The Worry Free Financial Strategy

Over the last decade, stock markets around the world have presented a number of challenges for investors.

Some would argue that this is not new, and that there is always some event, whether it is political or economic, regionally or globally, that impacts stock markets both here in Canada and around the world. This has caused many investors to seek better ways to obtain returns on their money. During the same period, both markets and professional money management have evolved, resulting in newer, innovative strategies that have lead us as advisors to review our approach to money management.

First and foremost, we continue to believe in using well-diversified, professionally managed investments. Diversification, when done properly, is the one "free lunch" in investing. For the core component of most portfolios, what does not work, in our view, is stock picking. Taking a risk on a specific company or industry is a risk that investors do not get paid to take. No matter how attractive a stock may appear, in large liquid markets this attractiveness (or lack of same) is already reflected in that stock's current price.

Comments from Daniel H. Kahneman, Professor of Psychology, Princeton University, and Nobel laureate, 2002, best exemplify this position. "The idea that any single individual without extra information or extra market power can beat the market is extraordinarily unlikely. Yet the market is full of people who think they can do it and full of other people who believe them." He goes on to state, "This is one of the greatest mysteries of finance: Why do people believe they can do the impossible? And why do other people believe them?" (Dow Jones "Asset Management", Nov/Dec 1998).

Invest. Don't speculate

Over time, very few professional money managers (i.e. "active" managers or stock pickers) outperform the market, net of fees. Moreover, only a fraction of active managers survive over the medium to long term. For the 5 years ending December 31, 2012, only 70.49% of the Canadian Equity Funds that existed in 2007 were still operating, and less than 10% had outperformed the S&P/TSX Composite Total Return index (source: SPIVA Canada Scorecard, 2013). The "survival rate" of US Equity Funds in the USA was the same, 70%, with only a 25% "success rate" of beating the index (CRSP Mutual Fund Database, the Center forResearch in Security Prices, University of Chicago, 2013).

What is even more of concern is that of the "winning" funds in the USA – those that did actually outperform their corresponding benchmark over 5 and 10-year periods ending in 2009 – only 26.1% and 23.6%respectively continued to "win"!

Let markets work for you

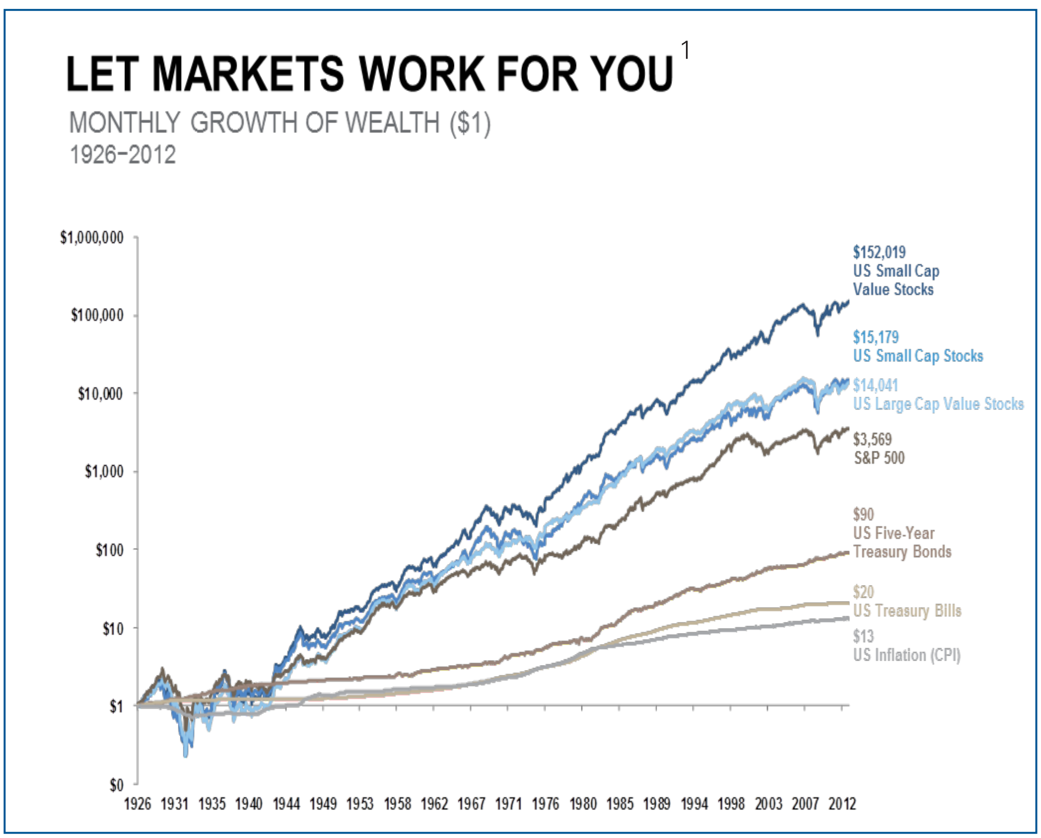
While the day to day gyrations of stock markets appear to be based more on emotion than logic, they are still the best way to determine the 'fair' value of a company. A share price is the result of thousands or millions of buyers and sellers coming together and buying and selling. To say that a stock is 'mispriced' and'overvalued' is to ascribe to the commentator the ability to perceive value where thousands have supposedlyfailed. Markets move in response to new information, and there is no shortage of that on any given day.Markets reward capital suppliers over time, consistent with the risks taken by market participants.

