Wealth Management
Dominion Securities

Portfolio Advisor

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Around the world

Global markets

Equity markets rose on hopes of a gradual economic recovery and ongoing stimulus measures. Rebounds in coronavirus numbers could threaten the ongoing rally and generate increased volatility through the remainder of 2020. Bond yields remained near historic lows, with little impetus to rise with the economy and inflation largely stagnant.

Canada

COVID-19 containment measures continued to take their toll on job growth and economic activity. The return of some restrictions as coronavirus infections have surged has slowed the pace of the economic recovery. But ongoing fiscal and monetary policies are likely to help heal the economy, with the stronger growth expected in 2021 predicated on managing through the latest resurgence.

United States

After a sharp rebound in early summer raised hopes of a quick economic recovery, rising infection rates, and a political stalemate in Congress that torpedoed continued pandemic relief for individuals and businesses, undermined the pace of the recovery. Growth looks set to return in 2021, if the recent COVID-19 resurgence can be managed without further economic damage.

Europe

With tourism at a near standstill, and ongoing damage from initial lockdowns, Europe's economy is likely headed for another poor showing in 2020. While a massive stimulus package will help, many European countries are likely to stagger into 2021 before the global economy picks up again, with monetary policy and an end to global travel. Risks remain around the U.K.'s eventual exit from the EU.

Emerging markets

While many Emerging Market nations have controlled the threat of the pandemic for now, other nations such as India continue to have trouble. A weaker U.S. dollar and low global interest rates should help boost exports and offset a drop in local demand, but 2021 growth will depend on renewed exports to developed nations and a return to more normalized economic conditions.

Perplexing pandemic performance

With the global economy in the doldrums, the stock market's booming performance seems to reflect a totally different reality, leaving many investors to wonder why.

Disconcerting disconnect

The economic damage wrought by lockdowns and measures to control the spread of COVID-19 has been deep and sustained, leaving the global economy in a severe recession. Although most economists agree the global economy will bounce back in 2021, this outlook is being tempered daily in the face of the recent resurgence in global infection rates and continued signs of a softening in the economic recovery.

And yet, despite the pandemic-induced economic woes, global equity markets have largely soared, including a 46% surge in the S&P 500 Index* from the low reached on March 23. This performance has left many investors baffled as to the cause of this apparent disconnect between the performance of the economy and that of the markets.

Looking back to the future

Historically, the apparent disconnect between the markets and the economy is fairly normal. That's because stock prices tend to reflect the outlook for the future earnings and prospects of a specific company. What the broader economy is doing at any given time can influence stock prices, but there's not always a direct correlation. Looking at the current situation, while the overall economy is struggling, certain companies have actually prospered during the pandemic.

FAANMGs boost S&P 500 performance

	1M	3M	6M	YTD	1Y	2Y	3Y
S&P 500	7.00%	13.60%	11.80%	8.30%	19.60%	9.80%	12.30%
S&P 500 ex. FAANG	6.10%	9.80%	5.00%	0.70%	9.20%	4.60%	7.70%
S&P 500 ex. FAANMG	5.70%	8.80%	3.20%	-1.80%	6.30%	2.70%	6.10%
S&P 500 Avg. Return 1926 - present	0.60%	1.90%	3.70%	n/a	7.70%	6.50%	6.20%

Note: Performance as of August 31, 2020.
Figures are annualized for periods greater than one year.
1-month, 3-month, and 6-month figures are calculated based on a 30-day month.
FAANMG represents Facebook, Amazon, Apple, Netflix, Microsoft and Alphabet (Google)
Source: Bloomberg, RBC GAM

Another important factor is that the performance of an index – such as the S&P 500 – does not necessarily reflect the performance of all or even the majority of stocks that make up that index. If one or a few sectors of an index surge high enough, they can pull the overall index up with them, covering the poorer performance of the rest of the market.

Tech-tonic shift

And that's exactly what's happened: there's been a massive surge in technology share prices. In fact, as the chart above shows, if we strip away the performance of key technology company shares – specifically Facebook, Amazon, Apple, Netflix, Microsoft and Alphabet (the parent company of Google) – the S&P 500's year-to-date return is actually negative.

Yet, this support for technology stocks even during the economic slowdown is reasonable. Their services and products are almost perfectly aligned with what their customers need in a socially distanced and locked-down world, including work-from-home support, telecommunications, online entertainment and education, web-based support, and point-and-click delivery services.

