TD Wealth

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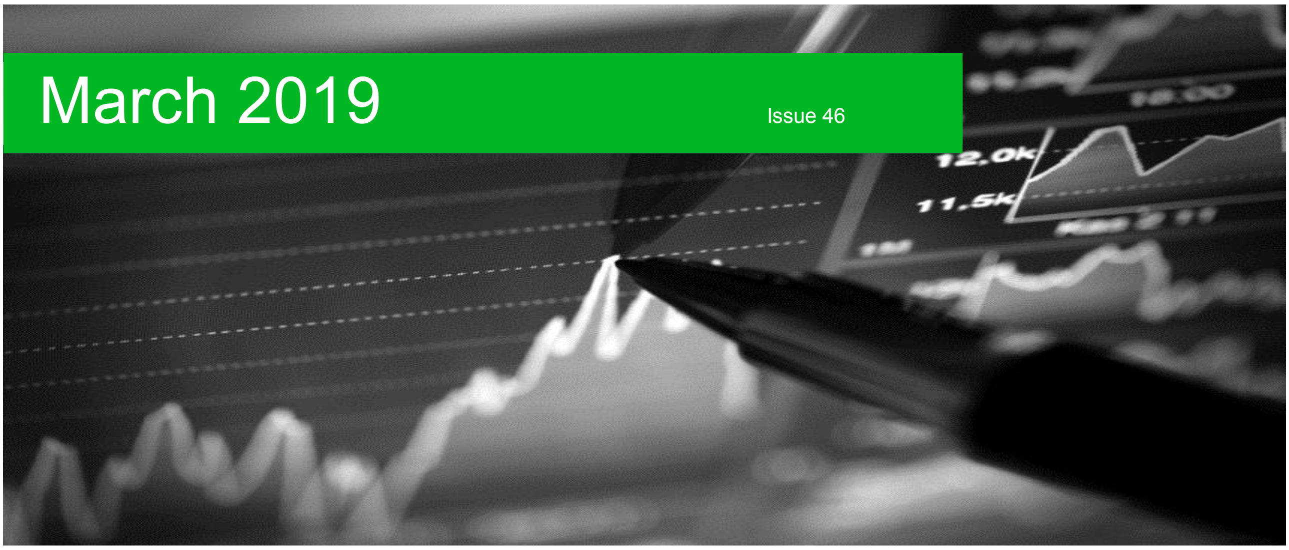

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Economic & Market Update

The Investment Advantage of Time

An old investment adage states: "Growth will bail you out, if you live long enough." This does not always hold true as investors who held shares in bygone era companies such as the United States Leather Company might attest.[1] But, for portfolios of investments, it generally holds true.

It is understandable that investors lose sight of this while battling the emotions related to market selloffs like we saw last year and back in 2008-09. There is a tendency to extrapolate recent negative returns and become concerned about a perpetuating trend.

Long-term investment horizons average out short-term fluctuations.

Short-term investment horizons can make an investor vulnerable to those fluctuations.

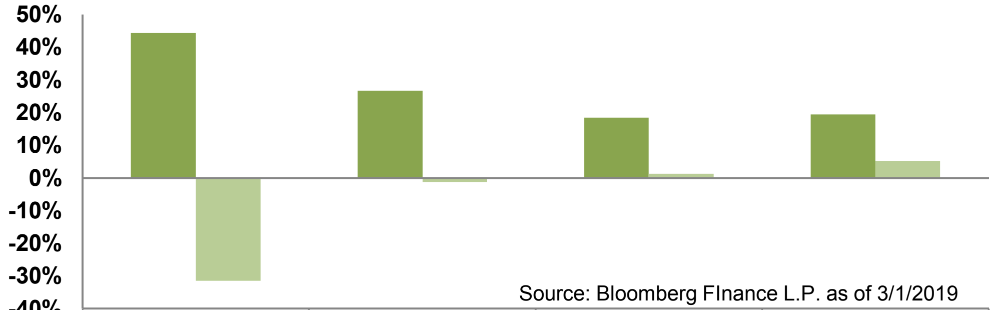
[1] The United States Leather Company was one of the original members of the Dow Jones Industrials Average when the index was first established in 1896. Because of the ubiquitous use of leather in industry and in finished goods at the turn of the last century, leather companies were prominent in that era. Not so much anymore, hence their general demise.