Pay attention to those factors that can be controlled

Since we cannot control nor predict markets, then what strategies can we employ to enhance investment performance? We at Polson Bourbonniere Financial Planning Group Inc. have identified four key factors that form the basis for our investment approach: i) Asset Mix, ii) Fees, iii) Transaction frequency (or investor behavior), and iv) Taxes. Let's examine each of these in more detail.

i) Asset mix

Studies have shown that asset "mix", i.e. how your investments are allocated among the various asset "classes" (stocks, bonds, cash, real estate, etc.), is responsible for the majority of the performance of a portfolio. Because from year to year



Source: Dimensional Fund Advisors, February 2013 there is little predictability in how markets will perform, as well as which asset classes will actually outperform, broad diversification in a blend of assets according to your personal tolerance for risk – or "asset allocation" as we call it – is critical to both long term performance and controlling short-term volatility. The higher the risk of a given portfolio, the higher the expected return and higher expected volatility.

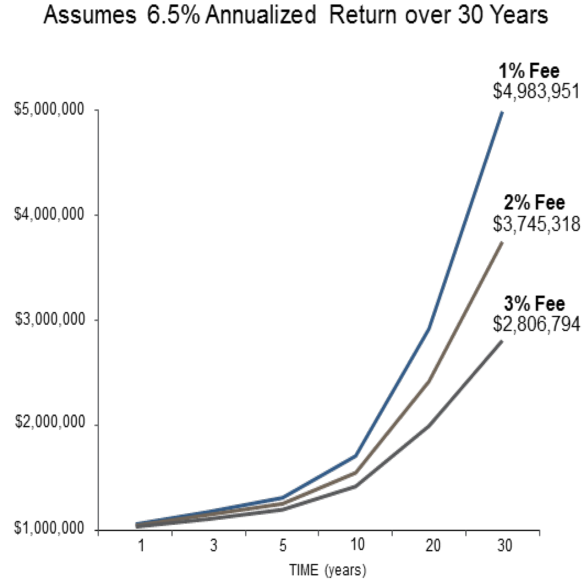
KEEP COSTS LOW[3]

NET GROWTH OF $1 MILLION

Over long time periods, high costs can drag down wealth accumulation in a portfolio.

