HOW ARE YOU FINANCIALLY?

THOUGHTS TIPS AND STORIES
ON THE ROAD TO LIVING WELL.

Draft Paper by Baha and Margaret Habashy

This draft is written for our children and grandchildren as well as all those who may wish to learn from our mistakes and our experiences.

It can be used for discussion with competent financial resources, but cannot be used as a legal document or professional advice or recommendation.

Most of what you will read here is based on or copied from a selection of 9 books we listed in the Appendix. They are recommended reading.

Our Story:

Jim asked my opinion about switching to a new job where he can earn more money. To start our conversation, I asked him "how are you financially?" As we talked, the look on his face communicated uncertainty and great concern.

Talking with Jim reminded me of my financial journey. Like most, in my twenties I was delighted with my newfound financial freedoms, in my thirties, my priority was dating and getting married. Then came the children and progressive job changes and promotions seem to provide lots of money.

In my fifties, I started to worry about retirement and what it means financially. **My search and engagement with financial advisors were disappointing, to say the least.** I was almost 60 years old when I realized the mistakes I made. It was then that I learned some important lessons I need to share with you

The Big Shift

In August 1999 I, Baha, had a solid high-paying management job. In September 1999 I lost that job and ending my 35-year career in the corporate world. I was fired. In January 2000, at 58 years of age, my workaholic lifestyle had left me with compromised health. Now, I was starting a new career with the uncertainty that comes with being an independent consultant looking for new clients every day. One glimmer of hope was the belief that the investments we had accumulated over the years would be enough should we wish to retire early.

Planning for retirement, we had been very careful to save all we could. We have tried and worked with more than 4 different financial advisors. In 1997 we entrusted our investments into the care of one of the best-known financial advisors at that time. When the stock market crashed in March 2000, we asked our advisor for a major review. To say that we were very disappointed in this well-known and well-paid financial advisor would be an understatement. In our disappointment, we learned that he was serving his personal interests more than ours. The major lesson we learned from this experience is **"If you do not manage your own money, do not expect anyone else to manage it for you."**

January 2000 seems like a long time ago. But the lessons we learned are fresh and real and during that time, we learned a lot. **This paper is written for our children and grandchildren as well as others who may wish to learn from our mistakes and experience**. In summary, here are the two main lessons we learned:

- Our heavenly Father will always meet our needs. The Bible promised, *"God will meet all your needs according to His riches in Jesus."* This has been our experience and our family life did not miss a beat.
- God also has "not given us the spirit of fear, but of love, power and a sound mind" With fear removed, we have experienced the spirit of sound mind. We recovered financially but more importantly, learned many good lessons which we hope to share in this paper.

How are you financially?

By no stretch of the imagination do we consider ourselves experts on the subject. Over the years we have learned from our mistakes. By reading books and talking to good people we have gained some common-sense insights. By God's grace, He has protected us from many common pitfalls.

If we were your financial coach, we would most likely ask you some 12 key questions. These are key questions that have helped us in developing our financial pathway.

Seeking simplicity, we hope to offer you these key questions along with thoughts, tips, and personal stories. We hope you can edit these, update them, and adapt them to form your personal view and stewardship plan.

What Is Your Attitude About Money?

Your attitude about money is influenced by many factors. Your nature and temperament play important roles. Also to a very great extent your nature and the experiences of life influence your attitudes and behaviour. In examining your attitude it is healthy to honestly visit your early childhood and growing years.

We would like to pay tribute to our parents and the upbringing they gave us. Growing up in Egypt, our family would have been considered wealthy by our village standards. But the truth is that my father was not wealthy by any stretch of the imagination. He was a simple businessman but was so generous that people thought he was very wealthy.

After his passing at a very young age, my mother, widowed with 7 children, never remarried. Our home was open to anyone who needed a meal or a place to stay. My oldest brother, at 19 years old, took over the family business and God prospered us as we kept our parent's traditions.

Suddenly, in 1962, a socialist Egyptian Government nationalized and took over our business. All they gave us was a promissory note that was worth less than the paper it was written on. Yes, we lost everything except our home. At this time my mother encouraged her children to immigrate to North America in search of a better future for our children and grandchildren.

Margaret grew up in a very modest home in rural Ontario. Orphaned by the first World War, her dad was shipped to Canada as cheap labour. His first years in Canada were very hard. These orphans were poorly treated by their hiring masters and they worked long hours to pay back the cost of bringing them to Canada.

