Financial Planning Guide

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FOCUS ON MUTUAL FUNDS

Tune out the noise stateside

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.

With TV, the Internet, and social media operating 24/7, global political and business events can quickly affect the markets. It's going to be important for investors to keep their perspective over the next four years and try to avoid anticipating what Trump — or anyone else — may or may not say about the markets. Remember, we are not investing for one day, or one year, or one presidential cycle — but for the longer term.

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

Canadian investors who avoid 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 additional diversification.

Let's get together soon to talk about U.S. opportunities for your portfolio. These range from broad-based mutual funds that track the entire U.S. market, to sector-focused funds, to currency-neutral options that smooth the effects of exchange-rate fluctuations. ■

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

Canada: 150 years old and plenty to celebrate!

MUTUAL FUNDS

The spectacle of the new, media-savvy U.S. president has made it hard to look away from events stateside. But we'd like to draw your attention homeward for a moment.

The International Monetary Fund (IMF) is predicting that Canada will post the second highest growth rate among advanced economies in 2017 and 2018.[1] Indeed, Canadian markets are well positioned to adapt to shifting global themes in 2017, including a rebound in commodity prices. Mutual funds offer a convenient way to take part in Canada's recovery.

Resource rebound

The resource sectors, such as materials and energy, helped the Canadian markets rebound in 2016, and this theme is playing out again in early 2017. The energy sector is feeling better about its prospects since U.S. President Trump came into office, and with pipelines getting the go-ahead in Canada and possibly the U.S., energy could benefit. The materials sector could benefit from the continued recovery in U.S. housing, along with the new administration's focus on building out infrastructure.

How to take part. There are many ways to take part in the resource rebound. Diversified natural resources funds may include energy and materials investments, while many core Canadian equity funds will also have market-weighted allocation to the resource sector.

Industrials and infrastructure

With Canada's economy picking up steam, the industrials sector is poised to benefit. Investing in infrastructure is a key part of President Donald Trump's economic strategy and was also a prominent feature of Prime Minister Justin Trudeau's economic update last fall. Infrastructure is also expected to give a lift to the industrials sector here in Canada, while providing support to the materials sector as well.

How to take part. Broad-based Canadian mutual funds will have positions in the industrial sector. Global infrastructure funds provide an opportunity to take part in the expected infrastructure renaissance in both Canada and the United States.

Bullish on banks

Economic growth in the U.S. and in Canada could prove positive for Canada's all-important financial sector, as should rising interest rates in the U.S. and less financial regulation south of the border. Canada's financial sector is attractively valued, and is home to many of the most stable blue-chip companies in the country.

How to take part. Many Canadian equity funds include banks among their top holdings, but there are also funds that focus exclusively on the financial sector.

Diversify through real estate

With positive economic growth expected for Canada and the U.S. and a lack of affordable rental units here at home, real estate investment trusts (REITs) could perform well. For investors, real estate provides opportunities to diversify their portfolios in ways that aren't connected with traditional stock markets.

How to take part. Real estate funds typically invest in REITs and public real estate companies.

REITs are also commonly found in income mutual funds. The majority of real estate funds hold commercial and corporate properties, although they also may include undeveloped land, apartment complexes, and agricultural space.

Investment considerations

Canada's prospects have always been tied to events in the U.S., and while the economic agenda south of the border currently aligns with ours, President Trump is still a wildcard, as are any potential revisions to the North American Free Trade Agreement (NAFTA) that may affect Canadian exporters.

As part of your diversified investment strategy, let's work together to find the amount of Canadian exposure that's right for you as well as individual funds that align with your investment objectives and risk tolerance. After all, what better way to celebrate Canada's sesquicentennial than by participating in the growth of our markets? ■

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

MONEY MANAGEMENT

Smooth out the cost of U.S. dollars

If you visit the U.S. frequently, invest or do business there, or plan to spend a lot of time in the States in retirement, a U.S.-dollar banking account can be convenient and save you time and effort when you need U.S. funds. Many Canadian financial institutions offer a range of U.S.-dollar savings and chequing accounts, which give you the option to save, write cheques, and earn interest in U.S. dollars.

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. dollars. Here's how it works:

Step 1. Open a U.S.-dollar banking account.

Step 2. On a regular basis, use the same amount of Canadian dollars to purchase U.S. currency. For example, you might exchange C$200 every month, C$500 every quarter, or C$1,000 every six months — whatever suits your cash flow.

Over time, this approach can help to smooth out the effect of exchange-rate fluctuations — all 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. ■

EYEOPENER

Are you prepared for a financial setback?

A recent bank survey[1] suggests that about half of all Canadian homeowners don't have enough money set aside to deal with a financial emergency — and that one-quarter of those surveyed had less than $1,000 in reserve.

How much is enough?

The general rule of thumb is to keep enough cash on hand to cover three to six months of living expenses — groceries, the rent or mortgage, utilities, phone, transportation, and other necessities.

The amount that *you* should be saving will depend on your personal circumstances. If you are single, have a secure job, and your skills are in high demand, you can probably get by with three months in reserve. If you have dependents or your income fluctuates because you work on commission or are self-employed, you may want to build a larger emergency fund.

Where to keep it

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.

We can help you figure out how much of an emergency reserve is right for you and choose the best place for it. ■

unprepared for emergencies

have difficulty managing regular homeownership expenses

have less than $1,000 in reserve

don't know how much they have in reserve

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

Guaranteed investments may not provide the returns you need

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 about $ 6.04 billion as of December.[1]

The downside of safety

But "safe" investments have risks of their own. 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]

And then there's the issue of taxation. 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 put $5,000 in a non-registered GIC earning 1.8% annually. At the end of the year, you'd have interest earnings of $90. At a marginal tax rate of 45%, you'd be left with net earnings of $49.50, or 0.99% on your original investment.

Don't forget about inflation

Still, earning 0.99% is better than losing money, right? Unfortunately, there's still 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 equity based mutual funds are worth considering.

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

A question of balance

Secure investments like GICs 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 mix of growth, income, and security in alignment with your long-term goals, time horizon, and risk comfort level. ■

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

There's strength in unity

When you hold mutual funds 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 fund duplication and lack of diversification. For example, if you hold a Canadian balanced fund and Canadian growth fund, there is almost certainly some duplication of the underlying 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.

Benefits of consolidation

Having all of your mutual fund holdings under the same umbrella, on the other hand, offers the following advantages:

- **We can more easily track and manage your holdings.**
- **We may have a clearer line of sight to potential tax-saving strategies.**
- **It makes it easier to allocate your investments into the most tax-friendly account (for example, holding fixed-income funds in a registered plan).**
- **Seeing all of your funds at a glance means we can truly sculpt your portfolio to your individual requirements.**

Let's talk about how we can ensure your investments are working together efficiently. ■

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