ISSUE 183

January / February 2018

mutual gains™

C.E. VANDENBERG & ASSOCIATES INC.

Financial Planning— Insurance— Wealth Management

Attentive - Attune - Attain®

We will listen carefully
to what you are saying
and be attentive to your desires
as well as your fears
so together we can build
and enjoy
a harmonious
and responsive relationship
in attaining your life's dreams
and through that
We will be attaining ours.

A Market Running Too Fast Will Stumble

In the first entry of the previous issue of Mutual Gains, I talked about how the length of the current "bull (up) market" cannot be used as the sole criteria for determining if we are nearing the end of an investment market's up trend.

No sooner did I post those thoughts, starting near the end of November, the equity markets in general moved up fairly quickly. This accelerated at the dawn of 2018. At time of writing (Jan . 17th), the increase has been over 4% in 21 days.

As you may recall, I said you needn't worry about that measurement, which is a news headline item, if you don't own "the market". If you are worried about permanent loss of money, that fact still remains true as any timeless fact does.

What I want to make you aware of though is this: after such a heated rise, which is still predominantly driven by a handful of very large businesses (again, mentioned in my most recent BloG posting at www.careyvandenberg.com/blog/), should one of the hot companies start to develop news around it, where people question it's sizzling tear upward, there could very well be a short term, negative market price movement, that effects many other companies.

This kind of event would actually be quite welcome. It gives investors a reality check and curbs quick decision optimism. I want to make you fully aware that this has often come in the form of a dip of 5 to 10% and you should be prepared for and expect this to happen. That is normal so take this as a heads up on what we could very well see sooner rather than later if things continue on was they have of late.

1 Aspect Of Investment Decision Making Explained

Successful investing is made up of an entire process, one which has has many different, smaller aspects. These, used together consistently over a long period of time, can only produce above average outcomes over the long term.

One of these investment decision aspects has to do with running financial scenarios on a company, assuming the worst kind of economic environment all the way through to the most optimistic outcomes. This produces an average range of returns that can be expected over generally, a 3—5 year period.

As an example, let's look at the fictitious NewTech Company (NTC). Today, NTC shares sell for $8 per share. Based on the worst case through best case economic scenarios, its shares should be worth between $14 and $19.50 dollars in 3 years. Buying at $8 today and assuming a worst case economic scenario (deep recession) a $14 share price in 3 years equates to a 20.51% annual compounded rate of return. Best case? 34.6% per year. Either extreme, or anything inbetween, would be a very favorable investment outcome.

Of course, as well all know, investments don't move in a smooth line. Events happen every minute, all over the world. Some may relate to your investment directly, others aren't relative. All news however, especially when you take into account extremes in sentiment, can move the share price of any company, NTC included, very quickly up or down, despite it having no relevance to the 3 year outlook for NTC.

Let's jump ahead 6 months. NTC shares have gone up rather quickly. Its shares now sell for $16. What do you do? Most anyone would continue to hold the shares because, "hey, it's gone up this much, it could go up a lot more". This would likely be the cursory thinking and decision, especially if the overall investment sentiment is upbeat. However, is that the right decision? Let's look at the return expectations again.

With the share price of NTC now at $16 share price and assuming a deep recession within 2 1/2 years, the share price could be trading at $14, based on the assessment that was done 6 months ago. This will produce a return of -5.2% per year. That is the worst case. The absolute best case now works out to 6.8% per year. For that to happen, everything needs to go perfectly right. Does your cursory thought (or decision) to hold on to this investment rocket ship, look like it is the right one? Would you invest your money today, based on the new numbers of what you can expect based on the worst and best return scenarios? I wouldn't.