Seeing the forest for the trees

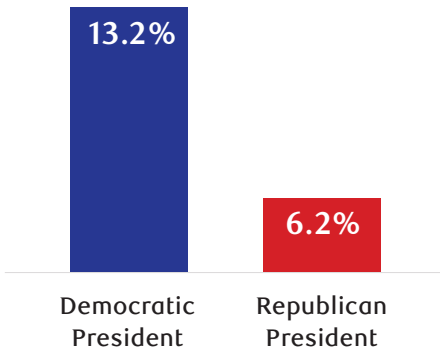
Now, as much as ever, it's important to keep a long-term perspective and remain well-diversified across all sectors of the market, as well as different asset classes such as stocks, bonds and cash, within your portfolio to help reduce risk. While markets and the economy work their way through these unpredictable and volatile days, an eye on the horizon seems the best way to "square the circle" that is sometimes the market vs. economy conundrum.

*S&P 500 Index performance from March 24 to September 30. Return in U.S. dollars. Source: RBC Global Asset Management.

Political interference

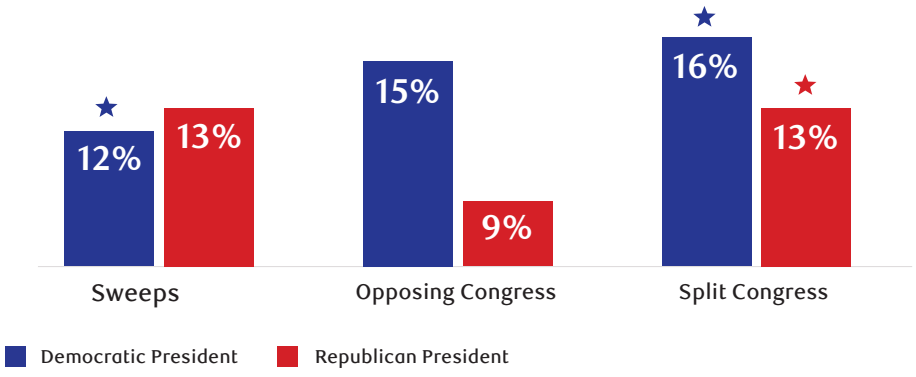
Do U.S. presidential elections matter to markets, and therefore to investors? What is the likely impact on both of a win by a Democrat versus a Republican? Historically, presidential election outcomes have delivered surprising results when it comes to equity market performance, defying the "common wisdom" that they perform better under Republicans due to policies such as lower corporate taxes and less regulation.

Annual equity returns by presidential party



Source: RBC GAM, Bloomberg. S&P 500 Index (USD) data as of January 1, 1928 to September 28, 2020. Returns of president term based on election dates.

Return based on government control
S&P 500 median returns



Source: RBC GAM, Bloomberg. S&P 500 return (USD) November 6, 1928 to October 6, 2020. Returns attributed to governments immediately after election and accounts for changes in government control following mid-term elections. Sweep accounts for period where president's party controls congress. Opposing Congress accounts for period where the opposing party of the president controls congress. Split congress accounts for periods where Democrats and Republicans each have control of one of the House of Representatives or the Senate.

With the recent U.S. presidential election, it is understandable that investors may be wondering what impact, if any, the election of one party and/or presidential candidate might have on investment markets and their portfolios.

The 2020 candidates have positions on key policies that investors do, on the whole, care about: taxes – both personal and business – and regulation. In this election, those positions have been clearly laid out, with the incumbent's record making clear where he stands – lower taxes, fewer regulations – and how his challenger offers the opposite: higher and more.

But beyond this, and recognizing that a president can't really do much without control over or the support of Congress to pass legislation, the more important factor over the longer term is who controls the House and Senate.

Playing in the Congressional sandbox

There is a famous final scene in the 1972 Academy Award-winning film *The Candidate*, starring Robert Redford. After pulling off an upset against his incumbent and well-entrenched senatorial opponent, Redford's character, stunned by the turn of events, turns to his campaign manager and says "What do we do now?" While the question is left unanswered, it is the crux of the outcome of a presidential election and its impact on markets: what happens next.

Indeed, for markets and investors, the answer is often determined by the policy positions of the new president and the composition of the Congress they must work with. Importantly, does the president's party hold power across Congress (a sweep), the House or Senate only (a split), or neither (opposing)? Looking at the chart above, it appears that, historically, a Democratic president who can play well with their political opponents in the Congressional sandbox has historically provided the best returns for investors – and once again, not so much the other way around.

A ballot for balance

Regardless of the outcome of this election, trying to anticipate how it will affect markets and your portfolio is next to impossible. Consequently, tuning out the election noise and "casting your vote" for a properly balanced portfolio designed to achieve your long-term goals remains the best strategy.

Giving in-kind: a double dose of good

As year-end approaches, consider the perfect trade: being kind with "in-kind" charitable donations.

