Wealth Management
Dominion Securities

Portfolio Advisor

Winter 2020

Market commentary

We have a constructive bias for equities with new highs forecast for 2020. Ultra-accommodative monetary policies already on the books, some additional fiscal stimulus, and a confident U.S. consumer should keep most developed economies growing moderately. That should engender growth in corporate earnings, dividends and buybacks.

As long as U.S. recession risks remain in the distance, as shown by our indicators, we believe portfolios should maintain a Market Weight allocation to equities.

Right alongside this is a heightened need for caution, acknowledging that the late stage of the business cycle carries particular challenges for the economy and stock market. In our view, GDP growth for the major economies is unlikely to kick into a higher gear that would usher in several successive years of above-average earnings growth. But as long as U.S. recession risks remain in the distance, as shown by our indicators, we believe portfolios should maintain a Market Weight allocation to equities.

Fixed income

The benchmark 10-year U.S. Treasury yield has held the 1.5%–2.0% range for nearly four months, recently returning toward the top end of that range. The German benchmark 10-year Bund yield remains negative, but has reached -0.2%, the highest level since May 2019. Global growth and inflation expectations have recovered on the back of recent central bank easing. But with the major global central banks now likely to be on hold for the time being, we continue to see the ceiling for developed sovereign yields to be near current levels, as broad uncertainty is likely to remain. RBC Capital Markets forecasts the U.S. 10-year Treasury yield to peak at 2.1% in 2020, while expecting the German 10-year Bund yield will gradually recover back to 0.0% by the end of 2020.

We maintain our Market Weight in global fixed income. Though global yields remain historically low, so too do their ceilings. As we expect market volatility to be higher in 2020 than it has been recently, we look to fixed income to provide some defense and stability for portfolios.

To learn more, please ask us for the latest issue of *Global Insight*.

RBC Wealth Management
Global Portfolio Advisory Group

The 2010s: Goodbye to the decade of disruption

This past New Year's Eve, as the bittersweet *Auld Lang Syne* played and we counted down the final moments to midnight to close out 2019, it was more than the marking of the end of another fascinating and, in economic and market terms, outstanding year. It also closed the chapter on a decade that brought breathtaking change in such areas as technology, the environment, politics and medicine. It was also a decade that featured one of the most sustained periods of economic and investment market growth in the modern history of mankind.

Ten years to remember

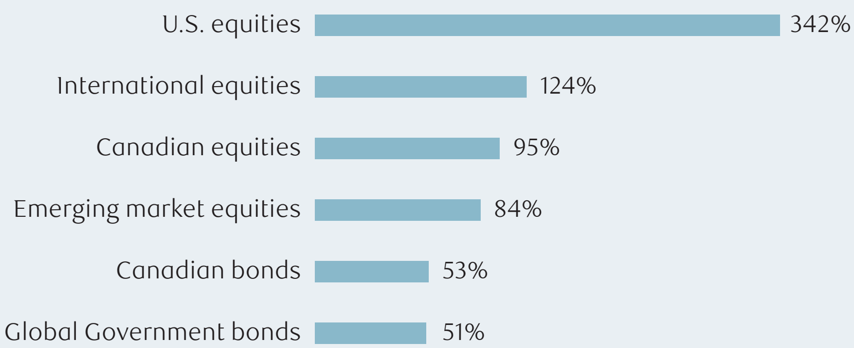
From iPads to self-driving cars, to the Ebola vaccine and nanotechnology, to 3D printers and lab-grown "meat", groundbreaking innovations and invention were the hallmarks of the now-past decade.

Along with countless innovations, the 2010s brought important changes to the world order, as China's economic rise continued at a breakneck pace, and the Obama presidency gave way to the Trump administration and the beginning of a reorientation of American politics and foreign and economic policy. Even the European Union faced its greatest test to date, with Britain poised to exit the EU as the decade closed out.

And, after decades of debate and denial, the climate emergency – the term of 2019 according to the *Oxford Dictionary* – became a front and centre social and political issue, undeniable in its importance and impact for both today and in the not-too-distant future.

The Terrific '10s

Market returns during the 2010s



Source: Morningstar, RBC GAM. Performance as of January 1, 2010 to December 17, 2019.

A decade of wealth-building

After the tumultuous end of the first decade of the 21st century, characterized by the market crash of 2007/2008 and the ensuing Great Recession, 2010 marked the beginning of a sustained recovery in the global economy. While North American and some European nations bounced back sharply in the early part of the decade, others, particularly in the Eurozone, stumbled out of the gates before finding their footing. Despite the rough start, by mid-decade the global economy was enjoying a mostly synchronized period of growth, as jobs, earnings and a recovery in real estate values soon helped battered consumers and businesses to bounce back.

