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Investment Vehicles

Listed below in order of safety and liquidity are a number of investment options. Mutual funds are described last. They are as liquid as Canada Savings Bonds (redeemable daily) but they are only as safe as the underlying investment. For instance, a Money Market Fund invests in Treasury Bills so it is very "safe" (does not fluctuate in value). A Specialty Fund may invest in Gold and Gold Mining Companies; therefore it is not "safe" (it does fluctuate greatly in value).

Deposit Accounts
You should keep an amount available for your monthly expenses in your chequing and/or savings account. The bank account should pay a high rate of interest and compound that interest as many times a year as possible. There are bank accounts available with no service charges as long as you maintain a minimum balance.

Canada Savings Bonds
Canada Savings Bonds are issued by the Government of Canada and sold through bankers and investment dealers in November of each year. They are very popular because they can be redeemed at any time with accrued interest and they offer competitive rates with term deposits and guaranteed investment certificates that are not as readily redeemable.

The interest rate is established each year for all outstanding Canada Savings Bonds. The interest rate on outstanding bonds has been increased a number of times in the past to prevent the widespread cashing in of the bonds. The term of the bonds vary from 7 to 12 years depending on the issue. Compound interest bonds pay interest either at maturity or redemption. Regular interest bonds pay interest each November 1. Redemption can be made at any bank in Canada with interest paid to the beginning of the month. The bonds must be held 90 days to earn any interest. Unlike Government of Canada Bonds, Canada Savings Bonds are redeemable, non-transferable and non-assignable, so no secondary market exists.

Treasury Bills
Treasury bills (T-Bills) are short-term money instruments auctioned by the Bank of Canada each Tuesday. Instead of an interest payment, T-Bills are sold at a discount and mature at par value. The investment return is the difference between the purchase price and par value at maturity. T-Bills are offered with various terms up to one year. T-Bills can be sold before maturity in secondary markets with the proceeds depending on interest rates.

Term Deposits
The chartered banks and trust, savings and loan companies accept deposits for a specific period of time at a fixed interest rate. Deposits for less than a year are

generally called “short-term deposits”. Those for one to five years are generally called “guaranteed investment certificates” (GICs). Those for amounts of $100,000 or more are known as “wholesale” term deposits.

The interest rate is established based on market conditions and is generally higher for longer-term deposits. The term of the deposit may be as short as 30 days or as long as 15 or 25 years. The minimum deposit is generally $500 for GICs, $5,000 for short-term deposits and $100,000 for wholesale term deposits. Keep in mind that Canada Depositors Insurance Corporation will only insure deposits up to $100,000 with terms of 5 years or less. Some term deposits may allow early redemption with a penalty. Some will allow transfer to another person, which has created a small secondary market through investment brokers.

Government of Canada Bonds
Government of Canada Bonds are securities issued by the Government of Canada in the form of bonds that generally mature from 5 to 25 years after date of issue. A large secondary market exists for these bonds and they trade based upon maturity dates and interest rates.

The interest rate is set at the issue date and interest is paid semi-annually. When sold in the secondary market, the purchaser must pay for the accrued interest since the last payment date. When sold in the secondary market, they will be sold at discount or premium to face value. This takes into account changes in interest rates since the bond was issued.

Mutual Funds
A mutual fund is a large diversified portfolio of securities administered through a limited company or trust and made possible by pooling the money of thousands of investors. A mutual fund is professionally managed by individuals or committees who have the time, training and temperament necessary for successful investing. This relieves you of the individual investment decisions; all you have to decide is which mutual fund or funds to choose.

Deciding which mutual fund to choose is not easy. There are over 5000 to choose from in Canada. Some are highly speculative, others are very conservative. Some invest in debt securities like treasury bills, bonds or mortgages. Others invest in equity securities like stocks, gold or real estate. Some invest in a combination of these securities.

Most mutual funds in Canada are open-end. This means that new units are created as investors demand them and old units are redeemed as investors sell them. Consequently, the total asset value of an open-end fund is constantly changing. You invest in the mutual fund by buying new units or shares of the mutual fund. The unit value, called the net asset value or NAV, is usually calculated at the end of every business day by taking the value of the assets, subtracting the liabilities and dividing by the number of units outstanding. Some mutual funds calculate the NAV only weekly or monthly.

When buying shares of a mutual fund, commissions and fees vary. A number of funds charge a commission of up to 6%. This is a “front end load” and is deducted from the amount you are investing. The balance is then used to buy shares of the mutual fund. Some funds charge a redemption fee on withdrawals from the fund. This back end load decreases the longer you have your money invested in that mutual fund. Some mutual funds have neither a front-end load nor a back end load. These funds are called no load funds and are generally provided by banks, trust companies and some investment managers directly to investors.

Discount Brokers are now selling “front end load” funds for zero commission (no-load). If you buy a Deferred Sales Charge fund from them (back end load), they will rebate to you a portion of the commission they receive.

Regardless of commissions that may be paid, all mutual funds pay annual operating expenses, administration fees to fund managers, and brokerage fees for sales and acquisitions of the securities. These expenses are paid from the revenue of the fund and influence the return to investors.

To choose a mutual fund, you should review the different mutual funds available by reading a financial newspaper. The national financial newspapers publish monthly tables comparing most of the different funds available in Canada. Note and compare management fees, operating costs, commissions and company history. Compare each fund’s performance over one year, three years, five years and ten years. A fund showing a consistent rate of return through market upswings and downturns generally indicates sound management.

Before buying a mutual fund, you must receive a prospectus (or simplified prospectus), an annual information return and financial statement of the fund. If you do not, then do not invest in the fund until you receive it.