The Stan Clark Financial Team's

PERSPECTIVES

In this issue...

Stan Clark
Senior Investment Advisor

Here's your special "Welcome" edition of PERSPECTIVES.

Each issue of Perspectives will present a quick, informative look at the world of finances and investing, from the perspective of the Stan Clark Financial Team.

We hope you find the stories entertaining, insightful and useful. We will have an occasional "Ask the Team" feature, and welcome your questions about investing or personal finances. We may also spring trivia quizzes on you – complete with prizes!

This publication is for you. Let us know what you'd like to see in Perspectives.

Stan

CIBC Wood Gundy

"We have met the enemy, and he is us." - *Pogo*

How emotions and biases affect our finances

By Stan Clark - Senior Investment Advisor

One of the most fascinating things ever to happen in economics was when an ingenious psychologist, Dr. Daniel Kahneman, decided to study it. In 2002 he won the Nobel Prize in economics for "having integrated insights from psychological research into economic science, especially concerning human judgment and decision-making under uncertainty." Kahneman actually created a new discipline, Behavioral Finance. In fact, his latest book *"Thinking, Fast and Slow"* was one of the New York Times top five non-fiction books of 2011.

What Kahneman discovered was shockingly contrary to the long-cherished beliefs of finance and economics: markets and the economy in general, are anything but efficient or rational.

Kahneman, and others since, have repeatedly shown that when it comes to matters of economics, finance and investing, people (including professionals) make systematic, repeated mistakes, are seldom aware of their mistakes and fail to learn from them.

Behavioral Finance explains the tech boom of the 1990's, the real estate boom of this past decade, and their corresponding busts. If more of our political and financial leaders were familiar with Behavioral Finance, it could have helped to prevent these.

For individuals, it explains recurring mistakes people make with their investing, borrowing, spending, and other crucial areas of their finances. Becoming more familiar with Behavioral Finance can help you avoid these mistakes, and benefit from the mistakes of others.

Kahneman's major discovery was that emotions and biases have far-reaching effects on our judgments and decision making. No matter how smart, educated or professional you are, emotions and biases affect everybody because they have been hard wired into our brains over millions of years of evolution.

Here are a few ways our emotional brains get in the way of good judgment:

- People are overconfident when making predictions ("home prices will always rise"). Confidence increases as we collect more information; unfortunately, forecasting accuracy does not.
- We have a strong "hindsight bias" leading us to believe the future is easier to forecast than it is. However, accurate forecasting is extremely difficult because our economy is so complex and because creativity, innovation and competition are things that simply cannot be forecast.
- People place more confidence in complex explanations than simple ones. But simple often turns out to be better.
- We evolved as story tellers: people are more comfortable with anecdotal data and stories than with facts, figures, and statistics. This causes us to be persuaded by a good story, even when the numbers don't add up.
- People are uncomfortable going against the crowd. We evolved as social animals and naturally feel comfortable staying with the group, even when the group is going where it shouldn't.
- People place far more weight on recent events and personal experiences, than on long ago events and the collective experiences of others. That is why we never seem to learn from history.
- We filter and process information selectively, giving more weight to information that confirms our emotional biases: we see what we want to see, and often ignore uncomfortable facts.
- We are far more strongly influenced by our emotional brain than most realize. Often our rational brain makes up arguments so we will believe what our emotions want us to believe.

Team Talk:

Elaine Loo
Associate Investment Advisor

Sooke Basin

What are your hobbies?

My kids and my puppy! They are pretty much my second job, nights and on weekends. I have no time for anything else – BUT I have no complaints either.

Which sports do you like?

Who needs sports and exercise when you have high-energy kids, plus a hyper dog! Just try to keep up with them – that will take care of your exercise requirements for the next 20 years!

Who has had the most influence in your life?

My Mom and Dad, even to this day. (please don't tell my husband Kevin this)

Are you a morning or night person?

I used to be a night owl. Then the kids came along. Now I can barely stay up past 10 pm!

Where did you go on your last vacation?

Family trip to Japan. It was the first big trip we have done and definitely the most memorable and cultural. Everyone had a blast and my kids still remember the trip. They keeping asking to go back!

The consequences of our all-too-human tendencies are significant, especially when dealing with finances and investments. Behavioral Finance is a huge and important topic that affects all of us every day. It's a fascinating area and I invite you to learn more about it. ■

Stan Clark is First Vice-President, Portfolio Manager and Senior Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Stan has direct responsibility for the team and oversees all areas of financial planning, investment selection and investment management.

Financial planning is important - and well worth it!

By Sylvia Ellis - Senior Estate Planning Advisor

People make plans for vacation travel. They also create plans for home renovations, weddings and even shopping trips. Why is it, then, that most people don't have a plan for their most important long-term financial decisions?

It's partly because financial planning can be daunting. You have to integrate so many factors: income, spending, savings, assets, liabilities, risk tolerance, family situation, goals… The list is indeed lengthy. And for your financial plan to work, all of these need to fit and be coordinated with each other.

