RBC Dominion Securities Inc.

Portfolio Advisor

Wealth Management
Dominion Securities

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Panos Sechopoulos Wealth Management
RBC Dominion Securities

Panos Sechopoulos, BA (Hons), MA (Econ), CFA, CFP, FMA
Vice-President, Portfolio Manager & Wealth Advisor
panos.sechopoulos@rbc.com
519-252-3645

Stella Dhono, BBA (Hons), PFP
Associate Wealth Advisor
stella.dhono@rbc.com
519-252-3178

Kelly Sutherland B.Comm. (Hons)
Associate
kelly.sutherland@rbc.com
519-252-3262

1922 Wyandotte St East
Windsor, ON
N8Y 1E4
www.pswealthmanagement.com
1-800-265-0890

Market commentary

Following a strong rebound at the beginning of the year, equity markets have shifted attention to slowing growth in the big three economies of the U.S., Europe and China, and the related downdraft in interest rates that was accompanied by an inversion of the Treasury yield curve – a cautionary signal. Markets are also contending with earnings growth and trade/tariff uncertainties.

These risks are balanced out by dovish central bank policies and signs U.S. economic growth should hold, while trends in Europe and China should stabilize/improve later this year. In our view, equity market valuations remain reasonable, with most trading near or slightly below their long-term averages. Consensus earnings estimates are also realistic. While we would maintain overall equity exposure at the “market weight” (benchmark) level in portfolios, vigilance is warranted.

Fixed income

The U.S. Federal Reserve’s (the Fed’s) significant policy shift in March to no fed fund rate hikes (from two) in 2019 set a new path for global central banks. Global economic weakness is driving the broad move to “easy street” and concerns are mounting as benchmark yield curves invert. The Fed projects one rate hike in 2020, but implied probabilities indicate an 80% likelihood of a rate cut by January, and market expectations predict one rate cut per year from 2019-2021.

There is the distinct possibility that rates could move lower, and we believe this makes “reinvestment risk” a potential issue for investors attracted by short-term rates equal to or exceeding long-term rates. As such, we maintain our “market weight” in fixed income, and recommend investors add duration with a focus on high-quality assets.

To learn more, please ask us for the latest issue of Global Insight.

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Donating shares: It's kind to give in-kind

While it's kind to give to charity, it can be even kinder to give shares in-kind. By donating stocks in-kind, it may allow you to reduce your tax bill, providing you with more funds to give. And donating in-kind can be an effective tax strategy when rebalancing your portfolio.

Canada: the true north strong and generous

Canadians are a giving people: according to a recent Statistics Canada study*, 95% of Canadians (15+) give something to charity – whether it's their time, money or in-kind items ranging from food and toys to antiques and artwork. The annual dollar amount of donations isn't too shabby either, totaling almost $13 billion. The vast majority of donations are smaller in size (under $175), and donations by dollar amount are heavily skewed: large donors account for most of the total dollar amount, with 84% of donations given by just 25% of Canadians and two-thirds by the top 10%.

In general, a Canadian taxpayer can claim a charitable donation of up to 75% of their net income, or 100% of their net income in the year of their death (and the year before that), under Income Tax rules. Any excess can be carried forward for up to five years. And the rules encourage generosity: donations of less than $200 generally produce a tax credit of approximately 24%, while those above $200 attract a tax credit of approximately 48% (note: tax credits vary depending on the donor's province of residence, taxable income and the amount donated).

Taking stock of giving stock: a smart way to give

Maximizing the impact of a charitable donation is a logical approach to giving due to the tax advantages for the donor. While any donation is a positive, if a donor can increase the amount they give by gifting an asset like stocks versus straight cash, then that just makes sense. This is because the donor may be able to eliminate any capital gains on the shares they gift to a registered charity.

The table above demonstrates the clear advantage that donating shares has over donating the proceeds of a share sale.

Donating cash vs. donating shares

	Sell shares and donate cash	Donate shares directly
FMV of donation **(a)**	$2,000	$2,000
Adjusted cost base	$1,000	$1,000
Capital gain	$1,000	$1,000
Taxable capital gain	$500	$0
Tax on capital gain ($500 x 50%) **(b)**	$250	$0
Donation tax credit ($2,000 x 46%) **(c)**	$920	$920
Total cost of donation = (a) + (b) - (c)	$1,330	$1,080

Assumptions: Net tax savings from donating shares: $250 ($1,330 - $1,080), assuming that donations of $200 have already been made. Marginal tax rate of 50%; donation tax credit of 46%. Also assumes the person has taxable income below the top bracket and donations in excess $200.

