Michie Wealth Management's Quarterly Investment Update

Wealth Management
Dominion Securities

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Saving For Retirement Is Easy – Try Spending It

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"We build our business on integrity and service. The highest compliment we can receive is the referral of friends, family and business associates. Thank you for your Trust."

Retirement – when pensions replace salaries, RRSPs become RIFs, and you begin to worry your golden years will be spent figuring out how to spend your nest egg. Here are some tips to help.

How can you replace the steady cash flow of a salary?

Before retirement, you may be paid bi-weekly or monthly for your services, and you address the mound of bills on your kitchen table. After you retire, passive income and government benefits trickle in only monthly, quarterly or even annually. The reality: bills don't care that your dividends come once a quarter. Fortunately, there are several ways to smooth your cash flow in retirement:

- Consider life annuities, which provide guaranteed income payments for the rest of your life and can be paid out monthly.
- Create a comprehensive financial plan that budgets your cash needs and determines a reasonable reserve for any intra-month or unexpected expenses.
- Ladder your dividends to provide smooth income.
- Schedule withdrawals from your RRIF, TFSA, non-registered accounts, etc. to replicate a regular paycheck.

Which account should you withdraw from first?

An effective withdrawal strategy is unique to you and considers your age, other sources of income, asset allocation and tax minimization.
That said, there are rules of thumb that can help:

- Withdraw from the least flexible sources of income first (eg. Locked in plans)
- Draw down on assets that trigger the least amount of taxation and maintain your registered accounts that can continue to grow on a tax free basis

How are your investments spent once you're gone?

When the day comes, there's a question we can all ask: how can I take care of my family and legacy with my remaining assets in a tax-efficient way? If you have a spouse, it's easy. Most assets that aren't already jointly owned can roll over to your partner on a tax-deferred basis. But when transferring assets to your children or other beneficiaries, it gets more complicated. At death, there us a "deemed disposition" of all of your assets. In other word, the CRA treats our investments as if our last words were "cash out my RSP and sell the house." Any accounts held on a tax-deferred basis – RSP, LIRA, RRIF, etc. are fully taxable. While investments in non-registered accounts and assets like your home are treated as if they are sold at fair market value, triggering capital gain and losses.

As intimidating as wealth transfer can be, there are many strategies to minimize estate taxes. It starts with an estate plan, which can include using insurance to create tax-free benefits, gifting assets to family while you're alive, or donating investments to registered charities.

Disruptive Technology: Growth, Opportunity and Risk

There's barely an industry of part of our lives that hasn't been affected by new technology. Smart phones, online shopping, artificial intelligence and self-driving cars are just a few of the seemingly endless ways technology has changed the way we live, work and communicate

From an investor standpoint, there isn't really a period of time that investors can look back and say "We've seen this exact thing before." Yet, virtually every industry has been affected by disruptive technology at some point in the past, and in general, disruption ultimately drives growth and brings new opportunity, but it can also bring an element of risk that must be accounted for in portfolios.

Disruption drives growth

It's easy to see the downside risks of technological disruption. Certain jobs are often lost and industries can disappear entirely. However, more often than not, disruption leads to new services and products, better efficiencies, and from an investor standpoint, helps drive long-term growth.

For example, over the last 150 years, the farming industry has seen horses replace manpower, tractors and mechanization replace horses, and farming techniques, year-round growing and fertilizers improve yields per acre. Today, these disruptions help Canadian farms produce more food than ever, including nearly 40 times more wheat and 44 more potatoes than they did in 1867. Today's Canadian farmers are also producing a wider variety of foods than ever before, and doing so with tremendous efficiency when compared to the past.

Disruption drives opportunity

While farming has not escaped the downside of disruption – lost farm jobs – technological advances have helped spawn and grow industries in areas such as food processing, storage and transportation, equipment manufacturing and fertilizer production.

Today, virtually every industry is undergoing change due to technological disruption, including:

- Automobiles – driverless and electric cars
- Retail – ecommerce and the decline of the mall
- Energy – renewables and batteries
- Finance – fintech, robo-advisors, peer-to-peer lending and crowd sourcing

The sharing economy and internet mobility are also affecting everything from travel, hotels and restaurants to the real estate, media and communication industries.

Protecting your portfolio

For investors, diversification remains the first line of defence when navigating an evolving market. Headline-grabbing stocks, or investing in a single disruptive sector, such as marijuana or bitcoin, may put your portfolio at unnecessary risk. On a similar note, failing to adjust your portfolio as your blue-chip companies of yesterday are faced with major disruption, could result in an equally unnecessary risk.

In addition to diversification, investors may consider avoiding industries which face too many disruptive headwinds, or step lightly into them. It will also continue to be important to invest in the highest-quality companies, rather than the "hottest" stocks or industries. Finally, quality management today must also include those who are open to new ways of competing and prepared to transform their business to remain competitive.

For more information, please ask us for a copy of our Global Insight article on disruptive technologies: Fast track to the future.

UPCOMING EVENTS

What To Expect From The Markets?

May 15th
6:30PM – 8:00PM
Oshawa Golf & Curling Club
160 Alexandra Street
Oshawa, Ontario

Please RSVP to Paula Austin at paula.austin@rbc.com or 905-434-6611.

Seating is limited and we encourage you to respond early.