Costs to consider include:

• Management fees
• Fund expenses
• Taxes



Source: Dimensional Fund Advisors, February 2013

A strategic approach to building a portfolio prevents short term reactions to unforeseeable market events. And, it's not enough to simply diversify by security. Deeper diversification also involves geographic diversification. Holding a global portfolio can assist in reducing risk and increasing expected returns.

ii) Fees

Fees matter. For a given level of index-like returns, a high fee investment will underperform a low fee one. Over longer periods, high costs can drag down wealth accumulation in a portfolio. Investment "costs" can include:

• management fees
ccommissions
• fund expenses
• taxes
• trading costs

Much debate has taken place over the years centering on the ability of a higher fee, "active" money manager to consistently generate superior returns after fees, versus a lower cost "passive" or index-type portfolio. As discussed earlier in this article, research has generally proven otherwise. Those "active" managers who fall into the small group who are successful and continue to "win", generally hold assets that vary significantly from the benchmark index. And, because of that, their strategies can have a place in an investor's portfolio.

iii) Transaction frequency

Having a plan and adhering to it allows investors to avoid common mistakes such as trying to time purchases, chasing hot stocks or funds, over-concentrating in certain markets, taking excessive risk, and trying to forecast winners. The television, print, and online financial media are in the business of entertainment, and their emphasis is often on short-term, sensational, and emotionally-charged headlines. These messages can lead investors to compromise their long-term focus and discipline, and often lead to poor investment decisions. We advocate a personalized investment strategy that allows you to be worry-free.

iv) Taxes

Investors in Canada face a range of income tax rates on investment returns from zero (Tax Free Savings Accounts) to over 50% (income subject to the Old Age Security clawback tax at the higher levels). In addition, the timing of a tax will alter its impact. A 50% tax deferred to age 75 might be less damaging than a 46% tax payable at age 50. Significant investment returns eroded by excessive tax are as corrosive as poor investment performance alone. Tax efficiency is an important component of investment success.

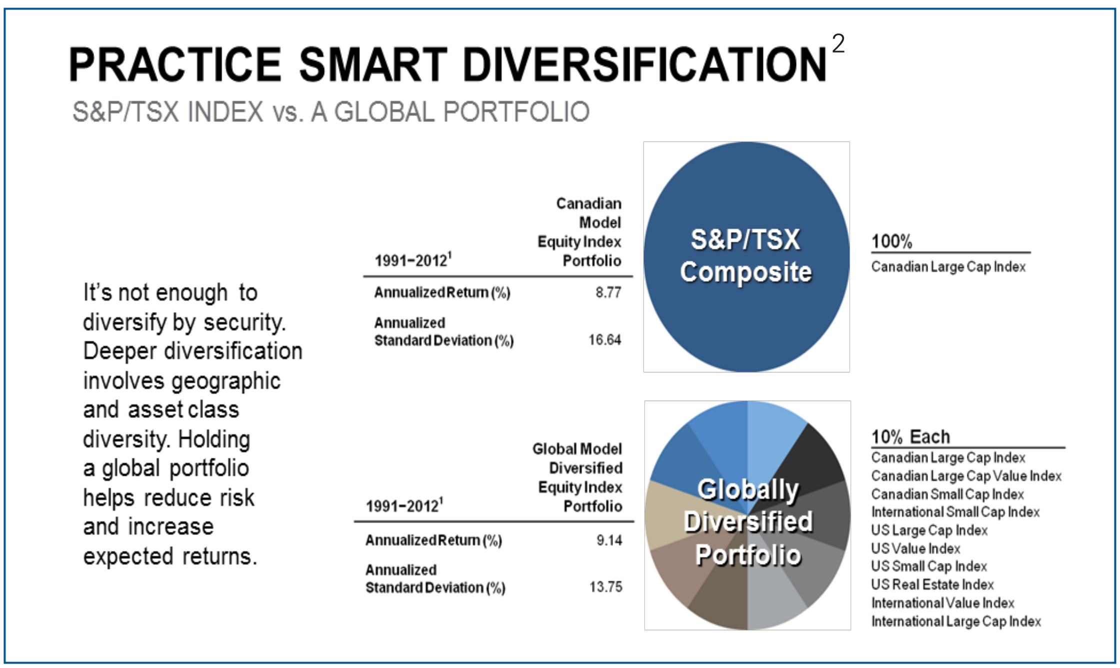
Canada Revenue Agency
www.cra.gc.ca

Core and explore

While we can expect a diversified, low tax, low fee Core portfolio to capture market returns over time, conditions or investor needs and preferences of a more short term nature may prompt us to consider other tactical strategies. For example, we may recommend dividend paying stocks to satisfy a desire for yield during a period of low interest rates. Or we may find gold attractive as a store of wealth during a period of high government debt. To deal with these types of issues, we may rebalance a portion of a portfolio to include 'Explore' investments.

