Three strategies to improve after tax investment returns

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These three strategies will help make you a more successful investor

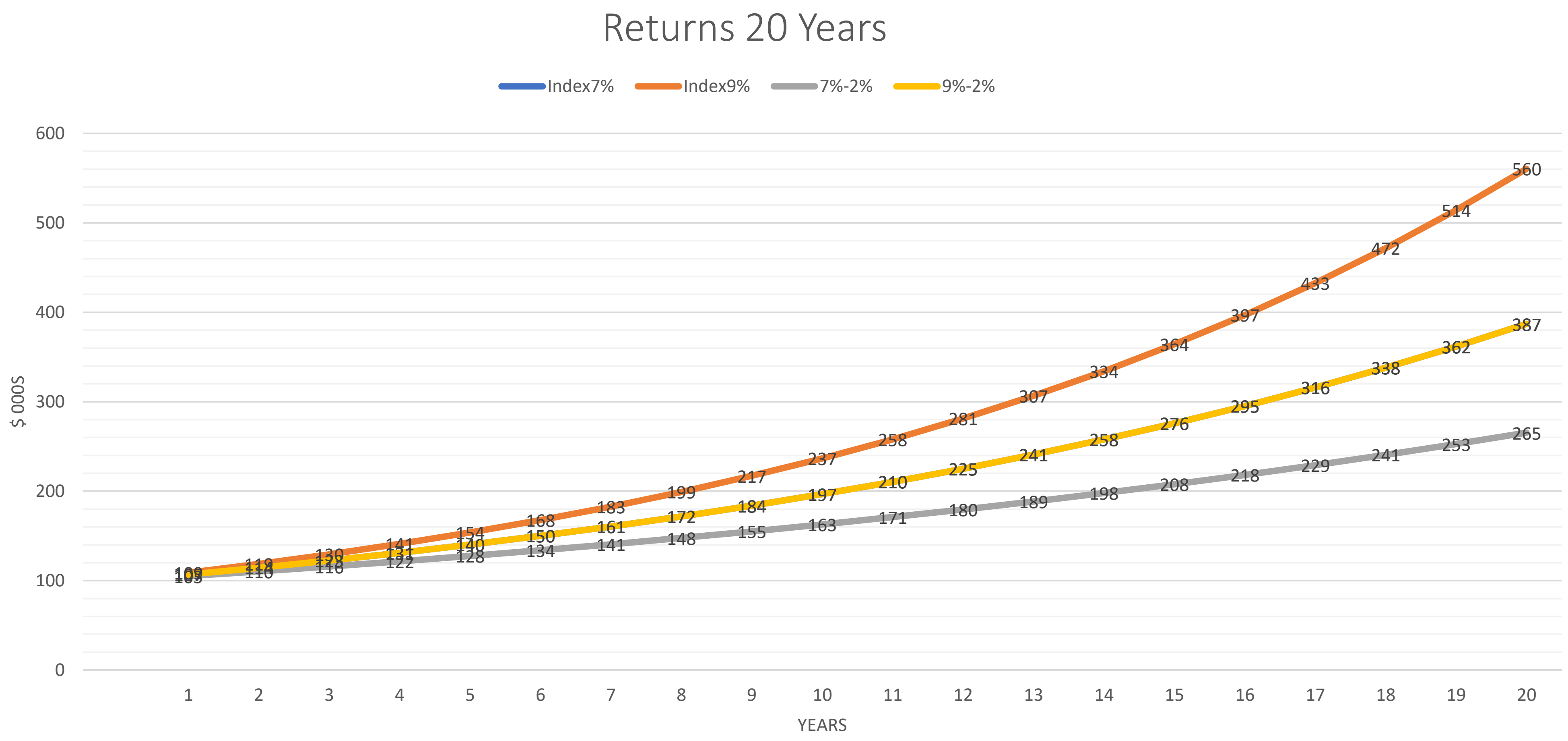
- 1. Keep investing fees to the minimum necessary
- 2. Minimize taxes through tax optimization
- 3. Diversify both assets and geography

Strategy 1
Keep fees to the minimum necessary

- 2% a year fees can reduce your gains by up to 44% over 20 years
- Canada has some of the highest mutual fund fees in the world
- Despite this, 92%+ of Canadian managed mutual funds underperform the markets
- Exchange Traded Funds (ETFs) charge fees as low as .05%
- No <u>Fiduciary Responsibility</u> unless specifically stated in writing

How 2% fees erode your gains over time

After 10 years, you could have 20% more, after 20, 44%



Most Canadian managed mutual funds underperform their Index

- SPIVA research: % of funds beating the index over 5 and 10 years

	5 years	10 years
Canadian equity	18	8
Canadian dividend	40	0
US equity	2	2
International equity	10	6

As of Dec 29, 2017

www.spindices.com.

