

# MacDougall Wealth Management Group Newsletter



Spring 2021

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## Beyond Buoyant Market Times: Why Advice Matters

If there's one thing that the pandemic has taught us, it is to expect the unexpected. The financial markets hit all-time highs to start the year, despite what has been happening on the ground. As markets advanced, many stocks invariably became winners. This has helped to drive confidence in many investors. While investing during bull market times may appear to be a winning strategy, longer-term investors should not forget that markets are cyclical in nature.

Seasoned investing involves a variety of elements that may easily be overlooked during good times. Over recent months, with the rise in attention to low-cost and commission-free platforms, many investors have found success in simply trading on momentum and noise, without understanding the fundamentals of their investments. In times like these, the prices of securities often become stretched, but over the long run, the markets will generally correct themselves to reflect the fair value of the companies traded.

A recent study looked at the trading activity on a popular commission-free platform over the past two years. It showed that the top 0.5 percent of stocks bought each day experienced return reversals, or losses, of approximately 5 percent, on average, over the following month. Why did

this happen? According to the study, many of these investors were inexperienced and tended to chase performance. Furthermore, the commission-free nature of the platform encouraged trading, which led to speculative behaviour.<sup>1</sup>

Seasoned portfolio management also involves managing risk. As advisors, we use techniques such as asset allocation, diversification, and rebalancing, while taking into account an investor's risk tolerance and time horizon, to adjust and help protect portfolios throughout the inevitable market cycles. Our focus is to help preserve capital while generating wealth over the longer term, recognizing that most investors will be investing over multiple market cycles.

What will happen during a market downturn, a time in which some investors may panic or make rash decisions? Professional advice can help to manage emotions during these critical times, something that many investors may find challenging. A study that tracked investors over a longer period of time showed that self-directed investors significantly underperformed the markets over time, likely because they acted on emotion. These investors often traded too frequently, having a tendency to sell winning investments more quickly and hold on to losing investments in the hope that they would regain their losses. The study concluded that, in the words of Benjamin Graham, "the investor's chief problem—and even his worst enemy—is likely to be himself."<sup>2</sup>

Wealth management advice can often go beyond investing. This may include exploring tax-efficient strategies, planning for retirement, using asset protection or enhancement tools and even supporting estate planning. There are many resources available to help guide the path to achieving your financial goals. And, by having support for the management of your wealth, you can focus on what is important to you.

1. [papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3715077](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3715077) • 2. [https://faculty.haas.berkeley.edu/odean/Papers%20current%20versions/Individual\\_Investor\\_Performance\\_Final.pdf](https://faculty.haas.berkeley.edu/odean/Papers%20current%20versions/Individual_Investor_Performance_Final.pdf)

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## Testamentary Trusts

A trust is a legal relationship between a person holding and administering property (the Trustee) for the benefit of another person (the Beneficiary). A trust which is set out in a Testator's Will and only comes into effect upon the passing of the Testator is called a Testamentary Trust. The Testator chooses the Trustee, the beneficiary, the assets to be held in the trust and the terms of the trust which will govern when and for what purposes the Trustee can distribute any part of the trust fund to the beneficiary. The Trustee has a fiduciary responsibility to the beneficiaries and must administer the trust in accordance with the terms set out in the Will. A trust is also a separate legal entity and the Trustee will be responsible for preparing an annual income tax return on behalf of the trust.

The terms of a trust are very flexible and the Testator is able to build it to suit the circumstances. In most cases trusts are set up as a protective mechanism to keep assets in a protected environment until the beneficiaries are ready to handle the assets themselves or for the lifetime of the beneficiaries if necessary.

The most important considerations when setting up a trust are:

1. The choice of trustee – this person(s) must be familiar with financial matters and ought to be very trustworthy. As well, they must be able to handle complex personal situations as well as complex financial matters. It is very important that the trustee be resident in Canada. The following may be appointed as trustee:
  - a. Friend
  - b. Family member
  - c. Lawyer or accountant
  - d. A professional trustee such as Natcan Trust, the trust department of National Bank.
2. Will the Trustee be compensated for taking on this responsibility? Will they receive a lump sum or an annual payment for the duration of the trust?
3. What assets or dollar amounts are going to form the trust property? Is the amount sufficient to justify the annual tax return preparation fee and the potential Trustee compensation?

4. The terms of the trust:

- a. How long is the trust to be in place? For a certain number of years, until the beneficiary reaches a certain age, or for the lifetime of the beneficiary are just some of the options.
- b. What distributions are to be made to the beneficiary?
  - i. Income and/or capital
  - ii. Specific monthly or annual payments
  - iii. Payments only for certain expenses
- c. What happens to the remaining assets or funds, when the beneficiary passes away or when the trust is terminated?