How We Did It...

Out of our diverse backgrounds, early in our married life we agreed that our attitude towards money is based on the parable of the Talents in Matthew 25. We are only stewards of what we are given. In that stewardship we have 2 clear responsibilities:

- Know what we are given and in total honesty communicate with God and each other.
- Spend, save, and invest what we are given where it has the greatest impact and will help us **"Glorify God and enjoy Him forever."**

When Canada entered the Second World War, her dad felt the need to play his part in defending his homeland. Leaving the woman he wanted to marry, he left all he had to do his part fulfilling his patriotic duty in the Royal Canadian Artillery. Her mom also served as a nurse in the Royal Canadian Air Force.

Returning from the war, her mom and dad married and started their family. Recovering from the impact of that gruelling war was harder than most veterans could express. Yet her dad tried every trade and job that came his way. Her mom and dad were not only good stewards of their limited finances. They committed never to indulge in living beyond their means. Their attitude towards money reminds us of Paul's instructions in Romans 13:8 *"Owe no one anything, except to love each other, for the one who loves another has fulfilled the law."*

How About You...?

How did your early childhood and growing years impact your attitude towards money?

WHAT ARE YOUR VISIONS?

The Bible says that *"without a vision, people perish."* Nothing stands still. You either grow or atrophy. You owe it to yourself and your family to have an aspiration for progress and growth. Whatever your present state, you have been blessed in many ways. Start by counting your blessings then paint a picture of your desired future state. The following video may stimulate your creativity https://youtu.be/NYIXLL0ycK0. Even if you are not an artist you can use a simple picture to stimulate your imagination. Here is an example of what you can do https://youtu.be/zESeeaFDVSw

DO YOU HAVE A FINANCIAL PLAN?

Benjamin Franklin said, ***"If you fail to plan, you are planning to fail!"*** Your financial plan should be part of your overall life plan.[1] Your vision and the sketch you created are your starting point towards creating your financial plan.

Your financial plan is a written document. Building on your hopes and dreams for yourself and your family, your financial plan communicates your financial stewardship, your investment philosophy, and financial priorities as well as your long-term view of life and even death. This is so important that money and possessions are the second most referenced topic in the Bible.

When you are single, life is simple. Financial stewardship becomes more complex when you are married and have a family. We assume you are a **happily married couple with children** and healthy extended family and community relationships.

In later pages, you will find more detail regarding some of the key parts of a financial plan. The following are the key points that you will need to consider in creating your long-term financial plan.

- **Vision, Objectives, and Goals**: Starting from where you are now, how do you picture your life and the life of your family over the coming 5, 10, 20, 30, 45, or 60 years from now?
- **Cash flow:** Can you list the sources of all your present income and expenses? These are reflected in a needs budget and wants budget as well as cash flow management tools.
- **Short Term Savings plan:** This should include:
  - Funds to cover the risks of losing your job. For this, it is wise to plan on 3 to 6 times your total needs budget.
  - Enough easy to access cash for emergencies as well as predefined needs (car breakdown, unexpected appliance, or home repairs…)
  - Monies for near-term unbudgeted needs such as gifts and special occasions not included in your wants budget…

  Note: These funds should be saved in low-risk, easy-to-access accounts.
- **Long Term Investment plans:** A good long-term financial plan must paint a picture of your long-term cash flow requirement, your family investment philosophy, and plans. Depending on your stage of life, the following are some of the elements that should be reflected in your financial plan:
  - Regular income and expenses (based on budget and saving goals)
  - Projected future income from government insurance and others
  - Assumptions of extra incomes

[1] For help see our book *Life Plans: Build a Better Future* https://nomoreoverload.com/product/lp-ebook/

- Projected expenses in today's dollars(assume age 100). Examples of what to include:
  - Periodic car replacement
  - Major home repair and appliance replacement
  - Family weddings, anniversaries, and special events
  - Children and grandchildren's higher education and weddings
  - New cars for extended family members
  - Long-term care or retirement expenses…(See footnote) [2]
  - Personal and family funeral expenses3
  - Inflation and taxes
- Investment philosophy, expectations, and asset allocation. This should explain:
  - Your investment time horizons
  - Your expected rate of return
  - Your risk tolerance which defines your asset allocation and product selections
  - Your present investments by account and product they hold.

