TD Wealth

Bayswater Group – Portfolio Update and Commentary (February 26, 2020)

OVERVIEW

We do not think this current bout of volatility will come as a surprise to any of our clients. As a rule, we have been very open about our concerns related to equity valuations, corporate and government debt levels, political unrest, and the like. Further, you may recall a note last year in which we identified these risks, and many others, as *known* unknowns and suggested that one must also brace for the impact of *unknown* unknowns. If you were at all confused at that time about the definition of an *unknown* unknown, you now have a tangible reference; that is, COVID-19.

While you may be prepared for volatility, we fully understand that it can be jarring to open your Facebook newsfeed and see that the stock market has dropped approximately 3%, 4%, or 5% on a given day. As always, we invite you to connect with one of us via email, phone, or in person if you have any questions about the current news cycle and its impact on your investment portfolio.

We are writing this note to remind you that we have been taking an increasingly defensive position in our portfolio for the better part of 18 months. We cannot guarantee our investment decisions will fully buoy stock market drawdowns, however, we are confident that our present allocation is capable of weathering the potential storms ahead.

We are also sending this note to let you know that we have been implementing some changes within the investment portfolio over the past few days. All of the trades were executed on Monday and Tuesday of this week; however, some of the securities bought and sold have multi-day settlement periods. With this in mind, it is likely that your online account summary will not properly reflect the changes until early next week. In the interim, various positions and account balances may seem distorted. Please know that the interruption is temporary.

Finally we are sending this note to update you on the current asset allocation of your investment portfolio. We appreciate that everyone's appetite for detail is different and are therefore breaking this note into two sections. For some, this initial overview may have answered any questions that may have been percolating over the past few days. If so, please do not feel obligated to press on further into the text. For everyone else, we hope the next section provides more colour to the narrative.

OUR CURRENT POSITIONING

Broadly, our existing asset allocation is remaining intact. While we are not strictly buy-and-hold investors, we do believe that most of the foundation needs to be in place before a significant market event occurs in order to effectively manage the risk is there.

We are conservatively positioned against traditional stock market risk. Notably, we only have approximately 35% long equity exposure. This allocation is divided between individual US and Canadian companies, as well as two core mutual funds whose managers we trust during volatile times because of their very long tenure, successful track record, disciplined process, and current investment thesis.

Our fixed income exposure is also conservative by traditional standards. It is invested mostly in short-dated, investment grade, corporate bonds and is supplemented with some US Treasury exposure and a small allocation to a credit opportunities fund. Overall, we have approximately 23% of the portfolio invested in fixed income securities. Again, the managers we are counting on have a proven track record through many market cycles. We are confident that their view on risk aligns with our own.

Notably, we have increased our allocation to gold bullion – now at approximately 11.25% in the portfolio. We view gold as a prudent hedge against short- to medium-term equity volatility as well as medium- to long-term currency devaluation. Structurally, traditional financial markets are increasingly dependent on a never-ending supply of new currency (*yes it apparently grows on trees*), which may or may not be sustainable. If it is sustainable, we think this supplementary gold position is more suitable than an additional fixed income allocation for investors with a medium- to long-time horizon; and, if it is not sustainable, we believe our investors will be grateful for the buoyancy gold can provide a portfolio during volatile times.

We have allocated a meaningful amount of money to several absolute return/alternative investment solutions. As we have discussed in most client meetings over the past 12-24 months, these managers are trying to generate positive returns regardless of the stock market's daily price moves. That is, they strive to take positions that either dampen traditional equity risk or are completely unrelated to it. While *past performance is no indication of future returns*, we are comfortable knowing that the managers in this cohort of the portfolio are among the most tenured in Canada and have consistently delivered for their investors during volatile periods.

Finally, we also have cash on hand that can be deployed if equity prices continue to decline.

Market volatility can be unsettling. We hope that this update and a peek under the hood will help to address any questions or concerns you may have. Please reach out to us if you wish to review your circumstances in more detail.

Bayswater
Group