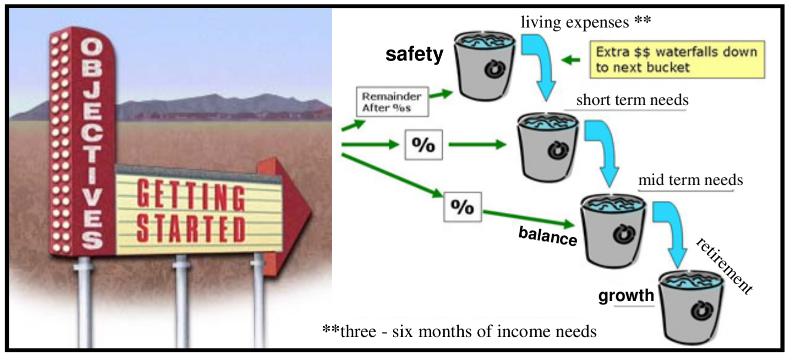
| Ten Year Period | US Market | Moderate Portfolio |
|---|---|---|
| 1977-1987 | 16% | 18% |
| 1985-1995 | 15% | 13% |
| 1999-2009 | -3% | 4% |



| Portfolio Blue Moderate Risk | Asset % Allocation |
|---|---|
| Large Stocks | 40% |
| Small Stocks | 26% |
| Real Estate | 9% |
| Emerging | 9% |
| Cash | 8% |
| Bonds | 8% |

From ifa.com
and CRISP data




Different buckets for different needs: safety, income, balanced, growth etc

## <u>3 BUCKET</u> PORTFOLIO SAMPLES

**Bucket 1**
**<u>Income</u>**
85% Bonds
15% Equity

| Bucket 1 1985—2009 | 3 months | 1 year | 3 year | 5 year | 10 year | 12 year |
|---|---|---|---|---|---|---|
| Average for the period | 0.5% | 7% | 23% | 39% | 89% | 95% |
| Worst period | -5% | –1.3% | 4% | 11% | 44% | 65% |
| % chance earning > 0% | 78% | 95% | 100% | 100% | 100% | 100% |
| % chance earning > 5% | 9% | 63% | 67% | 76% | 77% | 80% |
| % chance earning >10% | 0% | 21% | 19% | 17% | 0% | 0% |

**Bucket 2**
**<u>Balanced</u>**
65% Bonds
35% Equity

| Bucket 2 1985-2009 | 3 months | 1 year | 3 year | 5 year | 10 year | 12 year |
|---|---|---|---|---|---|---|
| Average for the period | 1.7% | 7.2% | 25% | 43% | 95% | 110% |
| Worst period | –11% | –10% | –3% | 7% | 41% | 75% |
| % chance earning > 0% | 73% | 88% | 97% | 100% | 100% | 100% |
| % chance earning > 5% | 12% | 66% | 72% | 69% | 88% | 85% |
| % chance earning >10% | 0% | 27% | 19% | 23% | 10% | 5% |

**Bucket 3**
**<u>Growth</u>**
20% Bonds
80% equity

| Bucket 3 1985-2009 | 3 months | 1 year | 3 year | 5 year | 10 year | 12 year |
|---|---|---|---|---|---|---|
| Average for the period | 2% | 7% | 27% | 47% | 115% | 190% |
| Worst period | -25% | -30% | -25% | -8% | 22% | 81% |
| % chance earning > 0% | 66% | 75% | 85% | 98% | 100% | 100% |
| % chance earning > 5% | 31% | 66% | 72% | 65% | 95% | 100% |
| % chance earning >10% | 6% | 49% | 42% | 36% | 25% | 50% |

**The % in Bonds should include**

- Short term
- Corporate
- Government
- Canadian
- Global and
- Inflation bonds

**The % in Equities should include**

- Canadian
- American
- International
- Large cap
- Small cap
- Growth
- Value
- Emerging market
- Real Estate
- Commodities and
- Option writing

A 12 year period <u>normally</u> provides a long enough time frame for returns to get back to their historical averages. The 12 year period between Oct 1997– Oct 2009 was just not one of those periods. The market crash of 2008 dramatically affected the past 12 year returns. We would expect the 12 year period 1998-2010 to be more reflective of "normal 12 year cycles."