Mutual Funds versus Exchange Traded Funds (ETFs)

- Mutual Funds can be Active or Passive
  - Sold through brokers or financial advisers or Bank advisors
  - Usually have annual trailing commissions up to 1%
  - Fees can be high:
    - .5% - 2.5%+
- ETFs can be Active or Passive
  - Sold like stocks through brokers
  - No trailing commissions
  - Often half the fees of an equivalent Mutual Fund:
    - .05% - 1%

How to implement this strategy

- 1. Set up an Online Trading account through your bank branch and buy index tracking ETFs.
- (For more info see InvestingForRetirees.com, ETF Workshop)
- 2. Set up an account with an advisory service such as BMO's SmartFolio
- 3. Set up an account with a RoboAdvisor such as WealthSimple
- 4. Hire a Fee Based Financial Adviser @ 1% and select Index tracking ETFs.
- 5. **<u>Never, ever,</u>** pay a Mutual Fund sales commission including DSC.

Strategy 2
Minimize taxes through tax optimization

- The best tax deal in Canada is the Dividend Tax Credit
- Interest producing investments into your RSP/RIF
- Depending on your taxable income, Dividend payers into your Taxable account and/or your TFSA (Never into your RIF)
- Capital gainers into your Taxable account
- For US$ income, buy Canadian companies co-listed in the US.
- US Dividends taxed the same as Interest income or RIF withdrawals

Effective Ontario marginal tax rates after age 65 by type of income (including clawbacks)

Bracket	Interest/RIF/RSP/Rent	Dividends	Capital Gains
19000-25000	70	62	35
25000-36000	20	-7	10
36000-46000	23	-4	12
46000-75000	33	9	17
75000-85000	44	30	22
85000-121000	52	41	26
121000-142000	43	25	22
142000-203000	48	32	24
203000+	54	39	27 MoneySense Magazine, February 2018

Tax benefits of dividends and capital gains

- Dividend tax rate = 70% or less of interest or income rate, depending on tax bracket
- Effective after tax Dividend yield = 1.2-1.3 or more times interest income
- Capital Gains = 50% of interest or income rate, depending on tax bracket
- Effective after tax Capital Gain yield = 1.4-1.5 times interest income

How to implement this strategy

- 1. Put fixed income investments in your RSP/RIF
- 2. Put dividend payers in your TFSA or taxable account, depending on your taxable income
- 3. Put capital gainers in your taxable account
- 4. Put US dividend payers in your RSP/RIF
- 5. For US$ income, buy Canadian dividend payers co-listed in the US (Banks, Pipelines, Infrastructure) and hold them in the US$ side of your TFSA

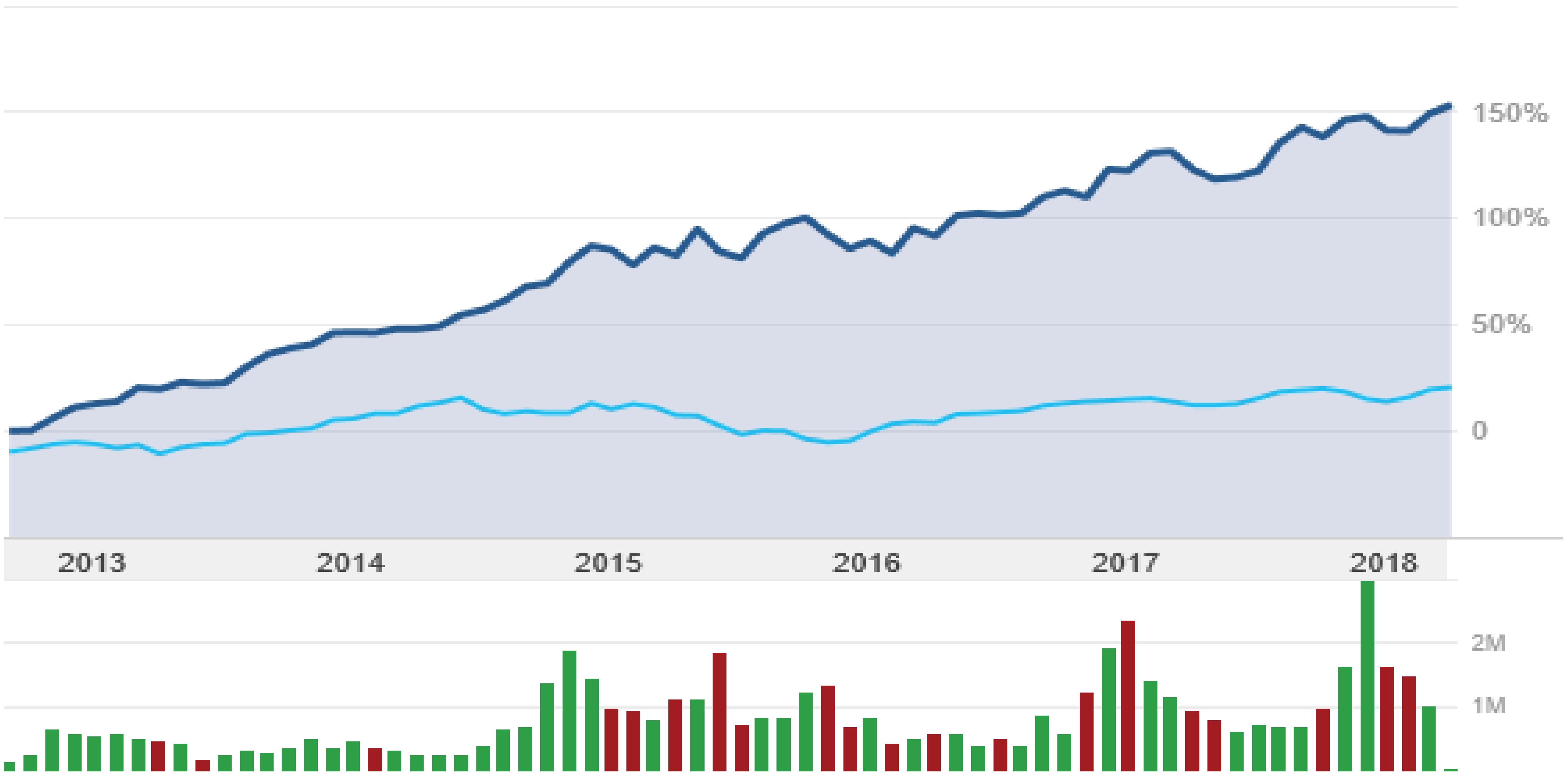
Strategy 3
Diversify by both assets and geography

