

# ODLUM BROWN REPORT

## 03 2018



**ODLUM BROWN**  
Investing for Generations®

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## Ignore the Market's Mood

Have you ever used the expression “woke up on the wrong side of the bed” to describe yourself or someone else? It’s typically used to label a grumpy or irritable person, especially when the reason for their unhappiness is unknown. Sometimes the market’s mood turns foul without good reason. We think that was the case in early February, and we believe that it would be a mistake to overreact to the recent market gyrations.

The recent pullback seemed to be triggered by good economic news. The worry, which we believe is overblown, is that the U.S. Federal Reserve will take the proverbial punch bowl away from the stock market party by raising interest rates in the face of stronger economic growth and higher inflation. The lack of corroborating evidence, our understanding of human nature and, hopefully, our experience are among the factors that calm our nerves, help us to ignore the market’s mood and focus on the fundamentals that matter.

Investors who sold stocks in early February were behaving as if a recession is around the corner, yet bond, commodity and currency markets are not reacting the way one would expect if an economic downturn were likely. Despite the 10% peak-to-trough correction in U.S. stocks, there hasn’t been the typical “flight to safety” into U.S. dollars, yen, euros or pounds. Nor has there been much movement in developed world bond yields. Commodity prices have also been relatively stable, although oil prices have been a little weak lately.

Fear and greed are powerful emotions; it’s human nature to extrapolate trends. We are hardwired to believe the outlook is good when stocks are going up and bad when they are going down. Consequently, our thinking typically fuels self-fulfilling behaviour and reaffirms market action as we buy in rising markets and sell in falling markets. The media adds gas to the emotional fire by sensationalizing market movements to increase its audience.

We don’t doubt that some investors sold in a panic upon learning on February 6 that the Dow Jones Industrial Average had its biggest daily point drop in history. The important facts, however, often differ from the headlines. In this case, it’s the percentage that matters, not the point count. While the 1,175 point decline was indeed large, it equated to less than 5% – significant, but not worthy of an ominous headline. The Black Monday crash in 1987 was a much lesser 508 points, but in percentage terms the decline was almost five times as bad at 23%. *That* was the biggest one-day drop in history!

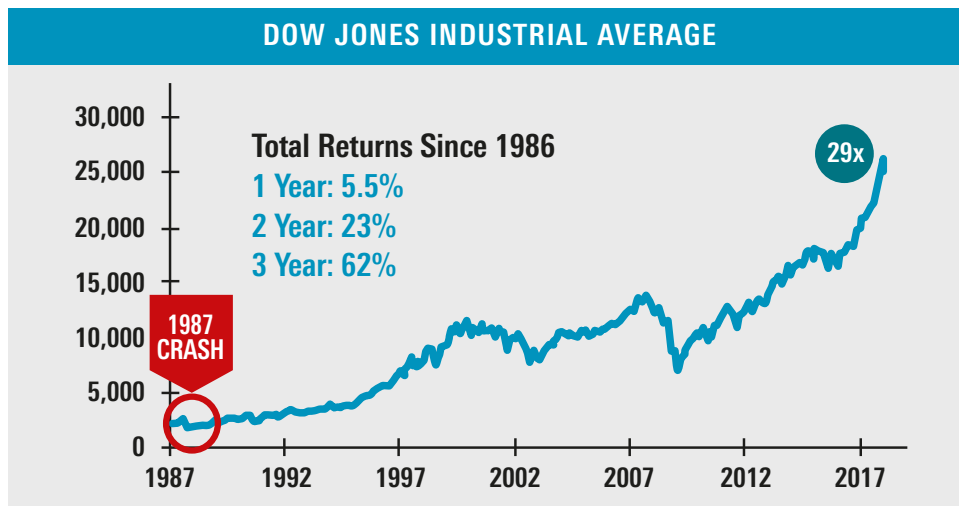
From peak to trough, the Dow experienced a 36% decline in 1987. The latest correction was less than one-third that amount as of mid-February.