The coronavirus pandemic has been an historic challenge for charities, as the number of those in need has skyrocketed. Conversely, the historic bull market run of the last 11 years has left many investors sitting on large capital gains in their stock portfolios. Combine the two, and, as we approach year-end, many investors have an ideal opportunity to be kind by giving securities (such as stocks) in-kind, providing to those in need while generating significant potential savings on their tax bills.

COVID crisis: the burden has not fallen equally

The arrival of the coronavirus has been shocking, deeply unsettling, and for some even tragic. However, after a period of adjustment, most Canadians have found ways to successfully adapt to the "new normal" by finding ways to fill our personal time, adopting new technologies to continue to work and connect with friends and family, and even using the opportunity to better appreciate our lives and to spend quality time with our loved ones.

But for the many – too many – who were already marginalized, living with food and/or shelter insecurity, or just getting by paycheck to paycheck, the pandemic's impact on the labour market and the economy has been devastating. According to the United Way of Canada, it's been particularly hard on women and children. Low-income earners have often been the first to put their health – and the health of their families – on the line just to keep their jobs. Many of the pandemic period job losses have hit the working poor the hardest, and have been the slowest to come back. The Toronto Daily Bread Food Bank has reported an increase in demand of more than 300% since the pandemic hit.

Donating cash vs. donating shares

	Sell shares and donate cash	Donate shares directly
FMV of donation (a)	$2,000	$2,000
Adjusted cost base	$1,000	$1,000
Capital gain	$1,000	$1,000
Taxable capital gain	$500	$0
Tax on capital gain ($500 x 50%) (b)	$250	$0
Donation tax credit ($2,000 x 46%) (c)	$920	$920
Total cost of donation = (a) + (b) - (c)	$1,330	$1,080

Assumptions: Net tax savings from donating shares: $250 ($1,330 - $1,080), assuming that donations of $200 have already been made. Marginal tax rate of 50%; donation tax credit of 46%. Also assumes the person has taxable income below the top bracket and donations in excess $200.

A capital idea: making the most of your charitable giving

Giving securities in-kind to charities is a smart way to support the causes that matter to you, help those in need during these difficult times, and can help reduce your tax bill.

In general, under Income Tax rules, a Canadian taxpayer can claim a charitable donation of up to 75% of their net income (or 100% in the year of death and the year before). Any excess can be carried forward for up to five years. And the more you give, the greater the impact: donations of less than $200 generally produce a tax credit of approximately 24%, while those above $200 attract a tax credit of approximately 48% (note: tax credits vary depending on the donor's province of residence, taxable income and the amount donated).

Here's where in-kind donations come in: donating the full market value of securities instead of selling those securities first, incurring capital gains and then donating the net, after-tax cash amount, maximizes your donation to those in need, while helping to reduce your tax bill.

Giving in-kind is a great way to significantly enhance the impact of your generosity. Talk to us about your charitable giving strategy and the most effective way for you to take advantage of donating securities in-kind.

Protecting the puck: the three-bucket approach

A straight-forward approach to helping retired and cash-flow-focused investors sustain their investment income and preserve their portfolios through all market conditions.

Old risks remain, new risks emerge

For most Canadians, the coronavirus pandemic has been a healthcare crisis that has brought about an economic shock and what appears to be a relatively short-term market downturn.

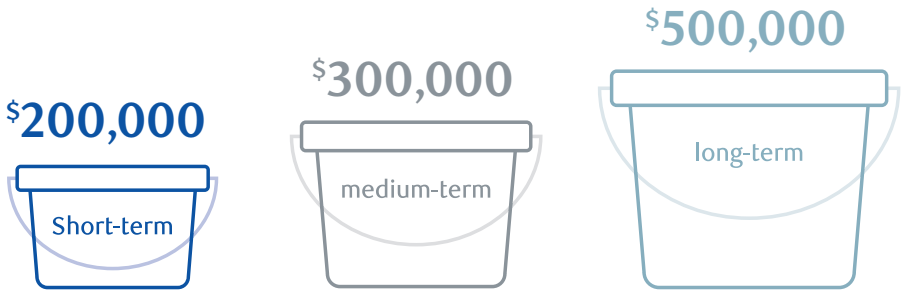
However, for most retired Canadians – the age group that is most at risk from its effects – COVID-19 is a deeply worrisome and potentially deadly risk. What's more, the pandemic brought with it the "COVID Crash" and subsequent sharp volatility. It further exacerbated the already historically low interest rate and bond yield environment that has challenged low-risk savers, as central banks slashed interest rates to stave off economic disaster.

These developments serve as an important reminder of the vulnerability of retirees and cash-flow-focused investors to economic conditions that together could threaten their ability to sustain their retirement cash flow and preserve their well-earned nest eggs. In short, it is a reminder of the need to help ensure that these types of investors don't have to change their lifestyles in the face of shrinking cash flow, or worse, face the ultimate risk of outliving their savings.

