

DIRECT INVESTOR



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Maintain a long-term perspective during times of volatility

Whenever the investment ride gets bumpy, as it was through parts of 2011, it's important to step back and keep volatility in perspective. Regardless of what markets are doing from day to day, the long-term trend has historically always been upward.

And in any kind of market — rising, falling or staying steady — it is important to keep in mind the principles of sound investing. A well-structured, diversified portfolio that's based on a long-term strategy can often be the foundation of investment success.

Focusing on the long term

For long-term performance, consider a mix of assets from the three main asset classes — cash or cash equivalents, fixed income, and equities — for your portfolio. Each can bring important qualities to your portfolio.

- **For security:** cash, GICs, money market funds, savings accounts. These investments provide a stable base for your portfolio as well as liquidity so you can get your money out on short notice. But the low returns generated by interest earnings may not outpace inflation over the long term.
- **For income:** bonds, bond funds. Fixed-income investments such as bonds and bond funds generate cash flow and are less volatile than growth-oriented investments. However, they can still fluctuate in value, decrease in value when interest rates rise and increase when rates go down.

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Key Dates

January 1st – New TFSA Contribution Room available for 2012

February 29th – RRSP Contribution Deadline

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- **For growth:** equities, equity funds. This asset class is the most volatile over the short term but has historically provided better performance than guaranteed and fixed-income assets and outpaced inflation by the widest margin.

The “Do I have the right asset mix?” calculator available on the *Calculators* page under the **Quotes & Research** tab within the online investing site can help you determine the target asset mix that’s right for you. And when you know you have the right mix of investments, you may be less tempted to sell — and lock in losses — when one asset class or investment experiences a temporary downturn.

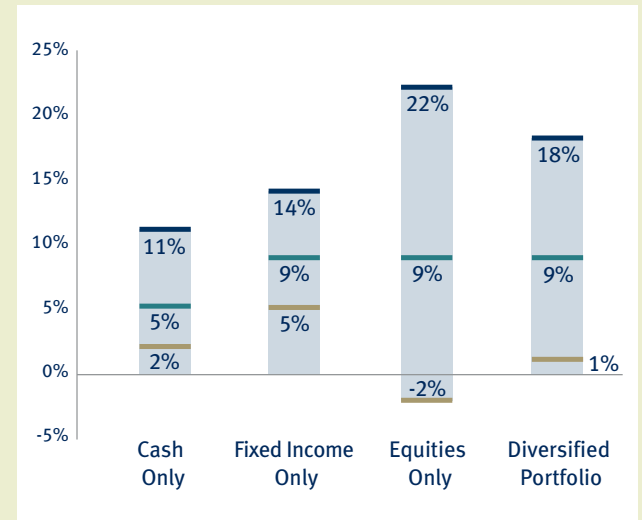
Do you know your investor profile and associated target asset mix, but you’re not sure if your actual holdings reflect that target? Try the Analyze & Rebalance tool found under the My Portfolios tab the next time you log into the online investing site to better understand how close or far off you are from your target allocation.

Remember inflation

Finally, don’t forget about the effects of inflation. Over the long term, secure guaranteed investments that pay interest and protect your principal may not provide sufficient returns to keep you ahead of increases in the cost of living. For example, if your GICs are earning 2% and inflation is running at 2%, you’re just breaking even.

While it’s important to have an element of safety in your portfolio, too high a concentration could hinder your ability to reach your long-term growth objectives.

The Benefits Of A Diversified Portfolio



■ Minimum Return ■ Average Return ■ Maximum Return

Source: RBC Global Asset Management

Diversified Portfolio represented by 5% Cash, 40% Fixed Income and 55% Equities; Cash – DEX 30-day T-Bill Index; Fixed Income – DEX Universe Bond Total Return Index; Equities – S&P/TSX Composite Total Return Index: five-year rolling returns for a 20-year period ended June 30, 2011.

