

The Fortnighter



Wealth Management
Dominion Securities

Spring 2023 – Issue #82



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There were several GIC maturities this past week in client portfolios. **1.3%!** My, how the financial world has changed over the past few years – rates for similar terms today are 3 times that.

And with last year's dismal stock market performance still fresh in investors' minds, is it any wonder the "stampede" to short-term GICs and money market funds with rates around 5%?

Now, 5% may appear wonderful, but long-time investors remember short-term yields much higher. Many fondly recall the 1981 Canada Savings Bond issue that paid an eye-popping 19.5%! "Now them were the good ol' days!"

But while everyone (supposedly) was loading up on that glorious CSB issue, I've yet to speak to a single investor who bought long-term bonds at that time. What were long-term bonds yielding in 1981? **15%!!**

Think about it. Those CSBs looked fantastic at the time – but their yield dropped by over 10% in the next couple of years. Conversely, a more long-term investor could have locked in **15% for decades**. Who did that? Professional bond managers, that's who.

If we've spoken recently, you will know that I've added a few **Bond Funds** to portfolios – and there are several reasons for this. The first is that an "institutional" bond manager will have access to fixed-income issues that you and I don't (the number of bond issues available to a "retail" investor is a fraction of what's out there)

- and the pros are well positioned to access better prices.

A second reason is something I call due diligence. In my opinion, no-one does a "deeper dive" into an issuer's financials than a fixed income portfolio manager. They really do the math - both in regard to an issuer's ability to make their interest payments and with respect to their solvency.

But the main reason I'm adding bond funds to portfolios now is something called "duration" – which is primarily about the term-to-maturity of the bond. While individual investors are conditioned to think "long term" means five years (the "traditional" longest term of mortgages and GICs), a professional bond manager considers long term to be 10, 20 and even 30 years.

The pros also know that when interest rates fall (as they are projected to do over the coming years), long-term bonds have the potential to increase in value – and the longer the duration, the bigger the increase. Short-term bonds and GICs not only have little potential for gains, as yields fall, they "roll over" at lower and lower rates. One day soon, you'll wake up and that short-term GIC or money market fund may well be yielding close to zero again.

OK, you say "I sleep better at night knowing my cash is safe". Fair enough, but the bond manager says, "I sleep better at night knowing my clients are being looked after for the next 20 years". Something to be said for a person who is both smart and nice!

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