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Financial Focus

Wealth Management
Dominion Securities

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Dear Clients and Friends,

Welcome to summer, my favorite time of year!

Let's reflect back on what has happened in the financial markets in the first six months of 2019. The year started off with a significant rebound from the December lows and investors were rewarded with gains until the end of April. May brought us more "Trump-disruption" as the U.S. – China trade negotiations deteriorated which resulted in short-term market losses for the month.

Our RBC analysts are optimistic that the U.S. and China will come to an agreement because they need each other. They are tied at the hip when it comes to international trade and it is in everyone's best interests to resolve this dispute and get back to business. We do believe a trade deal will be signed at some point because the two power nations have a lot to gain from it. It is important to remember that we will not allow day-to-day tweets from the White House to be the reason for investment strategy changes.

What about the recession risks? We are continuing to monitor risks of the U.S. moving into a recession over the next 1-2 years. I remind clients that the definition of a recession is two consecutive quarters of negative economic growth and can happen towards the end of a business cycle. Our RBC analysts feel that we are in the "late stage" of this market cycle, which is different than the "end stage". We have seen the yield curve invert this year, which means that short-term interest rates are higher than long-term rates, and this can be a sign of a coming recession. However, all of the other indicators that RBC is monitoring are currently not showing signs of a recession, including the current 50-year low in the U.S. unemployment rate. If more of those indicators start to change, then we will receive this information from our RBC Portfolio Advisory Group and will recommend changes to investment portfolios accordingly.

As I continue to remind clients, it is important to keep a long-term perspective with your investment portfolio. Trying to figure out what the market is going to do today or even next week is an impossible task and one that is not helpful in creating long-term wealth. Volatility also reinforces the value of diversification and the role of fixed income investments in client portfolios. Even with low interest rates, the primary role of fixed income in a balanced portfolio is diversification and reduced volatility from equities.

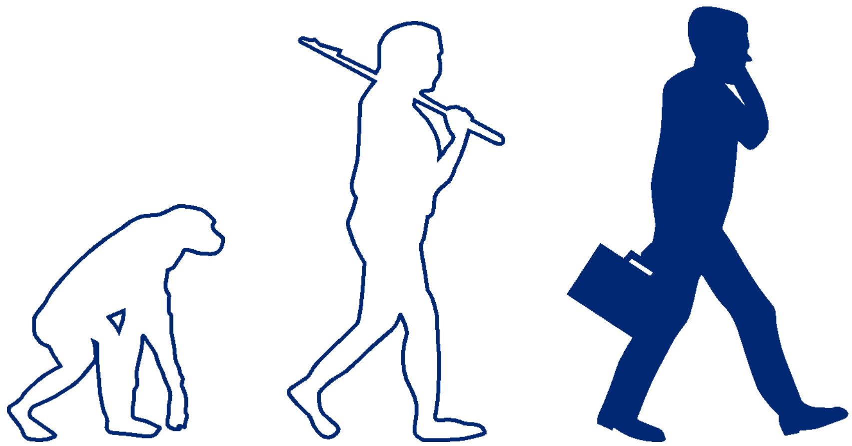
As always, I welcome any questions or comments.

Have a safe and happy summer,

Sandra

The evolution of the investor

Developed over tens of thousands of years, the deeply ingrained instincts that kept us alive for so long now often work against us as investors. But there is hope for us yet.



Surviving in a woolly mammoth world

In one form or another, humanoids have roamed the Earth for over two million years, slowly developing into what we call Homo Sapiens over 300,000 years ago. It was a precarious existence for our ancestors, having to survive in a hostile world with multiple threats, including animals, disease, the elements and each other.

Learning to play well with others

To survive, we developed key instincts, such as the all-important fight-or-flight. Sizing up a one-on-one with an ornery woolly mammoth, your instinct would likely (and wisely) have tended towards a flight to safety. But backed by 50 of your spear-wielding mates? That same beast was a tempting dinner.

So, we began to realize that there was “strength in numbers,” and that it was better to fit in with a tribe than to be on the outside looking in. We came to rely on the tribe for our survival.

Ancient instincts, common investment pitfalls

Gradually, mankind developed laws, policies and regulations – and the institutions to enforce them – to help eliminate many of the ancient threats to our survival.

But the same instincts we honed to survive can cost us when it comes to investing:

- **Fight-or-flight:** Research has consistently found that, due almost entirely to emotional reactions during periods of market stress that resulted in poor timing decisions, the annual return of an average investor over 20 years was significantly lower than that of the S&P 500 Index, and resulted in a difference of $120,000 on an initial investment of $100,000 (Dalbar, 2017).
- **Herd mentality:** Evidence shows that investors “follow the herd,” consistently buying high and selling low, which can hurt portfolio performance over the long term. As equity markets were soaring in the lead-up to the financial crisis of 2008/09, so were equity fund sales. And following the crisis when equity markets tumbled, Canadians redeemed their equity funds (IFIC, Morningstar, 2018).
- **The tribal grapevine:** Listening to the (unqualified) press – who are often rewarded for generating alarmist content – and friends and family for your investment information is fraught with risk. And, it is extremely difficult for even qualified forecasters to accurately predict where markets will go in the short term, and no forecaster has insight into your unique situation.

Homo Investorus: hope for the modern-day investor

Today’s investors have the benefit of research, expertise and well-regulated markets. A well-structured and thought-out plan based on your goals and risk tolerance is the best way to control your ingrained survival instincts and keep on track. Strategies such as regular investing can help us avoid emotional decisions based on short-term market movements. The first step to being a modern day – and successful – investor is to quell the caveperson within us. And, to find safety and security in the fact that, those who stand their ground against the real investment woolly mammoths are most likely to achieve their goals.