Past performance is not a guarantee of future results



The versatile TFSA – a great way to save at every stage of your life

Although it's been around for several years now, the Tax-Free Savings Account (TFSA) is still not well understood by many Canadian investors. Some people have not yet contributed and may be carrying significant allowable contribution room, accumulated since TFSAs were introduced in 2009. Others are unaware that their TFSA can hold mutual funds, exchange-traded funds (ETFs), stocks, bonds and more in addition to cash and cash-type investments.

The truth is that there are many advantages to using a TFSA to build wealth over the long term — as well as for shorter-term goals — particularly when used in conjunction with a Registered Retirement Savings Plan (RRSP).

Here are four scenarios that illustrate some examples for using a TFSA that could benefit you at different life stages.

1 Building a future together

Sandra and Rob are newlyweds in their late 20s who want to save money for their future goals.

Their goals at this early life stage tend to be short- to medium-term in nature and include accelerating their student debt repayments, saving for a car and putting money aside for a southern vacation.

But they want to start saving for their longer-term goals as well, including retirement. By starting RRSPs and TFSAs when they're young, Sandra and Rob know that they'll benefit from their long-term and short-term investments increasing in value in tax efficient accounts.

To help them make progress towards both their short-term and long-term goals, Sandra and Rob set up automatic contributions for both their TFSAs and their RRSPs.

Sandra and Rob find their TFSA savings are ideal for their short- to medium-term goals. They have chosen to invest their savings conservatively in liquid cash investments, and all of their interest income is earned tax free — and remains free of tax even when they withdraw it. Their TFSAs also provide the flexibility to withdraw at any time — so they can pay for the vacation and put money down on a car when the timing is right. And any amount that Sandra and Rob withdraw from their TFSAs is added back into their contribution room for the following year, so they will still be able to take advantage of their full TFSA limit in the future.

In the meantime, Sandra and Rob are starting to save for their retirement through regular RRSP contributions. Their contributions generate small tax refunds each year, which they can choose to put towards their short-term goals.

Pre-authorized contribution plans can be set up by completing the form located under the Forms section of the My Home tab of the online investing site.

2 Buying a home

Nancy, a 30-year-old legal assistant, is ready to buy her first condo. She is willing to wait until she finds the right unit, but she knows she may need to place a deposit or make a down payment at any time. Nancy needs a flexible account that lets her access her funds quickly.

She has found that her TFSA has been a good choice for saving for her purchase. Until she finds the right condo, she continues to build her savings and enjoy tax-free growth while still maintaining access to her funds.

She can go condo shopping with confidence, knowing that the funds are ready when she is. If she buys a unit that's under construction, she can make her deposit, then continue to save towards the purchase price while the unit is being built. If it's an existing unit, then she'll have access to the funds she needs for a down payment.

Nancy also started contributing to an RRSP when she was in her early 20s. She hasn't contributed a lot in the past few years, but she's still managed to accumulate a fair bit. If she needs additional funds for her down payment, she can withdraw up to \$25,000 tax free from her RRSP under the RRSP Home Buyers' Plan.



3 Paying for a child's education

Jim and Jean are approaching age 50 and have an 18-year-old son, John, who is in his last year of high school. He will soon be moving away to pursue a post-secondary education.

They started a Registered Education Savings Plan (RESP) for him when he was still in grade school, which will help offset some of his expenses. Jim and Jean are also using their TFSAs to help pay for John's schooling. They can make withdrawals tax free to put towards John's post-secondary tuition and other costs. The money will not be attributed to them for tax purposes, and they can replace the amounts they've withdrawn in later years.

When John turned 18, they also gave him the money to buy mutual funds or stocks for his own TFSA[†]. John doesn't expect to need these funds, but feels better knowing he can make withdrawals from his own TFSA throughout the school year if he needs to.

[†] The age of majority is 19 for residents of Newfoundland and Labrador, New Brunswick, Nova Scotia, British Columbia, Northwest Territories, Yukon and Nunavut which may delay the opening of a TFSA. However, the accumulation of contribution room will start at age 18.

