Wealth Management
& Capital Markets Perspective

Wealth Management
Dominion Securities

For the clients of Grimes Handscomb Asset Management of RBC Dominion Securities | Winter 2021

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Why investing in bonds still makes sense despite historically low interest rates

With the exception of a few spikes, over the last 35 years interest rates and bond yields have steadily declined. The recent efforts by central banks to spur borrowing to drive economic growth during the COVID-19 pandemic has pushed yields to their lowest levels in history, leading many investors to wonder if bonds are still effective in helping them achieve their portfolio goals.

The bonds that bind

One of the three major investment asset classes (along with equities and cash), bonds have existed in one form or another for hundreds of years. With their dual income structure of fixed interest payments and the return of capital at a stated maturity date, bonds have historically been very attractive to investors seeking income and security.

Bonds are issued by a variety of entities, including corporations and various levels of government, and in a wide variety of forms (e.g., standard, high-yield, convertible). They also offer various maturity dates over different timeframes. Generally, the longer the timeframe (e.g., a 10-year bond), the higher the interest rate, but the higher the price volatility (which means the price at which you could sell a bond prior to maturity has more variance).

In addition, issuers and the various types of bonds they issue are often rated by bond rating agencies, providing investors with guidance around their riskiness, i.e., their ability to maintain their interest payments and repay principal at maturity. This allows investors to decide on the degree of risk they are willing to assume, while gauging the performance of different issuers and bond types under different market conditions.

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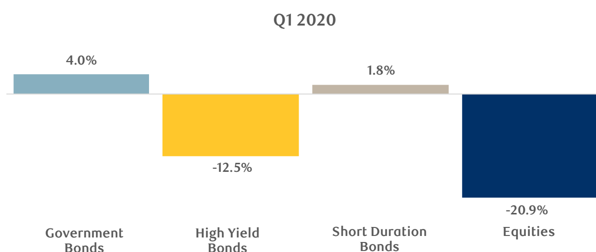
Portfolio ballast – three reasons to maintain bonds in your portfolio

Despite the historically low yields bonds are offering these days to investors, there continue to be very important reasons to consider them in your portfolio, including:

1. **Stability:** With their more predictable and less volatile returns, bonds are an important ballast to an investor's portfolio during times of volatility. When trouble strikes, bonds can help to reduce the risk – or volatility – of portfolios.

Government bonds provided a ballast during the COVID-19 sell-off



Short duration bonds = FTSE Canada ST Bond Index, equities = S&P/TSX Composite TR, high yield bonds = ICE BofA U.S. High Yield BB-B (CAD Hedged), government bonds = FTSE WGBI Hdg CAD. Source: Morningstar Direct.

2. **Diversification:** Bonds tend to have a negative return correlation to equities – when equities rise, bonds tend to fall, while they tend to rise in value when equities fall.
3. **Income:** While interest rates and yields may be low these days, there is a vast universe of bond issuers and bond types. When the risk is managed properly within a diversified portfolio, there can still be higher-yielding options for investors who need income and/or wish to generate income to offset weaker capital returns in their portfolio.

Some bonds should never be broken

Regardless of today's historically low interest rate environment, bonds can continue to play a critically important and effective part in protecting, diversifying and growing investors' wealth.

Around the world

Global markets

Equities achieved all-time highs to end 2020, driven by optimism that the pandemic will end soon and that global economic growth is building. Ultra-low interest rates, continued fiscal and monetary stimulus, and pent-up consumer and business demand underpinned valuations. Expectations were tempered by concerns over the pace of vaccinations, ongoing U.S. political challenges, and high global borrowing levels.

Canada

Per capita, Canada has contained COVID-19 better than the U.S. and many other wealthy countries. While this has meant more short-term economic pain, higher growth is expected in 2021, underpinned by continued stimulative fiscal and monetary policy. A full recovery of pre-pandemic GDP levels by late 2021 / early 2022 is likely, with risks to this outlook being high government and consumer debt.

United States

The pandemic continues to take a huge toll. New measures to control its spread threaten the steady economic growth since the initial spring lockdowns. But government and central bank stimulus, and the arrival of vaccines, provide hope for an economic rebound in 2021. The incoming Biden administration may also support growth by focusing on bipartisan efforts to stimulate the economy.

Europe

A COVID-19 resurgence is leading to renewed lockdowns and restrictions. While these measures will dampen economic growth, there is hope that European economies will benefit from higher global demand and travel as the pandemic comes under control. As a result of its messy "Brexit," the U.K. remains a concern despite striking a new trade deal with the European Union at the 11th hour.