NOTE: More on this later. This plan should be reviewed annually and revised as needed. A good financial planner should have the software tools to provide you with such a plan. Preferably, you may consider investing in your planning software that you can update regularly.

How About You...?

Which parts of this list apply to you at this stage in your life?

What Is Your Cash Flow?

Cash flow is balancing cash inflow and outflow. As stewards of what we receive, we should be intentional in managing how we spend, save or invest it. This need not be complicated.

Later, we will share a stewardship framework that we have used. It starts with having a budget. Your budget is the cornerstone of your financial system.

What Is A Needs Budget?

A needs budget includes all the items that we need to survive as a family. Anything that will sustain our health and safety should be included in your needs budget. This should include:

- Basic healthy food
- Housing, heating, and lighting
- Medical expenses
- Basic clothing
- Basic education
- Basic transportation/car expenses
- Basic insurance

"If you do not managae your cash flow it will manage you."

What Is a Wants Budget?

A wants budget has all the extras you would like to have **IF and WHEN** you have the income to support your wants. The best way to build your wants annual budget is based on how much you earned the previous year NOT on what you hope to earn the coming year.

How About You...?

Do you have a budget that paints a picture of your income, expenses as well as your saving and investment objectives?

[2] In light of the aging population, it is important to plan for your aging health care needs. For example, in our plan after age 85 we have included $5,000 per month for each of us to cover the costs of assisted living or live-in home care. Our funerals are pre-arranged and paid for.

[3] For more detail on this, see our book, *Who Cares*, at **https://nomoreoverload.com/product/wc/**

How We Did It...

When I lost my job in 1999, I confess I had some fear. Fear is the enemy of creative thinking and could have held me hostage for a long time. But I recalled that *"God will meet all your needs accrediting to His riches in Christ Jesus."* With this promise we engaged our children and created a **needs budget and a wants budget**.

Our needs budget was based on Philippians 4:19 that God's premiss to meet all our needs. It helped us realize that we can live on a lot less than we had been accustomed to. It enhanced our confidence in the fact that with God's help we will lack for nothing. This removed our fear and gave the ability to envision a future where we can do what we love to do without fear of financial stress."

Having decided to start our independent consulting practice, our wants budget was based on realistic optimism but also with sober judgment as directed in Romans 12:3 *"Do not think of yourself more highly than you ought, but rather think of yourself with sober judgment, in accordance with the faith God has distributed to each of you."* With that we recived good input from friends and consultants. We agreed that if God wishes, He will provide for our wants. We agreed that spending for our wants will be based on what we actually earn every year, not on what we hope to earn. In other words, each year we spent what we earned the previous year.

How Do You Manage Cash Flow?

Every good system requires the right tools and the right process. The two key principles to managing your cash flow are simplicity and less is more.

- **For Tools**

For software tools, you may consider a simple Excel spreadsheet that you can update every month. Better still, we recommend that you take a good look at tools such as Quicken, MS Money, or Mint.com. The key is to find a tool by which both husband and wife can have easy access and regularly update whichever tool you use. These tools provide an easy way to create and update your budgets.

To build your budget and keep track of your cash flow you will need a set of accounts with banks and investment firms. Keep these as few as possible. The following lists and the number of accounts that you should have.

- **One Joint Saving Accounts:** For simplicity, have an interest-bearing savings account. All incomes and cash received are deposited into this saving account. From there transfer needed funds based on budget and spending plans. In this account, you may like to keep your emergency funds and short-term needs funds.
- **Two Joint Checking Accounts:** These are your withdrawal accounts**.** Both of us must develop the habit of managing and reconciling our checking accounts.
- **Two Separate Credit Cards:** Both of us must build our credit rating and develop the habit of managing our Credit Cards. As long as you **COMMIT TO PAYING YOUR BALANCE ON TIME** credit cards are your best spending tool because they are insured, give you reward points or cashback using them, and provide easy record keeping.
- **Petty Cash for each of you:** It is always helpful to have some cash on hand. ATMs are always nearby.
- **Investment and Retirement Accounts**

These are long-term tools. For simplicity maintain the minimum number of accounts. For example:

- Only one Joint Investment Account
- Two Tax-free Saving Accounts - one each
- Two Registered/RRSP Investment Accounts - one each

- **The Monthly Process:**

1. Commit to regular batch processing. As much as possible, use your tool on a regularly predefined day of each month, for example, the first Saturday of every month:
2. Transfer your total budgeted amount from your savings account to checking accounts.
3. Pay all your monthly bills and donations from your checking account.
4. Collect all credit card receipts and match them to your credit card statement.
5. Download your bank and credit card transactions into your accounting tool. This is the reason why we recommend using a tool like Quicken, MS Money, or Mint.com.
6. Reconcile your bank and credit card statements.
7. From your accounting tool, print your spending to budget comparison and discuss any variances.
8. Be thankful for what you have and make adjustments as may be required. As you practice this, you will get better at it.