Looking back at the performance of the Dow over the last 30-plus years, as highlighted in the following chart, the 1987 crash is merely a blip in a long upward march. Despite the horrific correction, the Dow still returned 5.5% in 1987 (including dividends). Over two years, the total return was 23%, and in three years it was 62%. Someone lucky enough to own the Dow since 1986 would have a 29-fold gain.\*

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We make the comparison to 1987 because the economic backdrop and investor attitudes were similar to conditions today. The economy was strong, inflation was picking up and the Fed was raising interest rates.



Source: Bloomberg

We make the comparison to 1987 because the economic backdrop and investor attitudes were similar to conditions today. The economy was strong, inflation was picking up and the Fed was raising interest rates. The market had had a huge run-up back then, similar in magnitude to the advance made since President Trump was elected, and people had become used to a one-way market. When the market hit some turbulence, too many people tried to rush for the exits at the same time, which caused investors to panic.

The market ultimately recovered in 1987 because the underlying economy was strong, and we think the same will be true this time. With any luck, the market's mood will improve as spring approaches.



**MURRAY LEITH, CFA**  
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\*Assuming dividends were reinvested along the way.

## Prescribed Rate on Spousal Loans 2% Effective April 1, 2018

**The prescribed interest rate on spousal loans will increase to 2% effective April 1, 2018.**

You have until **March 31, 2018**, to lock in the current and historically low prescribed rate of **1%** on a spousal loan. This is significant because the prescribed rate in effect at the time the loan is entered into remains locked for the duration of the loan.

### What is Income Splitting?

Income splitting with respect to non-registered funds is the process of shifting investment income from a high-income earner to a lower-income spouse or common-law partner. Simply gifting money to a lower-income spouse will not achieve income splitting since the attribution rules in the Income Tax Act attribute any income or gains earned on the amount gifted back to the person making the gift.

### How is the Prescribed Rate Determined?

The prescribed rate, set quarterly by CRA, is based on the average yield of 90-day T-bills during the first month of the previous quarter and rounded up to the nearest whole percentage point.

### Disclaimer

Clients contemplating a spousal loan should seek tax and legal advice before initiating such a transaction.



**MICHAEL EREZ, CPA, CGA, CFP**  
Director  
Odium Brown Financial Services Limited

Odium Brown Financial Services Limited is a wholly-owned subsidiary of Odium Brown Limited, offering life insurance products, retirement, estate and financial planning exclusively to Odium Brown clients.

# Understanding Your Life Insurance Options

There is no “one size fits all” solution for life insurance. The type and amount of coverage one individual or family requires can be completely different from another, even though they may appear to be in a similar situation.

Once a proper Insurance Needs Analysis has been prepared and reviewed based on your individual family and estate planning needs, the next step is to decide what type of coverage to purchase. If your needs are simple, you may just need one type of coverage. If your situation is more complex, you may need more than one policy. The type of coverage required will depend on the purpose of the insurance coverage and the individual or family’s immediate needs and long-term goals.

## Insurance costs vary based on many factors:

- age at time of purchase
- gender
- lifestyle
- medical history
- the amount of coverage
- the type of coverage purchased

Generally speaking, there are three types of life insurance: term, permanent (also called whole) and universal.

## What type of life insurance coverage should you purchase?

### TERM LIFE INSURANCE

#### What does it provide?

- Temporary, renewable and flexible protection.
- Terms can be selected based on the length of time coverage is needed (e.g., 10, 20 or 30 years).
- Most plans are convertible to permanent insurance without having to requalify by giving new medical information.

#### What are the considerations around premiums?

- Very affordable, with low initial costs.
- Generally, these plans have high renewal rates after the initial term has ended.
- Premiums increase significantly at each term renewal. A new trend is yearly increases after the first renewal.
- Coverage ends in most policies by age 75-80.