The role of active management

In a low yield, low growth global economic environment, it is not surprising that fees charged by investment managers are undergoing increased scrutiny. At Polson Bourbonniere we have always focused on the net returns, the returns our clients actually get to keep. If an active manager has been able to either control volatility, deliver returns in excess of the market, or deliver a steady stream of income over time, then we feel that the higher fee has been worth it. We make the decision to hire an active manager when it addresses a client's financial goals, and when it can be accommodated within an agreed upon fee budget.



Source: Dimensional Fund Advisors, February 2013

The role of advice

We believe that financial independence is the combination of a successful investment strategy and a well thought out financial plan.

The value of advice

Much has been written in the financial press regarding the value of advice that Canadians receive from "financial advisors" and how that ties in with remuneration received – whether fees or commissions, or a combination of the two. Regulations are on the way that will require "transparency" - disclosure of fees or commissions that are currently embedded in financial products whether they be bonds, mutual funds, Exchange-Traded Funds (ETFs), limited partnerships, or others. This can only be a good thing for consumers, but it also has to be stacked up against value received from your advisor.

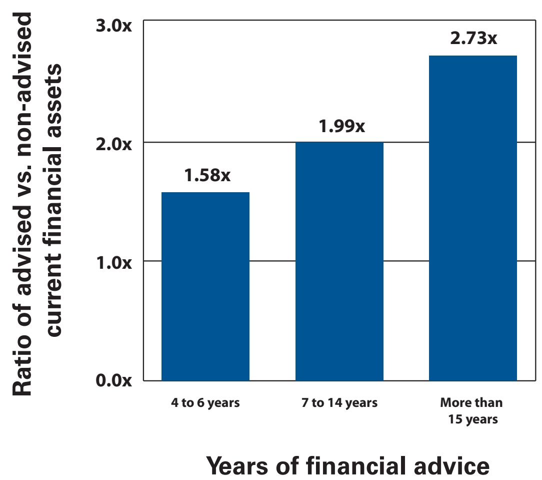
The durable value of advice is being confirmed in more and more research studies here in Canada and internationally.

Research reports released by IFIC (Investment Fund Institute of Canada) demonstrate that:

- Advised households have substantially higher investible assets than non-advised households, regardless of household income level.
- Advisors help individuals choose the right vehicles and plans to optimize outcomes for their own unique circumstances.
- Advisors help investors choose the right asset mix for their specific circumstances, objectives and risk tolerance.

The CIRANO (Centre for Interuniversity Research and Analysis on Organizations) Institute developed the largest and most extensive database in Canada in order to research the value of financial advice. A host of socio-economic, demographic and attitudinal information was collected from each respondent so that asset levels could be compared amongst effectively identical households.

Financial Asset Growth



IFIC - The Value of Advice Report, 2012

The researchers drew four main conclusions:

- Advice has a positive and significant impact on financial assets. The study reveals that the presence of a financial advisor contributes positively and significantly to the level of assets when the impact of all other variables is factored out. The impact on the level of assets is more pronounced the longer the tenure of the advice relationship.
- Advice positively impacts retirement readiness, even after factoring out the impact of a myriad of other variables. The researchers show that having a financial advisor increases the probability of a respondent declaring confidence in achieving a comfortable retirement.

The positive effect of advice on wealth accumulation cannot be explained by asset performance alone; the greater savings discipline acquired through advice plays an important role. The paper finds that advised households save at twice the rate of non-advised households.

Having advice is an important contributor to levels of trust, satisfaction and confidence in financial advisors – a strong indicator of value. An advised respondent has a 32% higher probability of declaring trust in financial advisors than a similar non-advised respondent.

