THE
Guardian

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DISPELLING SOME MARKET MYTHS

It has been a dismal and disheartening slide in global equity markets that actually started in the late summer/early fall of 2007. September and October 2008 were particularly savage, and a rally in December of 2008 and into the early part of 2009 was snuffed out by another rapid slide.

At time of writing however, we have seen markets jump back up somewhat. Since the Dow Jones Industrial hit a low on March 9 of this year, the index was up by more than 20% as at April 15th. Other North American indexes experienced similar results.

While encouraging news, it is felt by many that the current rally is unsustainable in the near term, as the global economy remains weak and corporate earnings have yet to recover. The aggressive fiscal stimulus is expected to take some time to fully kick into gear, and the American consumer, a key driver to global economic recovery, still faces significant headwinds in the form of onerous debt loads and a shrinking job market.

Taking this all into account, even the most bearish observers agree that eventually markets will recover, though the timing is almost impossible to predict. Meanwhile, in this somewhat negative environment, we find ourselves inundated with dire predictions from so called “media gurus” and self-appointed experts. Many of the negative assertions that receive the highest profile are based on somewhat flawed data. We review three of these common assertions heard in the current environment, and point out the flaw in the arguments.

1) Investors made no money from the mid 1960's to the early 1980's.

A Newsweek article published toward the end of 2008 asserted that the stock market as measured by the Dow Jones Industrial Average was no higher in 1982 than in 1965. First, despite its prominence, the Dow Jones Index is only vaguely representative of the stock market as a whole. Because it only contains 30 stocks and is price-weighted rather than market-weighted (in other words a stock trading at $50 (US) has 5 times the weight of a stock trading at $10), it doesn't truly represent how the overall market performs. In the 1970's in particular, the Dow Jones was laden with large household names referred to as "the nifty 50" that were chronic underperformers when compared to the market as a whole.

Second, and perhaps more important, looking at the overall price performance of any index ignores dividends, something that historically has accounted for 40% of returns. A closer look at the results from 1965 to 1982, using the more broadly based Standard and Poor's 500 (S&P 500) stock composite index shows that the capital appreciation (ie return excluding dividends) from December 31, 1965 to December 31 1981 was 33%. However, when factoring in dividends, the total return came to 152%.

The result is an annual return of 6%. While this is less than the historical long term return of 10% on large US Stocks, it is a very different position than being down over this period.

2) Stocks took 25 years to recover to 1929 levels.

A second common myth relates to how long it took for stocks to recover after the Great Crash of 1929.

If we look just at the price index, it is true that referring to year end price levels, it took until 1952 to match the market high achieved by the S&P 500 index at the end of 1928, giving the appearance of a disastrous experience for investors who held on after the Great Crash.

However, we see a different story if we include dividends. Once factored in, the annual average yield is 6%, or 4% adjusted for inflation.

3) Stocks lose money after inflation

An article in the November 8, 2008 Globe and Mail featured an interview with the head Wealth Management Strategist for a major US bank. He stated that in real terms the Dow Jones Industrial average fell 47% from 1960 to 1980. The assertion was that markets can be horrible places to be for long periods of time.

If we take a look at the year-end number for the Dow, both before and after inflation, we see that in 1959 it was 679, and in 1979 was 899, which adjusted for inflation equates to a level of just 344.

Again, it's tough to disagree with the argument that this 20 year period was disastrous for investors in real terms, until we look at a broader based measure of stock market performance and include dividends.

Again, referring to the more broadly based S&P 500, it gained 80% over the same period, but adjusted for inflation, equated to a loss of 31%. However, we see that once again, including dividends changes the picture dramatically. Including dividends, the total return was 275%, or an inflation adjusted gain of 43%.

On a total return basis, this works out to an annual real return in this 20 year period of only 2%. This lower than average long term return was due to a combination of lower stock market returns and much higher inflation than the historical norms. Accordingly, this period did indeed substantially underperform the historical real return. Still, underperforming with a real return of 2% is a very different story than losing almost half your money.

None of this is intended to say that stocks will always be a safe or pleasant haven for investors. And despite the overwhelming positive returns that long term investors in North American stocks have seen across virtually every time frame, there will always be those who state "it is different this time".

Just remember though, the only guide we have is what happed in the past. And as we noted at the beginning of this article, all market downturns eventually pass, and there is no reason to suggest this will be any different.

REGISTERED RETIREMENT INCOME FUND (RRIF)
STATUTORY MINIMUM MONTHLY INCOMES BASED ON $100,000
COMMENCING ONE MONTH FROM ISSUE

Best Current Rate: 3.5%

Age	1st Year	TOTAL PAYMENTS TO AGE 100
55	$239.00	$197,770.00
60	278.00	178,494.00
65	334.00	161,471.00
71	616.00	141,705.00

A R.R.I.F. can also be structured to pay a level income for a shorter period. Based on current interest rates, $100,000 will produce the following monthly income.

For 5 years: $1818.00
For 10 years: $1022.00
For 15 years: $756.00

MONTHLY ANNUITY INCOMES COMMENCING
ONE MONTH FROM ISSUE BASED ON $100,000

Age	LIFE (Payments cease at death)		LIFE 10 Year Guarantee		JOINT LIFE 10 Year Guarantee
	MALE	FEMALE	MALE	FEMALE	MALE & FEMALE
55	$569.65	$535.79	$562.06	$531.55	$501.91
60	631.90	588.76	621.63	583.14	540.50
65	709.73	634.34	677.65	632.14	580.00
71	832.71	732.39	757.21	694.81	636.02

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