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Advice Matters

WINTER 2019

Investment Outlook: 2019

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Scotiabank

With 2018 behind us, we reflect on what's happened and share our thoughts about what to expect over the coming year.

To be blunt, 2018 has been a disappointing year for investors. Almost 90% of all global asset classes have generated negative returns, the highest proportion recorded in over a century, according to data from Deutsche Bank.

Meanwhile, cash has outperformed both global equities and bonds for the first time since 1994. So, it seems fair to say that 2018 has been one of the more trying and unique periods for this current generation of investors.

In our opinion, it's not a lack of growth – three-quarters of all countries experienced rising activity levels – but rather a lack of confidence in the longer-term earnings outlook, which has weighed heavily on asset values across the planet.

A year filled with anxiety

Throughout 2018, investors needed to process a myriad of worrying business stories, such as mounting global inflation risks, excessive corporate debt, housing-bubble concerns (e.g., Australia, Canada) and threats to future economic growth. The collective hike in interest rates initiated by the U.S. Federal Reserve (the Fed) since late 2015 has only magnified these issues. And, the ongoing drumbeat of protectionism, particularly as it relates to the frayed trading relationship between China and the U.S., has compounded the situation.

If excessive monetary tightening, escalating trade wars and a growth slump form the basis for worry, then the investment outlook for 2019 is beginning to brighten. After a strong U.S. jobs report in the first week of January, Fed Chairman Jerome Powell laid the groundwork for taking a break from raising short-term interest rates in the coming months. Markets responded positively to the news, rebounding strongly after a tough start to the new year.

Positive trade deals

In December 2018, we also saw a truce called in the Chinese-American trade war. The two sides have indicated that they will work hard over the next three months to find common ground on contentious issues such as autos, agriculture and intellectual property. This is a big positive shift following a year littered by rising tariffs and bad blood between the two nations. In fact, the fear of rising protectionism that has entered into market psychology might be somewhat overblown.

Meanwhile a new deal, referred to as the United States–Mexico–Canada Agreement (USMCA), was signed. And, we witnessed the ratification of a free trade deal between the European Union (EU) and Japan, thereby becoming the world's largest bilateral free trade agreement, covering 33% of global gross domestic product (GDP). There have been lots of smaller bilateral deals popping up, such as the ones between the EU and Vietnam, and South Korea and the U.S. While saber rattling between nations has most definitely been on the rise, perhaps free trade is still alive and well.

Global economy looks good

Most importantly, the global economy seems set to continue along its upward path over the next year. This will be aided by ongoing growth in the world's two largest economies, the U.S. and China.

According to the U.S. Bureau of Labor Statistics, strong labour demand has pushed the U.S. unemployment rate down to 3.7%, the lowest jobless rate in

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about 50 years. This sets a good foundation for the consumer and, coupled with the lingering boost to businesses activity from President Trump's historic corporate tax cuts, should help to hold GDP growth near 2.5%.

With all of this in mind, our opinion is that the widespread pessimism witnessed across the investment spectrum is overdone.

It's important to keep in mind that after nearly 10 years of economic expansion, we have probably entered the later stage of the cycle. This is when one must be prepared for more frequent and intermittent volatility bursts, being aware that the share-price trends are most likely still positive.

The dynamics in the bond market should also change with the underlying economic fundamentals. The increase in global bond yields, which we experienced through most of 2018, will likely be arrested as the market begins to appreciate a slower pace of monetary tightening ahead. While we believe that the worst is in the past for the bond market, the ongoing economic and earnings expansion is likely to favour equities over bonds in a balanced portfolio.

Investor confidence will be key

The key risk to the financial markets outlook, in our opinion, is a generalized loss of confidence. Investors have become accustomed to, or maybe even psychologically reliant upon, hyper-stimulative central bank policy. There were more than 700 interest-rate cuts and $12 trillion of assets purchased directly from secondary markets by the global monetary authorities since the failure of Lehman Brothers over a decade ago. This has changed.

Even a gradual reversal in supportive central bank behavior could lead to greater downward pressure on asset valuations. There is perhaps collective concern that economies are at risk without the open-ended promise of direct central bank support.

