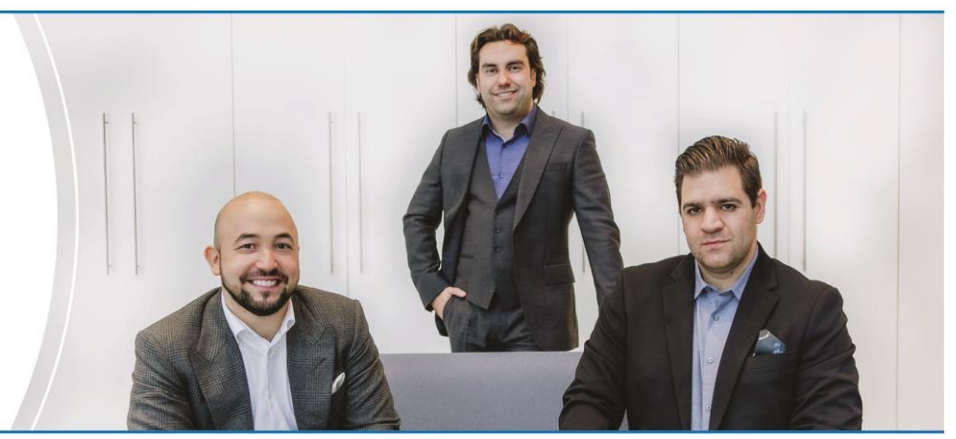
The Wrap Up



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With Plenty of Money and You

Earnings season caters to my inner nerd as waves of data, stories and projections prompt sharp movements in the stock markets. While the start of this earnings season yielded the NASDAQ's worst day since February, we are still only in the beginning and there are more important earnings to look towards in the weeks ahead. While I am tempted to discuss the emerging stories amongst chip makers (lack of qualified labour holding back US fab timelines) or to highlight Netflix's resilience (regardless of the market reaction, they increased their free cashflow guidance for the year), today, we are going to discuss cash.

'Cash is king' was popularized during the 1987 stock market crash by then Volvo CEO, Pehr Gyllenhammar. Since then, that expression has been used as a simple response to every negative market cycle: the dot com bubble burst? Cash is king. The housing crisis? Cash is king. The debt bubble forming and interest rates rising? Cash is king. The expression today is also used when referring to the health of a balance sheet or cash flow statement like it can be referred to in a transaction (which proprietor doesn't love cash transactions as opposed to paying those expensive credit card fees!?).

When the financial crisis hit and the developed world pivoted to a low interest rate regime for over a decade, the phrase faded, afterall ,cash could barely yield 1%. Over the last 12 months, however, higher interest rates and elevated economic uncertainty have brought this sentence back into fashion (every cycle repeats itself which is why I am waiting for top hats to make their

comeback). Towards the beginning of my career, Canada launched the tax free savings account (TFSA), with BMO offering a promotional rate of 3% on cash in the account. Within a year, I found myself offering GICs with rates closer to 1.25% and for almost a decade we never saw anything close to 3% on cash. When central banks raised their rates this cycle, we were treated to rates we haven't seen in more than 15 years: we can offer close to 5% on savings accounts and more than 5.5% on GICs.

Naturally, many of our clients were interested in obtaining 5% risk free, especially after their conservative bonds dropped more than 12% the year before. We have been happy to park short term funds or some of the profits from our winners in high interest savings accounts. Seeing so much money shift to cash, however, sets up a new question; when do we pivot out of cash and where do we pivot towards? There's a saying in poker of knowing when to fold them, well, with cash you have to know what to do with it before you miss out on an opportunity. During a golf game this week, our good friend from the investment world, Dimitri (he really wanted to see his name in this week's Wrap Up) asked us about an article from *Finance et Investissement* which talks about banks, liquidity and the likelihood that savings account rates were likely to come down. I am glad that he brought that article to our attention as we can now revisit our cash positions.

We discussed when to pivot and now we want to asses where to pivot towards. Ultimately, it depends on the objective of the funds; profits that were squirrelled away waiting for market opportunities must continue to be held in liquid instruments, therefore, even a lower yielding savings account or a cashable GIC may be appropriate. Equity markets are still elevated, with many company multiples close to the higher end of their trading ranges, therefore, we are not tempted to reinject large sums of capital back into the stock market (for now). Recently, we've started adding more to discount bonds (either by buying an ETF or by buying the bond outright) as we believe that we are closer to the end of the rate hiking cycle and less concerned about bonds losing their value due to higher rates. Especially for non-registered investors, there exists a strong incentive to dump the savings account for a discount bond.

Our high interest rate savings account is generating 4.75% which is fully taxable as it is interest income. What that means is if you are at the top tax bracket, half is going to taxes, leaving you with 2.375 % in your pocket. Some of the discount bonds we've been buying offer a more interesting rate after the tax payout. An NVCC Scotiabank bond, callable in less than 12 months, yields only 2.83% but it trades at 97.4 cents on the dollar. When the bond is called, it gets called at its par value, which is a full 2.7% higher from its purchase price and that 2.7% is considered a capital gain as opposed to being counted as interest income. The yield to maturity on this bond is 5.715% but the after tax return is a mix of capital gain and interest income, therefore, my after tax return is now 3.56%. Compared to the 2.375% net return on a savings account, or the 2.75% net

return on a GIC, this bond is much more appealing and, unlike the GIC, I can sell the bond before maturity.

This move is an example of how we continue to look for ways to add value for our clients. That extra 1.185% that the bond yields over cash, is an extra $1185 per hundred thousand or an extra $11,850 per million. I want to stress that the discount bond proposal is not the appropriate solution for everyone, however, it may be the ideal solution for those with large cash balances, short to medium horizons and limited risk taking abilities. If you are uncertain, the best you can do is ask us, as we are more than happy to help. This approach is part of our overall philosophy: as your advisors, we do our best to find these types of ideas as market conditions change. Our focus is on adding value and working with you to ensure that you are always one step closer to achieving your financial goals.

Healthy Distraction

The sky will shine a little less brightly this evening, as we say goodbye to another star with the passing of Tony Bennett. He is one of the last of an era of singers who had an identity, which he maintained over a 70 year career and when maintaining that identity was not always easy. It is difficult enough to remain relevant for a short period time, let alone a lifetime, and even with evolving tastes in music (and what I believe to be a severe decline in musical artistry), Mr. Bennett found a way.

In the last decade, he released some duet albums which included songs with Amy Winehouse, Carrie Underwood and, more prominently, Lady Gaga but even with those collaborations, he maintained who he was as a performer and as an artist. If you are looking for a soundtrack to your weekend, look no further than songs such as “I Left My Heart in San Francisco” and “Put on a Happy Face”.

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