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Best Asset Growth
Alberta & Okanagan

National Bank Financial
Wealth Management

Suite 200, 239 – 8th Ave. S.W.
Calgary AB T2P 1B9

Tel.: 403-531-8400
Toll Free: 1-877-531-8400
Fax: 403-531-8413

The Increasing Rate of Change

It has been said that "there are decades where nothing seems to happen and then there are weeks where decades happen." This spring was no exception. We have experienced change that occurred at unprecedented speeds, including physical distancing, home isolation and the voluntary shut down of economies. This led to equally unprecedented reactions: oil futures prices falling to negative levels and rebounding, entire industries being shut down, and record unemployment levels.

Equity markets reacted in a similar manner, falling and then rallying quickly. Typical bear market cycles last between 18 to 36 months. However, this past spring, we saw one that was compressed into a matter of weeks.[1]

Global policy responses have also been faster — and deeper — than ever. From the onset of the crisis, central banks have engaged in significant stimulus efforts in an attempt to stem the effects of the crisis. This increase in liquidity has likely been one reason why the equity markets advanced in April and May, despite what was happening on the ground.

What does the path forward look like? As humans, we grasp for certainty. Yet, uncertainty has always played a common role in the financial markets and unforeseen events such as these can make things even more unclear. One such example: economists attempting to quantify the effects of the shutdown on second-quarter gross domestic product predicted U.S. GDP estimates of between -8 and -50 percent.[2]

During these times of uncertainty, one of our most important roles as advisors is to manage risk. With a focus on preserving hard-earned capital, we maintain a disciplined approach to control risk in portfolios. At the same time, we are monitoring investments based on current market conditions and navigating the changing landscape.

In the near term, equity markets are likely to experience volatility as economic data and earnings continue to reflect the impact of the spring economic shutdowns. We face many near-term challenges as many economies start to reopen and attempt to return to a state of "normal."

As containment efforts continue, opinions are likely to significantly vary about the road ahead for the economy and the financial markets. We understand the challenges that come from an uncertain near-term outlook, but, as much as possible, investors should try to stay focused on their long-term goals.

We continue to work hard for you and your investments, managing risk during these difficult times and positioning portfolios for the inevitable changes that lie ahead. Please call if you have any concerns.

1. http://bloomberg.com/news/articles/2020-04-06/no-one-wants-to-call-canada-s-21-stock-surge-a-bull-market
2. http://bloomberg.com/news/articles/2020-03-22/fed-s-bullard-says-u-s-jobless-rate-may-soar-to-30-in-2q

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INVESTMENT STRATEGY

Consider the Benefits of Dollar-Cost Averaging

As we have seen with recent equity market reactions, short-term price movements are often unpredictable and nobody can be certain when the next upturn will begin. Such turns can occur when the outlook is bleak and the natural inclination may be to sell, not buy. In hindsight, all down markets look like buying opportunities. But in the moment, it's not always easy to commit money to an investment that has gone down in price, particularly in a bear market.

Those investors who use a dollar-cost averaging (DCA) program to build their long-term portfolios can have an advantage. A DCA program mandates regular, modest investments, rather than one major lump-sum commitment. As such, investors need not focus on predicting market movements.

DCA can fit nicely with personal cash flow, acting as a way of saving on a steady basis. Payments can be made at any regular intervals, such as monthly or quarterly. DCA can work particularly well with funds as you can buy exact dollar amounts of a fund, which may not always be possible with share purchases. However, there is no reason why DCA can't be used to build any security position, especially in these times in which broad declines have affected many securities.

The example (chart) uses S&P/TSX Composite Index returns to depict a DCA program through the extended bear market period we experienced from 2000 to 2002. Each quarter, $1,000 was invested. Despite poor market performance, the DCA program resulted in a modest gain of $1,130 ($17,130 less $16,000), plus the ownership of significantly more units which benefitted the portfolio as time went on. Had a lump sum investment of $16,000 been deployed at the beginning of 2000, it would have returned a small loss, with an overall value of $15,633 and 1,902 units owned (versus 2,084).

