RBC Dominion Securities Inc.

Wealth Management REVIEW

Wealth Management
Dominion Securities

www.rbcwealthmanagement.com | July 2017

In brief

When we invest in youth great things happen

To help celebrate Canada's 150th birthday, we gave thousands of young Canadians $150 and challenged them to make it count. See their stories at: **rbc.com/make150count**

Reduce your paperwork with eDocuments

Securely view your RBC Dominion Securities account statements, trade confirmations and other documents online, instead of receiving them in the mail. Switching is easy – simply contact your advisor to learn more.

Top-ranked services to help meet your financial goals

We're honoured to be ranked Canada's leading bank-owned wealth management firm for the 10th year in a row in the 2017 Brokerage Report Card published by *Investment Executive*.

The benefit of the doubt

By Jim Allworth

As we glide into the summer holidays, we would all like to be able to put our investment and economic concerns to bed for a few weeks or months. As usual, it is far easier to come to terms with the long-term outlook for the economy and equity markets. The short term always seems worrying.

The long term needs the answer to only one question: Is a recession on the horizon, in particular a U.S. recession? The answer, as it has been for almost eight years, is "no." And the changes that would cause us to alter that view are, so far, giving benign readings.

Importantly, credit conditions remain constructive. Central banks everywhere in the developed world continue to run "easy money" policies and banks are looking for creditworthy borrowers. Typically, both the cost and availability of credit become noticeably restrictive before a recession gets underway. In our judgment, getting from here to there will take considerable time.

It has to be noted that the monetary backdrop has begun to change. The Fed is raising rates, albeit very slowly. Most central bankers have stopped talking about further rate cuts.

The Fed has said it will begin slowly shrinking its balance sheet later this year, which should put moderate upward pressure on long-term interest rates. Meanwhile, the European Central Bank is expected to further scale back its bond-buying program from its current pace of 60 billion euros per month. So, one can argue global monetary conditions are gradually normalizing, if not tightening. But it's "early days" and, in our view, outright restrictive conditions are some way off.

One very reliable indicator of whether a recession is immediately ahead is the unemployment rate. It rarely changes trend: moving steadily higher while the economy is in recession and falling throughout an expansion. Today, the U.S. unemployment rate (see chart) is at 4.3%, close to a 50-year low. Canada's unemployment is trending similarly.

Since WWII, once the trend in unemployment turned higher,

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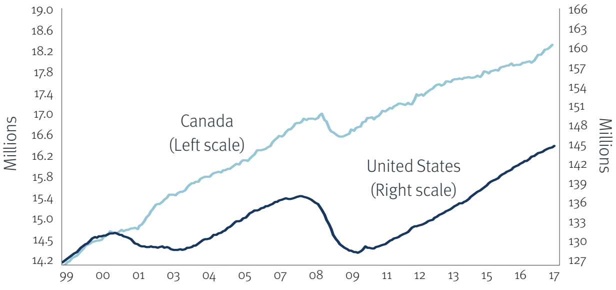
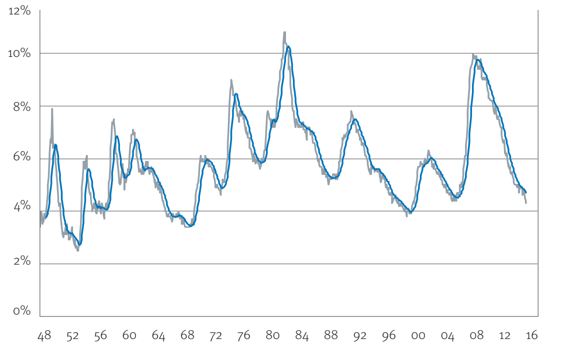
Employment



U.S. unemployment rate – 12-month moving average



On average the unemployment rate 12-month moving average turns higher four months before a recession begins. Sources: U.S. Labor Department; Statscan

the start of a recession was only a few months away. Currently it would take significant deterioration in employment data to deliver such a trend change, probably several months of outright job loss. Not impossible but so far unlikely.

