The Stan Clark Financial Team's

PERSPECTIVES

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Volume 9 - Issue 4 June 2018

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At New Year's, we all make resolutions. Now that we're halfway through 2018, I suggest revisiting those resolutions – and actually carrying them out. The key: changing bad habits. Michael Chu and I discuss the importance of planning for both life expectancy and inflation. Looking at active vs. passive investing, Michael suggests using the best of both. And Sylvia Ellis explains why you should be proactive about preparing your Will.

Stan

Behavioral finance

We're half way there: How to carry out your resolutions?

By Stan Clark - Senior Investment Advisor

Many of us make New Year's resolutions only to forget them – until the next New Year winds around. But maybe we should revisit our resolutions before then. Now, at 2018's midway point, seems a good time to freshen them up with some *Half-Year's Resolutions*.

According to a 2017 Ipsos poll, Canadians' top two New Year's Resolutions were:

1. Improve personal fitness and nutrition (33%), and
2. Focus on financial goals (spend less, save more, settle debts) (22%).

Whatever your goals, a key to achieving actual change is to focus on *habits*. A habit, according to Wikipedia, "is a routine of behavior that is repeated regularly and tends to occur subconsciously."

Habits often start as conscious, purposeful decisions. They can also begin without us even being aware of them. Either way, over time and with repetition we assign habits to the automatic part of our brains. We do most habits without even thinking about them.

There's a saying, "Humans are creatures of habits." We depend on habits for a large part of what we do. We likely couldn't survive long without them. Our conscious brains would become overwhelmed making the thousands of trivial decisions each week that our habits cover now.

But, while habits are necessary and mostly useful, we can also develop some harmful ones. Achieving positive change often requires us to replace bad habits with good ones. So how do we do this?

First we need to understand the *habit loop*. Habits comprise three things:

1. A **cue** – the thing that triggers the habit
2. A **routine** – what we do in response to the cue, and
3. A **reward** – the physical or psychic benefit to us.

A habit gets developed and strengthened as we repeat this habit loop over and over. In his book *The Power of Habit*, Charles Duhigg cites the "Golden Rule" of habit change: "You can never truly extinguish a bad habit. Rather, to change a habit, you must keep the old cue, and deliver the old reward, but insert a new routine."

So rather than trying to just stop doing something, identify the specific cue and specific reward. Figure out a new routine that will better meet your goals and deliver the same, or a similar, reward.

Let's say you want to quit snacking at work. The first step is to figure out what, exactly, is the cue or trigger for your snacking. You might discover that it's not hunger, but rather a need for distraction. Next time you feel that cue, don't respond by snacking. Apply a conscious effort and insert a new routine like going for a short walk or getting a drink of water. Hopefully you can find a routine where the reward feels good enough to satisfy you.

Or perhaps you spend too much money shopping online. You notice you shop when you feel stressed. By diverting your attention, shopping helps you relax. The key to changing the habit is to be aware when the cue arises, and then change the routine. Perhaps go for a walk, try balancing on one foot, stretch, or close your eyes and meditate. Try to find something that feels positive and substitutes for the shopping as a way to relax you.

At first, changing a habit will require conscious effort. It will likely involve accepting a reward slightly less satisfying than the old routine provided. But habits strengthen with time and use. If you stick with it, the new habit will get easier. Likely you will come to crave the new reward, perhaps even more than the previous one. Changing habits is also easier if you've committed to change to a group or another person, and they're supporting you.

Good luck with your Half-Year's Resolutions. Wouldn't it be nice to bring in 2019 with some great new habits already in place! ■

Team Talk:

Jocelyn Johansson
Associate Investment Advisor

Blackcomb base ski-out (April 15, 2018)

Where have you travelled recently?
In February we spent a blissful week relaxing in the Oahu sunshine. We rented a condo near the Disney Aulani Resort. We took our four-year-old son Callan to the Disney characters' breakfast. He loved meeting Mickey and Minnie Mouse, Pluto and his favourite, Stitch.