Instead of setting up a trust for the beneficiary, you could direct your executor to purchase a fixed term annuity which would provide payments to the beneficiary over whatever time frame you choose (eg. 5 years, 10 years, etc.) The longer the time frame, the less that the beneficiary would receive each year. You may wish to have a discussion with an insurance specialist to determine options that are available which might suit your intentions.

– Connie Hykaway  
Senior Advisor, Estate Planning



### Spring Cleaning Your Estate Plan

Here are five questions that may prompt a review:

- ① Is my plan structured in a way that promotes efficient administration and limits expense?
- ② Will my plan minimize family effort or even controversy?
- ③ Are my assets structured to limit exposure to potential liability (i.e., former spouses, creditors)?
- ④ Do I have protection in place to allow my family to make financial and healthcare decisions in the event I am unable?
- ⑤ Can my family maintain their current lifestyle if I am no longer able to contribute?

## Get the most out of your farm – How to evaluate a new project

In the context of farming, assets are considered productive, or non-productive, in their contribution to the bottom line. Productive assets generate funds directly and generally rise in value over long periods of time. For example, land, quota, or livestock. On the other hand, non-productive assets support productive assets but do not generate funds directly. These can include equipment, buildings, and inputs. The values of these assets reduce over time if they are not maintained or used. Both asset types are required to make your farm successful and can positively increase the long-term productivity and profitability of the farm.

Considering buying land, equipment, quota, or livestock, requires careful examination. Regardless of the project size, farm operators must consider the financial feasibility of the project. This may be limited given your current debt servicing level, or feasible if you carry excess cash. The producer needs to know and understand that the additional revenue an asset will generate is greater than the relative the cost incurred. As with any strong business decision, the goal is always to improve the profit margin and efficiencies of the operation.

The value of an asset is measured by its economic and market value. The economic value is tied to the profitability of the asset. The market value is the ability and willingness of someone to purchase the asset. Typically, market value fluctuates due to market supply and demand, commodity market fluctuations and individual purchasing power. The

economic value of assets within your operation is the ability of those asset to generate cashflow for you. Productive assets will have greater economic and market value compared to nonproductive assets. It is important to consider both of these factors, often an asset available for purchase could have a higher market value than economic value or vis versa.

The current low interest rate environment can present opportunities for producers to consolidate their debt and reduce overall costs. We encourage you to review your financials with us to identify any potential savings.

Feel free to reach out to a member of our team to consult on your asset profitability and debt consolidation needs.

- Edith Bovay  
Director Agriculture and Commercial Banking

## Food for Thought: the Rising Canadian Dollar

Over the past year, the Canadian dollar (CAD) has been gradually appreciating in value, rising by 15 percent after it fell to a low of 0.69 USD in March 2020. What's driving the loonie's flight?

Oil prices, which briefly turned negative in April 2020, were one reason why the loonie struggled. The CAD is largely impacted by the price of oil since Canada earns a large portion of its U.S. dollars (USD) from the sale of oil. As oil prices have rebounded to pre-pandemic levels, this has helped to strengthen the CAD.

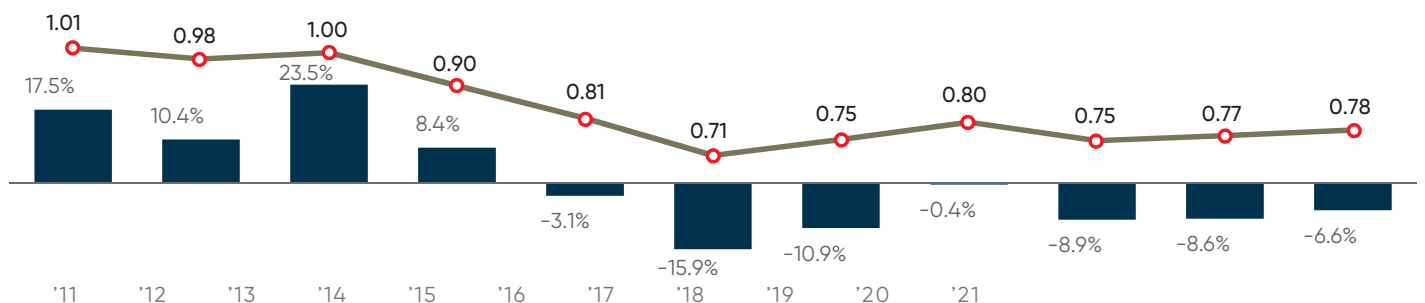
At the same time, the USD has been losing its lustre. Significant U.S. stimulus actions have increased the money supply, creating concerns about future inflation and placing downward pressure on the greenback. With near-zero interest rates and a yield on U.S. government bonds closer to that of other developed nations, this may reduce demand for U.S. treasuries and further weaken the USD.