But it's well worth the effort. A good plan will help you:

- save enough money to invest to reach your goals
- eliminate, reduce and defer income taxes
- determine the right asset mix for you
- protect your family against financial losses from death, disability or serious illness
- make sure your estate is distributed according to your wishes.

Because financial planning can be complicated, it's only human nature to put it off. Or, if people do create a plan, many become overwhelmed by putting it into effect. They let the plan lapse and it becomes outdated. Meanwhile, taxes, inflation and the wrong investments are limiting or diminishing their wealth.

We've found that the easiest way to avoid being overwhelmed with planning is to break it down into manageable, bite-sized pieces. Don't try to do everything at once; focus on what's most important and urgent. And treat your financial plan as an ongoing process rather than a one-time event. That way, you can always make solid progress on a schedule and time-frame you can work with.

At The Stan Clark Financial Team, we use a four-step cycle:

Step 1: Clarify your situation and your goals

This is where we take the time to discover what you are about: family, work, needs, goals and dreams. As with taking a trip, you need to know where you are and where you want to go in order to figure out how to get there.

Step 2: Create a personal financial plan

Once we have a clear understanding of your situation and goals, the next step is to put numbers to everything. This will help you answer the basic questions, such as: When can I retire? How much retirement income will I need? What size estate will I leave my family? From here, we review all of your financial affairs and identify the top priorities for you to act on.

Step 3: Customize your investments to fit your plan

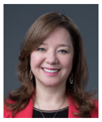
Your investments are a very important tool to help you achieve your life goals, so we need to get them on the right track as soon as possible. Together we review your plan and preferences and determine the strategies and guidelines we will use to manage your investment portfolio. We then monitor your portfolio, make necessary changes and report to you on a regular basis.

Step 4: Complete your financial action plans

Here we work through the priorities identified in your personal financial plan, on a schedule suitable to you.

Once we're finished, we go back to Step 1, review your situation and goals and start the process over again. We also do a "plan vs. actual" to see how you are progressing relative to your last plan. We recommend doing this every year and at least once every two years – or whenever your personal circumstances change significantly.

Planning helps avoid rushed, ill-considered and emotional decisions. Anything that's important to you deserves to be well-planned. This includes your finances! ■



Sylvia Ellis is the Senior Estate Planning Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Sylvia provides support to the team in projecting and planning client financial affairs.

Why we use rules-based strategies to invest in equities

By Michael Chu, Associate Investment Advisor

We believe that investors who disengage their emotions when they make their investment decisions have a much better chance of building wealth with returns that outperform both inflation and the market.

Contrary to what many investors believe, the stock market has provided very good returns. Over the past 100 years, the U.S. stock market produced returns averaging 11.1 percent per year compounded. That was more than 8% above inflation. However, many investors do not achieve these returns. One of the main reasons, we believe, is that investors often have a subjective approach to investing. A subjective approach is susceptible to emotions and biases, and this can result in lower returns over the long term.

Objective factors lead to better than average returns

Numerous studies have found that simple objective factors lead to better than average returns.

There are two main types of objective factors: value and momentum. Stocks with good value are those which have low prices compared to underlying company fundamentals. Good value can be indicated by factors such as:

- low price-to-earnings
- low price-to-cash flow
- low price-to-sales
- low price-to-book value, or
- low price-to-dividend

Stocks with good momentum are those that are doing better than expected. For example, companies where:

- analysts are raising their earnings estimates
- the company is reporting better than expected earnings, or
- the company's stock price is moving up much faster than average, indicating higher than expected results.

Research has shown that stocks with good value or momentum produced returns averaging three to five percent above the market. Stocks with poor value or momentum produced returns three to five percent below the market.

Avoiding traps and achieving better returns

The Stan Clark Financial Team uses rules-based strategies to identify and invest in stocks with good value and good momentum characteristics. Stocks are also replaced according to specific rules.

The important thing is to buy and sell according to the rules, and not according to traps like "gut feelings," "hot tips" and what most other investors are saying or doing. We believe a disciplined approach is the most reliable way of creating and managing a portfolio that can help you achieve your objectives.

In short, we believe rules-based strategies are an effective investment tool for investing in equities. However, investing in stocks using these strategies is not for everybody. You have to be comfortable with this philosophy and able to tolerate a certain amount of volatility. If you would like to learn more about the research behind this approach or to find out if it might be suitable for you, please contact us. We would be happy to have the opportunity to discuss it with you. ■

Michael Chu is an Associate Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Michael is a specialist in investment research and information technology.

Tax-Free Savings Account (TFSA): What you need to know

By Elaine Loo & Heather Guzak - Associate Investment Advisors

The Tax-Free Savings Account was introduced by the federal government in the 2008 budget. Canadian residents who are 19 years of age (in BC) and older can make a non tax-deductible contribution each year into a TFSA without paying tax on income and gains earned within the account, even when you make a withdrawal.