During times of uncertainty, DCA can be a useful strategy. It allows you to take the emotions out of investing, while continuing to put money to work. Even during down or bear market times, DCA is a good reminder that a thoughtful investing plan can result in real progress toward achieving your wealth-building goals.

Profiting Through a Bear Market: DCA Using S&P/TSX Index During 2000 to 2003				
12-99	8.4138	118.85	118.85	$1,000
03-00	9.4624	105.68	224.53	$2,125
06-00	10.1995	98.04	322.58	$3,289
09-00	10.3779	96.36	418.94	$4,348
12-00	8.9337	111.94	530.87	$4,743
03-01	7.6080	131.44	662.31	$5,039
06-01	7.7364	129.26	791.57	$6,124
09-01	6.8386	146.23	937.80	$6,413
12-01	7.6884	130.07	1067.87	$8,210
03-02	7.8515	127.36	1195.23	$9,384
06-02	7.1456	139.95	1335.18	$9,541
09-02	6.1804	161.80	1496.98	$9,252
12-02	6.6145	151.18	1648.16	$10,961
03-03	6.3433	157.65	1805.81	$11,455
06-03	6.9831	143.20	1949.01	$13,610
09-03	7.4211	134.75	2083.76	$15,464
12-03	8.2209	--	2083.76	$17,130

*Past performance is never indicative of future performance.

The End of the Office Era? Keep Good Records

Is the office era over? For many office workers, working from home became the new normal this spring. As such, some may be wondering if they are able to claim a tax deduction for home office expenses.

The Canada Revenue Agency (CRA) currently allows for a deduction in instances in which one of the following conditions is met: i) The work space is where you mainly do your work (more than 50 percent of the time); or ii) You use the workspace only to earn employment income, and it is used on a regular and continuous basis for meeting clients, customers, or others in the course of your employment duties.

Deductible costs are based on the type of worker claiming the deduction: employees, commissioned salespeople or self-employed workers. Each of these groups is entitled to deduct different expenses. Expenses generally include electricity, heating, maintenance and supplies. Property taxes and home insurance may be allowable for commissioned salespeople or self-employed individuals, and mortgage interest and capital cost allowance may be claimed for those self-employed. The portion that can be claimed is based on the area attributed to the home office, as a proportion of the total finished area of the home.

If individuals are not self-employed, in order to potentially deduct these expenses, your employer must complete CRA Form T2200: Declaration of Conditions of Employment. Any expenses reimbursed by the employer, such as internet or office supplies, cannot be claimed.

While the current CRA rules normally require that you spend more than 50 percent of total work time in the home office during the tax year to claim deductions, some accounting professionals have indicated that there may be exceptions. Given the unprecedented circumstances in which people have been mandated to work from home, the CRA may consider cases on an individual basis, or may potentially make changes to its policies.[1] As such, keep good records.

Over the foreseeable future, the 50 percent threshold may be met if continued distancing efforts result in fewer workers returning to traditional office spaces. For detailed information, please consult the CRA or seek advice from an accounting professional.

1. theglobeandmail.com/investing/globe-advisor/advisor-news/article-pandemic-led-flight-to-home-offices-brings-tax-perks/?fbclid=IwAR24-wttdbsJ4SfIoK1d5gRR77hoUEYUyeBa0GshEy5s9oi23TXpheggZQcrofessional

Economic perspectives

What is the Economic Path Forward?

It may be difficult to remember, but it was only months ago that we were in the midst of the longest economic expansion in history. How quickly things have changed. As a result, many investors are asking: what is the economic path forward?

Beyond the terrible health consequences of the pandemic, the short-term economic effects have been equally extraordinary. We have seen individuals, companies and industries affected in adverse ways. COVID-19 has also helped to accelerate certain existing economic and political trends: increasing automation, greater scrutiny of foreign direct investment, nationalism and the evaluation of domestic supply chains. It has also magnified continuing U.S.-China trade tensions.

