INVESTMENT FOCUS

From the Central Wealth Group of Raymond James Ltd.

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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

Investing Takes "Grit"

If there's one thing that the extended bull market run has taught us, it's that investing takes "grit". Often dubbed "the most hated bull market of all time", for many years now the media has been calling its top.

Grit is about having the same goal for a very long time, and sticking to it despite setbacks or failures. Researchers have determined that it can be one of the greatest predictors of an individual's long-term success, even more important than IQ or wealth.[1]

As investors, how do we maintain grit in investing?

Savvy investors start by having a plan in place. Portfolios are created with personal objectives in mind, to meet an investor's needs over the longer term. Each element has been selected to serve a purpose, in both up and down markets.

Then, they stick to the plan. This involves focusing less on short-term news and more on end goals. In good times, it means maintaining a realistic approach to returns and not chasing strong market performance. In difficult times, it often means tuning out the noise and continuing to save and invest.

Where are the economy and the markets headed? This is not a normal cycle left to run by itself. It has been largely supported by the actions of central banks. Over the summer, while the Bank of Canada kept interest rates on hold, the U.S. Federal Reserve lowered its overnight rate for the first time in over a decade (see page 3). Will this help to keep recessionary concerns at bay?

Of course, the economic cycle is immutable and there will be inevitable ups and downs. But there is often little value in trying to predict the markets or economy: your plan's overall success isn't dependent on calling the top of any cycle. Many investing mistakes come from trying to run a marathon in an hour. As the saying goes: "More money has been lost preparing for corrections than has been lost in corrections themselves."

Modern capital markets have always adjusted and progressed. It is a good reminder that over the past 25 years, the equity market went up by 393%, in spite of two recessions collectively lasting 32 months and three bear markets totaling 38 months — two of which saw market drops of over 40%.[2] We may forget that bad news almost never supersedes the power of true grit.

The investing journey is a long one and an investor's ability to keep focused can be one of the keys to longer-term success. And, it all can start with a little grit.

1. "Grit: The Power of Passion & Perseverance", Angela Duckworth, 2016. 2. S&P/TSX Composite Index, 8/94 to 8/19.

In This Issue

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Consider the Implications

Thinking About Gifting Funds to Adult Children?

Most of us have heard the statement: "*back in my day, I walked uphill both ways to get to school.*" But given the rising costs to own a home or earn a higher education, perhaps kids these days don't have it as easy as we may think. If we look back 35 years, the average cost of a home was only 1.6 times annual family income; today, it has climbed to around eight times average income. Tuition costs have also risen faster than inflation. One thing in today's favour? A mortgage today comes with lower interest rates, if you can afford it!

How Costs Have Risen in 35 Years: Costs in 1984 vs. 2019

Average Cost	1984[A]	Inflation-adjusted: 1984 figures in 2019 terms[F]	2019
Canadian home[B]	$76,214	$171,132	$480,000
Tuition[C]	$1,058	$2,376	$6,838
Family income[D]	$48,500	$108,902	$71,000
5-yr. mortgage rate[E]	13.6%	N/A	4.4%

A: 1984 figures: Globe & Mail "2012 vs 1984: Young Adults Really Do Have It Harder Today", R. Carrick, 12/18/12; B: cbc.ca/news/business/crea-house-price-march-1.5098120; C: Statistics Canada Table 37-10-003-01; D: Statistics Canada (after-tax) figures; E: Bank of Canada v122497, CANSIM 027-0015; F: Adjusted for inflation using Bank of Canada inflation calculator, www.bankofcanada.ca/rates/related/inflation-calculator/

Given these financial challenges, we are often asked about gifting money to adult children. There are other reasons to gift funds: It may be fulfilling to see funds put to work while you are alive or when most needed by a child; some wish to die with as few assets as possible; and others wish to take advantage of income-splitting opportunities.* If you are thinking of gifting funds to adult children, here are three things to keep in mind.

1. Plan ahead, with care. Before you consider gifting, ensure you will have sufficient funds for your own retirement. It isn't unheard of to have a situation in which parents have suffered financial difficulties down the road because too much was gifted to children. Often, contingencies such as health care aren't adequately factored in. Planning for longevity and its associated costs is something we can assist with. As life expectancies rise, this becomes more important than ever.

2. Let it go. If funds are truly a gift, there should be no strings attached. One concern that parents have if children are married/common-law is what happens in the event the couple splits. If there is a desire to protect funds in the family, this should be planned from the onset. Various arrangements, if executed properly, may be viable alternatives to a gift. For instance, if funds are to be used to purchase a home, consider gifting them to a trust for the purchase. Or, a loan may be chosen over a gift. As family law varies by province, seek legal assistance in the province where the child resides.

3. Clarify to avoid future discrepancies. It may be beneficial to create and retain documentation to avoid future disputes. If the intention is to eventually equalize your estate between multiple beneficiaries, the gift could be structured as an advance of a beneficiary's future inheritance. Either way, this should be clearly communicated or documented. There have been situations in which family members have questioned past gifts when settling an estate.

*The tax rules for attribution of income and tax on split income should be considered before implementing income-splitting measures.

Back to School: Funding an RESP for Grandchildren?

With kids now back in school, and with the rising costs of education, many grandparents have been asking about funding a registered education savings plan (RESP) for a grandchild's post-secondary education.