Driven by strong earnings growth and underpinned by historically low interest rates and yields, equities – particularly U.S. equities – and bonds spent an unparalleled decade providing investors with year after year of strong returns, with only 2018 and its gut-wrenching end breaking what had been an almost perfect 10-year record of wealth-building growth. "Disruptor" became the latest buzzword in the second half of the decade, with companies like Netflix, Tesla, Uber, Amazon and AirBnB upending their industries while thrilling their clients with their inspired business models.

Siri, tell me what the future holds?

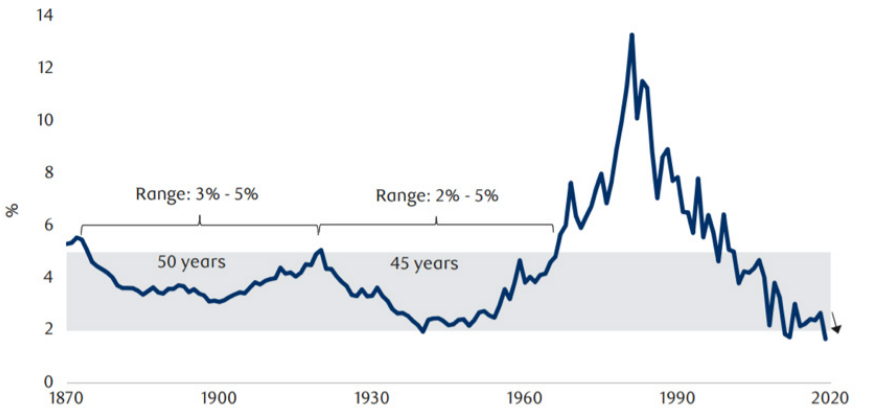
The 2010s started at a low point and ended on a high one, providing investors with plenty to celebrate as the decade drew to an end. What the 2020s will hold is anyone's guess, but it's likely to be full of further innovations, challenges and change. Sticking to your investment plan is sure to help you steer through to your goals – no matter what kind of disruptors pop-up in the decade ahead.

Less than zero

A closer look at low and negative interest rates and yields

Many of us well remember the early 1980s, when central banks jacked up interest rates to combat soaring inflation. But since the mid-80s, interest rates and bond yields, with only a few exceptional spikes along the way, have tumbled, bringing them to the lowest levels in modern history. And historically low rates and yields have also ushered in a new and unprecedented phenomenon: *negative* interest rates and yields.

Historial 10-year U.S. Treasury yields



Note: As of 10/31/2019. Source: RBC CM, RBC GAM

Today, over US $17 trillion of global debt is trading at nominal (before inflation) negative yields – which is almost 25% of all outstanding global debt*. Add to that the fixed-income products that have real (after-inflation) negative yields, and that number soars even higher.

When the yields come tumblin' down

While there are many factors – both structural and cyclical – that have brought about this long, gradual decline, here are some of the key reasons:

- **Slow real economic growth:** Falling economic growth rates in the developed world have meant lower business investment. Lower business growth requires lower borrowing costs, as businesses will not invest in new projects unless the cost of borrowing is less than the prospective return on their projects.
- **Low – *really low* – inflation:** By historical standards, inflation is extremely low and has remained so for years. The effect of this development on interest rates and yields – which are made up of an investment risk premium plus inflation – is that they will naturally fall when the inflation component declines.
- **Central bank policies and the glut of global debt:** As developed-world growth has fallen, central banks have gradually lowered interest rates to stimulate growth in spending. Key market and economic events have also spurred cuts, such as the 2008/09 Great Recession, when central banks cut rates to ward off disaster. In turn, lower interest rates and bond yields have stimulated borrowing at a sharply increasing rate, resulting in the ironic outcome that central banks need to (artificially) keep interest rates low to manage these historically high debt levels.

The bond investor conundrum

Negative interest rates and yields seem inconceivable: why would anyone want to lend money to someone only to be assured of a negative return on that transaction? But in today's world, investors are willing to concede return for security, even paying for the privilege of the (presumed) assurance that they will receive their money back in the future.

That's the conundrum for today's investor: yes, rates are low (even negative) but bonds still offer important benefits, including:

- Providing a predictable source of income
- Preserving capital
- Serving as a ballast for your portfolio during times of economic distress and risk aversion

Regardless of how long low yields persist, investors can continue to benefit from bonds to help protect their portfolios – so in a way, today's wonky math still adds up.

*As of 11/4/2019. Percentage of bonds in Bloomberg Barclays Global Aggregate Bond Index trading at negative yields. Source: Bloomberg, RBC Global Asset Management.

Pet symmetry

Taking care of your pets when you can't

With an estimated 57% of Canadian households owning a pet these days, it's clear that we love our furry (or sometimes slippery) friends. While the overwhelming majority of pets are cats and dogs (by raw numbers, cats have a slight edge over dogs), pets come in many shapes and sizes, from long and reptile to small and scurrying. But they all have one critical thing in common: they rely on us, their owners, for their safety, security and well-being.

