The Francis Forum

Fall Edition 2020

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INSIDE THIS ISSUE

Is the traditional 60/40 Balanced Portfolio Obsolete?

Written by Michael Prittie

Stock markets can be volatile at the best of times, never mind during a pandemic, given the geo-political and economic headwinds. The traditional approach to mitigating equity risk and the associated variability of returns is to add varying amounts of bonds and diversify through a mix of corporate and government securities. You or your advisor would look at other risks such as the credit quality of the issuer and also duration (a measure of a bond's sensitivity to changes in interest rates).

In today's environment, the forecast is for sustained periods of low interest rates and bond yields. With inflation running around 2%, the real return from bonds these days is zero at best and very likely negative – especially in a taxable account. A six-year Bell Canada Bond maturing in August 2026 currently yields about 2.90%. A five-year government of Canada treasury bond maturing in September 2025 yields about 0.30%. The average Canadian bond fund yields about 2.50% (source: Morningstar). Other than reduced variability, bonds are *not* going to provide you with an oceanfront view let alone a long-term sustainable retirement income. How can one expect to get ahead financially in this environment and not outlive your investment income?

To address this situation, you needn't look further than **Private investments**; Canada Pension Plan, OMERS, Ontario Teachers Pension Plan, Harvard Endowment, etc. all embrace both income oriented and private equity. Private Income investments often provide similar stability of price compared to public bonds yet deliver predictably higher yields. It is said that "the wealthy invest differently" and the wealthy have been using private investments for years, so why not you? There are many such high quality, proven private investments that are income oriented, and have predictable yields ranging from 6% to 9%. While often not quite as liquid as the public bond market, most investors are more than happy to trade off a much higher income yield with a wait time of one to six months for liquidity. To help identify liquidity needs, we utilize an investment matrix to determine just how much exposure to private investments is suitable for a client. Also, Mandeville portfolio managers can act as your accredited investor so you can gain access to invest in this asset class. This is because to play in the "private sandbox" you must meet a prospectus-exemption, which typically involves having net income exceeding $200,000 for each of the past two years, or greater than $1 million in net liquid assets. Not easy for most! Working with a Portfolio Manager in a managed account relationship provides another avenue to prospectus-exemption and access to the world of private investing.

Don't let low interest rates or lack of access hold you back from obtaining the wealth you desire. For further information on just how powerful private investments can be in creating and preserving wealth, please contact us. Combined with an Investment Policy Statement and a written Financial Plan, you greatly increase your chances of viewing the ocean instead of a parking lot.

- This article was also featured in FACES Magazine, August 2020

Michael Prittie is a Portfolio Manager and Senior Investment Advisor with numerous designations.

Sincerely,

Duane

Around the Branch

Kyle Taylor has been with us for three years and has decided to take a job closer to his family in Newmarket, Ontario. We would like to thank Kyle for his hard work over the years and wish him well in his future endeavors.

Going forward:

- For administrative issues please contact Natalie Nunn at (613) 728-0101 ext. 221 or by email at nnunn@mandevillepc.com
- For tax and financial planning issue contact James Hickman (613) 728-0101 ext. 226 or by email at jhickman@mandevillepc.com
- For trades and securities inquiries contact Adam Prittie (613) 728-0101 ext. 230 or by email at aprittie@mandevillepc.com
- For insurance and estate planning please contact Shawn Ryan at (613) 728-0101 or by email at sryan@mandevillepc.com

Please note that any emails that are sent to Kyle Taylor's former email will be automatically forwarded and handled James Hickman to ensure nothing is missed.

Efficient Markets & Portfolio Management

Written by Adam Prittie

There has been a long-standing debate as to whether the global financial market is efficient, and whether it is possible to accurately predict stock prices with any degree of certainty. Although we all wish there was a pricing model to find the exact future price of any investment at any given time, it is not something that modern finance has been able to find as any model capable of doing so would be short lived. To examine why this is the case, suppose a research model suggests that the price of a firm will rise dramatically by 20%. On the news of an imminent increase, it would make sense that investors would rush to purchase this security with the goal of capturing this imminent return. However, with the news of an imminent and significant increase in price, current owners of the security would be reluctant to sell, and the net effect would be an immediate price increase of 20% to reflect the good news of a coming price increase.

As such, the notion of an accurate price predicting model is improbable because historically, it has been found that forecasts of positive or negative future performance often results in that performance being realized immediately rather than the 'expected date'. This result may make it seem like the market moves in an irrational and unpredictable manner, but in reality this outcome is actually an exercise in market efficiency. Due to there being no accurate model to predict exact prices, market prices for publicly traded investments are a reflection of all currently available information, which means that changes in price must result from both existing as well as new information. Naturally, this makes sense as analysts continually compete to uncover the most recent and relevant information to determine the next best investment which is why in some instances, we see dramatic increases and decreases in a company's stock price or within the overall performance of a certain sector when significant news comes to light.