We will be watching these developments closely, particularly as to how asset prices react to further improvements in economic and earnings fundamentals. The failure to respond positively to these advances would suggest a deepening loss of confidence. Further action to protect capital would then be required. ■

INVESTING INSIGHTS

Words from the *wise*

With the start of the new year and investment sights set forward, here are some insights on what to expect in 2019 from three of our portfolio managers.

ERIC BENNER

Vice President & Portfolio Manager
1832 Asset Management L.P.
Scotia Global Balanced Fund

Global equity markets were choppy in 2018, with a nearly constant barrage of headlines about politics, trade and interest rates causing most country markets to finish the year in the red. Volatility is likely here to stay as we go into 2019, and all eyes are now focused on whether the global economy is slowing temporarily because of trade concerns, or at risk of recession. As long as global growth remains positive, even if slowing, the prospect for returns from stocks remains constructive. Against that backdrop, we remain focused on building defensive portfolios of attractively valued, high-quality businesses that we would be comfortable owning for many years.

BILL MCLEOD

Vice President & Portfolio Manager
1832 Asset Management L.P.
Scotia Canadian Dividend Fund

Growth was strong in 2018, but equity returns were markedly negative as volatility reemerged, sentiment turned negative and valuations compressed. Looking to 2019, there's an increasing likelihood of slower growth and continued headwinds from restrictive central bank monetary policy (i.e., interest rate hikes and quantitative tightening). Broad economic fundamentals remain positive; however, equity volatility is expected to remain elevated. Despite lower growth, the backdrop for equities is moderately constructive; however longer-term returns will likely be less robust. Our focus remains on finding quality companies with durable business models at reasonable prices and constructing/maintaining diversified portfolios to capture favourable risk-adjusted returns.

ROMAS BUDD

Vice President & Portfolio Manager
1832 Asset Management L.P.
Scotia Bond Fund

While investors may be expecting higher bond rates in 2019, we believe, and are positioned for, the two-year bond bear market to at least hit the pause button. In October, with the Universe Bond Index hitting the 3% yield level, we began to lock in longer-term investments. The global economy is being impacted by increased trade tensions and the end of supportive central bank policies. Inflation has likely peaked and will trend down into 2019. The recent rate-hiking cycle in the U.S. and Canada is likely done or nearly finished. Risk assets, including credit-based instruments, are likely to underperform returns for the government bond market. A surprise for 2019 could be that returns for the bond market will trend better than most expect.

MARKET INSIGHTS

4 tips for surviving volatile markets

For many investors, the mere mention of "volatility" can tie their stomach in knots. While wild market swings can be unnerving – even for experienced investors – they shouldn't derail your long-term investment goals. Here are four tips to help you keep your perspective when markets get choppy.

1 Ignore the market noise

If daily swings in the market are causing you to reach for the antacids, try doing something truly novel: ignore them. While perhaps easier said than done, ignoring the market noise will do wonders for your peace of mind and prevent you from making a hasty decision you'll likely regret.

The recent pessimism that's gripped the markets over the last few months isn't always based on economic fundamentals – or even rational. In early December, after two strong trading days, the Dow tumbled more than 800 points – a decline attributed, at least partially, to President Trump's ill-timed "I am a tariff man" tweet. While markets have been understandably sensitive to the ongoing trade dispute between the U.S. and China, they often overreact to short-term noise. Don't let it get you down.

It's important to remember that, as individual investors, we have no control over volatility. What we can control is our own mindset; the more level-headed we remain, the better our investment results will be over the long haul.

2 Stay focused on the long term

Assuming you've got a long-term investment horizon of at least five years, the current volatility will pass. Market pullbacks, corrections and even bear markets are a normal part of the stock market cycle. Consider this: since 1945, the S&P 500 Index has declined between 5% to 10% on 78 different occasions. The average recovery time to previous highs was roughly one month.[1]

A few years from now, market setbacks like the one we've experienced recently will most likely be tiny blips on a longer-term chart. While it's sometimes easy to fall prey to the daily market drama, the most successful investors have a long-term strategy from which they rarely deviate. Investing in quality companies with a proven track record of earnings and growth can help mitigate some volatility and keep you focused on your long-term investment goals.

