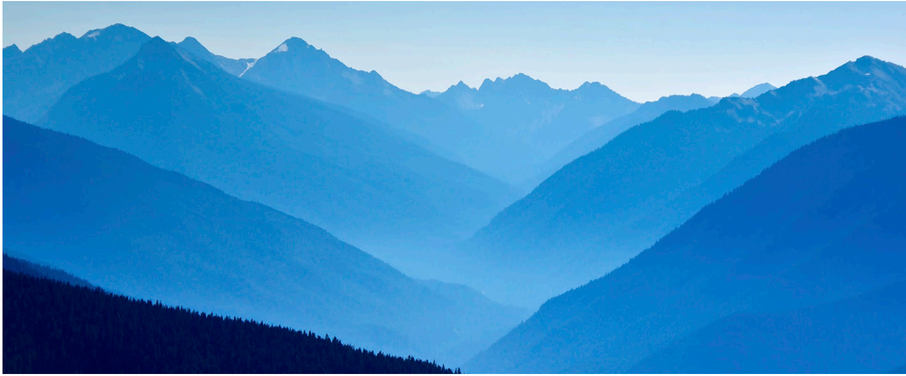

Wealth Management
Dominion Securities

Seven key investment trends

Investors are often focused on the day-to-day events affecting their investments: what the financial markets are doing, where interest rates are going, which direction the dollar is heading, and so on. This is especially true when the financial markets are going through periods of volatility. But what about some of the broader trends that may have an impact on how you invest? In this report we look at seven of these trends – including social, economic and demographic trends that have changed the way people invest.

Today's retirees need a larger nest egg to maintain their lifestyle and avoid outliving their savings.

Trend 1: Investing according to your values

People are increasingly concerned about the impact they are having on social and environmental issues through their investment choices. This rising awareness has led to the dramatic growth of socially responsible investing (SRI) over the last decade. According to the Responsible Investment Association, over $1 trillion of investments in Canada follow some form of SRI discipline. This includes mutual funds as well as pension plans such as the Canada Pension Plan and Ontario Teachers' Pension Plan.

There are many different approaches to SRI, but generally it can be defined as taking into account social and environmental considerations when making investment decisions. There are three main components to SRI:

1. Screening

Negative screens exclude certain companies based on social or environmental values, such as companies involved in tobacco or weapons production. Positive screens identify companies deemed to have a positive impact, such as producers of alternative energy. Bottom-up screens focus on those companies with the best social and environmental practices within a given economic sector.

2. Shareholder activism

Instead of simply ignoring companies that don't measure up to SRI standards, some larger institutional investors can try to change them from within as shareholders, for example through proxy voting practices.

3. Community and economic development

With this approach, investors actively seek out investment opportunities in companies that contribute to a community's social or economic well-being.

With the rapid growth of the SRI marketplace, there are more products to choose from than ever before. We can help you make the choices that are right for you. Please contact us for more information.

Diversifying globally reduces your reliance on the performance of any one single market. When one market goes down, another may go up.

Trend 2: Investing for a cause

In addition to considering the impact they're having on social and environmental issues through their investment practices, affluent investors are increasingly viewing their wealth as a vehicle for positive change through philanthropic activities. This, in turn, has led to the growth of investment products that facilitate philanthropy, such as charitable gift funds.

With a charitable gift fund, you can donate cash or other assets to a fund administered by a registered public foundation. You can then recommend which charities receive grants from your charitable gift fund, subject to the foundation's final approval. You receive a tax credit for the full amount of your donations. In addition, donations of appreciated securities are exempt from capital gains tax, enabling you to potentially make larger gifts.

A charitable gift fund appeals to individuals who want to establish an enduring charitable legacy, but don't require the level of control afforded by a private foundation, and would prefer a more convenient alternative.

RBC Dominion Securities has established a charitable gift fund for clients with philanthropic desires. Please contact us for more information.

Trend 3: Going global

Banks, investment firms and mutual fund companies have been telling their clients for years that they should diversify their investments globally to reduce risk and enhance return potential. There are many reasons why the global diversification message is so compelling:

- Diversifying globally reduces your reliance on the performance of any single market. When one market goes down, another market may go up.
- The strong performance of the Canadian stock market in recent years has left it relatively expensive compared to many other markets, including the U.S. and Asia. Over time, many of these markets have done just as well or better than the Canadian stock market.
- Canada's stock market is heavily concentrated in just three major industry sectors – the Materials, Energy and Financial sectors, which together represent three-quarters of the benchmark S&P/TSX Composite Index. As these three sectors go, so does the S&P/TSX Composite Index.
- Going global gives you greater access to a much wider range of industry sectors – and, as discussed below, diversifying by global sector is actually becoming more important than simply diversifying by country or geographic area.