In the short term, we are likely to expect deflationary pressures due to reduced spending and consumption, as well as a weaker housing market, as economies begin to return to a more "normal" state. While certain media voices raised the potential for an economic depression when projecting unemployment levels and economic growth declines, these historic troubles were likely compounded by a series of poor policy decisions, unlike today.[1]

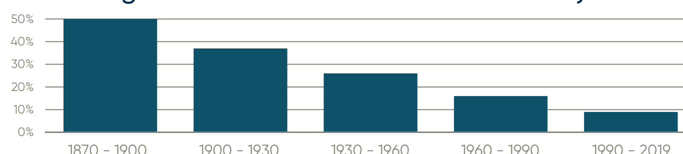
What is a Trillion? Unprecedented Stimulus...

We must not overlook the unprecedented support by global policy-makers in trying to minimize the implications of the crisis. Consider the U.S., where lawmakers have passed trillions of dollars in stimulus relief. To put the magnitude of one trillion into context, if we were to travel back in time by a billion seconds, we would be in 1989. However to go back a trillion seconds would take us to around 30,000 B.C.

Many central banks have engaged in quantitative easing (QE), which is a form of monetary policy, by purchasing financial assets to inject money into economies. The Bank of Canada began its first-ever move into QE in April by purchasing $1 billion of government bonds. Alongside record-setting fiscal policy spending, increases in the money supply have not only helped to support asset prices, but also economies. For some economists, this is one reason to remain optimistic about the rate and sustainability of recovery. Of course, there will be new challenges as a result of significant deficits and debt. There are also questions as to whether these efforts will be enough to help economies quickly recover.

However, economies naturally go through cycles and the speed of recovery from economic downturns has increased over time. Recessions occur when economic output declines after a period of growth. Our economy has spent less time in recession as technology has transformed it to be more service-based, and also due to increased central bank intervention.[2] A century ago, the economy was in recession nearly 40 percent of the time; today this is less than 10 percent.

Percentage of Time in Recession — US Economy[3]



While the longer-term implications are less clear, let's not forget that after the 2008/09 financial crisis, many economists worried about high rates of inflation and slower economic growth, both of which generally did not happen.[4] Instead we participated in one of the longest economic expansions of all time.

Throughout history, economies have continued to advance and progress. Despite the challenges ahead, there may be positive reasons to continue looking forward and maintain a longer-term perspective.

1. http://hbr.org/2020/05/the-u-s-is-not-headed-toward-a-new-great-depression?ab=hero-main-text; 2. https://www.cdhowe.org/sites/default/files/attachments/research_papers/mixed/Commentary_366_0.pdf; 3. The rate is similar in Canada but economic data prior to 1930 isn't readily available; https://nber.org/cycles.html; 4. Inflation rates did exceed central bank targets in 2011.

What Happens After a Bear Market?

We have encountered many new situations in response to COVID-19 — isolation, physical distancing, economic closures globally, and others — that have created uncertainties for the short term. Doomsayers cite these factors, and others, to suggest that this time is different and the current economic downturn will somehow last forever. However, economic cycles go up as well as down.

Equity markets are also cyclical. Bear markets happen from time to time. Yet, even in the worst situations, equity markets have eventually turned their course. The worst bear markets in history have seen drawdowns of over -86 percent (1932) and -56 percent (2007). Yet, the average returns following some of the worst bear markets were 53 percent, 78 percent and 143 percent over the ensuing one, three, and five year periods, respectively. Although the positive returns came after the depths of the bear markets, history reminds us that time can heal even the worst market declines.

Nobody knows the direction of the equity markets over the near term, but the long-term trend has been up.

In preparation, a disciplined approach emphasizing quality, diversification and a solid plan are expected to continue to serve us well over the longer term.