Recession-proof your portfolio with the three Rs

What do you do with your investment portfolio when you hear the infamous “R” word – recession? It’s easy. Just follow the three Rs: review, rebalance and relax.

In recent months, economists have been cutting their growth forecasts for the Canadian and global economies. While evidence of a slowdown is mounting[1], it is notoriously difficult to predict – economists have failed to predict 148 of the last 150 recessions[2]. The dreaded “R-word”, recession, is the economic term for two or more consecutive quarters of zero or negative economic growth (as measured by Gross Domestic Product). It is often trotted out when growth begins to moderate, but historically is rarely the outcome of such a slowdown, despite predictions to the contrary.

Recession: the nasty nine-letter word

Unfortunately, talking about a recession is one of the best ways to bring one about: hearing the “R” word, people begin to delay or abandon spending in anticipation of an economic slowdown[3]. This leads to a vicious circle: lower spending leads to lower business revenue, which leads to job losses, further worry, lower spending, more job losses and so on.

“R”-proofing your portfolio

Soaring or falling markets often generate strong emotional reactions, prompting investors to veer off course from their long-term plans. This can lead to common investment pitfalls like taking inappropriate risks, buying high and selling low, and moving to “the sidelines” (i.e. cash), thereby missing out when the markets recover.

Similarly, reacting to the “R” word by altering your investment plan is rarely the right move. Instead, investors would be well served to follow three other “R” words:

- **Review:** Wondering whether your goals are aligned with your investment portfolio’s asset allocation and structure? Whether your risk tolerance is accurate?

  These are important questions and concerns to review with your advisor as your financial circumstances or goals change. But keep in mind that a recession is usually a short-term event, and that your investment portfolio usually reflects goals that stretch over a longer time horizon – so, changing it in response to short-term developments is rarely advisable.

- **Rebalance:** Your portfolio should be balanced in the right way to meet your goals and to reflect your appropriate risk tolerance. If your portfolio has drifted off-balance over time due to market movements or other factors, or your goals or circumstances have changed, speak to your advisor to review your portfolio to see if it needs to be rebalanced.

- **Relax:** Once you’ve reviewed your portfolio, and rebalanced as required, you can relax with confidence.

Remember, the average recession lasts six to nine months, and the impact is usually quick and transitory – making hasty, unwarranted changes to your portfolio is usually not.

[1] *Economic and Financial Market Outlook*, RBC Economics Research (March, 2019).
[2] *How Well Do Economists Forecast Recessions?*, International Monetary Fund, Zidong An; João Tovar Jalles; Prakash Loungani (March, 2018).
[3] *A reliable indicator of an imminent recession? Look to the pundits,* David Parkinson, The Globe & Mail (February, 2019).

Seven tips for choosing your executor

The person you name as your executor has a very important responsibility – settling your estate according to your wishes. By naming someone as your executor, you may believe you are honouring them. However, you are also giving them numerous duties – not to mention a potential personal liability. That's why it's important to carefully consider who you choose as your executor.

In their Will, people often name the person closest to them to be their executor – they trust them to understand their wishes and to handle their beneficiaries appropriately. But the best person for the job may not be the obvious choice. Here are seven things to consider when choosing your executor:

1. Can they handle family dynamics?

Often, there is family conflict when an estate is being settled. This is especially true when you're transferring wealth from one generation to the next, or if you have children from multiple marriages. What's more, it can be an emotionally charged time – people are often not thinking straight, which can lead to misunderstandings.

When deciding on an executor, look for someone who is fair, diplomatic and able to manage complex family dynamics. Your executor may need to explain why you made certain decisions in your Will, and gently encourage family members to respect your wishes. If there's a dispute, they may also need to act as a mediator.

2. Are they savvy about financial issues?

Being an executor is a bit like being a financial advisor, accountant and lawyer – all rolled into one. Your executor doesn't necessarily need to be an expert in all these areas, but should be knowledgeable enough to deal with them, and know how to access experts when required. Consider naming an executor who is detail-oriented, has their finances in order, and has experience dealing with tax and legal matters.

3. Are they located near you?

It may be difficult for an out-of-town executor to travel back and forth, especially if they have career or family commitments. In addition, they may not be familiar with tax and legal issues in your province. As a result, it's usually a good idea to choose an executor who lives nearby.

4. Do they have the time?

Fulfilling the many responsibilities of an executor takes time. Among their many duties:

- Reviewing and probating the Will
- Making final arrangements
- Taking an inventory of the estate property
- Protecting valuables
- Managing investments
- Paying bills, debts and taxes
- Dealing with beneficiaries
- Working with tax and legal professionals

Simply put, all this can be very difficult for busy people – even if they are financially capable – so it makes sense to choose an executor who can make the time commitment.

5. Are they in good enough health?

Often, people name their spouse or close friend to be their executor. However, age and health can be a concern. Generally, it's a good idea to name someone who is younger than you, and likely to be in good health when the time comes to settle your estate.

6. Are they actually willing to do it?

Sometimes people name executors without even asking them, assuming they will feel honoured. That may be true, but it's also possible that they'd rather not take on the responsibility. Of course, they may be reluctant to say that, not wanting to hurt your feelings. Give them the opportunity to decline, guilt-free: "Are you sure you're OK with this? There are a lot of duties – I can choose someone else."

7. Do they need professional assistance?

When the time comes, many executors are surprised to learn how many duties they have as an executor, and that there are financial consequences – and potential personal liability – if they fail to carry them out properly. At this point, they often decide they need professional assistance from a corporate executor who has the expertise to settle an estate, and can act as a neutral third party with beneficiaries. You can also name a corporate executor in advance in your Will, to either support a friend or family member as their co-executor, or to act as sole executor.

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