The Fortnighter

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Gair Wealth Management
RBC Dominion Securities Inc.

Al Gair, BSc, MBA
Senior Portfolio Manager &
Investment Advisor
al.gair@rbc.com
604-665-5526

Bonnie Walmsley
Associate
bonnie.walmsley@rbc.com
604.665.5527

745 Thurlow Street, 20th Floor
Vancouver, BC V6E 0C5
www.gairwealthmanagement.com
1-800-427-7766

2022 was a pretty dismal year by a lot of measures, but for investors it was particularly disappointing. If you are a reader of the financial press, you will probably come across the descriptor "nowhere to hide" – a reference to the fact that even traditional safe havens such as bonds and gold got clobbered last year. Unless you had the clairvoyance to predict the Ukraine invasion (and load up on energy stocks), 2022 was a financial downer.

By the numbers, there were some pretty ugly results last year. The most common measure of "stock market" performance, the U.S. S&P 500 Index, fell close to 20% - it's worse performance since 2008. Our own TSX composite index was down about half that – but still, nothing to celebrate.

So now the good news. The key driver of the stock and bond market declines was inflation & interest rates – both of which rose dramatically in 2022. As you know, I'm a big believer in balanced/diversified portfolios – and we are finally in a position where that 20%/30%/40% of your portfolio that is in "fixed income" should now be making a meaningful contribution to your overall returns.

This is extremely important from a "risk vs. return" perspective. If more of our return objectives are met via safer fixed-income holdings, we can rely less on equities (stocks) to do our portfolio's heavy lifting.

A recent article in the business section of the Globe & Mail bears this important consideration out. Citing information from pension consultant Mercer Canada and Aon PLC, the article points out that (on average) the overall health of Canada's private pension plan sector actually improved in 2022. This was even after the average assets of the plans analyzed <u>declined</u> by about 15% in the year.

At first glance, this doesn't make sense – but it's about interest rates. By law, pension plans hold a significant portion of their portfolios in fixed-income securities to meet future obligations. Those investments have just increased dramatically in yield – making future obligations "easier" to achieve. Anything in your portfolio resemble a pension plan? An RSP for example (and if you're retired, your entire portfolio is most likely a "pension plan"!).

Two messages here. The first is that there's often a silver lining in any bad news – and in the case of last year's dismal market performance, it's the big rate-of-return "bump" we've now been handed on the income side of our (diversified) portfolios.

The second is that we should be taking advantage of these high yields now – they may not last. Central banks are determined to get inflation numbers down and yields will certainly follow. Those buying 1-year GICs now because yields are slightly higher than longer-dated maturities may be disappointed at their options when they look to re-invest in 12 months.