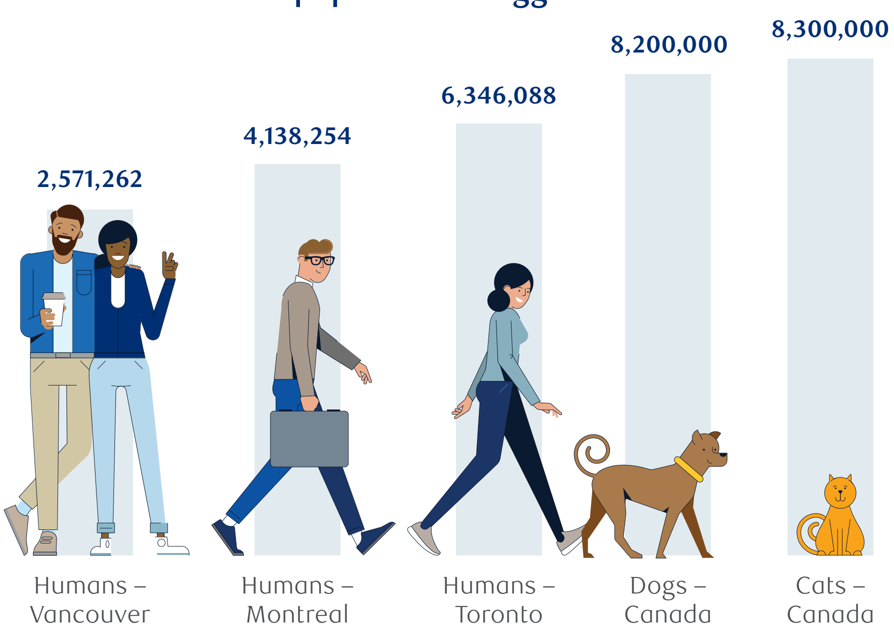
Our pawbligation

While we can debate endlessly as to who owns who – pet or human – we can't debate that our pets rely on us to feed and care for them, as well as to provide them with a secure environment. In short, we have an ethical obligation to secure their well-being. And while that may seem straightforward when we are in good health, it also means that we should make arrangements for someone to care for them after we're gone, or if we become unable or incapacitated in some way.

Avoiding a cat-astrophe: a little planning goes a long way

Canadian common law states that pets are considered to be the personal property of their owners. Consequently, they do not have the legal capacity to receive gifts made in Wills by their owners. So, how can you ensure that your pet is properly cared for when you are gone, or if you are unable to do so? Here are four ways to make them part of your estate plan:

Raining cats and dogs – The population of two of Canada's most popular four-legged friends



41% of households have at least one dog

38% of households have at least one cat

Source: 2018 Kynetec (formerly Ipsos) survey, conducted on behalf of the Canadian Animal Health Institute (CAHI).

1. **Testamentary gift:** You can make a gift in your Will of your pet to a trusted individual, along with enough funds to ensure that your "beneficiary" can care for your pet during your pet's life.
2. **Pet trusts:** You can set up a trust to provide funds to a third party for the benefit of your pet. One thing to consider: as there is no guarantee the person you assign to be the trustee will honour the arrangement to oversee your pet, you might consider appointing a "protector" whose role is to supervise the trustee.
3. **Pet foster programs:** Some humane societies offer "foster" programs, which allow a pet parent to enter into an agreement where a search is carried out for a suitable foster parent following an owner's death.
4. **Power of attorney:** If you become incapacitated, your pet or pets will need someone to care for them. You can put instructions in your enduring or continuing power of attorney for property (a Protection Mandate in Quebec) which enables your appointed attorney (mandatary in Quebec) to manage your assets and property, including care for your pet.

Our pets are often seen as one of the family, and as cherished friends and companions. Consulting with your legal counsel to ensure that there is continuity in their care can help avoid any "un-fur-tunate" outcomes once you are gone.

Better together: RRSPs and TFSAs

Since their introduction in 2009, Tax-Free Savings Accounts (TFSAs) have rapidly grown in popularity with Canadians, with the most recent figures showing that we own over 13 million TFSAs. And while the total assets in TFSAs ($232 billion) are still dwarfed by those in Registered Retirement Savings Plans (RRSPs) (over $1 trillion)*, they are catching up gradually as Canadians learn more about the benefits of these savings vehicles, and as the lifetime contribution amount – $69,500 as of 2020 – increases every year.

But since their introduction, a debate has raged about which is the better way to save – RRSP or TFSA? The simple answer is both, as the two account types offer excellent benefits for savers, and both can help you reach your goals.