Please contact us to find out if your portfolio has the right level of global diversification to reduce risk and enhance return potential.

Trend 4: Diversifying by global economic sector

A major trend affecting investors over the last several years has been the rising importance of sector diversification in reducing risk – and the declining importance of geographic diversification.

In the past, you could diversify your investments globally simply by investing in different geographic areas around the world. When the markets in one area went down, another would go up, balancing out your investment returns. But, increasingly, markets are moving in tandem with each other – especially those in North America – making geographic diversification less effective. As markets in different geographic areas are becoming more harmonized, so are global economic sectors. Companies in a specific sector tend to move more in sync with each other, regardless of their geographic location. However, the different sectors are not necessarily moving in sync with each other. For example, financial services companies tend to perform differently from health sciences companies – and this is happening on a global basis.

As a result, diversifying by global economic sector is now just as important, if not more important, than diversifying by geographic area. And with global economic sectors continuing to become more harmonized, this trend is expected to continue.

At RBC Dominion Securities, we offer a proven approach to sector diversification. Please ask us for more information.

One of the biggest trends over the last 10 to 20 years has been the demand for investments that produce satisfactory retirement income.

Trend 5: Breaking with tradition to reduce risk

Many high-net-worth investors, in particular, are diversifying with "alternative" investments – including segregated funds, principal-protected notes and hedge funds.

- Segregated funds are similar to mutual funds, offering exposure to a diversified portfolio of investments through a single investment vehicle. In fact, many segregated funds are linked to an underlying mutual fund. Because they are insurance products, they offer some unique features. Up to 100% of the original amount invested is guaranteed at maturity (usually 10 years) and if the fund holder passes away before maturity, the entire original amount is passed on to their beneficiaries.
- Principal-protected notes (PPNs) have grown greatly in popularity since the late 1990s among investors. Like segregated funds, PPNs also guarantee the initial investment amount at maturity, in addition to offering growth and income potential.
- Hedge funds can provide additional diversification benefits because they tend to perform differently than traditional asset classes such as stocks and bonds. There are several different hedge fund management styles, including "long-short" which uses offsetting long and short positions to reduce exposure to market risk. However, some hedge fund management styles can involve higher risk. As a result, hedge funds are considered appropriate only for "accredited investors" – high-net-worth investors with high risk tolerance.

We can help you determine if alternative investments are suitable for your investment portfolio. Please contact us to learn more.

Trend 6: Reaching for greater yield

One of the biggest trends over the last 10 to 20 years has been the increasing demand for investments that produce satisfactory retirement income. Traditionally, retirees have depended on interest-bearing investments, such as government bonds and GICs. However, there's often very little left over – after accounting for taxes and inflation. As a result, retirees have turned to other ways to generate income:

- Annuities can provide an income stream comprised of taxable interest income and non-taxable return of capital, effectively providing higher after-tax income compared to conventional bonds or GICs. With an insured annuity, a portion of your annuity payment pays for the premiums on a life insurance policy that provides a death benefit for your beneficiaries.
- Corporate bonds generally pay higher yields than government bonds. However, they can vary greatly in quality. Income-oriented investors typically look for higher-quality, investment-grade bonds rated "A" or higher, as opposed to lower-quality "junk bonds."
- Dividend-paying stocks have also become increasingly attractive among income-oriented investors. Dividends receive preferential tax treatment compared to interest income, helping investors boost after-tax income.

Contact us for a complimentary retirement income evaluation to find out how you can enhance your income.

Trend 7: Investing for a longer lifespan

People are generally living much longer – prompting a new approach to investing for retirement. Thirty years ago, people could expect to live for just a few years after retiring at age 65 – four years for men and 11 years for women. These shorter life expectancies meant that some modest savings, coupled with government benefits and possibly a company pension, were more than enough to cover living expenses.

But now, people can expect to live for nearly two decades after reaching age 65. This means that most retirees need a much larger retirement nest egg to avoid outliving their savings or having to make unnecessary lifestyle sacrifices. They also need to take a different approach to investing. Instead of investing exclusively in income-oriented investments like bonds and GICs – as in the past – retirees are increasingly allocating part of their retirement portfolios to growth-oriented investments like stocks.

Please contact us to learn more.

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