Will the loonie continue its upward flight? Here is some "food for thought." The "Big Mac Index," published by The Economist magazine, is a fun tool to make exchange rate theory digestible. It compares the purchasing-power

parity (PPP) of global currencies. PPP suggests that over the long run, exchange rates should adjust so that an identical basket of goods/services costs the same in each country. Instead of using a basket of goods, it creates an exchange rate by comparing the cost of a Big Mac in a nation's currency to its cost in the U.S. Comparing this to the prevailing exchange rate determines whether a currency is considered under- or over-valued. The bar chart shows the under/over-valuation of the CAD versus the USD based on the Big Mac. The actual exchange rate is shown on the blue line.

Currency fluctuations are a normal part of the financial markets. While a stronger CAD may provide better buying opportunities to purchase U.S. assets, for longer-term investors, the impact of currency changes on returns has the tendency to even out over time.

### Big Mac Index Over/Under Valuation: CAD vs. USD 2011 to 2021 (Jan.)



Source: January data: [github.com/TheEconomist/big-mac-data](https://github.com/TheEconomist/big-mac-data), accessed 2/11/21.

## The Short & the Long of It: GME & the Problem of Wealth Inequality

The rise and fall of GameStop (GME) shares captured the headlines in January. While it exposed the dangers of options trading, it highlighted a more endemic issue: the growing problem of wealth inequality.

GameStop had a significant amount of short positions held by large hedge funds.<sup>1</sup> Recognizing this, a group of retail investors, using an online forum, worked together to purchase shares and drive up the price.

### First, a Primer on Shorting Stocks

When you short a stock, you must borrow the stock from a broker and then sell it in the open market. Since it is borrowed, in order to exit your position at a later date, you must repurchase the stock to return it to the broker. If the share price declines in value, you have made a profit. If the share price increases, you suffer a loss. The higher the price, the greater the loss.

With GME, as retail investors purchased shares to drive up the price, those holding short positions needed to repurchase the shares to exit their positions and minimize their losses, which further pushed the stock price higher. Before long, the GME share price jumped from US\$17 to \$347, in what is called a "short squeeze."

### Does This Signal a Problem with Financial Markets?

Some have questioned whether the financial markets can effectively function when stock movements become so disconnected from fundamentals. But let's not forget that, over time, markets have always attracted speculation resulting in temporary periods of inefficiency.

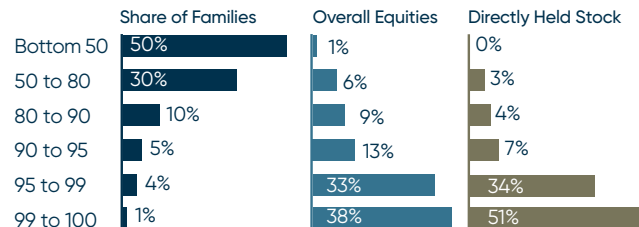
Individual investors are far from the point where they are disrupting the main purpose of equity markets: to help companies raise capital. Traders today do have a greater ability to influence stock market movements; retail order flows have reached 20 percent of the U.S. stock market's total, twice what they were in 2010.<sup>2</sup> Yet, it

is unlikely that the players creating large intraday movements for single securities can have the same impact on the overall market.

### A Problem: The Rise of Populism & Stock Market Inequity

However, the GameStop situation has highlighted a more pervasive issue. Some have compared it to the Occupy Wall Street movement,<sup>3</sup> representing a generation that feels left behind. Income inequality is at significant highs. No more is this evident than in the stock market. Consider that the top 20 percent of earners own nearly all of the stocks held by U.S. households.

### Wealthy Families Own a Greater Share of Overall Equities



Families grouped by percentiles of net worth:

Well-respected economist Jeff Rubin confronts these realities in his book, *The Expendables*, suggesting that we now stand at the edge of a "cliff" created after sacrificing our middle class and outsourcing production and jobs to low-cost China. The economic consequences stemming from the pandemic have only made this inequality worse. The anger from the GameStop situation has been palpable, and it is not likely to end here.

1. By some accounts, approximately 140 percent of the public float had been sold short
2. "Day Traders Won't Sack Wall Street," *The Wall Street Journal*, Mike Bird, Jan. 27, 2021
3. [cnet.com/news/reddits-amc-gamestop-surge-happened-because-of-anger-over-wall-street/](https://cnet.com/news/reddits-amc-gamestop-surge-happened-because-of-anger-over-wall-street/)

## Congratulations

### Shaylene Strangways

Wealth Management Elite Club Award.

"Shaylene has distinguished herself through the dedicated client services she provides and has projected a positive attitude within the firm."



Member, Elite Club 2020

### MacDougall Wealth Management Group

Wealth Management Excellence Award  
- Alberta and Okanagan Region

"The MWMG has distinguished themselves through the successful management of financial assets and has demonstrated superior performance in overall wealth management and exemplary community involvement"

2020 Awards of Excellence

Wealth Management Excellence  
Alberta & Okanagan

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