Know your TFSA contribution room

Your available TFSA contribution room for 2012 is comprised of:

- \$5,000
- any unused TFSA contributions from the previous year
- any withdrawals made in the previous year (excluding qualifying transfers and special distributions)

Please visit the Canada Revenue Agency website (www.cra.gc.ca) for complete details.

4 Planning for retirement

Beth and Colin are both in their early 60s and plan to retire within the next five years. They've been contributing to their RRSPs for many years, and expect that these registered savings will generate a significant part of their retirement income.

Since the TFSA was introduced, they've also been channelling as much as they can into their TFSAs each year before contributing to RRSPs. This will provide an extra source of funds they can draw on as needed. For example, by using their TFSAs to meet their cash-flow needs in their early retirement years, they can delay converting their RRSPs to Registered Retirement Income Funds (RRIFs) until the end of the year they turn 71.

Once they convert their RRSPs to RRIFs, they'll have to withdraw a minimum amount every year. However, by using their TFSAs, Beth and Colin may be able to take out only the minimum amount. One of the advantages of using their TFSAs to provide retirement income is that the withdrawals are not considered taxable income and therefore do not affect their eligibility for income-linked government benefits like Old Age Security. In addition, since there is no age limit on TFSAs, they can even contribute the amounts they have to withdraw from their RRIFs, to continue earning tax-sheltered investment returns.

To learn more about the many ways your TFSA can help you reach your goals, or to open an account, visit the [Accounts & Services](#) section of the [Investments Products](#) tab on the [online investing site](#).

Things to consider when choosing to contribute to your TFSA or your RRSP

According to client research from RBC, the decision on whether to contribute to an RRSP, a TFSA or both is one of the top five concerns that Canadians have about their finances. To help you allocate your savings most effectively, here are some factors you may wish to consider when making this investment decision:

- **When will you need the money?** If you need money sooner rather than later, a TFSA may be your best choice for saving. A TFSA lets you withdraw money at any time with no tax consequences. Withdrawals from your RRSP, on the other hand, are taxable in the year of withdrawal and subject to an immediate withholding tax when you take the money out.
- **Are you trying to lower your taxable income?** Unlike TFSA contributions, RRSP contributions generate a tax deduction. This may reduce your taxable income sufficiently to shift you into a lower tax bracket or maybe even generate a refund. So if you're concerned about your tax bill, RRSPs might be the preferred choice.

Market Outlook

Provided by RBC Global Asset Management Inc. on December 15, 2011

The global economy continues to eke out growth despite repeated market shocks and political earthquakes. These rumblings have not been entirely costless. Several fissures have begun to form, presenting threats to the recovery. The risk that Europe goes badly off the rails has grown over the past several months. Politicians and policymakers hold in their hands the capacity to avoid this worst-case scenario, but have so far displayed questionable dexterity. Political dysfunction has damaged confidence and fiscal drags are beginning to bite. It is increasingly clear that this economic cycle is little different from recoveries that have followed financial crises in the past. Simply put, the road back to normal is invariably long and slow.

In the absence of an obvious catalyst to turn around this gloomy mood, the economic outlook looks considerably grimmer. At worst, the developed world could enter a second phase of the financial crisis. More likely, an extended period of sluggish growth appears to be at hand. Risk aversion may remain somewhat elevated, bond yields may be lower for longer and stock markets will remain uncertain due to the likelihood of slower corporate profit growth and prospects for lower earnings multiples.

Muddle-through economic scenario still our base case

The current investment environment is characterized by two divergent potential outcomes. Our base case scenario has Europe muddling its way through the current crisis. Any fix will not likely be a perfect long-term solution, but rather one that persuades markets that a collapse is off the table. We expect any recession in Europe to be relatively mild and for recession in North America to be avoided. Global conditions should remain modest but positive, buoyed by firmer economic growth outside developed markets. The alternate outcome is for Europe's crisis to escalate dramatically, with negative consequences for risk assets and further declines in bond yields.

