

THE BOTTOM LINE

SEPTEMBER 30, 2008

"This thaw -- took a while to thaw, it's going to take a while to unthaw." --George W. Bush, on liquidity in the markets, Alexandria, La., Oct. 20, 2008

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www.manulifesecurities.ca**What is Going on Here?**

I'm sitting at the Cactus Club watching the Canucks game, chatting with my buddy about the stock market mess and the man beside me leans over and says " I couldn't help over hear your conversation and I have to say this is much worse than divorce; I've lost 50% of my assets and I still have my wife".

In the emotional cycle of stock market investing it is safe to say that the eavesdropper beside me has reached the capitulation stage. Without question the intestinal fortitude of every investor is being tested to the very limits of our collective resolve. With stock markets in a seemingly endless freefall as a result of the sub-prime mortgage crisis and subsequent financial market collapse, we are witnessing an honest to goodness, world wide, panic induced stock market selloff.

The whys and where-to-fores as to how we got into this mess are very well documented and need not be regurgitated on these pages, but suffice to say there is certainly sufficient blame to go around. Regulators, greedy bankers, rating agencies, lenders, speculators, borrowers, central bankers and even the media all had a hand in creating a world wide housing bubble not seen in history.

Further exacerbating the collapse of the financial sector has been the bursting of the commodities bubble which has seen oil as an example fall from its high of \$150 ish in July to \$80 ish at the end of September. All manner of commodities are in a freefall from their respective highs set earlier this year, to levels not seen for some 18 months, or more in some cases. With the resource sector in turmoil our dollar began a fall in late September that, as I pen this article, has seen the loon drop below 0.80 US\$ for the first time since May 2005!

Is the world coming to an end? The evidence does, in fact, suggest otherwise, however with each passing day it is more difficult to believe that. Things are indeed dire and while we are going to need a wee bit of luck to navigate through this quagmire, we believe that the decisive action taken by the world's central banks will ultimately work to get the credit markets moving again. Once the credit markets ease up a bit we should see a little less panic, fewer forced asset sales, and some rational thought return to markets general.

Warren Buffet recently wrote a letter to the editor of the New York Times (they of the great crossword!) and it is always fitting to see what he has to say about the state of the stock markets. His comments follow;

"The financial world is a mess, both in the United States and abroad. Its problems, moreover, have been leaking into the general economy, and the leaks are now turning into a gusher. In the near term, unemployment will rise, business activity will falter and headlines will continue to be scary.

So ... I've been buying American stocks

What is Going on Here? (Continued)

Why?

A simple rule dictates my buying: Be fearful when others are greedy, and be greedy when others are fearful. And most certainly, fear is now widespread, gripping even seasoned investors. To be sure, investors are right to be wary of highly leveraged entities or businesses in weak competitive positions. But fears regarding the long-term prosperity of the nation's many sound companies make no sense. These businesses will indeed suffer earnings hiccups, as they always have. But most major companies will be setting new profit records 5, 10 and 20 years from now.

Let me be clear on one point: I can't predict the short-term movements of the stock market. I haven't the faintest idea as to whether stocks will be higher or lower a month – or a year – from now. What is likely, however, is that the market will move higher, perhaps substantially so, well before either sentiment or the economy turns up. So if you wait for the robins, spring will be over.

A little history here: During the Depression, the Dow hit its low, 41, on July 8, 1932. Economic conditions, though, kept deteriorating until Franklin D. Roosevelt took office in March 1933. By that time, the market had already advanced 30 percent. Or think back to the early days of World War II, when things were going badly for the United States in Europe and the Pacific. The market hit bottom in April 1942, well before Allied fortunes turned. Again, in the early 1980s, the time to buy stocks was when inflation raged and the economy was in the tank. In short, bad news is an investor's best friend. It lets you buy a slice of America's future at a marked-down price.

Over the long term, the stock market news will be good. In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497.

You might think it would have been impossible for an investor to lose money during a century marked by such an extraordinary gain. But some investors did. The hapless ones bought stocks only when they felt comfort in doing so and then proceeded to sell when the headlines made them queasy.