This means you can save faster for all of your financial goals. It can hold any qualified securities, such as stocks, bonds and exchanged traded funds.

Contributions can be made in cash or securities in kind. Each year, your TFSA contribution room is made up of;

- your annual TFSA dollar limit, plus
- any unused TFSA contribution room in the previous year, plus
- any withdrawals made from the TFSA in the previous year (with the exception of any funds withdrawn because of an over-contribution).

Like your RRSP, the earlier you contribute, the more you will benefit. So, if you haven't opened a TFSA yet, or if you have one but have not contributed into it yet, you should do so soon. ■

Elaine Loo and Heather Guzak are Associate Investment Advisors for the Stan Clark Financial Team at CIBC Wood Gundy.

They are responsible for the day-to-day monitoring and maintenance of client accounts and investment portfolios.

Registered Retirement Savings Plan (RRSP): A few things to keep in mind

By Jocelyn Johansson - Associate Investment Advisor

There are many benefits to saving for your retirement in a Registered Retirement Savings Plan.

For instance, your contributions are tax-deductible and your savings grow tax-free while in your plan. Therefore, the earlier you contribute the more you will benefit. The deadline for contributions is 60 days after year end; avoid the rush and contribute early.

Be sure to double check your contribution limits and the amounts you have contributed, to ensure you do not over-contribute. All RRSP holders 18 years of age or older have a lifetime over-contribution allowance of $2,000. Beyond that, a penalty of one percent per month is payable on the excess amount. This information can be found on your most recent Notice of Assessment from the CRA.

If you have a spouse who earns a lower income and/or who is younger, you could benefit from a spousal RRSP. With a spousal RRSP, the contributor can deduct the contributions, while the money grows tax free under the spouse's name. You can contribute both to your own RRSP and a spousal RRSP, as long as the combined contribution does not exceed your own maximum allowable contribution. By building up the spousal RRSP rather than your own, you can delay the withdrawal of your assets until your younger spouse turns 71 years of age and converts the spousal RRSP to a RRIF.

If you make a withdrawal from a spousal RRSP, it will be taxed as income to your spouse, who is presumably in a lower tax bracket, and not you (as the original contributor). However, a withdrawal cannot be made within three years of the spousal contribution, or the income will be attributed back to the contributor.

Designating a beneficiary for your RRSP is an important part of estate planning. It ensures your RRSP will not be included in your estate; subsequently avoiding probate taxes. By avoiding probate, the process for transferring your RRSP assets to your beneficiaries is simplified, allowing for a quicker distribution. ■

Jocelyn Johansson is an Associate Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. She is responsible for the day-to-day monitoring and maintenance of client accounts and investment portfolios.

SCFT Trivia

Answer all four questions correctly to be eligible for a prize*.

Hint: You can find the answers inside this newsletter.

1. How many days after the beginning of the year is the RRSP contribution deadline?
   A) 30 C) 90
   B) 60 D) 120

2. How far above inflation have stock market returns been over the past 100 years?
   A) 12% B) 3% C) 8%

3. What type of securities can you hold in your TFSA?
   A) Stocks only
   B) Bonds only
   C) ETFs only
   D) Any qualified securities

4. Who won the 2002 Nobel Prize in Economics?

*NOTE: As this is a copy of our inaugural issue, the contest has been completed and the prizes awarded. You can still have fun looking for the answers, and don't forget to take part in a new contest when you receive your next issue of *Perspectives*.*

Ask the Stan Clark Financial Team...

***Q:* What do you consider when planning my Equity Target?**

A: We set an Equity Target for you based on your specific time horizon, your current financial situation, and how comfortable you are with market fluctuations. For your time horizon, we believe that any money you may need in the short term (3 to 5 years) should be held in fixed income investments, while any money you need for the long term (10+ years) is in the stock market. We calculate your Equity Target by matching each of your planned withdrawals with the best mix of fixed income and equities for that time horizon. We then combine each year's mix to calculate an overall Equity Target, which we review with you regularly. Once we set the target, we stick to it, rebalancing your portfolio whenever it deviates more than 5%. We also normally change your target whenever there is a material change in your financial situation.

***Q:* Why does my portfolio have so few companies in some industries?**

A: Our stock picks are determined by our disciplined strategies and we always try to choose the top ranked stocks. We have 16 different stock strategies and that usually gives us a very good selection of companies and industries to choose from. But sometimes it happens that an industry has no top ranked stocks, and the only way to get exposure to it would be to buy low ranked stocks. We don't like to do that, because it reduces your expected returns. We call that di-worse-ification, not diversification, and mutual funds and many money managers are guilty of doing this. We set limits to ensure clients are not too heavily weighted in any one particular industry, but don't buy any stocks unless they are very well rated. This approach allows us to reduce risk without reducing the expected returns.

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Where planning, investing and behavioral finance meet

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