[1] Putting pullbacks in perspective," GuggenheimInvestments.com, August 2018.
[2] Center for Interuniversity Research and Analysis of Organizations, 2016.

Investors who worked with a financial advisor for **more than 15 years** accumulated **3.9x** more assets compared to those who didn't.[2]

3 Avoid panicked selling

Overall, 2018 has been a difficult year for investors. North American markets are down for the year and many are concerned about slowing global growth. All the recent headlines might make you want to cash out your investments and wait it out on the sidelines.

That's an understandable feeling. However, it's not a good idea. Leaving the markets in the midst of volatility is usually motivated by fear, which is responsible for some of our biggest investment mistakes. Anyone who sold during the 2008-09 market meltdown locked in steep losses and most likely missed a powerful rebound.

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The Value of Staying Invested

Trying to time the markets can be a costly decision, as the graphic below clearly illustrates. Consider the impact of missing the best 10, 20 and 30 days on the value of $10,000 invested in Canadian stocks over the past 10 years.

Source: Bloomberg. S&P/TSX Composite Total Return Index, November 30, 2008 to November 30, 2018. It is not possible to invest directly in an index. Assumes reinvestment of all income and no transaction costs or taxes. Value of investment calculated using compounded daily returns. Missing 10, 20 and 30 best days, excludes the top respective return days.

4 Seek out financial advice

Staying invested during wild market swings isn't always easy. However, market volatility can be beneficial if it forces you to revisit your portfolio with an eye toward improving diversification or re-assessing your tolerance for risk.

Research on the value of advice has shown that investors who work with a financial advisor not only save at a higher rate than non-advised investors, but they also have a greater feeling of confidence about their financial future than those who don't work with an advisor.

Taking the time to develop a financial plan to help you reach your investment goals can go a long way to keeping you on track and remind you why you're investing in the first place – whether it's for retirement, your child's education or some other goal important to you. Contact a Scotiabank advisor today to develop a plan that makes sense for you. ■

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INVESTOR EDUCATION

Personal *tax tips*

As this year's tax-filing deadline approaches, here are some general tax tips that may help you keep more money in your pocket.

Save in tax-efficient accounts like RRSPs and TFSAs

While RRSPs and TFSAs have different benefits and limitations, you can have both accounts at the same time. With that in mind, let's take a look at some of the key differences.

Wondering which account is best for you?

RRSPs and TFSAs each have their own merits. A Scotiabank advisor can help review your personal circumstances and investment goals to help you choose the solution that works best for you.

	Registered Retirement Savings Plan (RRSP)	Tax-Free Savings Account (TFSA)
What do I need to open an account?	You need: • To have qualified earned income in the previous year. • To be a Canadian resident. • A valid Social Insurance Number (SIN). **There is no minimum age to open an RRSP.**	You need: • To be at least 18 years of age or older, or have reached the age of majority in the province in which you set up the account. • To be a Canadian resident. • A valid SIN.
Are my contributions tax deductible?	Yes, contributions are tax deductible.[1] • For 2018 you can contribute up to 18% of your previous year's earned income up to a maximum of $26,230, plus any unused contribution room from previous years.	No, contributions are not tax deductible. • For 2018, the maximum contribution limit is $5,500, plus any unused contribution room from previous years.[2] • The 2019 annual contribution amount has increased to $6,000.
Can I withdraw my money?	Yes, but any **withdrawals will be taxed as income** in the year you take it out. Once you withdraw money, you don't create additional contribution room.	Yes, and **it's tax free.** You can re-contribute the amount you withdrew in the following year.

The above chart provides highlights of RRSPs and TFSAs. It is for information purposes only and is not intended to be investment or tax advice. Investors should consult a professional advisor for specific investment and tax advice.

[1] Your RRSP contribution limit can be found on your most recent Notice of Assessment from the Canada Revenue Agency.