It is imperative that we do not confuse this unpredictability with inefficiencies in the market, as if we are to believe that price changes are a reflection of both existing and new information, we must classify this as an efficient market. In fact, if we could predict prices with certainty, this would be a reflection of inefficiency as it would indicate that all publicly available information is not priced into the security. Therefore, the concept that the price of a publicly traded investment will reflect all available information is known as the strong form efficient market hypothesis.

Considering this hypothesis, it may be difficult to grasp how prudent investing can be performed because if price changes are unpredictable, how can an investor reasonably build a properly diversified portfolio? One way this can be done is through the use of a research method known as fundamental analysis where analysts can use existing information in the market to analyze earnings history and growth rates, expected future dividend payments, debt coverage, quality of the balance sheet and income statement, as well as to examine the industry and economy as a whole to determine the future growth and value prospects of securities. This type of analysis is often used to verify the validity and integrity of available information to gain valuable insight into expected future performance and price movements rather than focus on a specific future price. In turn, an analyst can use this process to find firms that are run more efficiently than everyone else's estimates suggest, or to find firms trading at a deep discount if the research determines that a specific security is undervalued or generally overlooked by other publicly available research reports.

Taking this a step further, the role of fundamental analysis in tandem with a portfolio manager is key to optimizing and diversifying an investment portfolio as even in an efficient market, security selection becomes an exercise in rational investment choice for determining the best portfolio for a client's risk tolerance and objectives. Rational investment policy in an efficient market often revolves around tax considerations, retirement planning, long term objectives, and life goals of the client. A Portfolio Manager for high income investors may want to build a portfolio focused primarily on non-dividend paying equity investments rather than a portfolio of interest income in order to defer the realization of capital gains to a year of lower income (i.e. retirement years), or the portfolio manager may opt out of fixed income products and dividend paying equities in exchange for higher expected future returns on other equities to avoid heavy tax burdens on interest and dividend income. In addition to this, investors of different age groups have differing requirements - Young investors will have a greater emphasis on capital appreciation whereas retirees will have a greater emphasis on capital preservation and the role of the portfolio manager is to continually optimize the portfolio and adjust the balance of securities to best suit each stage.

In summary, the role of portfolio management in an efficient market is based upon a client's optimal position according to factors such as age, employment, tax bracket, and risk tolerance, meaning that the role of the portfolio manager is to use the information available in both the market and the client's life to construct a custom portfolio to suit each of the client's needs, not necessarily beat the unpredictable nature of the market.

Adam Prittie is an Investment Advisor at Mandeville Private Client Inc. - Capital Wealth Partners

Are you sure your family cottage will stay in the family?

Written by Shawn Ryan

Summer is here and for many Canadians, this means a trip to the cottage to enjoy the place with your family. My neighbour James is heading to his cottage in Portland on The Big Rideau to spend some time with his kids and grandchildren. He has owned his cottage for over 30 years and has many happy memories. For James, like for many Canadians, it is important that the cottage stays in the family so that his kids and grandchildren can continue to enjoy it for many years to come!

This weekend, James is going to unveil a plan to transfer the cottage to his kids this summer. James is a widower, he is 76 years old, and wants to see the kids enjoy ownership of the cottage now. Before he made this decision there were many things to take into consideration so let me explain.

Over the years many cottages and other vacation properties have increased significantly in value and are now worth substantially more than the original purchase price. When you die there is a problem; assets can be transferred to your spouse tax-free, but a transfer to your children may trigger a capital gains tax that must be paid before the children can enjoy the property. As a matter of fact, 50 percent of this increase in value is subject to taxation which could trigger a significant capital gains tax liability to your estate. In James case, the cottage is now worth $800,000 and he paid $75,000 30 years ago. The total capital gain is $725,000 and so 50% of this increased value ($362,500) would be fully taxable. If James waits until his death, this amount could be much higher.

If your estate does not have enough assets, it may be forced to sell the cottage to pay the tax, which means the cottage would not stay in the family. Many people are not aware of this tax time bomb!

So, you might ask, what are my options? Several different options will provide the cash required to pay this tax liability at death which may include:

- ✓ You or your family can start saving today,
- ✓ Your heirs can borrow the money from the bank,
- ✓ Your estate can sell the asset,
- ✓ You can purchase life insurance to cover this growing tax liability along with other estate taxes,

Or you can sell the cottage to the kids today. Another idea to reduce the tax bill on the cottage: James could take advantage of the “capital gains reserve” in our tax law. This provision allows you to report a taxable capital gain over a period of up to five years. Yes, he’d still have pay tax, but reporting the gain over five years allows him to keep that money in his pocket longer and most likely pay less tax over all because he may not be in the highest tax bracket today as he may very well be at death.