Risk and reward: rebalance your portfolio by donating shares

Periodically rebalancing your portfolio to reflect your strategic asset allocation and to ensure that its component parts are maximizing returns while minimizing risk is a critical component to investing success.

If you need to rebalance a portfolio because – through equity gains – there is an overallocation to that asset class, an industry group, a sector or a company, rather than selling the equities and reinvesting the proceeds, you could donate those specified stocks. In the end, the after-tax cost of the donation is less, so you have more to donate and you have reduced your portfolio's risk through rebalancing.

Please note that not all charities are willing to accept gifts in-kind, and so it is important to check with the charity to ensure that they are able to receive such donations.

For more information, please contact us today.

*General Social Survey on Giving, Volunteering and Participating, Statistics Canada, 2013.

The Canadian (Pipe?) Dream

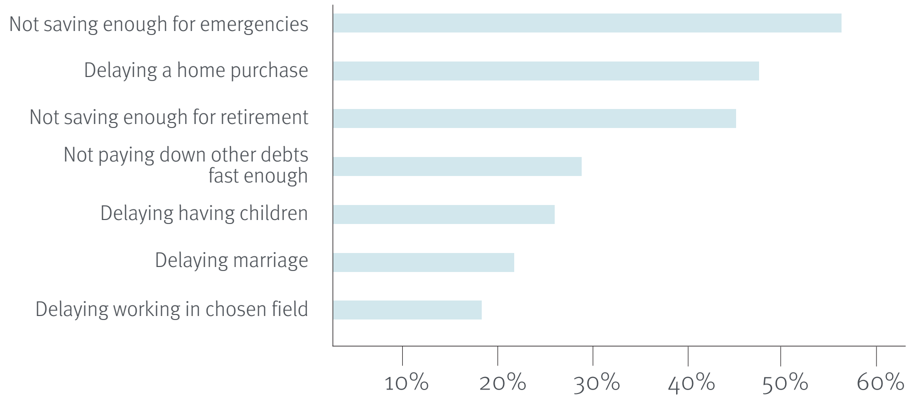
In this land, there are few limits to what you can achieve – that's the Canadian Dream. At least, that's what it was before mounting student debt and delayed life goals turned it into more of a pipe dream for many young Canadians. Fortunately, education planning can help.

In the past, the "life script" generally went like this: graduate, get a job, buy a house, start a family. But with 67%[1] of new post-secondary graduates now entering the workforce burdened with debt, these important life events are being delayed.

However, if they desire a higher income to help achieve their Canadian Dream, young Canadians need an university education, even if that means delaying important life goals. According to a Statistics Canada study[2] that followed a group of Canadian youth from the early 1990s, women with a bachelor's degree earned $442,000 more in average cumulative earnings through their thirties and forties as compared to women with a high school diploma. For men, the difference was $700,000.

Life goals impacted due to student debt

% of university graduate survey respondents



Source: Ipsos on behalf on BDO, RBC Economic Research, September 2017

Keeping the dream alive

Family has a key role to play in helping young Canadians afford the $19,498.75 average annual cost of one full-year of study[3]. And, fortunately, there are several strategies to help families fund education costs for younger family members. The key is to start early.

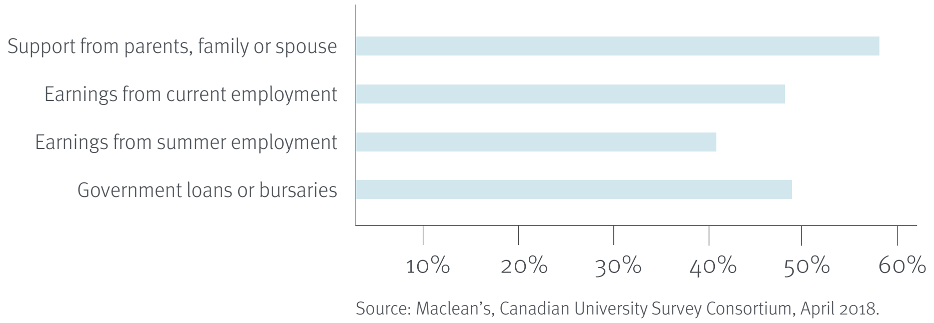
Registered Education Savings Plans (RESPs)

An RESP is a tax-deferred savings plan designed to allow you (the subscriber or contributor) to save for a beneficiary's post-secondary education. All the interest, dividends, capital gains and government incentives in the plan grow on a tax-deferred basis. Also, the federal government matches a portion of your contributions. No matter what your family income, the government pays a basic Canada Education Savings Grant (CESG) of 20% on the first $2,500 of annual contributions to a maximum annual CESG of $500 for each beneficiary. The lifetime limit is $7,200 per beneficiary.

