INVESTMENT FOCUS

From the Central Wealth Group of Raymond James Ltd.

Summer 2019

Central Wealth Group

Kenneth Stratton, CIM®
Portfolio Manager
Senior Vice President, PCG

Glen Hansen, CA
Financial Advisor
Senior Vice President, PCG

Alain Berube, CFA
Financial Advisor

Peter Vander Velde
CIM®, CMT
Associate Financial Advisor

Robyn Drummond
Licensed Assistant

Raymond James Ltd.
Suite 2300, Scotia Place Tower 1
10060 Jasper Avenue
Edmonton, AB T5J 3R8

Telephone: 780 414-2500
Toll Free: 1 888 414-2501
Fax: 780 414-2599

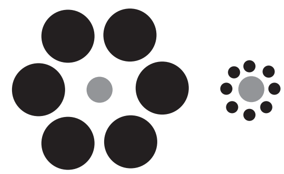
Pursue Your Plan with Confidence

When Tiger Woods won his fourth Masters Tournament this past spring, he ended an 11-year drought, creating not only a moment that went down in golf history, but also a lesson in unpredictability. Indeed, it is challenging to predict what will happen and when, and this applies not only to golf.

This unpredictability also extends to current financial climates, with the extended bull market run being unexpected by many. Despite sluggish economic conditions, the first four months of the year saw equity markets on an upward trajectory. But these are unprecedented times. Never before have central banks held rates at low levels for such lengthy periods. While the role of a central bank is not to stabilize markets, the markets have been calmed by decisions to hold interest rates steady.

In investing, there are many ways in which it mirrors the game of golf. "High percentage" players always consider the risks versus return before playing any stroke. Likewise, a well-constructed portfolio takes into account the same types of factors. Investing, like golf, is a game of patience and persistence, filled with many mental challenges.

One challenge that can affect golf performance is the impact of perception. Those familiar with the optical illusion below know that the circles in the middle are exactly the same size. Psychologists at Purdue University used this illusion in a putting green to make a golf hole appear larger or smaller by projecting circles of light around it. When people perceived the hole to be smaller, they were less successful in putting.



Similarly, perceptions can drive investing behaviour. Are there ways in which you allow outside perceptions to influence the way you invest? For instance, are you quick to compare portfolio gains to those of today's market darling, without considering quality, risk or diversification? Or, during volatile times, do negative media reports tempt you to make changes instead of allowing a portfolio the time to grow?

The discipline and patience needed to putt a birdie may be something we can apply to our own investing style. Bringing this sharpened focus is a great step toward mastering our own plans. Stay the course and pursue your game plan with confidence and persistence. Fore!

In This Issue

Federal Budget Recap

New Initiatives that May Impact the Young and Old

In late March, the federal government tabled their final budget prior to October's election. It was a collection of many different initiatives and here are some changes that may impact you or your loved ones, specifically targeting the young and the old.

The Young: Housing Affordability

While many children may be hoping for support from the bank of mom and dad to purchase a home, if this isn't part of your financial plan, the budget may offer some relief in two initiatives:

First–Time Home Buyer Incentive — A qualifying first-time home buyer with household income under $120,000 per year may be entitled to receive incentives of up to 10% of shared equity on a newly constructed home (5% on an existing home). No monthly ongoing payments will be required but the buyer must repay the shared equity mortgage upon re-sale of the home. An insured mortgage and shared equity amount cannot be greater than four times annual household income. This program is expected to begin in September.

Home Buyers' Plan (HBP) — The available withdrawal limit under the current HBP is proposed to increase to $35,000. Under current rules, a first-time home buyer can withdraw $25,000 from their registered retirement savings plan (RRSP) on a tax-free basis. Access will be extended to those who experience a breakdown of marriage or common-law partnership, even if they do not meet the first-time home buyer requirement.

Seniors: Retirement Support

There was also some good news to help seniors in retirement:

Automatic CPP Enrollment — Starting in 2020, Canada Pension Plan (CPP) contributors who are 70 years old or older will be automatically enrolled to ensure they receive benefits. Currently, an application must be launched in order to receive benefits and some have missed out because they apply late or not at all.

Advanced Life Deferred Annuity (ALDA) — Currently, an annuity purchased with registered funds must commence annuity payments by the end of the year that the holder reaches age 71. The budget proposes to allow up to 25% of a registered holding* to be used to purchase an annuity that begins payments at the latest by the end of the year in which the holder turns 85, for a lifetime maximum of $150,000 (indexed to inflation). This may present a tax-deferral opportunity, allowing retirees to keep more money in registered plans for longer, and may support those who are worried about outliving their retirement income.

Improved GIS — For low-income seniors, the basic earnings exemptions are proposed to increase to $5,000 per year (from $3,500) for Guaranteed Income Supplement (GIS) benefit eligibility. Earnings up to $15,000 per year will receive a partial exemption.

