Manulife Investments

WealthStyles®



RRSP tips
Helpful information you should know

When it comes to investing for your Retirement, Registered Retirement Savings Plans (RRSPs) are often the best place to start. The combined benefits of reducing taxable income in the present and the expectation of tax-sheltered compound investment returns over the long term can provide a compelling reason for investors to make the most of these savings plans.

There are a number of tactics you can use that will help you realize the full wealth-building potential that these plans can provide. What follows are a few tips on how to make the most of every dollar you invest.

1. START AS EARLY AS YOU CAN

You've likely seen numbers like this before, but they are worth repeating: to take full advantage of the taxable benefits associated with an RRSP, the sooner you start investing the better. As Figure 1 illustrates, the longer your savings have to compound tax free, the more you can benefit from the tax-sheltered investment returns that RRSPs provide.

As a means of comparison, the growth of the same investment held within a non-registered account is illustrated to show how tax deferral can work to your advantage over time. The RRSP investor starts at age 25, contributes $1,000 per year, receives an average eight per cent annual rate of return on the investment, and is subject to a tax rate of 40 per cent. The final contribution is made at age 71.

The non-registered investor starts at age 25, also wants to contribute $1,000 but has to pay tax on this amount first, leaving only $600 to invest per year, receives the same eight per cent return on investment, and is subject to a tax rate of 40 per cent. Again, the final contribution is made at age 71.

The end result is that by taking advantage of the tax-deferred benefits of a registered account, the value of the RRSP increased to $489,132 at age 71. This compares to the non-registered account whose value is a mere $248,152.


The difference: $240,980*

Growth of a registered vs. non-registered investment

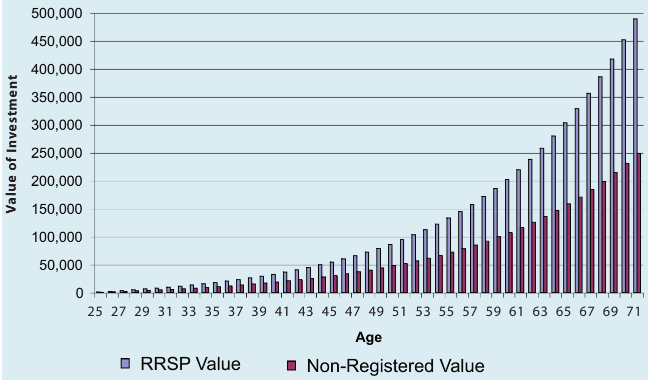

Figure 1

*This example assumes that the taxable portion of the fund return is 25 per cent, the tax rate on investment earnings is 25 per cent and the annual income tax payable by the nonregistered investor must be paid through withdrawals from the fund. For illustration purposes only.

2. MAXIMIZE YOUR CONTRIBUTIONS

Maximize your contributions each year to make the most of tax-deferred compound investment returns. Consider as RRSP loan if you don't have the cash, and then pay it down when you receive your refund each year.

If you have unused contribution room available, consider borrowing enough money to help you catch up. Many financial institutions offer RRSP loans at very attractive rates[1].

3. REINVEST YOUR REFUND

To get more retirement benefits from your RRSP, you can reinvest all of your refund back into your RRSP (if you have contribution room available). For example, if your marginal tax rate is 50 per cent and you invest $1,000, you would generate a $500 refund. If you spend the refund, your true after-tax commitment to your retirement goal is only $500. But if you invest that tax refund, you increase your RRSP by 50 per cent. Your RRSP investment now becomes $1,500, which represents a significant increase to your overall financial plan.

4. PAY YOURSELF FIRST

Consider contributing to your retirement through convenient, automatic withdrawals from your chequing account. If you are a mutual fund investor, a pre-authorized contribution (PAC) plan will allow to contribute as little as $50 either weekly, bi-weekly, monthly, quarterly or semiannually into a mutual fund that's right for you. A PAC plan lets you take advantage of dollar-cost-averaging, a strategy that can help lower investment risk. Dollar-cost-averaging can lower investment risk since you will be automatically buying fewer units when prices are high and more units when prices are low.



5. CONSOLIDATE YOUR INVESTMENTS

If you are the type of investor who doesn't want to spend a great deal of time managing multiple investment accounts, then you should consider consolidating your holdings with one advisor. By consolidating all of your RRSP holdings into a single account, you can still invest in many different types of investments and it will make it easier to adjust your investment strategy as your financial situation changes over the years. In addition, you won't have to pay extra RRSP administration fees that can cost as much as $100 per year for each account.

6. SEEK PROFESSIONAL ADVICE

To make the most of your retirement savings, it's important that you consider seeking professional advice. Research shows that investors who seek professional help tend to do better over time. Financial Research Corp., a financial services research and consulting firm based in the United States, studied U.S. mutual fund investor habits from 1990 through to the peak of the equity markets in March 2000. Its research provides strong evidence that suggests professional advice is key to obtaining better investment returns.

The most common errors made by individual investors include trading too often and bad timing. During the 10 year period of the study, investors without advisors realized a lower return on their mutual fund investments than the actual mutual fund returns. The study revealed that investors had consistently higher redemption rates and shorter holding periods than investors who used a financial advisor.

In 1996, the average investor had held a long-term mutual fund for 5.5 years and the redemption rate was 17.4 per cent. Four years later, at the height of the boom market, the typical investor held the same long-term mutual fund investment for an average of only 2.9 years and the redemption rate was up to 32.1 per cent.

In addition, individual investors compounded the negative effect of trading too often by making poor choices in terms of timing. The study found that many investors purchase funds based on past performance, usually when the funds are at or near their peak, which results in the investors not participating in the greatest gains.

If you are like most Canadians who hold the bulk of their retirement savings in their RRSP, seeking the advice of a professional advisor can help you avoid making these costly mistakes. Not only will your advisor help you build a well-diversified investment portfolio that can help reduce risk, they can continue to counsel you on the best ways to respond to changes in the financial markets over time.

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RRSP FACTS

- Average net worth for adult Canadians: $142,900
- Percentage of Canadian families with RRSP savings: 58
- Average value: $76,600
- Canadian private pension assets held in employer pension plans: $1,632 billion (2005)
- Number of Canadians contributing to an RRSP: 6.1 million for the 2005 tax year
- Amount contributed to RRSPs in 2005: $30.6 billion

Source: Statistics Canada, 2005 and 2006.

[1] Borrowing to invest may be appropriate only for investors with higher risk tolerance. You should be fully aware of the risks and benefits associated with investment loans since losses as well as gains may be magnified. The value of your investment will vary and is not guaranteed, however, you must meet your loan and income tax obligations and repay your loan in full. Read the terms of your loan agreement and the investment details for important information and discuss with your financial advisor before deciding whether to borrow to invest.

Commissions, trailing commissions, management fee and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

Compliments of:

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