Savings rates for Advised, Non-Advised, and Traders	
Advised	8.6%
Passive Non-Advised (excluding Traders)	4.3%
Traders	10.4%

Research from KPMG Econtech in Australia demonstrates that the provision of financial advice leads to improved savings behavior.

The study finds that those with a financial advisor save more than those without a financial advisor.

In *"The Value of Seeking Financial Advice",* a paper released by Marsden et al, a number of statistically significant relationships were revealed. These suggest that meeting with a financial advisor encourages individuals to engage in more prudent retirement planning activities.

Goal-related planning activities: Those with a financial advisor are more likely to have established long-term goals and to report that they had calculated their financial needs in retirement.

Plan implementation outcomes: Those with an advisor are more likely to have a supplemental savings account and to have more asset classes across all of their accounts.

Long-term financial outcomes: Those with a financial advisor report greater retirement confidence and significantly higher levels of emergency funds.

Winchesrer et al, in "*The Role of Financial Advice During Market Downturns*", examines whether investors with financial advisors are more likely to maintain long-term investment objectives during poor market conditions than those who do not receive advice. The researchers conclude the following:

An individual with a written customized financial plan is almost twice as likely to rebalance appropriately during a bear market than an investor with no written plan.

Investors who purchase financial advice are more than one-and-a-half times more likely to maintain a long-term investment strategy compared to investors who do not purchase financial advice.

We believe that as Certified Financial Planner (CFP)® professionals we play a number of important roles First, we help you simplify your life. We listen and connect with you, and design an investment or retirement plan that meets your goals, without needless complexity. By focusing on the bigger picture, your wants and desires -- when you want to retire, how much income you'll need, planning your estate -- we design portfolios that complete your objectives.

As discussed previously, we prevent you from bad investment behaviour – buying and selling at the wrong time, or relying on economic forecasts for your investment decisions. Studies have shown that there is a gap between the rate of return earned by investors and the returns actually earned by mutual funds. The average investor's returns lag the returns on mutual funds themselves. In fact, in a US research study, Morningstar Inc. confirmed that from 2003 to 2013, the average annual "return gap" for domestic stock funds was 1%, and 3.1% for international stock funds.

Why? Investors trying to time the market more often end up buying and selling at the wrong time. Better to figure out where you are today and where you want to end up. Then buy well-diversified investments with attention to cost, and be invested for the long term.

What difference does a CFP® professional make?

Consider the results of a study by FPSC.

- Canadians who work with a CFP® professional are more likely to report that their financial affairs are on track than those dealing with non-certified planners (78% vs. 54%).
- More Canadians who are using a CFP® professional believe that financial planning has helped them have greater peace of mind than those working with a non-certified planner (73% vs 63%).
- More Canadians who engage a CFP® professional believe they are closer to achieving some of their life goals as a result of planning than those working with non-certified planners (70% vs 61%).
- Canadians spend 36% more time with their CFP® professional than those working with a non-certified professional – and they also have longer term relationships with their CFP® professional.

At Polson Bourbonniere Financial Planning Group Inc. we pride ourselves on being CFP® professionals. We provide a range of services that help you stay on track with your financial affairs, on track to save, on track to retire, while at the same time dealing with the bumps in life, and living for today. What we do provides our clients with a strong sense of financial and emotional well-being.

Comprehensive financial planning, retirement income planning, insurance planing and estate planning are all available to you through your CFP® professional here. Let us demonstrate the value of our advice to you by taking advantage of these services.

1. In CAD.

All returns in USD except Canadian Market Stocks. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. US value and growth Research index data provided by Fama/French. Canadian index data provided by Fama/French. The S&P data are provided by Standard & Poor's Index Services Group. CRSP data provided by the Center for Research in Security Prices, University of Chicago. International Value data provided by Fama/French from Bloomberg and MSCI securities data. International Small data compiled by Dimensional from Bloomberg, Style Research, London Business School, and Nomura Securities data. MSCI World ex USA Index is gross of foreign withholding taxes on dividends; copyright MSCI 2013, all rights reserved. Emerging Markets index data simulated by Fama/French from countries in the IFC Investable Universe; simulations are free-float weighted both within each country and across all countries. Asset class filters were applied to data retroactively, rebalanced annually, and with the benefit of hindsight. Asset class returns are not representative of indices or actual portfolios and do not reflect costs and fees associated with an actual investment. Actual returns may be lower.