Playing portfolio defence

Fortunately, there is a way to ease these investors' minds when faced with the twin threat of low interest rates and yields on fixed-income investments and volatile markets: the three-bucket approach. As long as it is aligned to their investment objectives and suitable given their risk-tolerance, retirees – and those whose primary portfolio goal is to produce cash flow to support their lifestyle – may wish to leverage this approach to help ensure that they have enough income to provide for their short-term needs, while still growing their portfolio over the medium- and long-term:

Easy as 1-2-3:
An example of the three-bucket strategy using an initial investment of $1 million to generate required annual income of $50,000



3 years of cash flow plus emergency funds
$200,000 = $50,000 x 3 years plus $50,000 (emergency funds)

Buffer of 6 years of cash flow
$300,000 = $50,000 x 6 years

Remainder of portfolio

The three buckets:

- **Short term – Income (1-5 years):** The short-term bucket holds cash and short-term investments for cash-flow withdrawals and emergency funds, while also helping to reduce the impact of short-term market volatility on the portfolio.
- **Medium term – Buffer (6-10 years):** Holds income-generating investments, including low-risk, low-volatility equities for stable capital gains. This bucket serves as a buffer between the cash bucket and the long-term growth bucket.
- **Long term – Growth (10+ years):** Holds growth-oriented equity funds, which are more volatile but offer higher potential for capital growth to sustain the portfolio for the later years of retirement.

The best defence is a good offence

While hockey fans know that protecting the puck is a critical part of maintaining a lead, the other part is not getting so defensive that you are hemmed in to your own end by your opponent – more often than not, playing too safe leads to a loss. In order to protect your portfolio from impact of ongoing cash-flow demands, as well as the ravages of inflation, investors can use a well-structured and considered strategy that, if properly aligned to their investment objectives and risk tolerance, can help ensure they meet their long-term cash-flow needs and help preserve their retirement nest egg.

Speak to us today to discuss how we can help you or your loved ones "protect the puck" with risk-appropriate strategies like the three-bucket approach.

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The glitter of gold

Long seen as the ultimate store of value, gold has unique characteristics that have led it to be one of the most coveted assets the world over. Its recent sharp rise in value has re-focused attention upon it, prompting many investors to wonder what the glitter of gold is all about.

Golden ages

Gold has been around for ages: pieces have been discovered in Spanish caves that date as far back as 40,000 B.C. Ancient Egyptians smelted it as far back as 3600 B.C. Today, gold is prevalent around the world as a precious metal, rare enough to command real dollars to own, but ubiquitous enough to be enjoyed and valued by millions of people. It has at various times been used as a currency, for example by the Roman Empire. Currencies like the U.S. dollar and the British pound were once linked to the value of gold, underpinning their value.*

"Gold is money – everything else is credit." ~ J.P. Morgan

About half of the world's annual gold production – around 3,500 tons in 2019 – is used for jewelry, while the rest is divided up for use in technology, investment, and as reserves by central banks.*

In general, investors can access gold through commodity futures contracts, Exchange-Traded Funds (ETFs), mutual funds and direct ownership of gold-producing, publicly listed companies. Gold producers fall under the Materials sector of the S&P/TSX Composite Index, which is currently the second largest sector at 15.5% of the total index. Gold producers represent a significant portion of the sector, and includes Barrick Gold, currently the world's largest gold producer and the seventh largest company in the index by market cap.**

Gold standard

Gold can also serve investors and their portfolios in specific ways, including as a:

Portfolio diversifier: Gold has historically exhibited a low correlation to other more economically-sensitive commodities and assets classes, and is typically negatively correlated to the U.S. dollar, attributes that can provide diversification benefits to a portfolio.

Inflation-hedge: Gold's scarcity and perception as a "store of value" has long made it a hedge against high inflation, maintaining its value over the long term while rising prices erode the purchasing value of fiat currencies.

Safe haven: In times of uncertainty, upheaval and volatility, gold is seen as a relatively safer place to wait out trouble given its low correlation with other major asset classes and perception as a store of value. Historically, gold doesn't often decrease or increase with the same momentum as the market as a whole – but when volatility hits, this makes the shiny metal especially attractive, potentially providing a "buffer" against falling asset values.

From an investment standpoint, gold can be suitable for an investor's portfolio based on their specific investment objectives and risk tolerance. Wondering if gold is right for your portfolio? Please contact us to learn more.

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*Source: World Gold Council. October 2020.
**Source: S&P Dow Jones Indices LLC. All figures as of September 30, 2020.