

ODLUM BROWN REPORT

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ODLUM BROWN
Investing for Generations®

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An Unexpected Pandemic Silver Lining

Who knew a global pandemic would be good for your portfolio? Despite the turbulence caused by economic lockdowns, and the inflationary pressures unleashed upon reopening, asset prices have soared. The broadly based U.S. S&P 500 Index is almost one-third higher than its pre-pandemic peak. The recovery in Canadian stocks has been impressive, too, although our main benchmark index is up a lesser 13% from its pre-crisis record.

Not only did the extraordinary efforts of governments and central banks save the world from a deep and ugly recession, but their actions also greatly enhanced asset values. Aside from enormous government aid that directly supported the economy, asset valuations have been buoyed by two monetary policy levers: (1) ultra-low interest rates, which influenced prices like helium in a balloon; and (2) a huge increase in the money supply, which fuelled asset appreciation by creating demand for stocks, real estate and other assets.

We're impressed and surprised by the speed and strength of the economic and stock market recoveries. According to the National Bureau of Economic Research, the official arbiters of U.S. recessions, the latest economic setback was the shortest on record. The recession was only two months long, bottoming in April 2020 after starting the month prior when the world locked down. The Great Recession that coincided with the 2008/09 Financial Crisis lasted a year and a half, and it took the S&P 500 Index more than five years to regain its prior peak.

Prior to the pandemic, we were cautious regarding the outlook for several reasons. The economic expansion was already one of the longest on record; stocks were expensive, and we worried about the authorities' ability to manage the next recession. The latter point was of most concern.

At the time, interest rates were negative in Japan and much of Europe, and very low in the rest of the developed world. With limited scope to lower interest rates further, we feared monetary policy would be much less effective at reviving the global economy during the next inevitable downturn. We reasoned that fiscal policy would need to play a much greater role, and we were sceptical regarding that possibility given the level of social unrest and political polarization.

The pandemic rendered these worries moot. The crisis was so monumental that there was broad support for a "whatever it takes" approach to save the economy, using multiple and coordinated fiscal and monetary policy levers. Indeed, the size and scope of the support and stimulus were unprecedented.

Most importantly, the crisis has likely ushered in a new era of coordinated fiscal and monetary policy. While we have long-term concerns about large government deficits being financed by central banks, the near-term benefit is that governments are better able to manage economic inequality via fiscal policy than central banks can through monetary policy.

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Odlum Brown Joins BC Wildfire Recovery Efforts

As a proudly BC-based firm since 1923, we care deeply about this province and supporting the communities where our clients and team members live and work.

Odlum Brown has donated \$25,000 to United Way BC's United for BC Wildfire Recovery Fund. The United for BC Wildfire Recovery Fund raises funds to address important social needs like finding permanent housing, food assistance, trauma and mental health supports, and rebuilding social infrastructure. Learn more at uwbc.ca/wildfires.

We are also pleased to sponsor DAREarts Creativity Kits for Lytton, an emergency relief initiative which will provide curated arts kits to children and youth displaced by the Lytton wildfire. The Creativity Kits are designed to support young people in caring for their mental wellness through arts-based expression during this difficult time. This fall, Odlum Brown team members will assemble 200 kits to be delivered to BC communities. Learn more at darearts.com.

Our thoughts are with those impacted by the wildfires, and we wish all of our fellow British Columbians a safe rest of the summer.

The social unrest that stems from economic inequality has long been our biggest concern. The lower and lower interest rates central banks have fostered in recent decades have benefited the wealthy, who disproportionately own the assets that get inflated. Now that there is mainstream support for greater government-led fiscal initiatives, financed by central banks, there is much larger scope to deal with this inequality. It's a massive and difficult job, and governments will likely make errors at times, but there are policy possibilities on the table now that seemed unreachable before. That's a big silver lining from the pandemic, and perhaps it's a reason why investors are more confident about the future.

