The Stan Clark Financial Team's

PERSPECTIVES

In this issue...

Pg. 1 Introversion, extroversion and your finances

Pg. 2 Quarterly Economic Update

Pg. 3 Disability insurance: Do you have enough?

Pg. 4 SCFT Trivia

Volume 9 - Issue 3 April 2018

Stan Clark
Senior Investment Advisor

Citing Susan Cain's book *Quiet: The Power of Introverts in a World That Can't Stop Talking*, I discuss in this month's behavioral finance article how tendencies to extroversion and introversion can affect financial decisions.

In our *Quarterly Economic Update*, Michael Chu and I look at how developments thus far in 2018 may impact the economy. And Sylvia Ellis reveals advantages about having disability insurance that many people may not have considered.

Stan

CIBC Wood Gundy

Behavioral finance

Introversion, extroversion and your finances

By Stan Clark - Senior Investment Advisor

In his fascinating book: *Thinking, Fast and Slow*, Nobel Prize winner Daniel Kahneman, described our minds as a dual system of fast thinking (System 1) and slow thinking (System 2). Our fast- and slow-thinking modes render us vulnerable to errors in making important financial choices. But there's another fascinating dual system we all share: *introversion* and *extroversion*. Our levels of these two can also expose us to poor judgments and bad investment decisions.

In *Quiet: The Power of Introverts in a World That Can't Stop Talking*, Susan Cain compares introversion and extroversion, including how they affect our financial decisions. Cain says we have two different brains. In our primitive or reptilian brain, located in the brainstem, anger and fear arise along with aggressive impulses. The other brain, our neocortex, gives rise to abstraction, reasoning, curiosity, speech and other qualities that make us human.

Our primitive brain watches for danger. It sends signals urging caution. The neocortex seeks novelty and pleasure. To help us find and experience these, it promotes risk-taking. The extent our neocortex heeds the warnings from our primitive brain determines our place on the continuum from extreme extrovert to extreme introvert. Cain cites studies indicating one-third to one-half of us are mainly introverts in our behaviour; the rest, mainly extroverts.

Extroverts are more reward-sensitive. Their brains produce more of (or are more sensitive to) the excitatory chemical dopamine. Extroverts gamble because winning gives them a rush. Introverts resist gambling. It's not so much that extroverts don't receive the same warnings from their primitive brains as introverts. But extroverts have innate biochemical mechanisms that let them ignore the warnings.

Extroverts tend to prosper in bull markets. They get excited. They decide and act quickly when presented with opportunities. They generally experience enough wins to offset any losses their rashness incurs.

Cain suggests it was the presence of so many extroverts in power at investment banks, brokerages and other financial institutions – as well as on the boards of large corporations – that led to the Enron-style meltdown of the housing and stock markets in 2007-2008.

That's large-scale extroversion. At the personal level, Cain offers the example of Alan, a 60 year old extroverted midwesterner. Through hard work, Alan and his wife accumulated a million dollars for their retirement. In 2008, hearing the government was going to bail out a troubled car company, Alan bought $100,000 of that company's stock.

But the bailout didn't happen right away. Rumours abounded that the company would be allowed to fail. Its stock plunged. In a classic example of anchoring and loss aversion, Alan clung to his stock, fixated on profits he still hoped to make.

The stock kept falling. Alan finally sold, losing most of his investment. Bailout rumours resurfaced. Alan bought in again. And again the bailout didn't materialize. Alan sold at a big loss. He bought in yet *again* and sold at a loss – until he had blown $700,000 of his nest egg!

What happened?

Most likely, Alan's reward sensitivity kept him focused on making a killing with his stock. He saw the potential rewards. He visualized a major coup. As an extrovert, he ignored the warnings raised over and over by the primitive part of his brain.

Had Alan been an introvert, he probably wouldn't have made such risky choices. Introverts tend to avoid big risks. In bearish markets, they fare better than extroverts.

The lesson: If you are highly extroverted, take a close look at your investment behaviour. Approach the market with rules and strategies based on objective data, rather than on emotions.

Investing with a disciplined, rules-based strategy – as we encourage our clients to do – removes emotions from your decisions. For extroverts, it's a little like having an introvert around to offer sound advice at crucial moments. ■

Team Talk:

Elaine Loo
Associate Investment Advisor

Elaine & sons - April 2018

If you were immortal for a day, what would you do?
Skydiving and bungee-jumping! Both seem exciting but fear keeps me away, not to mention my phobia about heights. If I were immortal, I would go ahead.

