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Practical Wealth Creation Ideas

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Benchmarks: MEASURING FUND PERFORMANCE

With the exception of the TSE in 1998, the excellent results posted by North American markets over the past few years have accustomed investors to double digit returns. These

spectacular results, however, are an anomaly in the broader history of investing. Therefore, it is important to take a look at your funds with a sober eye to performance. Benchmarks can help here.

An index gives you an indication of how the overall stock market is doing. Typically, a broad-based Canadian equity mutual fund can be compared to the TSE 300, a large-cap fund to the TSE 35 or TSE 60, and a small to mid-cap fund to the TSE 200. For international stocks there are hosts of indices to choose from, but make sure you are using the one most similar to the holdings of your fund. Using the wrong one is both irrelevant and misleading.

While markets may have posted spectacular returns in the short-term, note that in the past 70 years, the Canadian market has typically averaged annual returns (including dividends) of approximately 10%.

Canadian-Based FOREIGN MUTUAL FUNDS

There's no denying that international markets often outperform our own, yet Canadians are restricted to holding a maximum of 20% foreign content in their RRSPs. To the rescue—newly developed RRSP-eligible foreign mutual funds that allow investors to hold as much foreign content as they wish.

RRSP-eligible foreign funds are clones of an underlying international mutual fund. They purchase forward contracts related to the value of the underlying fund. This allows the performance of both to track closely. In effect, these funds allow investors to have investments in international securities, but since the forward contracts are backed by Canadian short-term securities, foreign restrictions are not a consideration.

Since foreign equity markets, especially in the US, have historically outpaced the TSE, these new funds have the potential to boost returns and enhance diversification. Of course, RRSP-eligible foreign funds charge a slightly higher fee for this innovation. However, with the Canadian market continuing to lag behind many international neighbors, the extra fees may well be worth the potential for enhanced returns.