[2] $5,000 maximum contribution limits for each year from 2009-2012. $5,500 maximum contribution limit for each year from 2013-2014, 2016-2018. $10,000 maximum contribution limit for 2015 and $6,000 maximum contribution limit for 2019. If you have never contributed to a TFSA, you can contribute up to $63,500 for 2019. Contact the Canada Revenue Agency to confirm your available TFSA contribution room.

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Ensure that all available tax credits are claimed

Many tax credits are available, including credits for eligible medical expenses, child care expenses, youth and seniors' activities, and for first-time home buyers. In the case of non-refundable tax credits, some unused credits can be transferred to the higher-income spouse or common-law partner.

Find out about possible caregiver tax credits

Where you are responsible for the care of a dependant as a result of mental or physical infirmity, or disability, several tax credits may be available, such as the Canada Caregiver Credit or the Infirm Dependant Credit. In addition, fees paid for a dependant's nursing home or attendant care may be claimed – in some cases in combination with the "disability tax credit." As the rules around these possible tax claims can be complex, speak to your tax advisor to determine which tax claims might be available to you.

What's the difference between a non-refundable and a refundable tax credit?

Non-refundable tax credits are designed to reduce your federal tax payable, but they don't create a tax refund. With refundable tax credits, even if you don't owe any tax, the total amount of your refundable tax credits will result in a tax refund and will be paid to you.

Make spousal RRSP contributions

Spousal RRSPs are another effective way to split income during retirement. The long-term goal of investing in a spousal RRSP is to minimize taxes for a couple during retirement by putting retirement income in the hands of the lower-income spouse. By equalizing each spouse's retirement income, the overall tax bill is reduced by keeping both spouses in a lower tax bracket. Talk to your Scotiabank advisor for more details.

Keep in mind that these tax tips are not comprehensive and are general in nature. Everyone's situation is unique, and you should consult a tax specialist for advice specific to your financial situation. ■

IMPORTANT UPCOMING DATES:

MAR 1

March 1, 2019

Deadline for 2018 RRSP contributions

APR 30

April 30, 2019

2018 Personal Canadian tax return deadline

Did you know?

Keep all tax receipts and supporting documents

CRA recommends keeping your tax records for a minimum of six years. Tax records include your returns and the supporting documentation used to prepare them such as expense receipts, T4s that record employment income and receipts for charitable donations.

File your tax return on time

While filing your tax return on time won't reduce your tax liability, it will help you avoid penalties and interest. If you don't file on time, and you owe money, penalties are charged. In addition, if you don't pay your tax bill in full, interest charges will apply.

If you owe a substantial amount, you may want to consider speaking with your bank to obtain a loan to pay your tax bill, if you can secure a lower interest rate than the one charged by the Canada Revenue Agency (CRA).

FINANCIAL PLANNING

Investing automatically makes saving easier.

Investing automatically with a Pre-Authorized Contribution or a PAC can help keep you on track to meet your retirement goals faster and easier.

Investing
$100
per month

25 years

$58,812[1]

Investing $100 every month for 25 years could add up to $58,812[1]

PAC benefits

Eliminate the guesswork of when to invest

Avoid the stress of making lump-sum RRSP contributions

Take advantage of potential compound growth

And it grows with you.

Congratulations on your raise! As your life changes, your PAC can be topped up—so you can invest even more, automatically.

Almost half of Canadians (45%) have a PAC set up for their investments[2]

$250 – Median monthly PAC among Canadians[2]

Get started with as little as $25 per month.

You could see a big difference in your savings—but not your budget.

$117,624[1]
$200 monthly*

$127,287[1]
$100 bi-weekly*

Double up and save more.

You may be making bi-weekly mortgage payments. Do the same with your savings. It's a small change, but the benefits can add up!

* over a 25-year period

Make investing for retirement automatic.
Speak to your Scotiabank advisor to set up a PAC today.

[1] For illustrative purposes only. The example uses a hypothetical rate of return of 5.0%, assumes reinvestment of all income, compounded annually, and does not include transaction costs, fees, or taxes. The example does not reflect actual results or the returns or future value of an actual investment. [2] Source: Global Brand & Customer Insights, 2017 Scotiabank Investment Poll, March 2018.