If you could meet anyone, living or dead, who would it be?
I would love to meet my mom's dad. He is the only grandparent I never met. I often wonder what traits/genes we inherited from him.

What was the last movie, TV show or book that made you cry?
When I watched the Pixar movie Coco with my family, there were many parts that were so touching or so sad, I couldn't help but tear up!

If you could throw any kind of party, what would it be?
I would actually prefer a relaxing at-home party. Movie and popcorn with good friends and family would be the best way to spend time. I wouldn't even need a reason. Parties for no reasons are usually the best ones.

Quarterly Economic Update

Volatility returns, but economy still strong

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

Stock markets around the world started off 2018 strong, but ended the first quarter mixed. The World Equity Index, a gauge of stocks around the world, was up 1.3% for the quarter (in C$). At home, the Canadian TSX was down 4.5%.

Motion sickness

The recent flare-up of stock market volatility is a useful reminder not to be too complacent after a long period of uninterrupted growth and gains. But instead of paying too much attention to the day-to-day gyrations, we should focus on the key themes.

First, the global economy is still quite strong. The rate of growth and the geographic breadth suggest durability. Second, with economies operating near capacity, inflation will eventually increase, but the risks of too much inflation seem low in the short term. Third, the tax cuts in the U.S. are enormously positive for corporate earnings.

We also have to acknowledge some of the negatives, such as increased protectionism. The current tit-for-tat trade actions threaten to dilute the stimulus from tax cuts, undermining growth. However, many of the current tariff threats are just that: threats. They may just be posturing in order to secure better deals. The aging business cycle is another concern.

New Fed chairman

Newly appointed Federal Reserve Chairman Jerome Powell's first Federal Open Market Committee (FOMC) meeting went smoothly. As anticipated, the Fed indicated three interest rate hikes for the year. But the economy is fluid, so the Fed might not actually deliver all three hikes. For example, in 2016, the Fed forecasted four hikes, but ended up only hiking once. The Fed might anticipate higher inflation end economic growth, but these might not actually happen, as economic models are far from perfect. The good news is that Fed Chairman Powell seems more focused on maintaining financial stability, which is good news for the stock market.

Trade war...or not

We don't know if a full-on trade war will occur or not. But looking at previous scares like the Avian Flu or Y2K bug, we see that people can and do work hard to solve urgent problems they know about. With so much attention on trade tariffs and money, work toward a solution is inevitable.

By now, many have heard of the Smoot-Hawley Tariff Act. Passed in 1930, Smoot-Hawley was designed to "regulate commerce with foreign countries, encourage industries of the U.S. and protect American labour." Sound familiar? Those tariffs were among the highest in the U.S. in 100 years – and led to a trade war. According to top economist Ed Yardeni, this Act caused the Great Depression.

With today's tariff talk, fear-mongers, especially in the media, are drawing comparisons to Smoot-Hawley. But the comparison is premature. Smoot-Hawley actually collapsed global trade, while President Trump's actions might end up being more bark than bite. Don't forget that there were many other tariffs in history that did not lead to trade wars. Some tariffs are only targeted or temporary. Also, Republicans are traditionally against tariffs.

In today's case, the tariff talk is an attempt to get China to play by the rules regarding piracy of U.S. technology – an effort that is long overdue. The U.S. is targeting Chinese technology companies because of their policies that force American companies to give up tech secrets in exchange for being allowed to operate in China. China also has a policy of requiring products for sale in China to also be made in China, making the trade imbalance worse.

Inflation and interest rates

People like to pinpoint a cause for events like the recent increase in market volatility. In fact, there are a number of reasons for the volatility, but two concerns revolve around rising inflation and interest rates. In school, we learned that rising interest rates are bad for stocks. This is because higher interest rates make bonds more

	1st Quarter 2018	Trailing P/E	Earnings Yield	Dividend Yield
Canada (S&P/TSX)	-4.5%	17.0	5.9%	3.1%
U.S. (S&P 500)	1.8%	23.2	4.3%	1.9%
Europe	-0.2%	17.2	5.8%	3.5%
Japan	3.3%	14.0	7.1%	2.1%
EAFE (Europe, Australia, Far East)	1.0%	15.9	6.3%	3.2%
Emerging Markets	4.1%	14.7	6.8%	2.4%
World	1.3%	19.6	5.1%	2.4%

Source: Bloomberg

competitive against stocks, and the cost of borrowing increases for companies. Inflation also increases costs for raw materials and labour. This in turn, causes lower company profits, unless a company can pass on the higher costs to consumers. So, in theory, inflation and interest rates seemingly have a similar effect on stocks. But what are the results in the real world?