We are certainly grateful that the authorities unleashed a firehose of support for individuals, businesses and governments. They did the right thing. However, we do wonder if they should be dialing back some of the stimulus now that the economy is back on its feet and inflationary pressures are evident.

Central bank leaders argue that the recent surge in prices is a transitory phenomenon and that inflationary pressures will abate as businesses work through temporary supply bottlenecks. Interestingly, bond investors seem to agree with this benign outlook for inflation. After all, the yield on the 10-year U.S. Treasury bond recently dropped to 1.25% from 1.75% in March. One would expect bond yields to rise in the face of higher inflation, not fall.

We hope the authorities and bond investors are right. If they are wrong, and inflation is persistently higher, interest rates will probably rise, which could put downward pressure on asset valuation multiples.

Some believe stocks are already overpriced. Indeed, valuation multiples are near the high end of their historical range, but they are arguably justified by the fact that interest rates are well below average. Stocks can probably handle a modest increase in interest rates.

The challenge in the market today is finding stocks with a good margin of safety – a valuation that is discounted enough to limit downside risk and provide decent upside potential. In our view, most stocks are priced fairly relative to interest rates and to each other. In other words, there isn't a lot of low-hanging fruit.

Given the forgoing predicament, it's fair to wonder if it's a good time to take profits on stocks. Unfortunately, there isn't an easy answer to that

question because the alternative investments have risks as well.

Bonds will do well and provide a ballast for investment portfolios if the economic recovery falters and interest rates go down. However, they will drop in price if interest rates rise in the face of persistent economic growth and inflationary pressures. Cash or short-term money market funds are not great alternatives either in an ultra-low interest rate world because the income from these instruments is insufficient to cover inflation. Wealth erodes from a purchasing power perspective when it's invested in low-yielding fixed-income instruments.

It's sometimes tempting to take money out of the stock market with the hopes of redeploying it after a correction or a crash, but we have long counselled against this approach, as it's very difficult to successfully execute over an investing lifetime. Getting the timing right on both the sell and buy decisions is extremely difficult. In fact, we were recently humbled on this front. Having cash, gold and a generally defensive posture helped cushion the blow to the Odlum Brown Model Portfolio¹ when stocks plummeted as COVID-19 spread and the world locked down. But our performance lagged in the early part of the recovery because we didn't reinvest quickly enough. Stocks started pricing in the recovery much faster than we expected.

We are currently fully invested within our all-equity Model because we feel stocks are still attractive relative to the alternatives, even though long-term return prospects are muted by elevated valuations. Still, cash and bonds have a place in the overall asset mix, as one can rely on them to lower portfolio volatility and provide reliable funds, if needed. Quality, diversification and balance remain paramount.



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¹ The Odlum Brown Model Portfolio is an all-equity portfolio that was established by the Odlum Brown Equity Research Department on December 15, 1994, with a hypothetical investment of \$250,000. It showcases how we believe individual security recommendations may be used within the context of a client portfolio. The Model also provides a basis with which to measure the quality of our advice and the effectiveness of our disciplined investment strategy. Trades are made using the closing price on the day a change is announced. Performance figures do not include any allowance for fees. Past performance is not indicative of future performance.

Understanding Your Life Insurance Options

There are many different reasons to purchase life insurance. For example, to:

- Provide financial security for dependents by replacing income lost due to the death of a family member.
- Cover the debts owed or shared by the insured, such as mortgages and other loans.
- Pay final expenses and legal costs upon settling an estate.
- Cover final taxes payable on capital gains arising on various assets, including non-registered investments, vacation and rental properties, and taxes on the deemed disposition of registered retirement accounts.
- Balance or equalize distributions between beneficiaries.
- Preserve or enhance your estate for future generations, or fund charitable bequests.



What is the best type of coverage to purchase?

There are two main types of coverage: **term life insurance** and **permanent life insurance**.

Term insurance is initially more affordable and can be automatically renewed at guaranteed rates, without additional medical questions, but coverage typically ends by around age 80 with premiums becoming much higher at each renewal.

Permanent life insurance is intended to stay in place until the death of the person(s) insured.