In the January 2019 edition of the *Monthly Letter* I wrote about how it is uncommon to see consecutive negative years in stock markets. Including dividends, we have not seen this since 2000-2002 for the Dow Jones Industrial Average, and 1973-1974 before that.[2]

Chart 1:

Rolling Period Total Returns* for the Dow Jones Industrial Average

*** From 1969 to 2018, Including Dividends, Returns are Annualized**

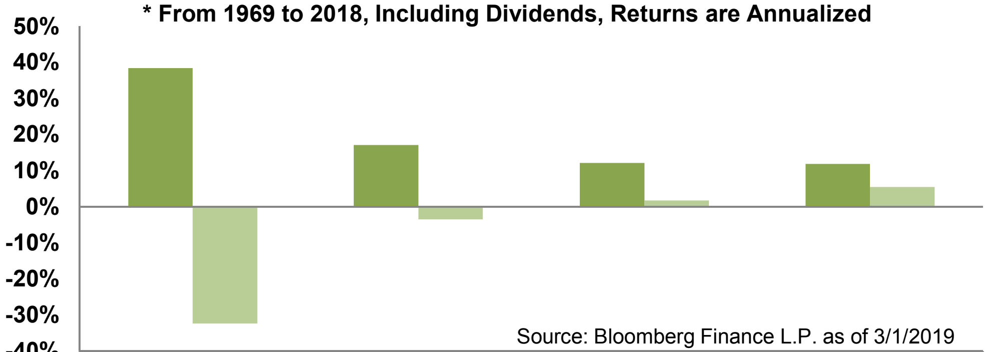


	1 Year	5 Years	10 Years	15 Years
Best	44.40%	26.82%	18.52%	19.46%
Worst	-31.46%	-1.18%	1.26%	5.35%

Chart 2:

Rolling Period Total Returns* for the S&P/TSX Composite

*** From 1969 to 2018, Including Dividends, Returns are Annualized**



	1 Year	5 Years	10 Years	15 Years
Best	38.41%	17.13%	12.15%	11.86%
Worst	-32.38%	-3.52%	1.69%	5.45%

Looking back at these return charts of stock market indices, any individual year can be negative. However, history has shown us that as time progresses, the odds of experiencing a positive return over a longer holding period improves (**Charts 1&2**). This is mostly due to the stock market index capturing the positive effects of economic growth. It is also capturing the impact of inflation, which does not add to *real* economic return, but makes things look better as it improves the nominal economic return.

The longer the holding period, the more tightly dispersed the results will be: less variability in the final annualized returns.

[2] Source: Bloomberg Finance L.P. as of 3/1/2019

If investors ignore 'The Advantage of Time', their emotions will likely be tested by the extremes over shorter holding periods. Some of these emotions might be euphoric as markets have shown a tendency to leap over short time frames. Alternatively, it could feel like the end of the world if the markets are suddenly down double-digits during a panic.

