Money Ideas

Summer 2022

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▶ MUTUAL FUND INVESTING

Is there opportunity in market volatility?

When markets are volatile, everyone's pleased with the upswings, perhaps eagerly checking out their mutual fund performance. But the downswings can be another story. Maybe those portfolio balances still get checked, but nervously.

Silver linings

Fortunately, during the wealth accumulation years, market downturns can bring opportunity. When share prices fall, the money managers behind your mutual funds see prospects for profit. They can add to current holdings at discounted prices or invest in companies on their watch list that were previously too expensive.

Just as money managers can take advantage of buying low, so too can investors. All you need to do is continue making regularly scheduled contributions, even when markets are down. Sometimes it may take patience and discipline, but when markets recover and fund values rise, the money managers' individual stock picks and your continued investments can boost your portfolio's value. It's a buying opportunity.

When to manage volatility

Market volatility doesn't always have a silver lining. When approaching retirement, you don't want to risk a significant market downturn that might cause you to postpone your retirement date. So most investors typically make their mutual fund investments more conservative to help preserve their portfolio as retirement nears.

During retirement, market downturns certainly don't represent buying opportunities – since you're now drawing income, not investing new money. Several strategies are available to minimize the effects of market volatility, including investing in mutual funds that have been historically less volatile and drawing retirement income from a money market reserve that allows time for any downtrodden equity investments to recover.

Talk to us if volatile markets, particularly the downswings, ever cause you to worry. We can discuss investment opportunities and also make sure your portfolio remains aligned with your risk tolerance. ◀

Why diversification matters

Investing can be unpredictable. Will interest rates remain the same, go up or fall – and when? Exactly where are we in the market cycle, and how long until we enter the next phase? Will a geopolitical event, health crisis or other incident shock the markets? Which mutual fund investments offer the most opportunity over the next year?

Everyone can try to make predictions, but no one can always know the answers. That's one of the key factors behind the strategy of creating a fully diversified portfolio. Since we can't predict the market leaders or underperformers year to year, it's best to cover all bases.

Benefits of diversification

A well-diversified mutual fund portfolio can benefit investors in three key ways.

Minimize risk. By spreading your investment dollars across a variety of investments, you ensure that you won't be over-invested in any particular underperforming market.

Enhance performance. Every January, investment analysts predict which markets will be among the year's leaders, and invariably every December we're reminded to expect the unexpected. However, if your investments are fully diversified, you will likely have some exposure to the year's market leaders, which can potentially enhance portfolio returns.

Reduce volatility. If a portfolio only includes a handful of funds that respond alike to the same economic conditions, portfolio returns could rise and fall sharply at the whim of the markets. A fully diversified portfolio is constructed with investments that react differently to economic conditions, which smooths out returns and reduces portfolio volatility over time.

A look at market indexes

Talking about portfolio diversification in theory is instructive, but the benefits are much clearer and more impactful when you view market unpredictability in reality. Take a look at the table below to note the following observations.

- The notion that an investment can go from laggard to leader in just one year is demonstrated by Global Bonds. In 2017, they sit at the very bottom rank, then in 2018 Global Bonds rise to market leader.
- To see how any investment can be unpredictable year to year, follow Canadian Equities from left to right to track a zig-zag path that hops up, down and in between.
- By diversifying, you have a greater chance of gaining exposure to the best-performing markets. In just the six years represented on this table, four different indexes held the position of market leader.

Ways to diversify

The broadest way to diversify a mutual fund portfolio is through investing in different asset classes, the major ones being equities, fixed income and cash equivalents. You can also be diversified within each asset class. For example, within equities, you can be invested in small-cap, mid-cap and large-cap companies – "cap" or capitalization referring to a company's size.

Investment style offers another way to diversify, as value and growth investments often take turns outperforming each other. Investing in a variety of geographic regions also provides all the benefits of diversification – and opens up specific investment opportunities less available in Canada.

If you would like to talk about the various ways your mutual fund investments are diversified, please get in touch.

Market leaders change year to year

Financial market indexes ranked in order of performance

- Canadian Equities
- U.S. Equities
- International Equities
- Emerging Markets Equities
- Canadian Bonds
- Global Bonds

	2016	2017	2018	2019	2020	2021
Best	21.1%	28.7%	7.7%	24.8%	16.6%	27.6%
	8.1%	17.4%	4.2%	22.9%	16.3%	25.1%
	7.7%	13.8%	1.4%	16.5%	8.7%	10.8%
	1.7%	9.1%	-5.6%	12.9%	7.3%	-2.5%
	-1.5%	2.5%	-6.5%	6.9%	6.4%	-3.1%
Worst	-2.0%	0.3%	-8.9%	1.4%	5.6%	-5.5%

Canadian Equities: S&P/TSX Composite Index | U.S. Equities: S&P 500 Index | International Equities: MSCI EAFE Index | Emerging Markets Equities: MSCI Emerging Markets Index | Canadian Bonds: FTSE Canada Universe Bond Index | U.S. Bonds: Bloomberg U.S. Aggregate Bond Index | Global Bonds: Bloomberg Global Aggregate Bond Index

All returns are in Canadian dollars. This table is provided for illustrative purposes only. Note that it is not possible to invest directly in an index. Source: Morningstar Research Inc., December 31, 2021.

Should you and your spouse retire together?

It may seem natural and expected for a couple to have the same retirement date, starting this new chapter of their life together. But it's quite common for spouses to retire at different times.

