IN FOCUS

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Independent Accountants' Investment Counsel Inc.™

The Quarterly Commentary

Is an economic recession coming? No one is sure. Some signs point to "yes" while others suggest "no" or at least "not yet." But given the possibility of a recession, how do we manage our clients' investments? In this article we examine current economic indicators of where the economy may be heading and conclude with our thoughts on how we manage investments in the face of such uncertainty.

The differences in the characteristics of past economic cycles and the importance of human psychology on economic activity make forecasting a recession a challenging proposition. Let's take a look at some of the economic data.

The third quarter of 2019 saw the current economic expansion in the U.S. extend into its 11th year, somewhat paradoxically fueling fears that the dreaded "R word" – recession – is just around the corner. Economies are cyclical in nature with periods of expansion that lead to relative peaks, followed by slowing growth or even contraction. A recession is defined as two quarters of back-to-back economic contraction. Recession fears were further reinforced this past quarter by an inversion of the yield curve (i.e. when the interest rate of a 10-year U.S. government bond is less than the rate of a two-year treasury bill). Persistent yield-curve inversion has been closely correlated with past recessions, but has proven to be an unreliable tool for forecasting when the actual onset of a recession will occur.

Slowing global growth points to the increased probability of economic contraction. The Eurozone and China, which are the two areas in the world other than the U.S. that influence global economic output in a significant way, both face major challenges.

Slowing growth in the Eurozone has been led by contraction in Germany in the second quarter, with further contraction forecasted for 2020. This contraction may be offset by France and Spain, which are faring somewhat better. Still, growth in the Eurozone is expected to be less than 1% in 2020. The imminent departure of the UK from the European Union adds a wild card to the equation but certainly cannot be expected to impact growth positively.

China's issues have been a little less apparent as weakening industry and manufacturing growth has been offset by continued internal expansion through property development. Recent data, though, shows that even its domestic growth rate has slowed. China is also dealing with pending political issues as it formulates a response to growing pro-democracy demonstrations in Hong Kong.

With the Eurozone and Chinese economies struggling and in the midst of trade uncertainties between the US and China, it is not surprising that U.S. manufacturing output shrunk over the last two quarters. And in the wake of trade tensions, there is concern that the services sector, which makes up one third of U.S. exports and approximately 1% of GDP, is showing some weakness, particularly in the intellectual property and transportation services subsectors.

Let's refer back to the 11-year period of economic growth in the U.S., now the longest expansion of the U.S. economy on record. That fact alone causes many to believe a recession is overdue, and the slowdown in global economic growth adds support for that belief. But as we noted, no economic cycle has been identical to previous ones. Previous economic cycles have seen higher growth over shorter periods of time following the turning point in the market. The rate of growth throughout this last 11-year expansion period has been relatively subdued. For the period from 2009 to 2018, the U.S. economy posted relatively modest nominal growth of approximately 41% and real growth of less than 23%. Despite continued stimulative monetary policy following the 2009 recession, American consumers and businesses were slow to return to markets and spent the first six years shoring up balance sheets.

Mike Williams
CFA, MBA

Advising Representative

Seemingly undeterred by slowing economic growth, the U.S. unemployment rate has continued to slowly edge down to just 3.7% in the third quarter of 2019. The low unemployment rate, which often signals that higher prices are on the way, has yet to cause the inflation rate to rise above the U.S. Federal Reserve Board's ("the Fed") target levels. In fact, considering the long end of the yield curve, investors are signaling that they expect inflation and interest rates to remain low in the foreseeable future.

While the Fed had raised its target overnight lending rate in 2018 to tame anticipated inflation as the economic expansion continued into the 11th year, it now appears to have reversed direction. At its September 2019 meeting, the Fed implemented a 25 basis point cut (after a previous cut in July) to its target overnight lending rate. Three members of the 10-member committee, pointing to slowing economic expansion and continued trade tensions between the U.S. and China, expressed the need for at least a 50 basis point cut. More recent data and market fears are increasing the probability of a third rate cut to the Fed rate before year end.

In summary, the risks to the economy are certainly increasing but there are some indicators – in particular consumer and business confidence (no doubt due largely to the low unemployment rates) – that suggest that moderate levels of growth expansion may continue well into 2020.