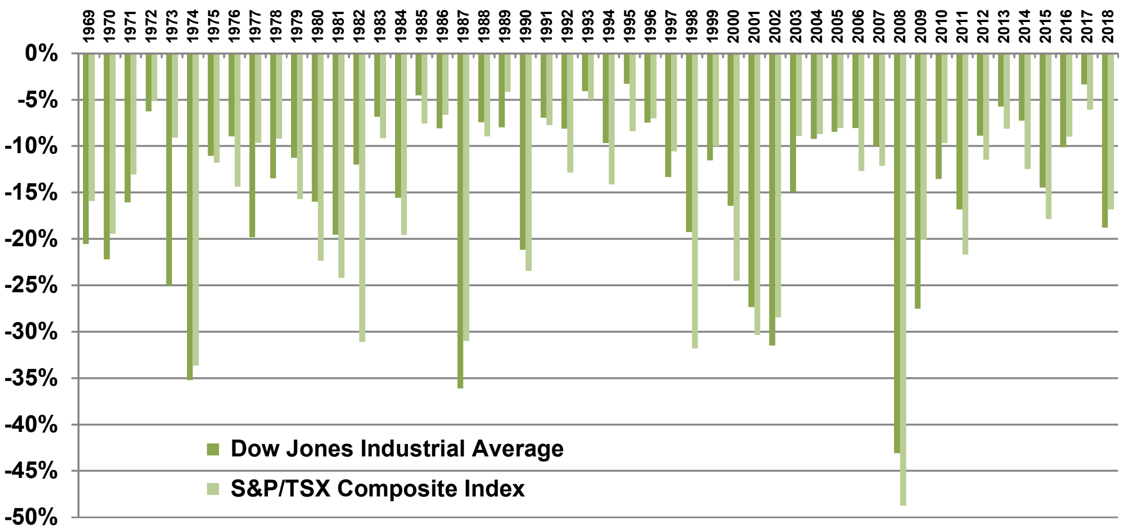
Chart 3 illustrates how frightening the short-term can be to an investor with a very limited horizon. Over a calendar year, all stock market indices will fall from an interim peak by a certain percentage. The only scenario that would avoid this would be if the indices rose every single day during the year. The average of the peak-to-trough decline during a calendar year over the last 50 years for the Dow Jones Industrial Average has been -14.48%.[3] For the S&P/TSX Composite Index it is -15.36%.[4] Significant selloffs are a normal thing in stock markets. However, despite that, over the last 50 years to the end of 2018, the Dow is up 2,664%, and an investor would have been up 14,796% if dividends were reinvested over this period.[5] The numbers for the S&P/TSX Composite Index (Canadian stocks) are less impressive, but still decidedly positive with the Index up 1,374%, and investors being up 2,684% if they kept reinvesting the dividends.[6]

A short-term focused investor will have to grapple with making a decision every time the market sells off.

Despite the longer-term impressive records of stock market indices, the short-term selloffs can still cause angst.

Chart 3:

Maximum Peak-to-Trough Declines Contained Within Calendar Years



Source: Bloomberg Finance L.P. as of 3/1/2019

[3] Source: Bloomberg Finance L.P. as of 3/1/2019.
[4] Ibid.
[5] Ibid.
[6] Ibid.

Markets are plagued with "short-termism" which is likely why the reactions of investors and the media tend to be more overly dramatic relative to what the historical evidence says about any selloff. This short-term focus is probably the result of a number of things including extremely low trading costs, an abundance of online market and securities data, and computerized trading. In the private markets, selling a company over and over is not common. If a private company changes hands once every five years, I would consider that to be rather often. However, in the publically-traded markets, five years is an eternity with respect to ownership turnover. **Table 1** illustrates just how quickly the entire shares outstanding for major company can fully turnover. The average holding period for Amazon, currently the third-largest company in the world with over $800 billion USD of market value, is 3.3 months! Essentially, investors in the market are implying that it ideal holding period for this massive company is about 100 days. So, if one's intent is to hold it for such a short period of time and then the markets start to selloff during that period, it is understandable that many of those types of investors will want to escape by selling the position.

Short-termism is very common as evidenced by the rapid turnover of the shares of in companies.

Trading behavior in the shares of Amazon imply that investors are concluding that the optimal time of ownership is about three months!