What memory from this past year makes you smile the most?
Callan completed his first season in the Whistler Kids Ski program. My entire family has skied since we were young, so it's fantastic for him to have the same passion. The photo is from the end of a long, happy ski day.

What's the next trip you're looking forward to?
We're headed to Palm Springs in July to celebrate five of my closest friends' 40th birthdays. Friends from Stockholm, Sweden will also be joining us. We've rented a huge house for a weekend of relaxing in the sunshine!

Asset allocation

Thinking for the long term: life expectancy and inflation

By Stan Clark, Investment Advisor, and Michael Chu, Investment Advisor

Life expectancy and inflation are probably two of the least popular topics in the world of finance. But just because people don't want to talk about these topics doesn't mean they're not important! In this article, we discuss the effects of life expectancy and inflation – and show that, in fact, they are indeed very important.

Most people are reluctant to plan too far ahead. However, you need an idea of your life expectancy to make shorter-term decisions, such as how much money you can spend during your retirement.

The average life expectancy has been steadily increasing. For a 65-year-old male, the average life expectancy is 86. For a female, it is 89. Moreover, the older you are, the longer you can expect to live. Below is a table of average life expectancies:

Average life expectancy (years further)

Age	Male	Female	Joint
65	86 (21 years)	89 (24 years)	91 (26 years)
70	87 (17 years)	90 (20 years)	92 (22 years)
75	89 (14 years)	91 (16 years)	93 (18 years)
80	91 (11 years)	93 (13 years)	94 (14 years)

Source: Canadian Institute of Actuaries (1997-2004)

The third column in this table shows the life expectancy of a couple. You may have noticed that the joint-life expectancy is longer than the life expectancy of either spouse. Now, this doesn't mean married people live longer. It's just that you have to plan for both spouses to die instead of just one. After all, since there are two people involved, it's reasonable to expect that at least one of them could live longer than average. What this means is that, people need to plan for a long life – and couples need to plan for even longer lives.

With such long time horizons to consider, we need to watch out for inflation. The cost of a Big Mac hasn't changed much between today and a year ago. But do you remember what it cost 10 years ago? How about when we were kids? A Big Mac then cost significantly less! Inflation has a huge negative effect over time – and money is only as good as what it can buy. People shouldn't fool themselves into thinking inflation won't significantly affect their wealth. Furthermore, all planning should be based on the real value of their wealth, that is, factoring in the effects of inflation.

Over the past 100 years, inflation has averaged about 3%. At first glance, this might not seem significant. However, as you can see in the table below, 3% inflation over 10 years means a 26% loss in the real value of your wealth. And, over 30 years, inflation consumes 60% of your wealth!

Loss due to inflation over time

Time	2% Inflation	3% Inflation	4% Inflation
10 Years	18% loss	26% loss	34% loss
20 Years	33% loss	46% loss	56% loss
30 Years	45% loss	60% loss	71% loss

Source: calculations performed by Stan Clark, CFA, CFP, MBA

The good news is that we can do something about this. On average, investing in bonds returns about 4%, just barely above the average inflation rate. But stocks return about 10%, well above the inflation rate. Investing properly can help offset the negative effects of inflation.

The key is to determine the right balance of stocks and bonds that is appropriate for you, based on your risk tolerance and your goals. Our integrated approach to financial planning, based on your input, can help you plan properly for both life expectancy and inflation. ■

Stan Clark is First Vice-President, Portfolio Manager and Senior Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Stan has direct responsibility for the team and oversees all areas of financial planning, investment selection and investment management.

Michael Chu is a Portfolio Manager and Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Michael is a specialist in investment research and information technology.

Investing

Active vs. passive investing? How about the best of both!

By Michael Chu, Investment Advisor

Investing in stocks can be categorized into two main approaches: *active* and *passive*. Let's start by looking at the active approach.

Active fund managers pick individual stocks that they think will do better than others. There are many different ways of picking individual stocks. Some managers will analyze the company, interview management and even talk to customers and competitors. They may also review historical trends and try to make forecasts on how the business will fare in the future. Investing actively seems to make a lot of sense, which explains why it is the most common method of investing. It's also appealing because people like to hear "feel-good" stories about their decisions.