For greater details, please get in touch.

*Including RRSP, RRIF, deferred profit sharing plan, pooled registered pension plan, registered pension plan. At publication, this initiative has not been enacted into legislation.

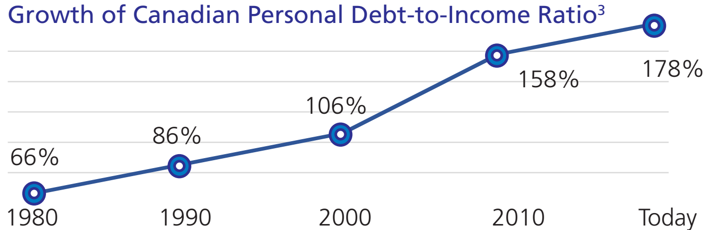
Does Canada Have a Growing Debt Problem?

Do we have a growing debt problem? Recent figures indicate that Canadians on average have a debt-to-income ratio of around 178% (Q3 2018).[1] This means that Canadians owe $1.78 in debt, including consumer credit, mortgage and non-mortgage loans, for every dollar of household disposable income.

According to the OECD, we place 8th in the developed world for high indebtedness.[2] In the U.S., where debt levels peaked at around 116% prior to the credit crisis of 2008, debt levels are now under 90%.

This ratio has risen over the decades. Consider that just 30 years ago, average Canadian household debt was only around 86% (see chart). Some have called Canada's rising debt figures disturbing, while others argue that this assessment might be overly harsh since the ratio lumps in those with significantly high mortgages (in cities like Toronto or Vancouver) and doesn't factor in a household's assets or the ability to pay off that debt load.

Growth of Canadian Personal Debt-to-Income Ratio[3]



Regardless, Canadians — individuals, corporations and even the government — have never been so indebted and we face longer-term consequences as this debt will eventually need to be repaid. When interest rates start to rise, these debt obligations will become more costly. However, one reason why central banks have kept rates low is to encourage spending and stimulate sluggish economies. The paradox? Low rates make borrowing more affordable, and have also pushed up housing prices, making us more indebted.

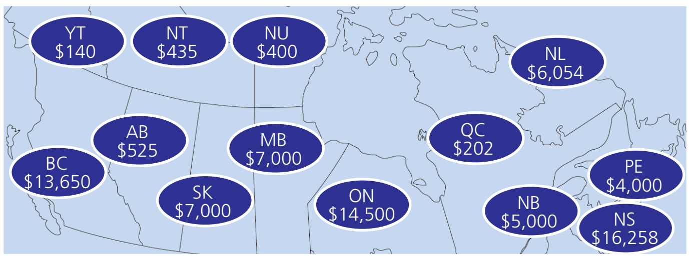
1. https://www.cbc.ca/news/business/statscan-household-debt-net-worth-1.4946036; 2. OECD ranking 2018; 3. Source: Statistics Canada.

Estate Planning

Keep Probate Fees in Perspective

In Canada, we don't have a "death tax," where significant taxes must be paid on the transfer of wealth at death. Consider that in some countries like the U.S. or Japan, estate tax can reach rates of up to 40 and 55% respectively![1] Yet, over the years, probate fees have become a de facto estate tax.

Estimated Probate Fees on a $1M Estate Value by Province[2]



Probate is the process by which a court confirms the validity of the will of the deceased individual. This declaration allows estate representatives and institutions to proceed on the basis of the instructions detailed in the will, without worry of future disputes. The fees vary by province — in most cases, based on percentage of the value of the estate.

It may make sense to try and minimize these fees; after all, not many enjoy giving up their hard-earned wealth to the government. In doing so, a basic strategy would be to pass as many assets as possible to heirs outside of the estate: registered plans and insurance with designated beneficiaries, as well as property registered jointly with rights of survivorship ("joint tenancy")[3], may pass outside of the estate.

But keep in mind that there may be dangers involved in trying to minimize probate fees. It could lead to other financial implications or headaches. Particular care must be taken when a beneficiary or joint tenant is not a spouse. For instance, joint tenancy means permanently giving up full ownership of your asset, which may include its control. If a joint tenant encounters financial difficulty, creditors may force the sale of a jointly-owned asset. There is also risk of a falling-out in any relationship, with spouses or others.

There may also be equalization issues. Suppose you have two grown children as your only heirs and you designate Child 1 as the beneficiary of an RRSP in an attempt to bypass probate, leaving the rest of the estate to Child 2.[3] When you die, taxes due on the fair market value of RRSP assets will be payable by the estate, potentially reducing the amount for Child 2.

Saving a few dollars in probate fees may result in other taxes. For example, putting an asset such as a house in joint ownership with a non-spouse may save future probate fees, but if they already own a principal residence, they may be subject to capital gains tax on the sale of the property.