Table 1:

Turnover of All Outstanding Shares

Company	Months
Netflix Inc.	1.4
General Electric Co.	2.7
Amazon.com Inc.	3.3
Facebook Inc.	3.8
Apple Inc.	5.5
Alphabet Inc. 'C'	7.9
Canadian National Railway Co.	8.1
Microsoft Corp.	8.9
Royal Bank of Canada	10.7
Toronto-Dominion Bank	12.0
Bank of Montreal	14.1

This shows how short the average holding period is for these companies. Compare this to how long owners tend to keep things like private companies or real estate.

Source: Bloomberg Finance L.P. as of 3/1/2019. This is calculated by taking the average daily volume over the previous 30 trading days and dividing by the total number of shares outstanding.

Longer holding periods go a long way in mitigating the challenges and emotions involved with shorter-term fluctuations. So why are so many investors seduced by short-term trading? It might have to do with greed, over-confidence, insufficient knowledge of market history, or a multitude of other factors that make us human. The costs associated with embracing 'The Advantage of Time' are the uncomfortable feelings of remaining invested during tumultuous times. However, the costs of ignoring 'The Advantage of Time' may involve self-inflicted inferior returns and the uncomfortable feeling of regret.

We can often be our own worst enemy and miss out on the longer-term potential of markets when a short-term focus causes us to be emotionally impacted by short-term fluctuations.

Model Portfolio Update[7]

The Charter Group Balanced Portfolio
(A Pension-Style Portfolio)

	Target Allocation %	Change
Equities:		
Canadian Equities	15.0	None
U.S. Equities	35.7	None
International Equities	9.3	None
Fixed Income:		
Canadian Bonds	25.5	None
U.S. Bonds	2.5	None
Alternative Investments:		
Gold	7.5	None
Commodities & Agriculture	2.5	None
Cash	2.0	None

There were no changes to the individual holdings or the asset allocations in The Charter Group's portfolio models during February.

No portfolio changes during February.

Markets continued to charge ahead from their interim lows of late December. As the U.S. Federal Reserve and the Bank of Canada have become significantly more dovish with respect to suggesting that there will be a pause in the trend of rising interest rates, stocks in Canada, the US, and internationally responded with enthusiasm. The portfolio models were all benefactors of this.

Markets continued to move upward as interest rate fears seem to have abated, for now.

It appears investors are more comfortable in their expectations for stable interest rates over the next year. There might have to be news of further accelerating stock market gains or economic and wage gains for the central banks to start raining on the parade.

[7] The asset allocation represents the current *target* asset allocation of the Balanced Model Portfolio as of 3/1/2019. The asset allocations of individual clients invested in this Portfolio will differ because of the relative performance of the asset classes since the last rebalancing and because of differences in the timing of deposits and withdrawals. The Balanced Model Portfolio is part of a sequence of five portfolios ranging from conservative to aggressive: Conservative, Balanced Income, Balanced, Balanced Growth, and Growth.

Historically high levels of government spending in the US as well as higher levels of government spending in Canada could keep stocks elevated in the short- to medium-term. Federal elections are on the horizon for both countries which tends to suggest that austerity won't be a characteristic of government budgeting anytime soon.

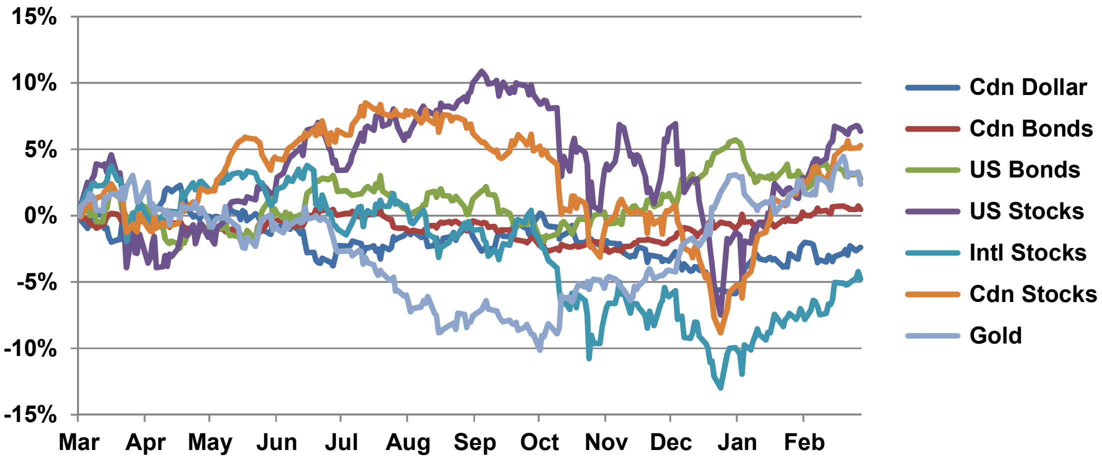
Current high levels of government spending in the US and Canada are stock market-friendly in the short- to medium-term.