- Canada is only 3% of world stock markets, and a chronic underperformer
- Determine your real risk tolerance
- Rebalancing is key to long term success
  - Forces you to sell high & buy low

XIC (Canada ETF) vs VFV (S&P 500 C$ ETF)

"Deadlast: TSX returns turn negative after 10 years of miserable performance."

G&M Feb 9, 2018



Time horizon is key

- Age is not the key factor – time horizon is
- **If you need funds within 5 years, stay out of stocks and medium-long term bonds**
- No return without risk
- “Ask yourself one question.
- Do I feel lucky?”
    - Dirty Harry, 1971

Asset class options (1)

- Equities
  - Canadian, US, International
  - Individual stocks
  - Mutual funds
  - Exchange Traded Funds (ETFs)
- Real Estate
  - Real Estate Investment Trusts (REITs)
  - Physical Real Estate

Asset Class Options (2)

- Fixed Income
  - GICs
  - Bonds
  - Bond Funds
  - Money Market Funds
  - High Interest Savings
  - Preferred Shares
- Cash
  - Money Market Funds
  - High Interest Savings

Pension

Focus on income growth rather than capital growth

- Most retirees want income and principal protection
- Portfolio Models available from Wealth Management companies focus on building assets rather than income.
- Tax optimization plays a key role in asset selection and location – ie registered or non registered accounts.

Ready made portfolio solutions

- BMO Smartfolio & other major banks' services
- Robo Advisors
- Canadian Couch Potato blog
- Vanguard One Fund Solution ETFs

- <u>BUT, none are designed for generating tax efficient income</u>

Model Portfolio – Conservative Risk

Weighted average distribution 2.8%

Asset Class	%	Div % est	First Account	Second Account
Canadian Div Stocks & REITs Canadian Broad Mkt	15 10	4 + 2.7	TFSA	Non Registered
US Stocks	10	1.7	RSP/RIF	Non Registered
International Stocks	10	1.8	RSP/RIF	Non Registered
Canadian Preferreds 60/40 Reset/Perp	20	4 +	TFSA	Non Registered
Short term bonds or GICs	30	2.4	RSP/RIF	
Cash	5	1.2	Non registered	

How to implement this strategy

- 1. Be comfortable with your risk level – don't overestimate tolerance for loss
  - Could you live with a decline of 30% or more of your capital? It happens – 1987, 2000-2002, 2007-2008
- 2. If you need money within 5 years, do not invest in stocks and medium & long term fixed income
- 3. Attend one of the Free NAFR Investing For Retirees Seminars starting in January, 2018

Investing For Retirees Seminars 2019

- Registration for these seminars begins in December on the NAFR Ottawa web site. An email will be sent to all members.
- Register early as these seminars sell out quickly.
- January 16 & 23
- January 30 & February 6
- April 10 & 17
- May 1 & 8
- May 15 & 22

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