[2] For illustrative purposes only. In Canadian dollars.

Canadian Large Cap is the S&P/TSX Composite Index. Canadian Value is the MSCI Canada IMI Value Index (gross dividends) for June 1998-present, and Barra Canada Value Index for January 1982-May 1998. Canadian Small Cap is the MSCI Canada Small Index (gross dividends) for January 1999-present, and Barra Canadian Small Cap Index for July 1990-December 1998. US Large Cap is the S&P 500 Index. International Value is the MSCI EAFE Value Index (net dividends), and International Large Cap is the MSCI EAFE Index (net dividends). International Small is: 1970-June 1981, 50% UK small cap stocks provided by the London Business School and 50% Japan small cap stocks provided by Nomura Securities; July 1981-present, compiled by Dimensional from StyleResearch securities data; includes securities of MSCI EAFE Index countries, market-capitalization weighted, each country capped at 50%. US Value is the Russell 3000 Value Index. US Small Cap is the CRSP 6-10 Index. US Real Estate is the Dow Jones US Select REIT Index. S&P/TSX data provided by S&P/TSX. Barra data provided by MSCI Barra. S&P data provided by Standard & Poor's Index Services Group. MSCI data copyright MSCI 2011, all rights reserved. Russell data copyright © Russell Investment Group 1995-2011, all rights reserved. CRSP data provided by the Center for Research in Security Prices, University of Chicago. Dow Jones US Select data provided by Dow Jones Indexes. Standard deviation is a statistical measure of risk. Generally speaking, the higher the standard deviation, the greater the risk.

1. Date range selected is the longest common time series of whole years of data available. Rebalanced quarterly.

Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. Not to be construed as investment advice. Returns of model portfolios are based on back-tested model allocation mixes designed with the benefit of hindsight and do not represent actual investment performance.

[3] In US dollars. For illustrative purposes only.

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Sources:

"The Financial Planning Standards Council (FPSC)" in partnership with the FPSC Foundation. Visit www.fpsc.ca for more information on this study.

"Econometric Models on the Value of Advice of a Financial Advisor", Professors Claude Montmarquette and Nathalie Viennot-Briot, Centre for Interuniversity Research and Analysis on Organizations (CIRANO).

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2013 Morningstar Investment Conference, Carl Richards.

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There are enough things in life to worry about.
Money shouldn't be one of them.
Let us show you how.™

Polson Bourbonniere Financial
HollisWealth

7050 Woodbine Ave., Suite 100
Markham, Ontario L3R 4G8
Main: 416.498.6181 or 905.413.7700
Fax: 905.305.0885
Toll Free: 1.800.263.0120
Website: www.worryfreeretirement.com

Ruth Ashton, CFP®
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 905.413.7710
Email: rashton@pbfinancial.com

Paul Bourbonniere, CFP®, CLU, CH.F.C.
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 416.498.6181
Email: pbourbonniere@pbfinancial.com

Lydia Bzowej, BA, CFP®, EPC
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 905.413.7703
Email: lbzowej@pbfinancial.com

Michael Derby, CIM®
Investment and Insurance Advisor
Direct: 905.413.7726
Email: mderby@pbfinancial.com

Allan Kalin, CFP®
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 905.413.7706
Email: akalin@pbfinancial.com

Derek Polson, CFP®
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 905.413.7709
Email: dpolson@pbfinancial.com

Kirk Polson, CFP®, CLU, CH.F.C.
Certified Financial Planner®
Investment and Insurance Advisor
Direct: 416.498.6181
Email: kpolson@pbfinancial.com

Office Hours
Monday to Friday,
8:30 a.m. – 5:00 p.m.

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