There will likely be trade-related headlines continuing on for the next few months as President Donald Trump appears to have informally extended the tariff deadline with respect to China. To be clear, it is the story of interest rates that continue to dominate investment markets. However, there could be some week-to-week volatility as the prospects for a trade deal ebb and flow.

Trade war talk involving the US and China could cause some week-to-week volatility over the next few months.

Below is the 12-month performance of the asset classes that we have used in the construction of The Charter Group Balanced Portfolio (**Chart 4**).[8]

Chart 4:
12-Month Performance of the Asset Classes (in Canadian dollars)



Source: Bloomberg Finance L.P. from 3/1/2018 to 2/28/2019

[8] Bloomberg Finance L.P. – The Canadian dollar rate is the CAD/USD cross rate which is the amount of Canadian dollars per one US dollar; Canadian bonds are represented by the iShares Canadian Universe Bond Index (XBB); US bonds are represented by the iShares Core US Aggregate Bond Index (AGG); U.S. stocks are represented by the iShares Core S&P 500 Index (IVV); International stocks are represented by the iShares MSCI EAFE Index (EFA); Canadian stocks are represented by the iShares S&P/TSX 60 Index (XIU); Gold is represented by the iShares Gold Trust (IAU).

Top Investment Issues[9]

Issue	Importance	Potential Impact
1. China's Economic Growth	Significant	Negative
2. Canadian Dollar Decline	Moderate	Positive
3. U.S. Fiscal Spending Stimulus	Moderate	Positive
4. Long-term U.S. Interest Rates	Moderate	Negative
5. Global Trade Wars	Moderate	Negative
6. Massive Stimulus in China	Moderate	Positive
7. Short-term U.S. Interest Rates	Moderate	Negative
8. Canada's Economic Growth (Oil)	Medium	Negative
9. Stock Market Valuations	Light	Positive
10. East Asian / South Asian Geopolitics	Light	Negative

[9] This is a list of the issues that we currently deem to be the ten most important with respect to the potential impact on our model portfolios over the next 12 months. This is only a ranking of importance and potential impact and *not* an explicit forecast. The list is to illustrate where our attention is focused at the present time. If you would like an in-depth discussion as to the potential magnitude and direction of the issues potentially affecting the model portfolios, I encourage you to email me at mark.jasayko@td.com or call me directly on my mobile at 778-995-8872.

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The Charter Group is a wealth management team that specializes in discretionary investment management. For an annual fee, we manage model portfolios for private clients and institutions. All investment and asset allocation decisions for our model portfolios are made in our Langley, B.C. office. We do not outsource any of the decision-making for our model portfolios – there are no outside actively-managed products or funds. We strive to bring the best practices and the calibre of investment management normally seen in global financial centres directly to the Fraser Valley and are accountable for the results.

Accountability is further enhanced by the fact that we commit our own investable wealth to the same model portfolios in which our clients are invested.

The information contained herein is current as of March 1, 2019.

The Charter Group is part of TD Wealth Private Investment Advice, a division of TD Waterhouse Canada Inc. which is a subsidiary of The Toronto-Dominion Bank.

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