Forward Returns Following History's Worst Bear Markets, S&P 500

Peak	Trough	Drawdown	1 Year	3 Years	5 Years
1929, SEP	1932, JUN	-86.2%	162.9%	170.5%	344.8%
1937, MAR	1938, MAR	-54.5%	35.2%	38.2%	84.5%
1968, NOV	1970, MAY	-36.1%	34.8%	50.6%	42.2%
1973, JAN	1974, OCT	-48.2%	38.1%	72.7%	117.5%
1987, AUG	1987, DEC	-33.5%	23.2%	55.5%	121.7%
2000, MAR	2002, OCT	-49.1%	24.4%	59.0%	105.1%
2007, OCT	2009, MAR	-56.8%	53.6%	98.0%	181.6%

Source: fortune.com/2020/03/19/coronavirus-stock-market-predictions-bear-market-stocks-bottom-what-to-expect/

During Uncertain Times: Avoid These Investing Mistakes

Uncertain times often highlight the mistakes that investors can make with their portfolios. During buoyant markets, making money may not seem difficult. However, the reckoning often comes when markets turn down. Suddenly, mistakes can become glaringly apparent.

Here are some of the more common investing errors:

Overlooking Diversification

The concentration of assets in too few areas can be a common problem. Despite the broad-based market declines we have recently experienced, certain sectors have performed very differently. Some technology companies have outperformed as a result of distancing practices, whereas industries dependent on travel and tourism have suffered significant short-term setbacks. Even during non-crisis times, regardless of the high quality of investments, there is always the danger that a bad quarter or certain industry developments may adversely affect equity values.

No single asset class has consistently performed at the top over time. As such, it is important to maintain a healthy balance of diversification across your assets.

Tax Errors

Don't overlook the effect of taxes on your investments. Remember that different forms of investment income can be taxed differently. In a non-registered account, the nominal return from dividends of an eligible Canadian corporation would be higher than the same fixed-income return on an after-tax basis. Capital gain returns are generally taxed at even lower rates. Pay attention to asset location: different income can be taxed differently depending on the type of account (i.e., registered, non-registered) from which income is generated. Using tax advantaged accounts such as Registered Retirement Savings Plans and Tax-Free Savings Accounts may be great ways to help minimize taxes.

Also important: don't be reluctant to sell a security solely because taxes will be triggered. If the fundamentals suggest change or a portfolio needs to be rebalanced, don't let the tax tail be in control.

Failure to Adjust

The financial markets are constantly changing and the prospects of specific companies, industries or even entire classes of securities can be attractive today, but not tomorrow. Be ready to adapt. Equally important, your needs may change and your holdings may require periodic adjustments as circumstances evolve. Remember, you are not marrying a particular security: the purpose of investing is to earn a solid return, not own XYZ company forever.

Acting on Emotion

Fear and greed are said to be the drivers of market sentiment. When euphoria prevails, unsavvy buyers often rush to purchase investments. In contrast, market downturns may offer bargains, yet many investors sit on the sidelines or, worse, decide to liquidate portfolios.

Having an investment plan with well-defined objectives can help control emotional pressures. Working steadily towards measurable goals helps to focus on outcomes rather than the process. Other tactics may include a dollar-cost averaging program (page 2), which helps to prevent emotion from dictating investment purchases. Avoiding daily attention to the performance of investment accounts may also help to limit emotional responses.

National Bank Financial Wealth Management
Suite 200, 239 – 8th Ave. S.W.
Calgary AB T2P 1B9
Tel.: 403-531-8400
Toll Free: 1-877-531-8400
Fax: 403-531-8413

Dean Despas, CIM®
Investment Advisor
Senior Vice-President
Direct: 403-531-8431
Cell: 403-630-0243
dean.despas@nbc.ca

Charlene Procyshen, B.ADMIN
Senior Investment Associate
Direct: 403-531-8463
charlene.procyshen@nbc.ca

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