Getting the recession call right matters because U.S. recessions have always been associated with bear markets for stocks. Absent compelling indications that an economic downturn is close, we choose to give equities the benefit of any doubt.

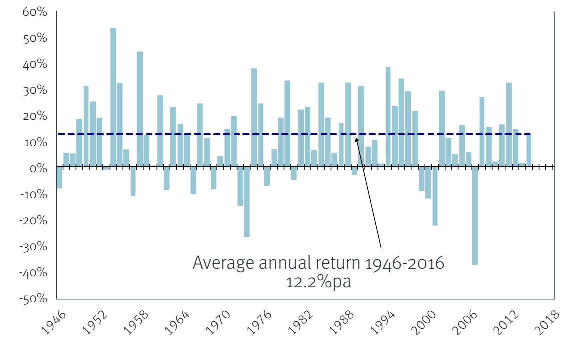
As usual, the short term looks more problematic. Today for U.S. investors, two issues rise above the constant political noise: the U.S. economy's apparent inability to move beyond 2% growth and stock market valuations that appear stretched.

Investors are confounded by a U.S. stock market that keeps on rising – the S&P 500 price/earnings multiple has moved from 15x at a correction low in early 2016 to about 20x today – even as earnings have barely moved higher over three years and the economy has stubbornly refused to shift out of second gear. The index is up 9% year-to-date and 35% over the past 17 months.

Paradoxically, the Canadian economy has developed unexpectedly strong momentum and earnings have improved but the TSX has lost 1% so far in 2017.

P/E multiples tell you almost nothing about where the market is headed next or even over the next year. Low P/Es can go distressingly lower and already high ones stretch dizzyingly higher. There are no reliable "lines in the sand."

S&P 500 Annual returns



Source: RBC Dominion Securities

Last year, the total return delivered by the S&P 500 (dividends plus price appreciation) was, quite unusually, almost dead-on the 12.2% per annum long-term average since the end of WWII. A glance at the chart shows that determining whether this year or next year are likely to be up or down, or above or below average, is not much better than a coin flip.

And inside the annual results shown here there is plenty of intra-year volatility. Corrections are a fact of investing life and while it always looks, after the fact, like they happen for reasons that should have been seen looming in advance, in our experience that is largely an illusion born of hindsight.

We expect there will be at least one correction of note before we get to the next "bear market" for stocks, probably more than one. But it would be less than forthright to suggest that spotting its arrival or extent correctly would be anything more than accidental.

For now, enjoy the summer weather content in the knowledge that the factors which normally make equities the best-performing asset class over reasonable holding periods remain intact.

For more thoughts on the prospects for financial markets, ask for our July issue of *Global Insight*.

Jim Allworth is co-chair of the RBC Global Portfolio Advisory Committee.

Giving and inheriting wealth across generations

Four key insights from the Wealth Transfer Report 2017

One of the greatest transfers of wealth in history is currently underway, with an estimated $400 billion being passed down to inheritors in Canada within a generation.

Transferring wealth across generations is a concern shared by many families. How can you protect your wealth for your family? How can you prepare your family to receive their inheritances? And, if desired, how can you ensure your family legacy continues beyond just one generation?

To help answer some of these questions, we undertook an in-depth study on how well prepared families are to give and receive inheritances. We interviewed over 3,100 people who are concerned about wealth transfer.

What we learned is that many families can do more to prepare the next generation through formal financial education, family discussions and comprehensive wealth transfer planning.

1. Start financial education early

Getting a solid financial education early is one of the key factors in being prepared to inherit wealth. Our wealth transfer survey showed that the earlier a family member receives their financial education, the more confident they are in their knowledge of wealth. Two-thirds of respondents who started their financial education before the age of 18 rated themselves as confident, compared to 58% who started ages 18-35, 49% who started ages 35-55 and 41% who started ages 55+.

Yet the survey also showed that people don't start receiving their financial education on average until age 27. One of the main reasons is simple procrastination: 35% of respondents intend to educate their children about wealth but have yet to start.

The lesson? It's never too soon to start educating your children about financial matters – and the earlier you start, the more confident your beneficiaries will be about managing wealth. Consider starting early with the basics, such as budgeting, saving through bank accounts, and understanding investment fundamentals.