#### When does it pay?

- If you die before the policy expires.

#### Who is it suitable for?

- Those with temporary needs, such as outstanding debt, mortgages, periods of family dependency, child’s education, protection while building retirement or investment savings, and business loans.

### PERMANENT LIFE INSURANCE (WHOLE LIFE INSURANCE)

#### What does it provide?

- Lifetime protection, typically with guaranteed premiums and guaranteed cash values.
- The required premium-paying period may be for life or guaranteed for a limited number of years (e.g., 10 or 20 years).
- Policies may include enhancements in the form of a policy dividend or an annual performance credit, which can be used to reduce future premium payments, purchase more insurance coverage, increase cash value growth or some combination of these options.

#### What are the considerations around premiums?

- Higher initial costs.
- Required premiums in some plans may lack flexibility if ongoing premium payments cannot be made.
- Many plans offer reduced paid-up insurance or extended term options should you wish to stop paying premiums in later years.

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## Odlum Brown’s 24<sup>th</sup> Annual Address

Thank you to our clients and friends

who joined us throughout BC for our

24<sup>th</sup> Annual Address.

Video presentations and speech

transcripts will be available online this

month at [odlumbrown.com/2018aa](http://odlumbrown.com/2018aa).

- Other valuable features include cash values that can be used to pay premiums for a limited amount of time if a premium holiday is needed, accessed by way of a policy loan or taken in cash should you no longer require the insurance coverage.

**When does it pay?**

- When you die; no expiry date.
- Tax implications may apply if a policy is surrendered for the cash value prior to death.

**Who is it suitable for?**

- Individuals who wish to have coverage that lasts a lifetime.
- Some common reasons include estate creation, wealth transfer, conservation of family assets such as recreational property, estate equalizing between beneficiaries, maximizing pension benefits, charitable bequests or simply guaranteed funds to pay final taxes and expenses.

**UNIVERSAL LIFE INSURANCE**

**What does it provide?**

- Lifetime protection combined with tax-deferred investment options.
- Additional premium deposits above the required or guaranteed cost of insurance may be deposited and invested at the discretion of the policy owner in various investment-linked options. Positive returns from the linked investment funds are exempt from taxation while the funds are in the policy or if the funds are paid out as a death benefit.
- In many cases, a goal is to have sufficient funds in the policy so that the investment-linked returns pay the ongoing insurance premiums. CRA limits apply to the amount of deposits and the overall growth that can remain tax sheltered.

**What are the considerations around premiums?**

- Flexibility in premium deposits above the minimum premium requirements.
- Success of the policy may be tied to investment returns that require ongoing monitoring and management. Returns can also be negative. Negative returns or failure to obtain the returns projected may result in the policy requiring additional premium deposits in future years to meet long-term goals and to continue to provide coverage for life.
- Insurance charges can be level for life or based on a yearly annual term cost.
- Yearly costs are lower initially, which maximizes the premium deposits going toward the investments in the early years. The downside can be higher costs later if expected returns are not obtained.

**When does it pay?**

- When you die; no expiry date.
- Tax implications may apply if a policy is surrendered for the cash value prior to death.

**Who is it suitable for?**

- Individuals who wish to have coverage that lasts a lifetime.
- Some common reasons include estate creation, wealth transfer, conservation of family assets such as recreational property, estate equalizing between beneficiaries, maximizing pension benefits, charitable bequests or simply guaranteed funds to pay final taxes and expenses.

Exploring the different types of life insurance options available with your Insurance Specialist is the best way to determine which option(s) will best fit your individual needs and circumstances.

If you would like more information on the insurance options available through Odium Brown Financial Services Limited, contact us through your Odium Brown Investment Advisor or Portfolio Manager.



**RITA AGER, CFP, CLU, CHS, CPCA, FEA**  
Insurance Specialist  
Odium Brown Financial Services Limited

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