In deciding on the type and amount of coverage that is right for you and your family, you will want to consider variables including your age, health, budget, existing coverage and obligations, as well as your short and long-term goals.

Who should consider term life insurance?

This type of coverage is often well suited to individuals or young families when:

- More coverage is needed now at the most affordable price.
- The insurable need is expected to diminish over time. For example, after 10, 15 or 25 years, or once a mortgage, business loan or other debt is repaid.
- The term policy's conversion options to permanent insurance (at a higher rate) would be adequate, if a more enduring need for insurance develops.

Since term insurance becomes increasingly expensive at pre-set term renewal dates, using some permanent life insurance may be more appropriate to meet certain objectives, as described below.

Who should consider permanent life insurance?

This type of coverage can be for any permanent need, such as for individuals or families who:

- Want to have the security of lifetime coverage without escalating premium costs.
- Plan to make intergenerational wealth transfers or charitable bequests, or to equalize their distribution of family or business assets.
- Plan to maximize initial income from pensions or retirement plans, using insurance to meet the needs of surviving family members.
- Want to have funds available for final expenses, probate and income taxes.
- Want the flexibility to increase their policy cash value and coverage amount through deposits that can be invested and tax-sheltered.

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SCIENCE WORLD

New! Odlum Brown
Partners with Science
World

Odlum Brown is proud to announce a new long-term partnership with Science World, a not-for-profit, family-friendly science centre based in Vancouver, BC.

Through 2024, we will be the Presenting Sponsor of the all-new **Online Environmental Education Program**. This accessible program, launching this fall, is designed to bring nature-focused education to learners and their families across BC.

We are also pleased to sponsor **Backyard Adventures, Science World's Feature Exhibit for Fall 2021**. Running from September 29 – January 14, **Backyard Adventures** will stimulate curiosity about the science that exists right in our own backyards, and emphasize the benefits of staying healthy and active outdoors.

For more information on these exciting initiatives, visit scienceworld.ca.

Under the umbrella of permanent life insurance, there are plans available for a wide range of insurance uses. Although product names vary, they generally fall into these two main types: whole life and universal life.

A few key commonalities and differences between these policy types follow:

	Whole life	Universal life
Policy components	Typically consist of two policy components: insurance and investment (cash) values .	
Policy funding	<p>Premiums and deposits can be level for your lifetime or for a specific period of time (e.g., 10 or 20 years).</p> <p>The insurance company determines required monthly premiums.</p> <p>Many plans also allow for additional deposits (within policy limits) to increase coverage and values over time.</p>	<p>The insurance company determines the minimum premium amount to cover the cost of insurance.</p> <p>The policy owner determines (within policy limits) any excess deposits they wish to invest within the policy.</p>
Underlying investments	The insurance company determines and manages how premiums, including any additional deposits, are invested.	The policy owner chooses how to allocate extra deposits to tax-sheltered investment options (within policy limits).
Policy dividends, returns and values	The insurance company distributes policy dividends , which the policy owner can direct to increase coverage, increase cash values, reduce annual premiums or a combination of the above.	<p>Policy values depend on deposits made and returns achieved.</p> <p>Investment returns can be used to pay premiums. Excess deposits and returns may also increase the cash values and the death benefit.</p>
Access to cash values	Cash values can increase over time and be accessed by way of loans or withdrawals (conditions and taxes may apply).	
Features and options	Many plans offer features and options to safeguard the coverage purchased and guarantee future values.	

When it comes to life insurance, there is no one-size-fits-all solution. To better understand your risks, clarify your objectives and explore which options best fit your needs, we invite you to consult with one of our Odium Brown Financial Services Limited (OBFSL) insurance professionals, accessible through your Odium Brown Investment Advisor or Portfolio Manager. As your needs or objectives change, we will be here to serve you and your family, for generations.



RITA AGER, CFP, CLU, CHS, CPCA, FEA
 Insurance Specialist
 Odium Brown Financial Services Limited

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