Since the financial crisis, stock markets have enjoyed rock-bottom interest rates and low inflation. But the recent increases might be a headwind. The U.S. 10-year interest rates are currently around 2.7%, up 1.3% since bottoming out about two years ago. According to Ben Carlson of Ritholtz Wealth Management, there have been 17 instances since 1962 where interest rates rose more than 1%. The average performance for the S&P 500 during these rising-rate environments was almost 22% for the period. Stocks only fell three times when interest rates went up more than 1%. So, stocks have held up well during rising interest rate periods in the last 50-plus years. This doesn't mean what we studied in school wasn't useful. It just means that in the real world, stock markets are complex and interest rates are just one factor.

What about the effects of inflation? Here the track record for stocks is lower. From 1928 to 2017, when inflation was less than 3%, the S&P 500 had median returns of 16%. When inflation was above 3%, the median returns were still positive, but only 6.5%. A similar pattern occurs in periods of rising inflation. When inflation was lower than the previous year, median returns on stocks were 18.3%. But when inflation was higher, median returns were only 5.6%.

Therefore, it seems investors should be more concerned with inflation than rising interest rates. The good news is that inflation in the U.S. is only 2.1%, well below the long-term average of 3%. In theory, economies operating near capacity should result in more inflation. However, powerful structural forces are keeping inflation down: competition from globalization and deflationary technological innovation, as well as aging demographics.

NAFTA

North American Free Trade (NAFTA) negotiations are ongoing. It seems that negotiators are largely spinning their wheels as they struggle with aggressive U.S. demands and what Canada and Mexico are willing to give up. The most likely outcomes are: no changes, modest changes or termination. No or modest changes would be the ideal for all three countries. Termination of NAFTA would be problematic, resulting in higher costs, supply-chain issues and worker permit problems. Termination would likely hurt all three economies.

Further complicating negotiations are the upcoming Mexican presidential elections and U.S. mid-term elections. On the positive side, other trade deals have been struck, including the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). This deal binds a number of Pacific Rim countries, including Japan, with Canada and Mexico. The U.S. was originally part of this deal but dropped out. Canada also has a new trade deal with Europe.

Global growth

Since 2016, economies around the world have continued to experience synchronized growth. While stock market volatility and media scare stories might indicate otherwise, consider the following: Global trade is at record levels. Global manufacturing remains high, not just for the U.S., but also Europe and Japan.

Springtime for earnings

As companies begin reporting their earnings for the first quarter of 2018, we will start to see the real effects of the tax cuts. For the S&P 500, revenues are expected to grow almost 7% this year. Earnings expectations were revised sharply upwards by almost 20%, mainly due to tax cuts.

Looking forward

Overall, stock valuations are higher but still reasonable, especially when compared to bonds. We remain cautiously optimistic about the future. Of course, we can never be sure about what will happen in the short term. That's why it's important to have a time-tested financial plan, based on long-term data, that also provides a tailored asset mix for your investments. For your stocks, we continue to build diversified portfolios of companies that have strong characteristics for doing well in the future. ■

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.

Financial Planning

Disability insurance: Do you have enough?

By Sylvia Ellis, Senior Estate Planning Advisor

What would happen if you suddenly became disabled and were unable to work or carry out your regular activities? And if you no longer had an income to meet ongoing expenses, how would this affect you or your family?

Many people think first and foremost about life insurance. In reality, disability strikes far more frequently than premature death. Whether temporary or long-term, disability can happen to anyone, at any age. It can come on suddenly from an accident or illness, or develop over time.

So, what are your chances of becoming disabled for three months or longer?

If you are 50, you basically have a one-in-three chance of becoming disabled. And if you are disabled for longer than 90 days, on average the time will extend to 3.1 years.

Let's hope you beat the odds! But what if you don't? What are your sources of income if you don't have enough saved?

Well, there's…

Government benefits – But can you really count on them? Canada Pension Plan only pays for the most severe disabilities. As of 2018, Employment Insurance only covers a maximum benefit in B.C. of $547– which is taxable – per week, for 15 weeks. Lastly, Worker's Compensation pays for only work-related injuries.