Reasons for retiring apart

An age gap of several years or more is behind a great many couples' decision for one spouse to retire before the other. But a variety of situations can lead to retiring at different times. One spouse may retire earlier than planned due to ill health. Or a spouse may leave their job to look after an elderly parent who needs care. Perhaps one spouse receives an early retirement offer from their employer. Or one spouse might work past the traditional retirement age because they find their work fulfilling, while the other spouse looks forward to retirement.

The financial factor

The decision of whether or not to retire at the same time often involves a financial factor. Take the situation of a couple with an age gap. Say one spouse is 65 and the other is 60. They're thinking about both retiring now, so they'll have more of their younger years to enjoy retirement together. However, if the older spouse retires now, and the younger spouse works for a few more years, the additional savings may give the couple a more comfortable retirement lifestyle. Also, while the younger spouse receives income, the retired spouse can possibly delay withdrawals from retirement savings.

How does this couple decide? It can be a lot easier when you involve us with the financial side of the decision. We can show you what your estimated level of retirement income and overall financial picture could be with a staggered retirement and a synchronized retirement. Then you can consider both the personal and financial factors to make an informed decision.◂

Managing asset allocation in an RESP

A Registered Education Savings Plan (RESP) has three important phases where the asset allocation between equity, fixed-income and cash-equivalent mutual funds is critically important.

Initial years

If an RESP is opened fairly soon after a child's birth, the long time horizon allows for a heavy focus on equity funds for greater potential returns. Starting a plan with 75% or more in equities is quite common. But equally important is the risk tolerance of the person who opens the RESP, known as the subscriber. An aggressive investor might start with 90% of their plan in equity funds, whereas a conservative subscriber may start with 75% in fixed-income funds, and the plan chosen could be perfectly suitable for each person.

The conservative investor, like all subscribers, can still take full advantage of the Canada Education Savings Grant (CESG). The first $2,500 of annual contributions triggers $500 in grant money, to a maximum of $7,200 for each beneficiary.

Middle years

Whatever the initial asset allocation happens to be, it's common for subscribers to gradually reduce equities and increase fixed-income investments to some degree during the middle years of an RESP. It's all about protecting your investments from the risk of a significant or prolonged market downturn when there is not enough time remaining for the markets and RESP to recover and grow. To illustrate, some subscribers with a moderate risk tolerance might have an RESP that's approximately 50% equities and 50% fixed income when the child is about 8 to 10 years old.

Approaching graduation

Different subscribers' asset allocations may vary greatly in the early years, but they'll typically be quite similar by the time secondary school graduation nears. In these final years, equities are reduced, sometimes to zero. Fixed-income investments increase and cash equivalents are introduced. For many subscribers, the entire plan may be invested in cash and low-risk investments before it's time to withdraw funds for tuition and expenses.◂

Paying down your mortgage versus investing in mutual funds

When you have the money available, are you better off making extra payments on your mortgage or investing the amount to save for your retirement?

Investing is often viewed as the better choice if your portfolio's expected rate of return is higher than the interest rate on the mortgage. This is reinforced when investing in mutual funds in a Registered Retirement Savings Plan (RRSP) or a Tax-Free Savings Account (TFSA) – RRSP contributions offer a tax deduction, and TFSA contributions provide tax-free growth and withdrawals.

Paying down the mortgage can make financial sense for conservative investors who gauge that mortgage interest savings will outweigh earnings on low-risk investments. Also, many people just want the peace of mind of paying off their mortgage.

For some individuals, the answer is doing both. Contribute the available money to mutual funds in your RRSP, then apply the tax refund or savings to pay down the mortgage.

The mortgage versus investment decision isn't always easy. We can help you determine which solution best meets your particular needs. ◀

Preparing an estate directory

Imagine if an estate executor (or personal representative, liquidator or estate trustee, depending on the province) was about to administer an estate, and all they had was the will. They would have a tough time searching for contact people, important documents and hidden information. That's why it's important to develop an estate directory including everything your executor needs.

Start with the contact information of your lawyer, accountant, advisor and beneficiaries. State the location of your will, insurance policies, tax returns and safety deposit box. Provide bank account information. List assets, including registered plans and investment accounts, real estate and valuable items. Record login information and passwords for online accounts. Also, list debts, whether credit cards, a mortgage, loan or line of credit – and include monthly bills.

Be sure to keep your directory in a safe place, tell your executor the location, and review the information periodically in case updates are required. ◀

Do your registered plans have room for improvement?

Whenever you have extra funds to invest, it's a great opportunity to make up for any unused contribution room in your registered plans. Topping up your mutual fund investments in tax-advantaged vehicles is a real boost towards achieving your financial goals.

For your Registered Retirement Savings Plan (RRSP), you can find the amount on your Notice of Assessment. Look under the RRSP Deduction Limit Statement to see the unused contribution room carried forward from previous years.

Your Tax-Free Savings Account (TFSA) contribution room accumulates each year from age 18, regardless of when you opened the account – and can be carried forward indefinitely. You can also replace any TFSA withdrawals that you made before the current year. To find your TFSA (and RRSP) contribution limit, log on to your Canada Revenue Agency (CRA) My Account, use the MyCRA app or call the Tax Information Phone Service (TIPS) at 1-800-267-6999. You can also request the TFSA Room Statement from the CRA at 1-800-959-8281. ◀