How do we manage our clients' investments during such uncertainty? We can assure you that we possess no crystal balls and cannot predict the future. We believe the key to successful long-term investing through economic thick and thin is strong portfolio construction that adheres to the principles of diversification, value and discipline:

- We diversify our clients' investments throughout industry and geographic sectors of the economy, with each sector having different and often offsetting responses to expansion and contraction through an economic cycle.
- We select investments in which we see value – i.e. companies that can weather economic storms and continue to pay income to its investors through economic downturns.
- We ignore the "noise" and exercise steady discipline, always focusing on maintaining diversification and pursuing our search for value in the marketplace.

Time will tell whether or when a recession actually sets in for North American and global markets. In the meantime, we will maintain our long-term view of investing and continue to adhere to our time-tested principles.

How The Markets Performed

Equity markets were up over the third quarter of 2019, with strong monthly gains in September resulting in positive quarterly returns in all geographic regions. Returns outside of Canada were helped by an increase in the U.S. dollar, which increases the value of securities quoted in Canadian dollars. While the Canadian market did trail the U.S. during the quarter, the S&P/TSX Composite Index slightly outpaced the S&P 500 Index during both the previous 12 months and year- to- date. Preferred shares posted a mildly positive three-month return to the end of September on the back of relatively flat rates during the quarter.

Jordan Carter, CIM

Advising Representative

Key Indicators		Sep-19
90 Day Tbill		1.62%
CPI (Y/Y) (Aug)		1.9%
$U/$C		$0.76
Major Market Returns	**3 Month Total Return**	**12 Month Total Return**
S&P/TSX Composite	2.5%	7.1%
S&P/TSX Preferred Share	0.6%	-10.4%
S&P 500 Composite (C$)	3.0%	6.8%
MSCI EAFE (C$)	0.3%	1.6%
IAIC Equity Sector Benchmarks		
Consumer	-1.0%	5.4%
Financial	4.1%	2.3%
Utilities	4.6%	17.4%
Industrial	-0.1%	11.5%
Resource	0.0%	-0.5%

What Happens If You Die Without a Current Will?

Oliver Lee, B.Math

Vice President IALIA

Life & Living Benefits

IALIA
Independent Accountants' Life Insurance Agency Inc.

EXECUTIVE SUMMARY

Most of us know that having a will is important, but statistics show that what we know about wills and the action we take with wills are very different. While most people understand the importance of having a valid will, it often gets overlooked as an item that requires a regular review to ensure that your previous instructions match your current financial situation. Even if you have a valid will, it is possible to die in 'partial intestate'. Dying in partial intestate means that for some reason your will does not deal with the whole estate or a segment of your will is considered invalid.

Below are some points that should be seriously considered before deciding against a will and how you could expect the estate will be distributed according to the current rules of intestacy.

WHAT YOU NEED TO KNOW

Anyone who has assets, debts, or dependants should have a current will. Most everyone wants their family to be looked after when they die. By not leaving a legal will behind, your family may not be cared for appropriately. Death takes a huge emotional toll on a family and not leaving a valid will can make things a lot worse.

While this list is by no means exhaustive, here are some consequences for your estate should you not have a valid will:

- Depending on the province, common-law partners may not be entitled to the estate as per the rules of intestacy.
- When someone dies intestate, an application must be made to the courts in order to appoint an estate administrator. Therefore, the deceased forfeits the opportunity to appoint an executor of their choosing.
- Most provinces recognize posthumous birth under their intestate rules. Any children conceived before death and born after death are considered to have been alive during the deceased's lifetime.
- There is no opportunity to select guardians for any minor children.
- Due to the laws of intestacy your spouse could end up with significantly less than intended, therefore possibly not be able to maintain his or her lifestyle.
- While everyone likes to think that their family would peacefully and fairly distribute their assets, this is usually not the case. Money has a way of bringing out an ugly side in people. Having a will can prevent this conflict and ensure everyone is treated fairly.
- There will be no outlined plan for dealing with any taxes or capital gains that may arise from your death.
- Estate litigation can be very expensive for your family.
- There will be no opportunity for charitable giving at your death.

