Summer 2017

# Financial focus

## Time to tune out the noise

U.S. President Donald Trump enjoys having his say on social media, and the weight of his words has moved markets. Health care, aerospace, and automotive are just a few of the sectors that have seen stock price movements after Trump weighed in.

Over the next four years, it's going to be important for investors to maintain their perspective.

### STAY FOCUSED

With TV, the Internet, and social media operating 24/7, global political and business events can affect capital markets in a flash. Anytime this happens, it's important to remember that the vast majority of us are not investing for one day, or one year, or one presidential cycle — but for the longer term.

Remember too that the U.S. remains an attractive investment destination. Not only is it the world's biggest economy, the International Monetary Fund also expects the U.S. to lead developed nations in economic growth in 2017 and 2018.[1]

### STAY DIVERSIFIED

Canadian investors who shy away from U.S. equities may miss out on opportunities in sectors better represented south of the border — such as information technology, health care, and consumer products. In addition, many companies in these innovative sectors do a great deal of their business in international markets, providing further diversification.

With ready access to a wide selection of U.S. equity funds as well as stocks listed on the S&P 500, NASDAQ, and other U.S. exchanges, there are plenty of opportunities to explore.

**NEXT STEP: Let's get together soon to talk about U.S. investments and your portfolio.**

1 International Monetary Fund, *World Economic Outlook Update*, January 2017.

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The long sunny days of summer are an ideal time to relax and reflect on your goals and how they might be evolving.

Whether you're looking long-term or near-term, saving for a new deck or for the future, we are always available to review your options with you, and to discuss how any recent life changes may affect your portfolio.

We remain committed to helping you find ways to make investments work harder – even when you're taking a summer break.

# Global economy on the upswing

After a disappointing 2016, the world economy is gaining momentum. The United States continues to lead the way, but a rebound in China's economy is also lifting emerging markets. This is helping to bolster corporate earnings expectations, which is usually good news for stock markets. Indeed, all major global equity markets hit new highs in early 2017.

Although the National Bank Financial Economic & Strategy Group continues to recommend an overweight position in equities relative to fixed income, caution is warranted at this stage in the market cycle. Valuations are stretched, and economic and political risks remain. As always, what's right for your portfolio will depend on your tolerance for risk and your investment objectives.

## U.S. LEADS THE WAY

The U.S. economy continues to perform well. Labour markets are surging, and economic stimulus (in the form of deregulation and tax cuts to business) is expected to help. While inflation has risen, price pressures should remain contained by a strong U.S. dollar and two expected increases in interest rates.

The National Bank Financial Economic & Strategy Group notes that the world economy expanded just 3% in 2016 — the worst performance since the 2009 global recession. Slowing industrial output kept the lid on growth, especially in Japan and the Eurozone. But the global economy appears to have turned the corner, and growth of 3.3% is expected in 2017 and 3.4% in 2018. Solid trade activity in China should continue to bolster emerging markets.

Here at home, Canada's energy sector is on the mend, and the economy is bouncing back nicely as a result. Growth should pick up this year as exporters respond to improving U.S. demand and the newly approved trade agreement with Europe.

## PROFIT EXPECTATIONS RISING, BUT RISKS REMAIN

Economic momentum is having a positive effect on corporate profit expectations. Global earning revisions have turned positive for the first time in six years, helping sustain the uptrend in equity markets. However, this positive backdrop for equity markets is being blurred by relatively high valuations and political risks — including growing trade protectionism, high debt levels, and political instability.

In Europe, the economic and political fallout from Brexit is still playing out, while in Greece (which is still mired in a 10-year economic slump), government debt looks unsustainable at 180% of Gross Domestic Product.

And while tax cuts and deregulation are expected to boost U.S. economic growth, the new government's protectionist agenda is a risk, as it could derail the progress made in integrating the global economy.

**NEXT STEP: We'd be happy to review global opportunities with you in light of ongoing economic developments, your tolerance for risk, and your investment objectives. Please give us a call today.**

# Expecting to need U.S. dollars? Smooth out the cost of purchase

For Canadians who frequently visit the U.S., invest and/or do business there, or plan to spend a lot of time in retirement south of the border, a U.S.-dollar bank account is a convenient way to access U.S. funds.

But with the U.S. dollar expected to remain strong in 2017, you may be concerned about currency exchange costs. An easy solution is to take a "dollar-cost averaging" strategy to purchasing U.S. money:

On a regular basis, use the same amount of Canadian dollars to purchase U.S. currency. For example, you might exchange C$300 every month, C$1,000 every quarter, or C$1,500 every six months — whatever suits your cash flow.

Over time, this approach can help to smooth out the effect of exchange-rate fluctuations — all the while earning interest on your savings. When you need to access U.S. funds in the future, they'll be readily available, and the exchange rate won't matter.