The sale of the cottage will be structured as a sale at fair market value, not a gift. Furthermore, he’ll have to ensure that he doesn’t have a legal right to the sale proceeds immediately (otherwise he’ll pay tax this year, the year of the sale), but set this up so that he has a right to the proceeds only over the next five years – or longer.

James could sell the property for its value of $800,000 to the kids and take back a promissory note for that amount. The terms of the note will give him a right to demand payment of one-fifth of the sale proceeds each year for the next five years. James does not have to demand payment (so the kids don't have to come up with the money to pay him if he so chooses). Furthermore, James can forgive the promissory note in his will, with no tax consequences to his kids.

There are many ways to deal with this important matter along with other estate issues so a little planning can ensure your dreams of passing the family cottage to your family will come true.

Shawn Ryan, CFP, TEP is an Estate Planning and Insurance Specialist at Mandeville Insurance Services Inc. - Capital Wealth Partners

Here are 3 exercises you can do while stuck at home during COVID-19

This living room workout can work for anyone, B.C. trainer Beth Spooner says

Written by: Beth Spooner

Push-ups are a classic exercise you can do in the comfort of your living room and they can be modified for every fitness level. (Shutterstock / shurkin_son)

Is the couch calling to you more than cardio these days?

Understandable.

Maintaining a fitness routine while cooped up indoors is a challenge that B.C. trainer Beth Spooner can help with.

Spooner, president of Fitness on the Go, joined CBC's *The Early Edition* Wednesday to offer pointers for people who want to start, or keep, working out during the COVID-19 pandemic.

"Now is a fantastic time to start if you've never been exercising," said Spooner.

Don't forget to warm up

First things first, you have to warm up those muscles, especially if you've been hunched over a computer or listless in the living room.

Spooner suggests doing some jumping jacks to wake up your muscles. She recommends two sets of 60 seconds each.

Get low

It's squat time.

This simple exercise requires no equipment and targets your backside, legs, back and abdominal muscles all at the same time. You are using major muscles in a squat, which means they need lots of energy to work and the bigger the muscles, the more calories you burn.

Here's how to do it:

Plant your feet just slightly wider than shoulder width apart. Shift your weight to your heels, keep your chest lifted, and lower your backside until you resemble someone sitting in a chair.

Squats. You may hate them, but you'll probably like the results. (Shutterstock / antoniodiaz)

Spooner says you can use a knee-high chair or couch behind you as a guide. If you can't lower all the way down to sitting positing, just go down as far as you feel comfortable.

Then rise up, squeezing your glutes — the muscles in your backside — and repeat.

"You want to drive up through the heels, pushing the floor away from the body," said Spooner, who says your shins and chest should be parallel.

Aim for 20 squats to kick off your at-home circuit, Spooner says.

Push it real good

Get down and give me 20.

Gym class shudders aside, the classic push-up is still around for a reason.

Spooner says if you are new to the old move, the easiest way to start is actually standing up.

To do this, stand at a wall with both palms flat against it, then mimic a push-up from a vertical position.

Spooner suggests working from the wall, to the stairs if you have them, slowly progressing until you are comfortable doing a floor push-up.

Push-ups can be done against a wall for anyone not ready to hit the ground yet. (Shutterstock / Artsplav)

The wall and floor variations follow the same steps: retract your shoulder blades, lower your body weight, pretend you are pushing the wall or floor away from your body. Repeat.

"This is a great overall upper body strength and development exercise," said Spooner, adding that it is also a great calorie burner.

Twenty of these should do it.

Cramped cardio

Even indoors, you don't have to cut cardio out of your routine.

Spooner says your cardio exercise should be done for 60 second sets. You can do as few, or as many, sets as feel comfortable.

High knees is the cardio option Spooner suggests.

To do this, stand with your knees hip-width apart and lift your left knee up to your chest. Alternate legs at a jogging pace.

Get that heart rate up with a little high knees action. (Shutterstock / Artsplav)

If high knees doesn't thrill you, Spooner says jogging or marching on the spot is also beneficial. You could also try running up the stairs or more jumping jacks.

Go ahead and do the circuit again if you are feeling ambitious.

Spooner said moving your body is "a huge stress relief." And everyone could use a little of that these days.

Beth Spooner

https://www.cbc.ca/news/canada/british-columbia/home-fitness-covid19-tips-1.5509405

Client Seminars and Upcoming Activities

- Due to Covid-19 we have postponed our seminars and client events until further notice as the safety of our clients and staff is always our first priority.
- Our branch is following strict Covid-19 protocol for the protection of everyone. We are happy to have clients visit us in person – however; until further notice, Natalie Nunn will provide each visitor with Covid-19 screening questionnaire in advance of any visit. These <u>must</u> be completed, signed and submitted before your visit. Masks are mandatory in the building and branch. Otherwise telephone and interactive ZOOM review meetings are always available.

Thank you.

Duane