RRSPs and TFSAs: similar, but different

Both RRSPs and TFSAs have unique characteristics, offering Canadians benefits that will help them grow their savings and reach their goals. Both offer account holders important investment and tax benefits, specifically tax-free growth of any investment income produced within either account. This "sheltering" allows account owner's funds to compound and grow at a faster rate.

However, there are a few important differences between them, as captured in the chart below.

The right account for the right goal

Generally speaking, RRSPs work best for long-term savings goals like retirement, with some notable exceptions being for a home purchase or education funding (tax-free withdrawals are allowed under the First-Time Homebuyer's Program and the Lifelong Learning Plan). As withdrawals are fully taxable at the account holder's marginal tax bracket, the general idea with RRSPs is to wait until one has entered their retirement years before withdrawing funds to support their cash flow needs; conversely, contributors benefit from the tax-deductibility of their contributions when their marginal tax bracket is higher.

For many Canadians, RRSPs are seen as a long-term savings vehicle due to their more restrictive rules and the taxability of withdrawals. Given their far greater flexibility, TFSAs are often used for shorter-term goals or simply as a savings account, but can be ideal for longer-term goals like retirement, too.

	RRSP	TFSA
Contributions	Tax deductible	Not tax-deductible
Withdrawals	Fully taxable	Not taxable
Eligibility	You must have earned income	You must be a Canadian citizen and have reached the age of majority of your province of residence
Contribution limits	18% of your earned annual income from the previous year (less any pension adjustment), to a maximum limit as set by CRA (for 2020 it is $27,230)	$6,000 for 2020 and a lifetime limit as of 2020 of $69,500
Carry-forward	Yes, until the year you turn 71	Yes, indefinitely
Ability to contribute after age 71	No, must convert to a RRIF or annuity by the end of the year you turn 71 or close the plan	Yes
Withdrawals affect government benefits?	Yes	No

RRSPs and TFSAs: different, but the same

While different from RRSPs in many ways, TFSAs are the same as RRSPs in one important way: they provide important tax saving and compounding benefits to help investors grow their wealth. Whether you should use a TFSA, an RRSP or both for your savings needs largely depends on your unique goals and circumstances. We can help you make the right choice for you.

*Statistics Canada, 2016.

An increasingly undeniable truth

A new RBC report helps debunk the myth that socially responsible investing hurts returns

Here's some good news for investors who want to align their ethical beliefs with their investing practices: there is a clear correlation between strong sustainability business practices and company performance. This is according to key findings from the 2019 RBC Global Asset Management report, *Does socially responsible investing hurt investment returns?*

The booming universe of Responsible Investing

Responsible Investing (RI) has been around for over a hundred years, and involves applying social and environmental factors to choose investments. With almost US$31 trillion invested globally in RI mandates as of 2018 – a 34% increase from 2016 – this approach to investing is growing quickly.*

RI is an umbrella term that captures many types of investing approaches under it – including socially responsible investing (SRI), engagement, screening, sustainability-themed investing, integration of environmental, social and governance practices (ESG), and impact investing. Presently, SRI mandates rule the RI world, with $19.8 trillion in assets.*

SRI: the principles of principled investing

SRI is a portfolio construction process that attempts to avoid certain investments according to defined ethical guidelines. In other words, SRI is values-based, and involves the formal integration of social values into the traditional investment process. It focuses on screening out or excluding particular investments based on a defined set of values. An example of this may include screening out investments in companies affiliated with the tobacco, alcohol or gambling industries.

Doing right doesn't have to hurt

While SRI appeals to many, one question continues to linger for individual and institutional investors: does adopting SRI help or hinder investment returns?

RBC Global Asset Management's report concludes that there is a clear correlation between strong sustainability business practices and company performance. The report looked at dozens of independent, third-party academic and industry studies and concluded that SRI does not result in lower investment returns.

Here are some of the key findings:

- There is a positive relationship between stock price performance and strong governance practices, strong environmental performance and high employee satisfaction.
- The use of aggregated sustainability scores to determine the impact on performance has demonstrated evidence of a positive impact.
- Companies with high environmental, social and governance ratings outperform the market in the medium term (three to five years) and long term (five to 10 years).
- Strong corporate responsibility practices improve operational performance of firms.
- Corporate social responsibility considerations in stock market portfolios do not result in financial weakness.
- Companies that prioritize sustainability manage environmental, financial and reputational risks better, which increases likelihood of reduced volatility of cash flows.

Is SRI right for you?

While evidence continues to mount that SRI doesn't hurt – and may even enhance – investment returns, it is important to speak with us about whether SRI is right for you. But investing according to one's principles is getting easier and more widespread – and that truth is undeniable.

* Global Sustainable Investment Alliance, Global Sustainable Investment Review, 2018.

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