A Rough Ride Back to Normal

Please see some highlights from a focus article included in the Global Insight March Edition. If you would like to read the full article, please feel free to contact us for a copy or access it through our team website (www.michiewealth.com) under the "Client Resources" section.

Equity markets had been so calm for so long, so investors can be forgiven for forgetting how a "normal" stock market behaves. The rough ride of the last few weeks has taken some excessive valuation and investor complacency out of the mix. But it is unlikely to have any noticeable effect on the global economy or on the encouraging corporate earnings outlook. The correction may have further to run, but we expect new highs and a resumption of the long-term bull market later in the year.

Dissecting the correction

But what triggered the downturn? And was the sharp advance in the market's P/E multiple up into the January peak justified? Probably not is the answer to the second question, at least not over so short an interval.

The most widely cited trigger for the stock market downturn was a US Labor Department report that showed the average hourly earnings in the manufacturing sector had unexpectedly surged, raising the spectre of an increase in inflation and even higher bond yields and therefore lower P/Es. As we have noted, the resulting market decline quickly became self-reinforcing and self-fulfilling despite the fact the hourly earnings surge was quickly assessed by some as extreme-weather aberration.

We think there is more to the story. Two things are usually pointed to as factors that can provoke a change in P/E multiples. One would be a change in the discount rate (the 10 year US Treasury yield) used to calculate the present value of future earnings – the lower the discount rate the more future earnings are worth today, justifying a higher P/E ratio. So, when the 10-year yield moved sharply higher from a depressed 2.06% in September to a chunky 2.70% in January, one would have expected the P/E multiple to move down. Instead, it moved higher, from 17.4x to 18.4x 2018 estimated earnings.

The other factor that could argue for a change in the market's P/E ratio would be a shift in the long-term average growth rate of S&P 500 earnings per share. In this case, many investors believe that tax cuts have unleashed an increase in the long-term growth prospects. We are not convinced.

So far, what we know for sure is that the reduced tax rate should boost after-tax margins by an equal amount to the tax savings in 2018 and that American companies should be able to sustain that improvement through 2019 – corporate managements have said as much. Beyond that is much murkier.

For now, we know about as much as we can know about what earnings should be reported this year and next. CEOs in the US have given forthright guidance about what effect tax cuts will have on the bottom line and about their enthusiasm for the business outlook. We expect it will be at least 6 months, probably longer, before events could conspire to seriously challenge RBC Capital Markets' upbeat view that has S&P 500 earnings per share rising by 17% this year to $155, and by a further 7% to $167 in 2019.

Fallout shelter

Worries that the recent market volatility will produce economic fallout are misplaced, in our view, and in the view of Fed Chairman Jerome Powell, who stated in his recent congressional testimony that the Fed believes the market gyrations will have little or no effect on the course of economic growth. Our recession indicators, several of which typically give long advance warning of an impending economic downturn, are all still giving firmly positive readings.

Outside of the US, German business confidence is at a 30-year high. Confidence across most of the Eurozone is similarly elevated. Japan, China, and India all seem to be thriving, ad is Canada despite concerns about the potential for adverse trade and NAFTA outcomes.

But this correction could have further to run before a sustainable turn higher can get underway. Very often, market downturns that feature some panic selling, as this one did, go on to rally for a while before subsiding into a retest of the lows over some weeks or months – enough time to allow for complacent optimism to give way for pessimism and concern.

That may or may not be the course the markets follow this time, but when the longer-uptrend does eventually get re-established, we expect the slope of the advance will be somewhat shallower and less of a straight line that what investors have become used to over the past two-and-a-half years.

No sign of a U.S. recession on the horizon.

Recession scorecard

Start of recession	Yield curve	Inflation trends	Labor market	Credit performance	ISM Mfg.	Earnings quality	Housing market
Nov '73	↓	↓	↓	↓	↓	–	↓
Jan '80	↓	↓	↓	↓	↓	–	↓
Jul '81	↓	↑	↑	↓	↓	–	↓
Jul '90	↓	↓	↓	↓	↓	↓	↓
Mar '01	↓	↓	↓	↓	↓	↓	↔
Dec '07	↓	↓	↔	↓	↓	↓	↓
Present	↑	↑	↑	↑	↑	↑	↑

Key: ↓ Recessionary ↑ Expansionary ↔ Neutral

Note: Past performance is not indicative of future performance
Source - RBC Wealth Management's national research correspondent as of 3/1/18

In The Community

Both Nick and Jason are active members of the Launchpad Committee, a group of young leaders committed to helping the health of the community through support to the Lakeridge Health Foundation. On April12th, Launchpad hosted their second annual Nightshift event where teams are matched with a medical professional to test their resolve in a medical emergency simulation.

The Durham Regional Police Association took this year's generosity to a new level by committing to match every dollar raised up to $10,000! After an evening of great fun, Nightshift successfully raised **over $27,000** with funds directly benefiting the paediatric department of Lakeridge Health.

We are ecstatic to be part of such a great cause and look forward to great success in our upcoming events!

Welcome Back!

We would like to welcome Candice Goodbrand back to our team! Candice is returning to her role as an assistant, coming back from her maternity leave spent with her two sons Mavrick and Nixon.

Thanks very much to Cassandra Gillen who provided coverage for our team during Candice's absence. Cassandra joined us as a recent graduate from Durham College and will be continuing her career with RBC Dominion Securities. We wish Cassandra all the best!

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