Today people who hold cash equivalents feel comfortable. They shouldn't. They have opted for a terrible long-term asset, one that pays virtually nothing and is certain to depreciate in value. Indeed, the policies that government will follow in its efforts to alleviate the current crisis will probably prove inflationary and therefore accelerate declines in the real value of cash accounts."

Equities will almost certainly outperform cash over the next decade, probably by a substantial degree. Those investors who cling now to cash are betting they can efficiently time their move away from it later. In waiting for the comfort of good news, they are ignoring Wayne Gretzky's advice: "I skate to where the puck is going to be, not to where it has been."

"I don't like to opine on the stock market, and again I emphasize that I have no idea what the market will do in the short term. Nevertheless, I'll follow the lead of a restaurant that opened in an empty bank building and then advertised: "Put your mouth where your money was." Today my money and my mouth both say equities.".....Warren E. Buffett is the chief executive of Berkshire Hathaway, a diversified holding company.

While he talks about allocating funds to the stock market, to the extent one has exposure to stocks, Buffet's logic implies a holding pattern while we work our way through this rough patch. The Oracle of Omaha recently made two high profile investments to back up his remarks; \$5 Billion into Goldman Sachs and a further \$3 billion into G.E. That is most definitely putting your money where you mouth is!!

BOX SCORES

GIC Interest Rates**2008 (%)

	July	Aug	Sept
1YR	2.13	2.13	2.13
3YR	2.73	2.73	2.73
5YR	3.08	3.08	3.08

Annualized Rates of Return to September 30, 2008 (%) ***

All Cdn \$	1YR	3YR	5YR
TSX	-14.4	4.7	12.0
S&P 500	-17.0	-2.8	0.2
TSX DEX	4.6	3.4	4.8
*EAFE	-25.2	-1.3	5.0

*Europe, Australia & Far East Index

**source: Bank of Canada web site.

***Morningstar

Tax Free Savings Account

It may seem odd timing to talk about a new investment account but the new Tax-Free Savings Account (TFSA) is a very flexible planning and savings tool and will fit into most anyone's portfolio very nicely. The TFSA has become law and is scheduled to take effect in 2009. Here's a refresher on the basic features of the TFSA ;

- Will allow non-deductible contributions of \$5,000 per year for Canadian residents age 18 and older
- Unused contribution room will accumulate and can be used in subsequent years
- Investment income (including interest, dividends and capital gains) will grow tax-free
- Withdrawals (including original contributions and investment income) will be tax-free
- Withdrawals are allowed at any time, for any purpose and will create new contribution room for the following year – this is in addition to the \$5,000 granted each year - unlike RRSP withdrawals that result in the permanent loss of contribution room, TFSA withdrawals will restore contribution room by the amount of the withdrawal
- TFSAs can be used as collateral for a loan
- Interest on money borrowed for TFSA use will not be tax-deductible
- Investments eligible for RRSPs will generally be eligible for TFSAs – this includes stocks, bonds and mutual funds.

There are several creative ways in which to take advantage of a TFSA and following is one clever way to income split:

Dwight and Debra, ages 45 and 43, have been married for 15 years. Dwight is an electrician and Debra volunteers as a counselor in her community.

Because Dwight is the primary income-earner (Debra earns some investment income from a small inheritance), he is taxed on the majority of the family's employment and investment income. For some time he has been seeking ways to split this taxable income with Debra, particularly because she is in a lower tax bracket. Spousal RRSPs have been used for long-term investments, but their nonregistered assets remain a concern.

The TFSA is a solution. Even though the family's income is earned primarily by Dwight, both Dwight and Debra will receive \$5,000 of TFSA contribution room each year. Unlike RRSPs, TFSA room is not based on income earned. Also, because spousal attribution rules (tax rules that prevent income splitting between spouses) do not apply to TFSA contributions, Dwight can contribute \$5,000 to his TFSA and give Debra \$5,000 to fund her TFSA allowing for tax-free growth on \$10,000 each year! Cool, eh?

Source: Mackenzie Financial

GIC's

In these turbulent times some people simply need the comfort of a guaranteed interest rate for some of their money. Did you know that we have access to some of Canada's leading financial institution's GIC products including Van City Credit Union. Call us for more details.

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