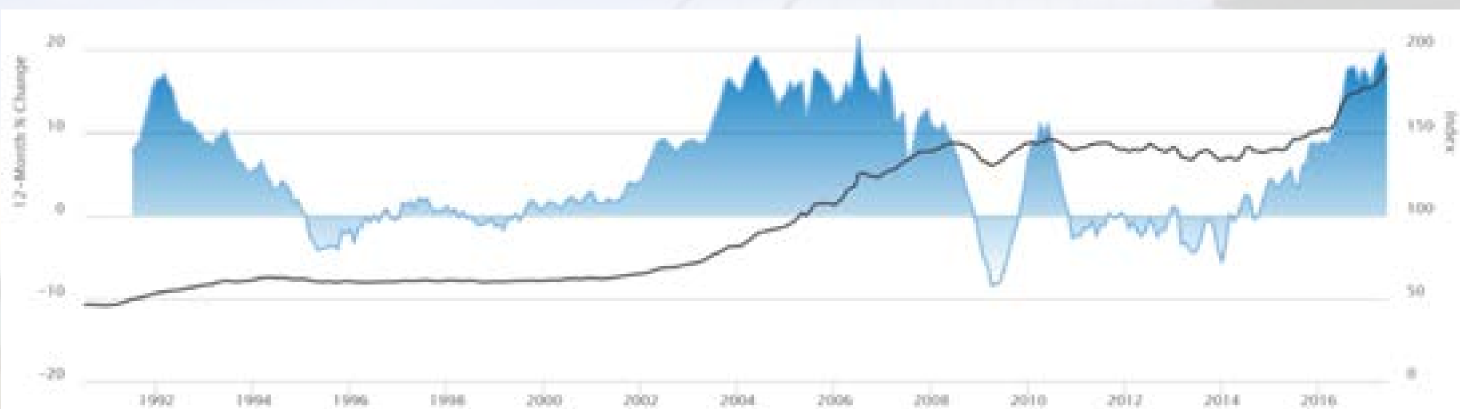
That is one of the many different aspects of a complete, well disciplined investment process. As I think you can see, this 1 aspect seems quite simple. It is in theory however, knowing and doing are worlds apart. Consistently doing helps produce outsized returns while at the same time reducing the risk of permanent loss. This 1 aspect, among a process of many other individual investment decision making pieces, helps one and even a team of investment management professionals not succumb to emotion and simple thinking which by far, is the predominant path taken in a world that moves faster and faster.

Some Canadian Property Price History (A Reality Check)

When you own an asset, whether it be ownership in a business (which you can buy a piece of through the public markets or through a managed investment portfolio), a piece of property (ie a home) or a collectable (ie 60's automobile) the price can go up dramatically over a relatively short period of time. It can also do a lot of nothing for a long spell.

Over the years, we have seen residential property prices go up by more than 10% per year for several years in a row. Over the past couple of years, property prices made jumps in price many of us have never seen before. When we experience these, it often leads to a conviction that the future will continue like the recent past. The longer the trend continues, the more we believe it will continue. That kind of thinking is called "recency bias". It is one of the many ways, as studied in Behavioural Finance, how we are our own worst enemy when it comes to making investment decisions.

Below is a Canada wide chart showing a rolling 12 month % change in price on residential property prices from about July 1990 through June 2017 (the bottom black line shows historical price trend over this same period):



As you can see, along with the big blue peaks of positive yearly price changes, the facts show that property prices also can have long bouts of flat prices (black line shows that from 1994—2002 as well as from 2008—2015. As well, contrary to popular belief, prices do decline. Source: HousePriceIndex.com Teranet and National Bank of Canada

Mortgage Paydown OR RRSP Contribution?

This is a question that has been asked continually for as long as I've been a Financial Planner. Today, the answer is the same as it has always been. Many however don't heed what is best, they simply go with what they "feel" is best. Generally not a good way to make decisions (despite feelings being touted today, more so than ever, as the best way to make a decision or path to take). But I digress… slightly.

The end result most people want when retirement age rolls around is; 1) to have their mortgage paid off and 2) to have a retirement income that can replace most if not all of their working income. The reality is there is only so much money you can use per month (X) to take care of these 2 goals. To work with the X you have, you can A) Decide to use X to first paydown your mortgage and then, with whatever is left over, to contribute to your RRSP or B) Make the smallest mortgage payments you can by stretching the amortization as far as you can and with the balance of your X dollars, contribute to your RRSP. The numbers show though that, whether you choose A or B, when you retire, you will be in exactly the same financial position IF (remember that IF)…. The interest rate of your mortgage is the same as the rate of return on your RRSPs. Of course, for most people, that “IF” isn’t the case.

With interest rates on borrowed money so low, it isn’t too hard to get a rate of return on your RRSP investments that is higher than the lowest rate you will pay on a mortgage (at time of writing the lowest mortgage rate is 2.26%). So, based on simple math, if your RRSP can earn more than 2.26% over a long period of time, you are better off minimizing your mortgage payments and maximizing your RRSP (and that doesn’t even take into account the tax savings you get from making an RRSP contribution which makes the RRSP contribution a far better choice).

