

Exciting opportunities for RBTT shareholders

By Claire Fletcher

On March 26, 2008, the shareholders of RBTT voted in favour of the proposed amalgamation of the RBTT Financial Group with a Caribbean subsidiary of Royal Bank of Canada (RBC). Subject to regulatory approvals, the transaction is expected to close in May or June 2008 when RBTT shareholders will receive a total per share consideration of approximately TT\$40.00 payable in a combination of cash (approximately 60% or TT\$24.00) and RBC common shares (approximately 40% or TT\$16.00).

For many shareholders, this raises two questions. First, should I hold on to my RBC shares or sell them in the open market? Second, how should I reinvest the cash portion of the consideration? Those who are tempted to hold on as shareholders in the enlarged company need to consider first and foremost not the tax issues or the complexities of having a stake in a Canadian firm, but the fundamentals of value.

RBC (RY on TSX and NYSE) is Canada's largest bank and one of North America's leading diversified financial services companies. The Company remains focused on leveraging its domestic banking success internationally through a series of strategic acquisitions. Following the close of the amalgamation with RBTT, RBC will have one of the largest banking networks in the Caribbean, with a presence in 18 countries across the region.

In addition to diversifying risk through the expansion of its international operations, RBC like most Canadian banks has far more conservative risk management policies than its U.S. and European peers and has escaped relatively unscathed from the sub-prime scandal. So with the financial sector beaten down by the recent credit crisis, now may be a good time to invest in international banking stocks with strong fundamentals.

Over the last 10 years, RBC has outperformed many of its rivals and at 12 times earnings is also cheaper. Also a good income stock, RBC pays a 4% dividend, which has increased every year since 1996. Based on current valuations, analysts recommend a hold on the stock and predict an average 12-month target price of about US\$56.

So RBC has a lot going for it. But despite these pluses, shareholding in a Canadian bank may not be a suitable investment for most RBTT shareholders. It's difficult for a small investor in Trinidad & Tobago to follow a Canadian bank to see how it's performing, and there are tax issues and currency exchange issues involved.

For many RBTT shareholders, particularly the smaller ones, it makes more sense to sell up and invest in a local bank you can track more easily – Republic Bank is our main tip for the year. Although RBC has made verbal commitments to the creation of a depository receipt structure listed on the TTSE, this is unlikely to happen until later this year at best.

RBTT shareholders who wish to sell their RBC shares on the NYSE or TSX can do so through West Indies Stockbrokers Limited (a wholly-owned subsidiary of RBTT). Besides offering superior multi-currency execution capabilities at a competitive cost, WISE's International Brokerage Account also provides easy access to your money, a competitive foreign exchange service and online account information.

But before you cash in your RBC shares and reinvest those US or Canadian Dollars in the local stock market, RBTT shareholders should consider using this opportunity to build or add to an existing international portfolio. Aside from the potential gains, the inclusion of foreign securities is an integral part of a diversified investment strategy.

Whether you decide to invest directly in the stock market, or purchase shares in an exchange-traded or mutual fund, adding international exposure to a portfolio will normally reduce the risk without lowering returns. Although investing overseas to reduce risk might seem contradictory in the current environment, perhaps now more than at any time, the importance of proper diversification cannot be overstated.

Since the onset of the U.S. sub-prime crisis last year, the international financial markets have been in turmoil, yet the T&T stock market has so far remained unaffected. In fact, during the first quarter of 2008, the local equity market gained 7.3% while the U.S., non-U.S. developed and emerging markets finished down 9.4%, 8.9% and 11.0%, respectively. Admittedly, the recent TTSE rally is largely in response to the RBC-RBTT amalgamation, but whatever the reasons, history shows that the T&T stock market returns are typically uncorrelated with other markets.

Investors would certainly have benefited from exposure to domestic stocks in recent months, but let us not forget that the international markets have significantly outperformed the TTSE over the past three years. While the T&T stock market sank deeper into the doldrums between 2005 and 2007, the international markets were reaching historic highs and enjoying double-digit returns.

The point is that no single type of investment performs well all the time which is why investors with a well-diversified portfolio always fare best in the long run. The way you spread your money across various types of investments is responsible for 91.5% of your investment return while all other factors combined – including security selection and market timing – account for the remaining 8.5%.

For RBTT shareholders with little or no exposure to the international markets, the sale of RBTT presents an excellent opportunity to participate in some of the world's most active and fastest growing financial markets. This is especially true for those shareholders who have opted to receive their cash consideration in US Dollars, but is equally applicable to all RBTT shareholders.

The average RBTT shareholder prior to the RBC-RBTT amalgamation is probably overweight in local equity and taking on unnecessary concentration risk by holding too much of one stock. The same applies to the average RBTT shareholders post-amalgamation. By holding RBC shares, shareholders have simply transferred this company-specific risk from one stock to another.

A concentrated position can have a dramatically negative impact on the long-term wealth-creating ability of a portfolio. The risk comes from the extreme reliance a portfolio has on one position. If the stock does poorly, it can pull the entire portfolio down. As a general rule, you should never have more than 20% of your portfolio in any one stock.

The easiest and least costly way to avoid concentration risk is to invest in mutual funds. These funds bring the benefits of diversification and money management to the individual investor by pooling the money of many investors and investing in a wide range of stocks, bonds or a combination of the two.

Offshore mutual funds offer the added advantage of immunity to Withholding Tax which will cost RBC shareholders 15% of their dividends. With so many funds to choose from, most investors are better off soliciting the help of an investment advisor. If you would like advice on mutual funds or any other investment opportunities you can contact West Indies Stockbrokers Limited.

WISE offers free consultations with an experienced, unbiased investment expert who will review your portfolio and make recommendations based on your personal financial goals and appetite for risk. With access to a broad spectrum of local and international investment products, WISE can help any RBTT shareholder decide the best way to reinvest.

Claire Fletcher is the New Product & Market Development Manager at West Indies Stockbrokers Ltd. and can be reached at 625-WISE or clairef@wisett.com.