







## You Asked...

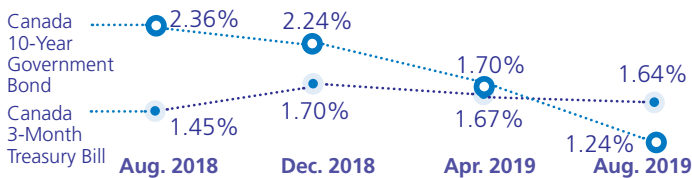
# The Yield Curve and Interest Rates: What Do They Mean?

If you've been paying attention to the markets or the media lately, there has been a lot of talk about the yield curve.

What is the yield curve? Simply put, it is a graph that plots the interest rate yields of bonds over time. Usually, longer maturity bonds have a higher yield than shorter maturity bonds because investors are compensated with higher returns for tying up their money for a longer period of time.

However, in March of this year, the yield curve inverted for the first time since the financial crisis of 2007/08. This means that a shorter-term bond has a higher yield than a longer-term bond. One year ago, the yield on a Canada 10-year government bond was 0.91% (or 91 basis points) above the rate on a 3-month Treasury bill. In August, it was around 40 basis points *below* (see chart below). For many economists, an inverted yield curve has historically been one indicator of an impending recession.

### The Difference a Year Can Make: Rates on Select Bonds

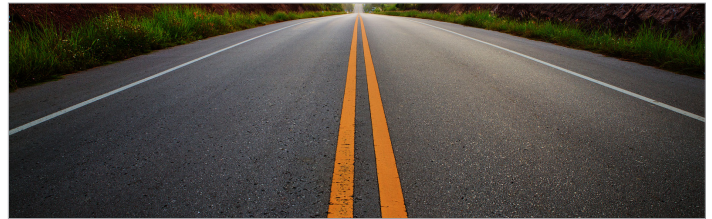


Source: Bank of Canada: 8/1/18, 12/1/18, 4/1/19, 8/8/19.

### Does this mean a recession is in sight?

There's an old joke that says the markets predicted nine of the past five recessions. This is to say that predictions are often more pessimistic than what happens in reality. Of course, as long as we have a business cycle, every recession prediction will eventually be correct, it's just the timing that is often wrong.

While it is true that global economic growth has slowed, these



are unprecedented times. Never before have central banks held interest rates at these low levels for such long periods of time. In July, the U.S. lowered its overnight interest rate for the first time in over a decade, citing slower global growth and uncertainty from U.S./China trade tensions. Here at home, interest rates were held steady (at press time) due to a variety of bright spots: over the summer Canada's productivity, measured by GDP and trade surplus, posted surprising growth; employment still remains at historical highs; and many companies have posted positive results.

### Negative interest rates: The new normal?

In some parts of Europe and in Japan, negative interest rates have continued for years. Central banks have kept overnight rates negative to dissuade commercial banks from maintaining large deposits with the central bank and instead encourage them to lend to businesses and consumers who will spend funds. This is to try and boost economic activity, growth and inflation.

### What does this mean for investors?

Equity markets can react favourably to lower interest rates. As finding income in fixed income products becomes more difficult, investors may look to more risky assets like equities. However, slowing global growth is expected to impact global equity markets, and growing global indebtedness continues to be a concern; the future consequences of which are not fully understood.

## Before Year End: Do Good; Save Tax!

'Tis almost the season of giving. If you are planning on taking equity gains after the extended bull run and may be faced with the prospect of a substantial capital gains tax liability, why not consider doing some good, while saving tax at the same time?

Even though capital gains are taxed at one-half the regular rate, it may not be palatable to see an asset value reduced by the Canada Revenue Agency. If you were to instead donate appreciated shares "in kind," you would receive a donation receipt for the gross value of shares and not be subject to the capital gains liability. However, shares must be donated; do not sell them first and donate the proceeds, as part of the tax benefit will be lost.

Be sure to give yourself enough time to do this before year end. The donation must be received by the charity before the calendar year end for it to apply to your 2019 personal income taxes, but time may be required to settle the transaction. Call for assistance.

### Five Facts About Charity



France is the first country to forbid food waste by supermarkets; by law they must donate it to charity.<sup>1</sup>



Late actor Paul Newman commercialized his homemade salad dressing in 1982. "Newman's Own" donates all after-tax profits to charity: US\$525 million to date.<sup>2</sup>



The "Giving Pledge" consists of 204 of the world's wealthiest from 23 countries pledging at least half of their wealth to charity.<sup>3</sup>



George Lucas sold the rights to Star Wars in 2010 and pledged the majority of \$4 billion in proceeds to educational charity.<sup>4</sup>



John F. Kennedy donated his entire presidential and congressional salaries to charity during his time in office.<sup>5</sup>

1. npr.org/sections/thesalt/2018/02/24/586579455/french-food-waste-law-changing-how-grocery-stores-approach-excess-food; 2. newmansown.com; 3. givingpledge.org; 4. forbes.com/sites/briansolomony/2012/11/04/donating-star-wars-billions-will-make-george-lucas-one-of-the-biggest-givers-ever/#606f8e5d2adb; 5. upi.com/Archives/1962/11/14/JFK-Donates-Full-Salary-To-Charity/3714224962880/