Life though, doesn’t just work on simple math. There are external factors that come into play, the biggest being, do you have the financial discipline to actually take the remainder of X, and have it consistently go into your RRSP AND keep it going for at least as long as you are making mortgage payments, come hell or high water?

The other 2 are ones I will have to give the upper hand to “feelings”. If you can’t sleep at night with the debt you have I would suggest to you firstly that maybe you have put yourself in a debt position that you shouldn’t be in. You have bought too much home. If you are very nervous by nature and you want guarantees on your investments and feel stressed by any kind of payments then, it’s okay to pay off your home first. You will however have to recognize that you won’t be building your wealth nearly as quickly and thus, will most likely have to work many more years to retire (unless you have some smokin’ pension plan).

The Top 10 Estate Planning Mistakes

1) Not Having A Will—When you don’t have a Will and you die, your money and assets will most likely go to who you don’t want them to. Depending on the province, if you have a common law spouse, they may inherit nothing. Separated but are not legally divorced? Your ex will get almost <u>everything</u>. Those are just 2 examples.
2) Writing Your Will Up Yourself—Yes, you can save about $500 to $1,000 but on even on a modest estate worth $500,000, consider the money paid to a lawyer to draw up your Will, as an insurance cost; insurance against you doing something wrong.
3) Joint Accounts To Avoid Probate—I’ve mentioned more than once that generally this is a bad idea. Yes, you may save on probate costs but you may trigger negative income tax consequences as well as losing control of the asset while you are alive.
4) Joint Ownership of Houses To Avoid Probate— Same as above plus… unless you document that you are gifting the house to whomever you are adding to the title, you may not actually save on Probate.
5) Assuming That Your Children Get Along— It is almost impossible to determine with certainty how your children will get along when faced with having to divvy up your estate. Assume the exact opposite of the best picture you have in your mind.
6) Choosing An Executor Who May Not Have The Skill or Temperament— Your Executor should be; prudent but decisive, very detail oriented, communicates well, can handle conflict, is a good mediator, financially savvy and comfortable with technology. As well, they need to young enough so as to most likely be around when you aren’t.
7) Name Multiple Executors— It adds a lot of extra administration and time in settling an estate. If you can’t think of 1 Executor you can fully trust, to act in the best interests of all the beneficiaries, keep looking.
8) Not Giving Part Of Your Estate Sooner— Gifts of things or experiences to other family members (money for education or a family trip) while you are alive can have a much bigger impact on everyone involved than lump sums of cash when you are gone. Giving meaningful donations to outside charities while you are alive can create conversations with your beneficiaries on why it is important for you to do this.

Credit Cards With Extended Warranty Feature

I have always believed that paying for insurance on things that, should they happen, won’t have a significant, almost devastating financial impact on you is a waste of money. I’m talking about insurance on the small things, like trip cancellation insurance should you become sick or insurance on electronic devices should they fail to work as long as you expect them to. My opinion has softened a bit on this, specifically as it relates to the additional warranty coverage you can get with many credit cards today. Here’s why.

A friend and long time client and I had an email discussion about credit cards. In our conversation, he told me a couple of experiences (among the many he has had) on his experience with his Visa card’s extended warranty coverage. The first, the most recent case, is with a freestanding basketball hoop he had purchased. It blew over in a recent windstorm, mangling the hoop and a support bracket. He says it sounds like Visa will be giving him a refund for the full cost of this item. He will know shortly.

This 2nd case is the most amusing. Several years back, his wife was vacuuming. My friend’s neck tie was laying on the floor, in her way. She wasn’t going to clean up after him so she tried vacuuming around the tie. That however didn’t work as well as she had planned. The tie got pulled up into the beater bar of the vacuum cleaner and mangled the tie. He called Visa, explained what happened, told them the value of the tie and without much question, sent him a cheque to cover the cost of a replacement.

Needless to say, a really big LOL on my end. I am smiling even while typing this. So, for in some cases, the additional warranty protection can make sense, particularly if you don’t pay for it. If we keep our eyes opened to the potential of how this feature can be used, you and I can be laughing all the way to the bank . No harm in asking the credit card company, right?