Sale of assets – The question here is: Will you be able to sell and get the fair market value?

Borrowing – This is a tough one. If you can't borrow from the bank because you're not working, your only other option may be to look to family and even friends to help you. Do they have the money to spare? And how

would you feel if you had to ask them to financially take care of you?

Age	25	30	35	40	45	50	55
Percent	58%	54%	50%	45%	40%	33%	23%
Average #of years	2.1	2.5	2.8	3.1	3.2	3.1	2.6

Derived from 1985 Commissioners Individual Disability Table A

Group benefits plan – You may think to yourself, "I'm covered at work through my group long-term disability plan, so I'm okay." Are you, though?

Exactly how much of your income will be replaced? If your plan covers at least 60% of your pay, you may have enough. If you're a higher-income earner, however, this may not be the case. Some plans have a maximum benefit, such as $5,000 per month.

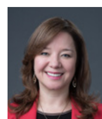
Another important thing: What is your group plan's definition of disability? Some plans may define it as being unable to perform the essential duties of your regular occupation for 12 or 24 months. After that, the definition changes to "any" occupation for which you are reasonably suited by occupation, training or experience. Some plans may go further and define disability without consideration of the availability of such occupations.

So, while it's good to have group long-term disability, it may not be the best coverage or enough.

Finally, a source of income could include…

Individual disability insurance – An individual plan can be the most comprehensive and flexible coverage available because *it can be tailored to your needs*. You can choose when the benefits start following disability, and for how long. You can elect a policy that cannot be cancelled and one in which the price cannot be increased. Most policies have the option to add – at an additional cost, of course – a *return-of-premium rider*. This means that, if you have not claimed after a certain period of time, you can choose to have all of your premiums paid back. There are many ways you can tailor these plans that make them well worth looking at.

Your earning potential is your most valuable asset. We urge you to review your personal situation and current coverage to determine if you're protected. As always, we'd be happy to assist you and provide a second opinion, should you wish. ■



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. Susan Cain describes the behaviour of introverts in the stock market as:
   - a) cautious, so unlikely to seize investment opportunities
   - b) homebodies unlikely to go consult financial advisors
   - c) avoiding risks, so likely to fare better than extroverts in bearish markets
   - d) not adventurous, so unlikely to invest diversely.
2. Heading into the second quarter of 2018, the global economy is still quite strong because:
   - a) growth rate + geographic breadth suggest durability
   - b) the risks of too much inflation seem low in the short term
   - c) U.S. tax cuts are positive for corporate earnings
   - d) all of the above.
3. The U.S. Smoot-Hawley Tariff Act of 1930 resulted in high tariffs, leading to:
   - a) a greatly strengthened U.S. economy
   - b) the Great Depression, according to economist Ed Yardeni
   - c) surprisingly minimal impact, both in the U.S. and abroad
   - d) a continuation of the prosperous 1920s.
4. If you become disabled and can't work, your most reliable back-up income will be from:
   - a) disability insurance
   - b) your group work plan
   - c) government benefits
   - d) friends and family who will lend you money.

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 May 31, 2018.

Trivia challenge runs April 25 - May 30, 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

CIBC Wood Gundy

The Stan Clark Financial Team
Where planning, investing and behavioral finance meet

Phone: (604) 641-4361 Toll free: 1 (800) 661-9442 Fax: (604) 608-5211 Email: StanClarkFinancialTeam@cibc.ca www.stanclark.ca

Stan Clark is an Investment Advisor with CIBC Wood Gundy in Vancouver, BC. The views of Stan Clark do not necessarily reflect those of CIBC World Markets Inc. This information, including any opinion, is based on various sources believed to be reliable, but its accuracy cannot be guaranteed and is subject to change. Clients are advised to seek advice regarding their particular circumstances from their personal tax and legal advisors. Insurance services are available through CIBC Wood Gundy Financial Services Inc. In Quebec, insurance services are available through CIBC Wood Gundy Financial Services (Quebec) Inc. If you are currently a CIBC Wood Gundy client, please contact your Investment Advisor. CIBC Wood Gundy is a division of CIBC World Markets Inc., a subsidiary of CIBC and a Member of the Canadian Investor Protection Fund and Investment Industry Regulatory Organization of Canada.