But what about the actual track record of active fund managers? We can refer to the *SPIVA Canada Scorecard*[i], which reports the performance of actively managed mutual funds in Canada. The *Scorecard* also corrects for survivorship bias, which means including funds that have been closed, most likely due to bad performance. Over three-, five- and 10-year periods, the majority of Canadian mutual funds did not outperform their benchmarks. Specifically, over 10-year periods, only 9% of Canadian equity funds and only 2% of U.S. equity funds outperformed. In other words, more than 90% of funds underperformed. The amount of underperformance is notable, too. Over 10-year periods, Canadian equity funds underperformed on average by more than 1% per year, while U.S. equity funds underperformed more than 3%. Shocked? Yet it's all too true. The long-term underperformance of funds has been around for a long time.

It is important to note that, there have been shorter periods, say fewer than five years, where active funds have done better than their benchmarks. But these periods haven't lasted, and they've always been followed by periods of underperformance.

So, traditional active management doesn't work well – but not because these managers haven't been doing their homework. Rather, it's because human decision-making is systematically flawed and unreliable. Biases and emotions make it difficult to be objective. Through the teachings of behavioral finance, we know that people are often ruled by greed, hope and fear. This awareness provides us with an opportunity to use a rational, disciplined method to invest. In a sense, we are taking advantage of the flaws in human nature.

The realization that traditional active management doesn't work well has led to continued growth in the passive approach to investing. Passive investors will just buy an entire index or basket of companies that represents the market. Their objective is to match the market, not outperform it. These investors are willing to give up their chance at outperforming for the guarantee that they will not *under*perform. This strategy might seem appealing – it's simple and low-cost and will probably outperform most traditional money managers.

But passive investing has its drawbacks, as well. Buying an index means buying almost all of the stocks in a certain market. For example, the Canadian TSX Index is made up of the biggest companies that trade in Canada; about 250 of them. Even if a stock is clearly overpriced, the index must hold it. And the way most indexes are designed, the more overpriced a stock becomes, the more the index will own of it. Despite this flaw, indexes still tend to outperform most mutual fund managers. This is because of the pre-defined, set criteria that indexes use to "choose" stocks. Even if the criteria is not that good, they help indexes avoid the human emotional mistakes made by most traditional active managers.

So, what's the best approach to investing? Suppose you created your own "index" – using set criteria that made sense and helped avoid the most expensive companies. We've talked about some of these criteria before: price-to-earnings ratios, price-to-book ratios, dividends and momentum. Why not take the best of both worlds? Create a systematic approach to investing, essentially a hybrid of passive and active investing that is automatic. If a stock meets the criteria, then it's purchased. If it doesn't, then it's sold. This is similar to how the passive TSX index will mechanically add or drop a company based on predetermined rules.

Does all this seem familiar? It should, because it's exactly what we do. Essentially, with our rules-based approach, you are "indexing" your portfolio to be a specific, time-tested investment strategy. By doing so, you are combining the best qualities of passive and active investing.

Keep in mind that disciplined implementation is the key to success. It's not just *having* a good strategy – but also carrying it out. ■

[i] *https://us.spindices.com/documents/spiva/spiva-canada-mid-year-2017.pdf*

Michael Chu is a Portfolio Manager and Investment Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Michael is a specialist in investment research and information technology.

Financial Planning

Why you need a Will

By Sylvia Ellis, Senior Estate Planning Advisor

I'm sure you've seen many articles on the need to have a Will. You may already have your Will in place and up to date! But you'd be surprised at how many people don't. In fact, a CIBC survey conducted in 2015 estimates that almost half of Canadians don't have a valid Will.

If you're one of them, consider asking yourself why. Maybe you're thinking, "I'm too young, so it's not that important right now." Or maybe, "I'm too busy." Or, "It costs too much." You could also be assuming that, if you die without a Will, your assets will simply pass to your spouse or other beneficiaries. But what if, for example, you have children, perhaps from another marriage – or if you have in mind certain intentions for your money?