At the end of the day, keep perspective: probate fees may be little more than a nuisance in the objective of effectively settling an estate.

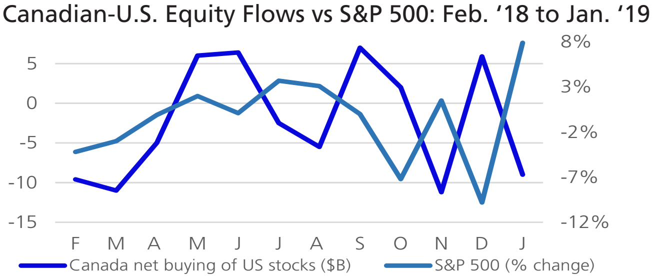
1. E&Y Worldwide Estate & Inheritance Tax Guide 2018; 2. At 1/9/19, based on provincial website estate administration schedules; 3. Not applicable in Quebec.

During Volatile Times, Sitting Still Can Be Difficult

This summer vacation, are you looking forward to doing nothing? For many of us, sitting still can be difficult. No more is this true when it comes to investing during periods of market volatility. After all, as humans we are hardwired to want to take action in times of vulnerability. We're all familiar with the phrase: "don't just sit there, do something!"

However, a recent Globe & Mail article highlighted that some investors may be their own worst enemies during periods of volatility. During the volatility we experienced in 2018, Canadian inflows and outflows into U.S. stocks lagged market

Canadian-U.S. Equity Flows vs S&P 500: Feb. '18 to Jan. '19



Source: "Investors are their own worst enemies", Globe & Mail, T. Shufelt, 3/27/19.

performance (see chart). Investors put funds into investments after market gains, lagging the market by about a month, and sold investments after market drops, resulting in performance chasing.

Of course, there may be good reasons for selling securities, such as rebalancing to restore asset allocation or taking gains after a long bull run. But if simply reacting to rises or drops in the market is driving these decisions, many investors may be better off by just staying put.

Renowned investor Warren Buffett once described his investing style as "lethargy bordering on sloth." Perhaps there may be some good investing insight hidden in those restful summer vacation plans: go ahead, don't just do something, sit there!

Risk Tolerance: Shouldn't Change with the Markets

One of the questions we've had from clients during the prolonged bull market is: how often should I change my risk tolerance?

The answer is — likely, not often.

Risk tolerance is the personal comfort level that an investor has with financial risk in the markets. In the most basic sense, it is your ability to stomach swings in the markets in exchange for potentially higher future returns. Risk tolerance doesn't vary greatly. Consider the answer to this question: how would you respond to a 15% drop in your investments? Most people's reaction and level of comfort in this situation would likely not vary over time.

With time and evolving circumstances, however, your capacity to take on financial risk may change. This is your ability to withstand a financial shock and it may have an impact on your risk tolerance. Here are some events that may impact risk capacity:

A major life event, such as a marriage or having kids. Marriage or the birth of a child may lower your capacity for risk as you account for large expenses, such as a new home or a child's education. Often, spouses differ in their risk tolerance levels. Some studies have shown that men tend to have a higher risk tolerance than women, so common ground may need to be reached when managing finances.

A health crisis. Unexpected medical bills or your ability to generate income into the future may impact your timeline and ability to achieve your financial goals.

Changes to net worth or income. Your level of wealth may impact your capacity for risk. For instance, the greater your excess income, the easier it may be to weather a downturn without it affecting your lifestyle.

One Reason to Adjust Risk Tolerance: Age

As you age, changes to risk tolerance levels should be expected. You may become more risk averse because you may not have the same sources of income and you will need to preserve your wealth for retirement. With a shorter time horizon, recovering from market volatility may be also more challenging, which may prompt you to lower your risk tolerance level.

When Not to Make Adjustments: Fluctuations in the Markets

Your risk tolerance should not fluctuate based on market conditions. Changing your risk tolerance in response to market performance can be seen in a similar light to attempting to time the markets by buying and selling shares to predict future market price movements. It may be tempting to want to lower your risk after you have incurred a loss, just as you might want to raise your tolerance after benefitting from a gain. But the performance of your portfolio or the markets, and the emotions of fear or greed, should not be a cause to reevaluate your tolerance to risk.

Please Get in Touch

If you have any questions about this, or any other investing matters, please call.

Central Wealth Group

Ken Stratton | 780 414-2555
Glen Hansen | 780 414-2556
Alain Berube | 780 414-2530
Peter Vander Velde | 780 414-2557
Robyn Drummond | 780 414-2505

Raymond James Ltd.

Suite 2300, Scotia Place Tower 1
10060 Jasper Avenue
Edmonton, AB T5J 3R8
www.centralwealthgroup.ca