Tech Gems— Finimize

Looking for a simple, quick read, to slowly educate you about the financial world? Something that will increase your knowledge, a little bit, day by day? I think Finimize is the best, clearest and most interesting to read. It breaks a topic down to What's Going On Here?, What Does This Mean? And Why Should I Care? At the top of the email, it will tell you exactly long it should take you to read. In this quick paced world, where so many of us have so little time, Finimize is the gem of gems for financial info. It is supposed to be geared for Millennials but it's excellent for anyone. I read it.

Hhhmmm…

Bull markets don't die of old age, they die of excesses and recessions. As of today, our team does not see any signs of that. Signature Global Advisors, Oct. 2017 #HigherLonger

A hypothetical investment in an actual portfolio from September 2008 through 2016 would have produced a return of 17.19% / year. If you sold because of fear and then invested again at a later time, you would have received a 4.87% / year return. The difference in dollars on $150,000 originally invested is $543,710 vs $210,990. Why so dramatic? Because 5 of the 9 best days occurred within 1 week of the 10 worst days. #ReactingOnFearSabotagesWealth

A fantastic company (or asset) can be a money losing investment (permanent loss) if you pay a high price for it. #BewareBandwagon

FOMO = Fear Of Missing Out #Bitcoin (see also, above)

When nearly every meeting turns to the merits of Bitcoin, or marijuana stocks, or artificial intelligence, or self-driving cars, we certainly get the sense there's a speculative element to this market. Nearly everything is going right and expectations are that this environment will continue. In many cases, the good news is priced in. Geoff Scott, Cambridge Global Advisors, Dec. 2017 #AlwaysLeaveRoomForBadNews

When you take all costs to develop a property into account, a developer needs to sell new condos at well above $1,400 per square just to achieve bank financing, let alone a profit. Some buyers of newly completed condos are already re-selling their units for less than they paid at pre-sale during construction. Western Investor, Dec. 2017 #CracksAreShowing

Calgary and Edmonton are growing faster than Vancouver in absolute population growth. MetroVancouver.org #VancouverIsPricingItselfOut #EmptyHouses

More than 60 million cars currently use embedded Blackberry technology for in vehicle infotainment. Finimize Dec. 2017 #ChartingANewPath #LessCompetition

Nissan leads in global sales of electric vehicles (EV's) with the Leaf. Toyota, a long-time champion of hydrogen power, will introduce a car with 50% more driving range than its current hydrogen-powered Mirai sedan, in a technology push that defies a rising wave of battery-driven vehicles. Globe & Mail, Oct. 2017 #HydrogenVsElectric #TeslaCompetitors

China is home to the largest digital payments platform. The combined size of China's financial tech firms dwarfs that of any other country in the world, including the USA. Finimize, Sept. 2017 #TheNewEntrepreneurialPowerhouse

The age 65 retirement and pension start age was first implemented in Germany 200 years ago, when life expectancy was much lower than it is today. IPC Conference Call, Oct. 2017 #75TheNew65?

56% of people financing a vehicle today choose a term of 7 years or longer. Globe & Mail, Oct. 2017 #BanksLoveYouBorrowing

List of 15 cars that people keep for 15 years include 9 different Toyota models, 2 Hondas, 1 Acura, 1 Nissan, 1 Subaru and 1 VW. Jalopnik.com #BMW&MercedesLookGoodBut

The "GreenDP" in BC eliminated the tolls on Lower Mainland bridges and the traffic increased 27% as measured on the last Tuesday of September 2017 compared to the same day the previous year. Traffic on the other bridges remained unchanged. Tolls were removed to try to fix traffic congestion south of the Fraser. Peace Arch News, Nov. 2017 #DecreasingCostIncreasesUse.Duh!

The evidence suggests that the thing we are convinced is such a big advantage (smaller class sizes in school) might not be such an advantage at all. We have become obsessed on what is good about small classrooms and oblivious to what can also be good about large classes. David & Goliath, Malcolm Gladwell #BeliefVsReality

"The best time to plant a tree was 20 years ago. The 2nd best time is now." Chinese Proverb #RegretsNoActionsYes

"If I held in my hands the power to eliminate physical pain from the world, I would not exercise it. My work with pain-deprived patients has proved to me that pain protects us from destroying ourselves." The Gift of Pain (book), Dr Paul Brand & Philip Yancey #PurposeOfPain