Emerging markets

For 2021, the growth outlook continues to improve for China and India, though for different reasons. China continues to ably manage the virus and has exceeded expectations at every turn. For India, it is instead because of a significantly lowered 2020 outlook for the country, with the implication that any 2021 rebound can be significantly more vigorous.

How the U.S. election affects Canada-U.S. trade

The 2020 U.S. election saw incoming President Joe Biden's Democrats gain control of Congress by maintaining their majority in the House and winning back the Senate. The new balance of power in Washington is important when it comes to trade policy – and could have a major impact on Canada since the U.S. is by far our largest trading partner.

New "trade winds" stirring

The election campaign saw a number of policies floated by the Biden team, including broad-based environmental and healthcare programs, as well as enhanced regulation of "Big Tech" companies like Google and Facebook.

The Biden administration will likely pursue at least some new policies on trade, and this is crucially important for Canada, which sends approximately 75% of its exports in goods and services to its southern neighbour. After the trade actions of the previous Trump administration – including the imposition of trade tariffs on Canadian aluminum, lumber and other products and services, as well as the renegotiation of the North American Free Trade Agreement – what's in store with a Biden presidency?

1. **Climate change:** Biden has promised to rejoin the Paris Agreement and to reduce greenhouse gas emissions to a net-zero level by 2050. This policy approach suggests that his administration may take action on increasing green- energy production and reducing carbon-based emissions. This might have a significant impact on the Canadian energy sector, including whether or not the Keystone XL pipeline project to expand oil exports to the U.S. goes ahead. The Canadian auto sector might also be affected by the Green New Deal, for example shifting demand to battery-powered vehicles. The U.S. focus on "green policies" might also spur development of related industries in Canada, driving up exports.
2. **Made in America:** On the campaign trail Biden often referred to the need "to ensure the future is made in America," raising concerns that Canadian companies might be shut out of government procurement spending – or worse. The close-knit nature of the two country's manufacturing supply-chains is likely to preclude a policy like this from affecting Canada again, but it does remain a possibility.
3. **Make America friendly again:** In a departure from the Trump administration's approach, global trade institutions like the World Trade Organization are likely to be re-cast as key partners instead of adversaries in a Biden administration – and this is good for Canada, the significantly smaller of the two countries. It also signals a more constructive approach to trade and alliances in general by the U.S.

While it remains to be seen how the new Biden administration's trade policies will specifically affect Canada, one thing's certain: given the size of our trading relationship, Canadians will be keeping a close eye on shifting trade winds.

Administrative corner

Tips to streamline your tax reporting:

- Tax slips will be mailed beginning in early February until approximately the end of March. In addition to your tax slips, your tax package will include your fee summary, gain / loss report and foreign property summary.
- Please provide the tax package in its entirety to your accountant. If you would like your accountant to receive a duplicate copy of your tax package, please let us know.
- For a more efficient and environmentally friendly option, consider switching to eTax. With electronic delivery, you'll receive your tax package securely via WM Online, saving time and paper. To learn more about this option, please contact us directly.

RBC Dominion Securities – Tax reporting schedule	
RBC DS completes all tax reporting by	March 31, 2021
Important personal tax deadlines	
Personal income tax installments	March 15, 2021 June 15, 2021 September 15, 2021 December 15, 2021
Personal income tax return filing	April 30, 2021
Self-employed income tax return filing	June 15, 2021
Balance owing for taxes payable	April 30, 2021

TFSA and RRSP information

TFSA information	
Maximum annual contribution limits	$5,000 each year 2009 - 2012 $5,500 each year 2013 - 2014 $10,000 for 2015 $5,500 for 2016 - 2018 $6,000 for 2019 - 2021
Maximum contribution limit since inception	$75,500 from 2009-2021, if born in 1991 or earlier and eligible resident of Canada during those years
RRSP information	
RRSP maximum annual deduction limit	18% of the prior year's earned income to a maximum of: $27,230 for 2020 – deadline March 1, 2021 $27,830 for 2021 – deadline March 1, 2022

Benchmarks

Equity market 12-month trailing return (for month ending December 31, 2020)	
S&P/TSX composite total return index	5.6%
S&P 500 total return (C$)	16.1%
S&P 500 total return (U$)	18.4%
DJIA total return (C$)	7.6%
DJIA total return (U$)	9.7%
Nasdaq composite price return (C$)	40.8%
Nasdaq composite price return (U$)	43.6%

RBC CM Canadian bond market indices 12-month trailing return (for month ending December 31, 2020)	
Short-term index	5.3%
Intermediate-term	10.1%
Three-month T-Bill (C$)	0.8%
Three-month T-Bill (U$)	0.7%

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