2. Provide more structured education

Starting financial education early resulted in greater confidence about financial matters. However, how that financial education is provided is also important. Our survey found that the most common way inheritors learn about wealth and money is through general family conversations over the course of their lives. The least common: formal financial programs offered by professionals. But respondents rated this type of financial education as most effective (79%), compared to family meetings (65%) or general family conversations (60%).

3. Discuss your intentions in advance

Most often, people receive their inheritances without having a discussion with their benefactor in advance. According to our survey, only 35% of respondents had a discussion and, when they did, it usually concerned the value of the inheritance (73%). Far less often, benefactors discussed key points like what to do with the wealth (33%), how the wealth will be transferred (29%) or who could help manage the wealth (15%).

Many survey respondents noted that they would have appreciated more upfront discussions about key points like these, to reduce misunderstandings between family members and better prepare them to receive their inheritances.

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Without this preparation, all too often, inheritors end up making poor financial decisions, jeopardizing the family legacy.

4. Create a comprehensive wealth transfer plan

When it comes to planning the wealth transfer, 54% have taken the important first step of creating a Will, while another 26% have gone to the next step and created a full wealth transfer plan, including a Will. A surprising one-third have done nothing at all.

Creating a full wealth transfer plan has many benefits. Those who have created a full wealth transfer plan report greater confidence that the next generation will sustain their wealth (58%) versus those who done no preparation (33%). What's more, having a full wealth transfer plan can help preserve the value of the estate, minimize family conflict during an emotionally difficult time, and ensure your wishes are carried out as you intended.

Creating an up-to-date Will, considering any testamentary trusts, determining power of attorneys and naming executors are all key steps.

But that's just a start. The following may also be valuable tools: creating family trusts to transfer wealth during your lifetime, preserving your estate value using insurance-based strategies, providing financial education opportunities to beneficiaries, navigating blended family situations, planning for a family business succession, establishing philanthropic endeavours, and so on.

For more information about wealth transfer planning, please contact your RBC Dominion Securities advisor.

Interest rates applied to account balances as of June 22, 2017*

	Canadian dollar accounts	U.S. dollar accounts
All credit balances	0.05%	0.05%
Debit balances under $10,000	4.70%	6.50%
Debit balances $10,000 – $24,999	4.45%	6.25%
Debit balances $25,000 – $49,999	4.20%	6.00%
Debit balances $50,000 – $99,999	3.95%	5.75%
Debit balances $100,000 and over	3.70%	5.50%
All debit balances for registered accounts	4.70%	6.50%
All credit balances for registered accounts	0.05%	0.05%

The interest rates that will be in effect for debit balances in cash and margin accounts fluctuate with the Royal Bank prime rate as follows:

Debit balances	Canadian dollar rates†	U.S. dollar rates†
Under $10,000	CAD Prime + 2.00%	USD Prime + 2.25%
$10,000 – $24,999	CAD Prime + 1.75%	USD Prime + 2.00%
$25,000 – $49,999	CAD Prime + 1.50%	USD Prime + 1.75%
$50,000 – $99,999	CAD Prime + 1.25%	USD Prime + 1.50%
$100,000 and over	CAD Prime + 1.00%	USD Prime + 1.25%

† Based on Royal Bank prime rates as of June 22, 2017. CAD Prime = 2.70% and USD Prime = 4.25%. Rates are subject to change.

* RBC retains the right to change interest rates on a discretionary basis. A committee comprised of individuals representing various authorities within RBC Dominion Securities administers these interest rates. These rates are adjusted from time to time based on various factors, including, but not limited to, competitive analysis, Bank of Canada and other bellwether rates and/or cash rates. Interest amounts less than $5 are neither charged nor paid on regular accounts, and interest amounts less than $1 are neither charged nor paid on special product accounts. Rate changes of less than 1% will be processed on the 22nd of the month. The average daily cash balance for the month determines the tier that will be used to establish the rate. For interest rates on balances other than CAD or USD, speak to your advisor, or go to www.rbcds.com/cash-margin-rates.html.

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