While it is possible for grandparents to open an RESP for grandchildren, it is important to exercise caution for two reasons. First, if multiple RESPs exist for the same child, total contributions need to be carefully monitored so they don't exceed the maximum of $50,000 per beneficiary, as penalties will apply.

Second, if the beneficiary doesn't pursue post-secondary education, under certain circumstances RESP funds may be transferred back to a contributor's registered retirement savings plan (RRSP). However, grandparents beyond the RRSP age cannot transfer funds to a registered retirement income fund (RRIF). As such, taxes and penalty taxes would apply to earned amounts. Thus, if parents have already opened an RESP, it may be better to gift funds to parents and have them make the RESP contribution.

Are there other funding alternatives?

Setting up a trust* may be an alternate solution. There are no contribution limits, but unlike an RESP there are no tax deferral or CESG benefits. If set up correctly, it may be possible to have withdrawals taxed in the hands of a beneficiary, which may be beneficial if (s)he has a lower tax rate. However, keep in mind that once a child gains control, usually at age of majority, the funds can be used for any purpose, not just education.

To discuss more about these or other options, please call.

*Note: Setting up a trust may be a complicated legal arrangement and a tax expert should be consulted to ensure it is carried out in the way intended.

You Asked…

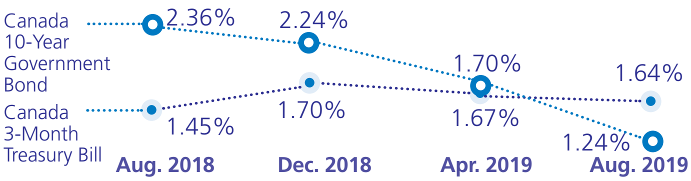
The Yield Curve and Interest Rates: What Do They Mean?

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

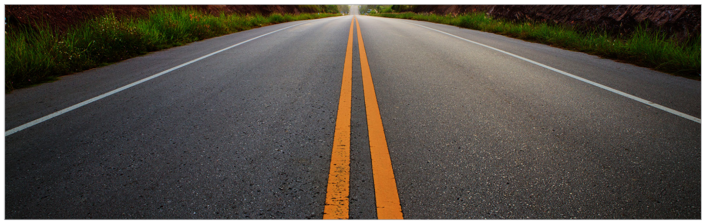


Source: Bank of Canada: 8/1/18, 12/1/18, 4/1/19, 8/8/19.

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.[1]
- 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.[2]
- The "Giving Pledge" consists of 204 of the world's wealthiest from 23 countries pledging at least half of their wealth to charity.[3]
- George Lucas sold the rights to Star Wars in 2010 and pledged the majority of $4 billion in proceeds to educational charity.[4]
- John F. Kennedy donated his entire presidential and congressional salaries to charity during his time in office.[5]

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/briansolomon/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/

Investing Stats: Averages Can Be Misleading

Statistics are very important tools in the investing world, whether to analyze returns or project future investment potential. We often use averages — the central value in a set of data — to help explain investment performance. But, sometimes averages can be misleading. While it is helpful to understand what a portfolio can potentially deliver over the long term, on a short-term basis these same averages may do more harm than good. If you are investing with the expectation of achieving average market performance each year, you're more than likely to experience an emotional ride.

The amusement park provides an interesting analogy. If a roller coaster was viewed only by its average speed, you might not see the whole picture. Canada's Wonderland, the nation's largest amusement park, recently unveiled its record-breaking roller coaster, the Yukon Striker. It boasts three world records, two of which are enough to get most people's adrenaline rushing: fastest dive at 130 km/hour and tallest coaster at 245 feet high! But consider that from start to finish this 3.4 minute wild ride runs at an average speed of only around 19 km/hour — a sloth-like speed if you were driving a car. This makes it seem like a walk in the park, doesn't it?

Often, averages don't tell the whole story, so we should exercise caution when using them in isolation. The same principle applies to investing. A strategy's long-term average returns or the returns of the market over the long run may not be the best yardsticks to gauge what will happen in the short run.

Take, for example, the S&P/TSX composite index. Over the past 25 years, the long-run average return was around 6%. But when looking back at historical returns each year, annual performance rarely was around 6% — it hovered close to this mark in only five of 25 years (see chart, right).

When investing in equities, the reward of greater longer-term expected returns comes in exchange for tolerating the normal periods of volatility. This is especially important to remember during challenging years, when annual returns may present disappointing drops. Preparing ourselves for the inevitable down periods in every market cycle may help to minimize the risk of making hasty decisions. During these times, long-term averages provide a good reminder of why it is important to hold on.

Take time to look beyond the averages in the short term and remember their purpose in helping to explain the bigger picture.

S&P/TSX Composite Index Annual Returns 1993 to 2018

Average Index Return ~6%

-15%+	-10% to -15%	-5% to -10%	0% to -5%	0% to 5%	5% to 10%	10% to 15%	15%+
							2016 17.5%
							2009 30.7%
	2018 -11.6%				2017 6.0%	2010 14.5%	2005 21.9%
	2015 -11.1%				2014 7.4%	2006 14.5%	2003 24.3%
	2011 -11.1%				2013 9.6%	2004 12.5%	1999 29.7%
	2002 -14.0%		1998 -3.2%		2007 7.2%	1997 13.0%	1996 25.7%
2008 -35.0%	2001 -13.9%		1994 -2.5%	2012 4.0%	2000 6.2%	1995 11.9%	1993 29.0%

Source: S&P/TSX composite index, 1/1/93 to 12/31/18.

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

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