Distribution of Your Estate

If an individual dies without a valid will (which can include outdated will instructions), then the estate is distributed according to regulations set forward by provincial legislation. Every province has its own legislation for their intestate rules. It is important to be familiar with the rules in your province. The distribution is dependent on a variety or marital/family situations. Typically, each scenario unfolds as follows:

1. Surviving Spouse, No Children

In situations where the deceased has a surviving spouse but no children, the entire estate is passed to the spouse.

2. Surviving Spouse, Surviving Children

Preferential Shares

When the deceased leaves behind a spouse and one or more children, in most provinces the notion of preferential shares come into play. Preferential shares dictate that a certain amount of the net estate is directed first towards the spouse. Depending on the province you reside in, the amount of the preferential share could range from $50,000 to $200,000. *

If the value of the estate is less than the dollar amount set out by the province, then the spouse receives the estate in its entirety. If the value of the estate exceeds the dollar amount set out by the province, then the preferential shares come into play. The spouse receives the preferential share amount and then the remainder of the estate is divided between the spouse and children.

Beyond Preferential Shares

The net value of the estate that exceeds the preferential share amount is shared between the surviving spouse and children. This distribution is defined by provincial jurisdiction. Where there is just a spouse and one child, the majority of provinces distribute one half of the residual estate to the child and one half to the spouse. If the child has predeceased the parents, then their share is distributed down to their children (if they had any). This distribution is based on degrees of kinship, and is referred to as per stirpes.

Where there is a surviving spouse and more than one child, the distribution differs by province. Generally one-half to one-third goes to the spouse, with the remainder being divided up equally among the children. In most provinces the children's shares are distributed per stirpes. If there is no surviving spouse then the estate is shared equally by the children.

*Provinces that do not recognize preferential shares include New Brunswick, Newfoundland and PEI.

Keeping Our Record of Your Personal Information Up To Date

In order for our investment management team at IAIC to make appropriate investment decisions for you, we must always be up to date on your personal circumstances that are relevant to your financial situation and objectives.

For example, a material change in any of the following could impact our decision-making:

- Marital status
- Job / business
- Income / net worth
- Health
- Personal residence (especially a move to outside of Ontario)
- Investment time horizon (when do you need cash in the future)
- Appetite and capacity for investment risk
- Investment objectives

If you experience any of these types of changes in your life, please inform us directly, either by phone or electronically (see contact information below).

We are required to keep your personal information up to date. It is our practice that if we have not had a meaningful conversation with you in the past year about your personal circumstances such as those listed above, we will reach out to you directly in order to update our records and determine if any investment strategy changes are needed. We may reach out to you by phone, letter or electronically. In these times of identity theft, if you are uncertain at all about the legitimacy of our request for information, please contact us to verify that the request is indeed legitimate and originating from IAIC.

We look forward to hearing from you!

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What Happens If You Die Without a Current Will? (cont'd)

3. No Surviving Spouse, No Children

If the deceased leaves behind no spouse or children, then the estate is distributed to their heirs. In all provinces, except Quebec, if an individual dies without a spouse or children, the estate is passed to their parents in equal shares. If the individual is predeceased by their parents, then the estate passes equally to any brothers or sisters.

If there are no surviving siblings, then the estate is then passed down to any nieces or nephews. In the case that there are no nieces or nephews, then the estate is distributed equally among the deceased's next of kin.

4. No Heirs

If a person dies without any heirs, then each province has legislation that dictates the estate passing to the Crown in a process known as escheat.

THE BOTTOM LINE

Not having an updated will is risky business and there is virtually no benefit that comes from neglecting to have one created. The processes that go with dying intestate are complicated and may cause your family more grief then necessary when trying to cope with your death. A will is perhaps the most important part of any financial plan. No matter what stage of life you are in, it is never a bad time to contact your team of professionals and ensure you have established a well thought-out estate plan that fits your personal circumstances and goals.

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eStatements are more secure, available anytime/anywhere and reduce our environmental impact.

Register at www.iaic.ca and simply click on "Sign up for eStatements & Client Portal Access" or call 1-877-291-3040

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