**NEXT STEP: Both cash and margin accounts at National Bank Financial-Wealth Management can be held in either Canadian or U.S. dollars. Ask us for complete details.**

## Contingency planning — How to prepare for a financial setback

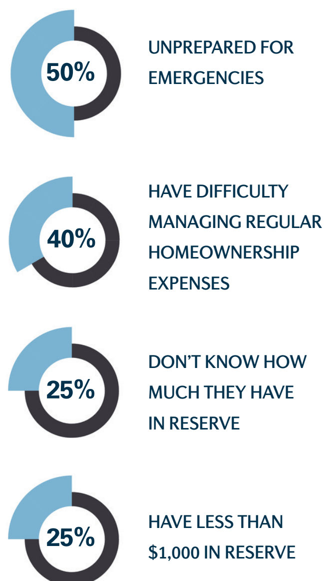
The general rule of thumb is to keep enough "emergency" cash on hand to cover three to six months of living expenses — groceries, the rent or mortgage, utilities, phone, transportation, and so on. The amount appropriate for you, however, will depend on your personal circumstances. If you are single, have a secure job, and your skills are in high demand, three months' worth of expenses might suffice. On the other hand, if you have dependants, or your income fluctuates because you work on commission or are self-employed, a larger emergency fund might be more appropriate.

You'll want the money you put away for financial setbacks to be completely secure and easily accessible. Money market funds, cashable Guaranteed Investment Certificates (GICs), and high-interest savings accounts are all good options.

**NEXT STEP: We'd be happy to help you determine the appropriate amount for your emergency reserve and to choose where to hold it for security, accessibility, and maximum returns.**

[1] Manulife Bank of Canada, *Debt, dollars and decisions: Three generations of homeowners talk about debt and money management*, November 2016.

**MOST CANADIANS FINANCIALLY UNPREPARED[1]**



Investing Strategy

## There's strength in unity

Diversification is a key element of successful investing. However, there is one instance in which it can actually work against your best interests. When you hold investments across a number of different accounts or at multiple institutions, you open yourself up to a host of potential problems.

### THE DANGER OF A DIVIDED APPROACH

Taking a scatter-shot approach can result in asset duplication and lack of diversification. For example, if you hold a Canadian equity fund along with individual holdings in bank and railway stocks, there is almost certainly some duplication of securities.

Other drawbacks include portfolio sprawl, excessive fees, and less-than-optimal tax efficiency. In addition, managing more than one account can eat up your personal time as you grapple with multiple statements, tax slips, and account representatives.

### CONSOLIDATE — AND CONQUER

Having all your investments under one umbrella makes it easier to:

- Track and manage your holdings.
- Take advantage of tax-saving strategies, such as tax-loss selling.
- Allocate your investments into the most tax-friendly account (for example, holding assets that generate interest income in a registered plan).
- Truly sculpt your portfolio to your individual requirements.

**NEXT STEP: Let's talk about how we can ensure your investments are working together as efficiently as possible.**

Investment Planning

# Guaranteed investments: The illusion of safety

Ongoing market volatility has many Canadian investors beating a path from equity investments to low-risk vehicles like Guaranteed Investment Certificates (GICs) and money market mutual funds. In fact, net redemptions of equity mutual funds in 2016 totalled $6.04 billion.[1]

### THE DOWNSIDE OF SAFETY

But, "safe" investments have risks of their own, such as:

**Low returns.** With interest rates remaining near record lows, returns are likely to be negligible. In May 2017, for example, the best available rate on a three-year GIC was less than 2% at most institutions.[2]

**Top tax rates.** Outside of Tax-Free Savings Accounts, Registered Retirement Savings Plans, and other registered plans, interest income is fully taxed. So if your combined (federal and provincial) marginal tax rate is 40%, 40 cents of every interest dollar you earn is taxed away.

What does that look like in dollars and cents? Here's an example: Suppose you have $15,000 in a non-registered GIC earning 1.8% annually. At the end of the year, your interest earnings will be $270. At a marginal tax rate of 53.31% (the top rate in Quebec), you'd be left with net earnings of $143.91, or 0.96% on your original investment.

**Inflation.** As if the tax bite weren't bad enough, there's also inflation to take into account. As of December 2016, inflation (as measured by changes in the Consumer Price Index) was running at 1.5% annually.[3]

In other words, once you factor in low interest rates, income taxes and inflation, those "guaranteed" returns could actually be costing you money. That's why equities are essential.

### EARNING 'REAL' RETURNS

Over the longer term, equities have historically outpaced inflation by a greater margin than assets that generate interest income. In addition, equities have the potential to generate dividend income and capital gains, both of which are taxed more favourably than interest income when earned outside of a registered account.

What about volatility? It's true that equities may fluctuate in value over the short term. However, a big part of our mandate is to mitigate that risk. We do that by making sure your portfolio is diversified and focussing on the long term.

**NEXT STEP: Secure investments will always have a role in most portfolios. The key is to use them strategically, not as a refuge from short-term volatility. You can count on us to keep the balance of growth, income, and security appropriate for you.**

1 IFIC Industry Overview, January 2017.
2 ratehub.ca.
3 Statistics Canada, Consumer Price Index, December 2016.

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