Data Paltrack and ifacanada.com

Achieving a good return is only possible if you <u>do not</u> bail out in bad years - example bucket #3 had a –30% drop in a one year period ending Feb 2009. For more details on each portfolio, please visit ifacanada.com. Berkshire returned over 20% from 1965-2008 but only if you did not bail out in the year 1974 when it lost 49%. See sample below.

**Buffett's Berkshire Stock**

| $10,000 Growth 1965 - 2008 | Worst 1 year 1974 | Worst 5 years 1972 - 1976 |
|---|---|---|
| $40 million; 20% | $5,100; - 49% | $5,300; - 47% |

**Bucket Investing Strategy:**
Create one bucket for your each of your needs such as:

1. short term plans(1-5 years) - vacations, car purchase. etc
2. mid term plans (6-11 years) - education, home purchase, etc
3. long term plans (12 years plus) - starting business, retirement, etc
4. Other personal goals________________________

**To keep things simple and easy, design three to a maximum of five major buckets for various portfolio needs.**
Each portfolio in each bucket will have various degrees of risk (volatility).

**PORTFOLIO CONSTRUCTION**
**CONSIDERATIONS**

- Inflation
- Deflation
- Depression or Recession
- Stagflation
- High Interest or Low Interest
- Bear markets or Bull markets
- High currency or Low currency
- … etc

An efficient PORTFOLIO strategy can help create order out of the daily chaos that often surrounds the investment process. The concept of asset allocation is far from new. In fact, even as far back as 1605, Miguel de Cervantes was doling out the same advice as today's investment strategists - he said simply, *"don't put all your eggs in one basket."*

**Here's the theory:** Many asset classes have distinct characteristics and historically don't react in tandem under the same market conditions. When some assets are falling in value, others may be rising. By strategically diversifying your assets, you help offset declines in any one particular class and smooth out the ups and downs of your portfolio. Proper rebalancing is a critical part of any good investment program.


"Let's change our investment strategy.
From now on, you start fetching the paper,
and I will handle all the investments."

## Building Your Personalized Portfolio

**EQUITY ALLOCATION** ______ %

**___% Candian Core**

**___% Canadian Equity Corp**
60% Canadian Large Cap*
20% Canadian Value*
15% Canadian Growth*
5% Option Writing*

**___% USA Vector Equity**
65% US Value*
35% US Small Cap*

**___% USA Core Hedged**

**___% USA Equity Corp**
35% US Large Cap*
20% US Value*
10% US Growth*
5% US Mid Cap*
5% US Mid Value*
5% U Small Cap*
10% US Small Cap Value*
5% Option Overlay*

**___% International Vector**
65% Intl Value*
35% Int'l Small*

**___% Inter'l Core Hedged***

**___% Int'l Equity Corp**
35% Int'l Large cap*
25% Int'l Value*
20% Int'l Growth*
15% Int'l Small Cap*
5% Option Writing*

**___% Int'l Real Estate**

**___% Int'l Alternative Corp**
70% Global Real Estate*
30% Global Commodities*

**___% Emerging RAFI**

**___% Emerging Market**
50% Emerging EAFE Market*
10% BRIC*
10% Latin America*
10% China*
10% Small Cap*
10% Option Writing*

**___% Other**
______________________
______________________

*** these allocation pre-set by fund**

**BOND ALLOCATION** ______ %

**___% Canadian Income Corp**
30% Cdn Government Bond*
20% Cdn Short Term Bonds*
20% Preferred Shares*
15% Cdn Large Cap*
5% Income Trusts*
10% Option Writing*

**___% Global Government**

**___% Global Corporate**

**___% Global Real Return**

**___% Short Term Bonds**

**___% Other Bonds**
______________________
______________________

*** allocation pre-set by fund**