Living trusts

A living trust (or *inter-vivos* trust) can be created during your lifetime and can be a powerful tool, depending on your circumstances, as it can allow you to dictate how much you give, to whom, and for what. For example, say you want to financially support grandchildren's post-secondary costs to alleviate the burden of debt post-graduation. You can set up a living trust with the terms drawn up according to your wishes, which may be that the assets are to be used exclusively for funding educational pursuits. When your grandchildren receive their grants, any capital appreciation or other income earned in the trust will be taxed in their hands, which presumably would be at a much lower tax bracket.

How students fund post-secondary education



Source: Maclean's, Canadian University Survey Consortium, April 2018.

To learn more, please contact us today.

Notes:
[1]Ipsos (for BDO and RBC Economic Research), Three in Four (77%) Canadian Graduates Under 40 Regret Taking on Student Debt (September 2017).
[2]Statistics Canada and RBC Economics, The Cost of Credentials (June 2018).
[3]Maclean's, The cost of a Canadian university education in six charts (April, 2018).

Portfolio, sweet portfolio

Many Canadians are counting on their "home, sweet home" to help fund their retirement years. But it's also important to consider your investment portfolio.

A tale of five cities (and an equity market)
The S&P/TSX Composite Total Return Index vs. select Canadian real estate markets

Based on an initial $300,000 investment with no leverage over the past 25 years

Market	End value	Rate of return
S&P/TSX Composite Total Return Index	$2,410,431	8.3%
Toronto	$1,170,577	5.4%
Vancouver	$1,125,502	5.2%
Montreal*	$1,021,881	4.8%
Calgary	$983,057	4.7%
National avg.	$931,739	4.5%
Halifax	$831,220	4.0%

Sources: All data as of December 31, 2018. Housing price data compiled by RBC Global Asset Management Inc. from Canadian Real Estate Association (CREA). Source of the S&P/TSX Composite Total Return Index is RBC Global Asset Management Inc. All returns are annualized, and where applicable, compounded assuming reinvestment of all distributions. *Please note that data for the Montreal market is not seasonally adjusted.

Despite soaring home prices over the last few decades, many Canadians might be surprised to learn that, over the last 25 years, the average long-term growth of home prices in the country's major markets has been far less than the growth of the country's leading equity market index. That's not an argument against home ownership. Instead, it serves as a good reminder that diversifying your investments to ensure you take advantage of the long-term growth potential of equities is a smart way to get you "home, sweet home" to your retirement goals.

A house is a home, not (just) an investment

For most Canadians, a home is the single largest and most significant purchase they will ever make in their lives. In doing so, they leverage their often small amount of equity (usually as little as 5% to 25% of the purchase price) and cover the rest by taking out a mortgage from the bank.

Of course, that's one of the most significant and wonderful aspects of home ownership: you can enjoy the purchase immediately, while paying the cost of it over a very long period of time, often as long as 25 years. From Day 1, you can take advantage of the leverage of paying only a fraction of the cost to live in a property that can be worth as much as 20 times that down payment. And, each mortgage payment you make builds your equity, taking you one step closer to full ownership.

The unloved but (hopefully) appreciated investment portfolio

Unlike a home, an investment portfolio doesn't allow us to enjoy the experience of bringing our first child home to it; of watching the height measurements of our kids grow ever higher on the kitchen wall; or, to remember the many anniversaries and birthdays we've shared with our families and friends over the years in it.

Without an emotional attachment and real enjoyment being derived from it, we tend not to love or care about our portfolios in the same way. But if we can't exactly love them, we can – and should – nonetheless appreciate them for the wealth that they can create for us, wealth that ultimately works to support the achievement of our goals. Because, despite our widespread belief that our home values grow faster than our investments, as the chart to the left shows, the equity market's long-term return significantly outpaces that of homes in all major markets across the country – in some cases as much as doubling it.

Foundations of wealth

Your principal residence is where your heart is – but shouldn't necessarily be seen as your sole "principle" investment. Seeing your home this way can ignore significant risks, including the high costs of ownership (e.g., financing, taxes, upkeep and repairs). As well, a home is an illiquid asset, which can represent a real risk if you need to remove your equity at a certain time. Equities, while historically providing stronger long-term returns, also have their own associated risks and costs which need to be considered, including volatility. But, when taken together, the virtual "bricks and mortar" of your investment portfolio can work together with the actual bricks and mortar of your home to build the foundations of your wealth.

To learn more, please contact us today.

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