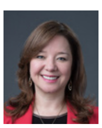
If you die without a Will, you are considered to have done so *intestate*. This means the provincial government – not you – decides how your assets will be divided.

Each province has rules that define your estate's beneficiaries and how much each is entitled to. Generally, the rules run along family lines. But they can often result in unintended inclusion or exclusion of beneficiaries. And *that* can lead to substantial financial costs you could have avoided.

Some reasons to be proactive about drafting your Will include:

- If you have minor children, you lose your say in how they may be cared for. Portions of your estate are usually paid into court and administered by the surviving parent or a court-appointed guardian. An issue here is that, at age 18 (this varies province to province), a child could take charge of their full entitlement.
- B.C.'s new *Wills, Estates and Succession Act* rules came into effect March 31, 2014. If you die intestate, your spouse will merely have the right to purchase the home you lived in from the estate within six months of the grant of probate. Also, the child and parent entitlements will vary depending on the connection to the marriage.
- One way to defer income taxes on death is to leave property that has appreciated to your spouse. With no Will, a portion of your estate may be left to your children or others, resulting in a higher tax liability to the estate.
- If you have charitable aspirations, one way of reducing your estate taxes is by making gifts in your Will. This wouldn't happen without a Will.
- In your Will, you can establish a *testamentary trust*, which has its own benefits. It is worth noting that the federal government eliminated the tax benefits of testamentary trusts, but in certain circumstances, they remain an effective planning tool in your Will.

Will planning is one area where we strongly recommend you seek assistance from a specialized legal advisor. Making a Will is more than just signing a document. It involves reviewing your potential estate, and planning to minimize the cost of probating and administering it. The few hours you spend with a legal advisor planning your estate could save your spouse, children and other beneficiaries much time, effort and money. ■



Sylvia Ellis is the Senior Estate Planning Advisor for the Stan Clark Financial Team at CIBC Wood Gundy. Sylvia provides support to the team in projecting and planning client financial affairs.

SCFT Trivia

Play our trivia – support the cure!

For every correct entry we receive in our trivia contest, the Stan Clark Financial Team will contribute $1 to CIBC's "Run for the Cure" to raise money for breast cancer research. Each correct entry will also be entered into the draw for this month's prize. Email or phone in your entry today.

Answer all four questions to be entered into the draw for this month's prize. Hint: You can find the answers inside this newsletter.

1. In his book The Power of Habit, Charles Duhigg says you can change a bad habit by:
   a) making New Year's resolutions to do so
   b) figuring out a new routine that gives you the same, or a similar, satisfaction
   c) adopting a more nutritious diet
   d) getting more exercise.
2. Over time, the effect of inflation:
   a) can have a huge negative effect, especially if you don't plan for it
   b) is fairly negligible; only in the short term do you have to worry about it
   c) only impacts people with low savings and few investments
   d) depends on how many Big Macs you eat.
3. Passive investors give up the chance to outperform to guarantee they won't underperform:
   a) True b) False.
4. If you have minor children and die intestate, that is, without a will:
   a) portions of your estate are usually paid into court and administered by the surviving parent or a court-appointed guardian
   b) at age 18, a child could take charge of their full entitlement
   c) child and parent entitlements will vary depending on the connection to the marriage
   d) all of the above.

Email answers to: **stanclarkfinancialteam@cibc.ca**
or call (604) 641-4361

One prize winner will be chosen by a draw from all those who submit correct answers. The draw will take place on June 29, 2018.

Trivia challenge runs May 30 - June 28, 2018. No purchase necessary. There is one prize to be won. Simply complete the trivia questions correctly to be entered in the draw. Limit 1 entry per person.

Chances of winning depend on number of eligible entries and whether you correctly answer the trivia questions. Open to adult Canadian residents (excluding Quebec). For full challenge rules, write to: The Stan Clark Financial Team, CIBC Wood Gundy 400-1285 West Pender St, Vancouver, BC V6E 4B1. © Stan Clark 2018

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Where planning, investing and behavioral finance meet

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