The Eurozone has continued to deteriorate, engulfing erstwhile bystanders such as Italy, and knocking on the doors of Spain and Belgium. Unfortunately, politicians are stuck in reactive mode. They require market stress to secure the public support needed to implement bailouts. The ECB is doing a wonderful job of providing unlimited liquidity to European banks, but even unlimited liquidity has its limits when banks begin to run out of acceptable collateral. The most likely course of events for the Eurozone is that policymakers take several more months to arrive at a coherent and truly workable solution. Bouts of volatility and pessimism are probable until this proper final fix is struck.

Our models indicate that the U.S. is not presently in a recession, but is at risk of tumbling into one within the next

year. The threat comes less from domestic U.S. conditions, and more from the possibility of a European misstep with global consequences. Even absent a recession, growth prospects remain uninspiring. America is still riddled with dysfunctions, and these are holding back a proper economic recovery. The housing sector remains stubbornly resistant to significant improvement, but we are increasingly of the mind that the stage is being set for a halting, modest housing recovery. The labour market is also misbehaving. Job growth now looks to be picking up moderately, but it will struggle to eat into the overhang of unemployment.

Canada continues to appear more sprightly than most. The combination of credit growth, job growth, and high and steady commodity prices are the ticket for ensuring ongoing economic gains. However, it remains highly unusual for Canada's economy to significantly decouple from the U.S., especially given the Canadian dollar's tendency to act as a shock absorber. As such, we forecast a downshift in economic growth in Canada in 2012.

Dollar a safe haven when risk aversion returns

We cannot know yet whether the U.S. dollar lows last summer marked the bottom of the dollar bear market, or whether the 8% bounce since is merely a safe-haven rally. We can assert, however, that the European crisis, like the financial-system collapse of 2008, has made it obvious that the greenback remains a safe-haven currency, and that all other currencies are secondary when risk aversion takes hold of the market. With a number of unresolved issues in Europe and critical funding needs concentrated in the first quarter of next year, the spreading crisis will eventually weigh down the euro. With regard to other currencies, the past year's 'currency impasse' characterized by volatility in foreign-exchange values without sustainability, may very well extend into 2012. We want to take advantage of the volatility and favour establishing or adding to U.S. dollar exposure during its sell-offs in the belief that the volatility will eventually be resolved to the upside.

Benign inflation and short rates remain low

Global inflation is still a bit high due to the lingering effects of higher commodity prices from the spring of 2011, but this influence is rapidly ebbing. The likely trajectory for inflation is down to normal, or even sub-normal, levels given the substantial global economic slack that persists. The modus operandi for the world's central banks remains to keep the pedal to the metal. For countries like the U.S., the U.K. and Japan, this means unchanged policy rates since their accelerators are already pressed against the floor. European Central Bank President Mario Draghi seems more willing to deliver monetary stimulus than his predecessor, likely translating into further policy easing in the coming months.

Significant upside risks to bond yields

Most major countries continue to enjoy near-record-low bond yields despite the unfolding crisis. The reasons that yields remain so low are simple: the short end of the yield curve is being pulled lower by stimulative central banks, and investors chasing yield have compressed the premium required for holding longer-term bonds. Growth prospects are limited, constraining the real bond yield, while inflation looks to be mostly contained, holding down the inflation component of the yield. Elevated risk aversion is boosting demand for bonds, and several central banks are actively engaged in quantitative easing, creating an additional major source of demand for their own sovereign bonds. The combination translates into extremely, and persistently, low bond yields.

It isn't clear how long this perfect storm depressing yields will last. It will be hard for yields to move sustainably lower from here unless the feared collapse of the Eurozone becomes a reality, whereas the scope for eventual increases is much greater as the crisis fades and growth in Europe resumes. We do not need a "solution" to Europe's crisis to drive yields higher. Rather, a "fix" that allows progress would be sufficient for bond yields to begin their return to normalcy.

