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Volatility returns

Investors may reconsider the risks they take on within their RRSPs

- By: Megan Harman
- Source: Investment Executive
- February 15, 2018

Canadian investors kicked off 2018 with an appetite for risk, thanks to the strong performance of equities markets over the past couple of years. But after a few days of sharp sell-offs in early February, some financial advisors now find RRSP season challenging, as clients face a startling reminder of the rapid pace at which gains can turn into losses.

“I hope investors are smart and patient enough to use this as a buying opportunity,” says Jason MacKay, senior vice president and national sales manager with Toronto-based Invesco Canada Ltd., in reference to recent drastic declines in stock markets – including multiple sessions during which the Dow Jones industrial average plunged by more than 1,000 points. "On the flip side, though, I do believe you will see some of the sentiment move toward more stable strategies."

This year started off strong for many investment fund companies, with healthy sales in a broad range of categories. For example, Toronto-based Mackenzie Financial Corp. had its best January in history in terms of investment fund sales, according to Damon Murchison, senior vice president, retail distribution, with Mackenzie.

The firm reported mutual fund gross sales of $882.5 million for the month, up from $698.3 million in January 2017. In addition, Mackenzie's ETFs generated $267.2 million in net inflows in January.

"This has been a very positive time for us," Murchison says. "The most encouraging part is that the flows are broadly distributed – it's not one or two things that are driving this."

Sales of mutual funds and ETFs have been strong for Toronto-based Bank of Montreal as well, says Robert Armstrong, vice president of multi-asset solutions, with BMO Global Asset Management. "So far this year, we've seen very attractive positive inflows."

Investors were in the mood to take on more risk in January compared with recent years, Armstrong notes. He observed investors shuffling some assets into equities and away from fixed-income.

"Generally, investor sentiment has turned positive," Armstrong says. "Investors have moved up the risk spectrum a little bit."

Recent fund sales at Invesco reflect a similar trend, MacKay says: "You're seeing an appetite for risk, for stand-alone equity funds for the first time in a long time. You're seeing a move toward global equities, global fixed-income and emerging markets."

The growing appetite for risk also is noticeable on the ETF side, says Mark Noble, senior vice president, sales strategy, with Toronto-based Horizons ETFs Management (Canada) Inc. In particular, "thematic" ETFs, including those tracking industries such as cannabis, blockchain technology and robotics, have attracted high volumes of sales. For example, he notes, Horizons Marijuana Life Sciences Index ETF was the top-selling ETF in Canada in January, with inflows of almost $250 million.

Although such ETFs can carry considerably more risk than a broader market index fund, "they offer the potential for outsized returns," Noble says. "More investors are chasing those kinds of high risk/high reward asset classes."

However, recent stock market volatility could cause some clients to reconsider the amount of risk they're comfortable having in their retirement portfolios. The sudden market correction that took place in early February came as a shock to many clients because markets had been moving higher for an extended period.

“Investors have gone without seeing any volatility in the marketplace for about two years,” Armstrong says.

A key part of your job as an advisor is ensuring your clients are prepared when markets plunge unexpectedly, says Adrian Mastracci, senior portfolio manager with Lycos Asset Management Inc. in Vancouver.

“Lay out a plan for both the upside and the downside,” Mastracci says. As long as your clients’ portfolios are designed to reflect their long-term goals and their risk tolerance, he adds, their investment strategies shouldn’t be affected by short-term market noise.

For strategic investors, market dips present an opportunity to buy a desired stock or fund units at an attractive price. Says MacKay: “These bouts of volatility can be great opportunities to add to positions, or maybe even to initiate new positions.”

For clients concerned about volatility, balanced funds are an attractive option, as unitholders can participate in market gains while providing some downside protection, Murchison says.

“Balanced funds are in that sweet spot, where you’re getting the returns that you need to grow your portfolio to achieve your goals,” Murchison says, “but you can sleep at night because the risk that you’re assuming isn’t as high as the overall market.”

Mackenzie’s balanced funds, such as Mackenzie Global Strategic Income Fund, are among the top-selling funds for the company so far in 2018, he adds.

Sales figures for mutual funds and ETFs suggest that investors are becoming more comfortable in exploring opportunities outside Canada and the U.S. Following a strong run in U.S. equities that has stretched valuations – and recent underperformance by Canadian stocks relative to other global markets – clients and their advisors increasingly look abroad for more attractive return prospects.

“There’s a big movement toward looking at stocks outside North America,” Noble says.

Case in point: international equity ETFs in Canada attracted inflows of $1.3 billion in January, while Canadian equity ETFs experienced net outflows of $812 million, according to a report from Montreal-based National Bank of Canada.

On the fixed-income side, rising interest rates threaten to drive down the value of clients’ bond holdings this year. Says Noble: “This could be a year in which, feasibly, some bond categories could provide negative returns on a total year basis.”

Still, Canadian investors continue to show demand for fixed-income. Fixed-income ETFs in Canada attracted inflows of almost $1 billion in January, according to National Bank’s report.

In addition, MacKay says, global fixed-income funds, such as Invesco Global Bond Fund, are proving popular because their broad diversification helps to reduce risk in a rising interest rate environment.