MONEY 101

'Tis the season for paying down holiday debt…

Spent too much during the holidays? Now that the holiday season has come to an end, many may find themselves with higher-than-usual debt or credit card bills. Here are a few tips to help you take control of holiday debt.

1. Get a handle on your debt

Make a list of all your debts – including payment due dates, minimum payment amounts, interest rates and the timeframe in which you'd like to pay off your debt. Set a realistic date to pay off your debt, based on your income and regular household expenses.

2. Choose a repayment strategy that works for you

Focus on paying down the credit cards with the highest interest rate first. If this seems too intimidating, try paying down your smallest debts first so that you'll gain momentum as the debts are paid off.

3. Use bonuses and income tax refunds

If you are fortunate to get a year-end or holiday bonus, or a tax refund, these funds can be used to make a dent in your holiday debt.

4. Look into reducing your daily or regular expenses

Consider cutting back on daily expenses and applying the savings towards paying down your debt or saving for next year's holiday season. You can look into carpooling to work, working from home and bringing your lunch to work. Review your cable and mobile phone bills to ensure you have the right plan – determine whether you're actually watching all the channels you're paying for or really need unlimited calling – modify your plans accordingly.

5. Consider consolidation

You might want to consider consolidating your debt with a personal loan or transferring the balance to a credit card with a lower interest rate. This may give you the opportunity to restructure your debt with more favourable terms. Ensure you stick to your repayment plan and pay off the debt as soon as possible. ■

Getting ready for next year's *Holiday Season*

No time like the present to start saving

Determine a budget for holiday shopping that you can afford and set aside money specifically for it – for example, $50 each month will add up to $500 in 10 months. It should include all the things you'll be buying over the holidays such as gifts, cards, gift wrap, decorations and food for special occasions. Don't forget to set aside money for Christmas lunches and dinners and holiday attire.

Make a list

If you have a list when shopping, you'll be less likely to impulse buy and more likely to stick to your budget. Your list should include the name of the people you plan to buy for and the estimated cost of their gift. Resist the temptation to purchase gifts that are not on your list.

Look for sales throughout the year

Once you have an idea of the gifts you will be purchasing, watch out for sales of those items throughout the year. Sign up for e-mail or text messages from the retailers you are most likely to buy from and check their website frequently.

Pay cash whenever possible

Paying cash for holiday spending can help you stay on budget. If you choose to use your credit card, try to stay within a total that you can afford to pay back in full to avoid interest charges. Try to use only one credit card and preferably one that allows you to accumulate points that you can use towards holiday purchases.

Have a plan to pay off big ticket items

If you plan to purchase a computer or big-screen TV, ensure you have a plan in place to pay it off.

Host a white elephant gift exchange party

This is a fun Christmas activity where participants get to choose among a number of gifts and try to walk away with the best one. You need only purchase one gift, and the participants decide the maximum amount of money to be spent for the gift – the price is typically capped at $20. This type of gift exchange is great for those on a tight budget. ■

FACTS & FIGURES

Beyond dollars and sense

Why having a financial plan is so important

According to a study from the Financial Planning Standards Council,[1]
Canadians with comprehensive financial plans reported higher levels of:

FINANCIAL well-being 85%

EMOTIONAL well-being 62%

Overall **CONTENTMENT** 45%

...compared to those **without a plan.**

[1] Financial Planning Standards Council, The Value of Financial Planning, 2012.

The study also showed that those with comprehensive financial plans feel:

More on track with their financial goals and retirement plans

Their ability to save is improved

More confident that they can deal with financial challenges in life

Better able to indulge in their personal spending goals

MARKET PERFORMANCE (YTD Returns in local currency as at December 31, 2018). Source: Bloomberg

▲1.41%	▼-8.88%	▼-4.39%	▼-8.19%	▼-14.36%
FTSE Canada Universe Bond Index	**S&P/TSX Composite Index**	**S&P 500 Index**	**MSCI World Index**	**MSCI Emerging Markets Index**

You're richer than you think.® Scotiabank®

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