Equities struggle to look beyond crisis

Global equity markets have exhibited unusually high volatility since mid-summer. Periods of optimism have been followed by offsetting periods when fear and risk aversion have dominated. Equity investors have been forced to balance this near-term uncertainty against historically attractive valuations, and at times, uncertainty has won out. During this period, equity markets have been trading in a well-defined range. Our view remains that it will be difficult for stocks to rise above the top end of the recent range without a significant breakthrough in the European sovereign-debt crisis. Similarly, equities are unlikely to decline into the bottom half of the range unless we see an intensification of the various crises confronting the global economy, an increase in the risk of recession, or falling profits.

While markets have recovered since early 2009, valuations remain attractive. Today's depressed P/E multiples suggest investors are sceptical earnings growth can be sustained

given the risk that Europe's fiscal crisis will trigger a broader recession. With the benefit of hindsight and sustained economic growth, and the restoration of investor confidence, these valuation levels may one day seem outlandishly low.

Corporate profitability and fundamentals are extremely healthy. It has been well documented how aggressively firms cut costs during the 2008-2009 financial crisis, and how reticent they have been to resume hiring as growth recovered. This caution has helped direct a near-record share of each dollar of sales to the bottom line. There is little to suggest that purse strings will be loosened appreciably in the near future, and so as long as modest growth prevails, margins should be maintained and overall earnings can continue to rise.

Asset mix – modestly overweight stocks, underweight bonds

While risks to growth are easy to enumerate, a durable solution to Europe's fiscal crisis is a work-in-progress that should, over the coming months, provide investors with greater certainty that a worst-case outcome will be averted. Today's extremely low yields on U.S., Canadian and U.K. government bonds will be difficult to sustain in any environment that includes modest economic growth and progress toward crisis resolution. We are also closely monitoring evidence that the global economy is still expanding at a decent pace. This, too, will help confidence recover. As that happens, bond yields will likely rise from current ultra-low levels and result in capital losses for bond holders. Given this view, and its implied risk of higher bond yields, we remain underweight fixed income. Within equities, we are maintaining our modest overweight position. Although growth next year will remain weak, severely depressed equity-market valuations provide upside potential. As long as growth is sustained, normalizing valuations will ultimately drive future returns. However, our overweight stance is relatively modest in recognition of the fluid situation in Europe and unusually wide divergence between the potential outcomes of the crisis. For a balanced global investor, we recommend an asset mix of 57.5% equities (benchmark: 55% within an allowed range of 40% to 70%), 35.0% bonds (benchmark: 40% within an allowed range of 30% to 60%), with the balance of 7.5% in cash.

The complete RBC Investment Strategy Committee's Global Investment Outlook, including the recommended asset mix by investor profiles and the definitions of the investor profiles, can be found on the Market Insight page under the Markets tab on the RBC Direct Investing site.

President's message: 2011 – a year in review



With a fresh New Year unfolding before us, it's a great time to reflect on the past year's events and look forward to the opportunities that lie ahead.

Highlighting our ongoing commitment to providing you with the very best service, RBC Direct Investing™ received Dalbar Inc.'s Direct Brokerage Service Award in January, for the fourth consecutive year.

In February, the Personalized Learning Plan launched. It has been created to help you find the online resources (including articles, Show Me videos and more) that are best suited to your individual investment needs.

In the spring, Pre-Authorized Contributions were extended to TFSAs and RESPs in addition to RRSPs – making it more convenient to save for your important goals. Spring also saw the introduction of a new online account application that simplifies the opening of additional RBC Direct Investing accounts.

Throughout the year, many clients have also benefited from the launch of Rep-Assist, a service created in response to your needs. Rep-Assist makes it possible for one of our telephone representatives to guide you through our online investing site and help you make the most out of our tools using secure screen-sharing technology.

For 2012, the team here at RBC Direct Investing remains committed to delivering an exceptional investing experience. Stay tuned for details on innovative new additions.

Thank you for choosing RBC Direct Investing. I wish you much success in the coming year.

Sincerely,

Jason Storsley, CFA
President and CEO
RBC Direct Investing Inc.



RBC Direct Investing™

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