How About You...?

How do you manage your cash flow?

How We Did It...

If you are not careful managing cash flow can be a source of family stress. For this reason, it is important to agree on key principles, as well as the right management tools and processes. For principles:

- We committed to be totally transparent in all we have or spend.
- While we both committed to be of one mind, we tried to allow for different point of views and individual ownership of the various budget items.

To do this we assigned primary responsibility to certain budget items based on who is better able to understand and manage the needs. For example, Baha took responsibility for home repair and renovation, car expenses, taxes… while Margaret took responsibility food and groceries, gifts and holiday spending …

If we disagreed on how much to allocate to an item, we respected each other's opinion. To reconcile our differences, we have found helpful to each think of the amount we feel is appropriate and then take the average as the amount we both commit to follow.

For example, if we are going to a family wedding and Margaret feels we should be extra generous but Baha feels we cannot afford a lot. We respectfully share our opinions. On separate slips of paper, we each write how much we should spend and take the average. (Margaret says we should spend $500. Baha thinks $320 is all we can afford. We agree on the average $410).

DO YOU SAVE OR INVEST?

To answer this, we need to define the difference between saving and investing.

- **Saving** is setting aside the money you don't spend now for emergencies or a future purchase in the foreseeable short term. It's money you want to be able to access quickly, with little or no risk, and with the least amount of taxes. Areas for which you save are funds you will need in emergencies, cash for your needs budget for 3 -6 months should you lose your job, predefined and expected needs over the coming month or 1-3 years.
- **Investing** is, on the other hand, buying assets such as stocks, bonds, mutual funds, or real estate with the expectation that your investment will make money for you. Investments usually are selected to achieve long-term goals. Areas for which you may invest include retirement and children's education savings plans.

WHAT IS YOUR INVESTMENT PHILOSOPHY?

The first most important question in defining your investment philosophy is to answer the question: **Are you a passive or active investor? Do you believe in Strategic or Tactical asset allocation?** [4] Your answer and what you believe will impact how you invest and the kind of advice or help you seek. Two primary investment philosophies have been debated by many over the years. You must decide which one directs your thinking and behaviour.

- **Active-Investors** typically believe they can outsmart the market and outperform the market in comparison to market indexes and benchmarks. They believe they can time the market by actively trading at what they believe is the right time. They frequently change their holdings and/or asset allocation based on information they collect and what they believe is likely to happen at a future time.
- **Passive Investors,** in contrast, invest to match the performance of a specific market or markets. They believe in a buy-and-hold mindset. They develop an investment policy statement that reflects investment purpose, investment time horizons, desired returns, and risk tolerance.
  Most often, passive investing is accomplished through the use of Mutual Funds or Exchange Traded Funds (ETFs). Passive investing tends to be simpler and lower cost. The most common model of diversified passive investing is in the growing use of ETFs.

Which is Better? This is a personal choice. After much thinking, we admit that we are not smart enough to time the market or forecast what will happen to the stock of a specific company.

The financial industry has a very poor track record of forecasting the market. The way analysts are compensated for their roles has made their reporting questionable at best.

We sincerely believe that the best economist, financial advisor, market analyst, or portfolio manager cannot outperform the market in the long term. For the fun of it, here is a couple of quotes from people that are much smarter than we ever can be:

- "*Economists exist to make the weathermen look good"* Andy Haldane, Chief Economist of Bank of England
- *"The only function of economic forecasting is to make astrology look respectable*." John Kenneth. Galbraith. Economist and Intellectual.

[4] ***VERY IMPORTANT:*** *See the Appendix for links to video clips that explains the difference between Strategic or Tactical Asset Allocation as well as the fundmentals of ETF development .*

You owe it to yourself to learn what is best for you. Based on our experience and honest belief, we can not expect any financial advisor to predict what will happen to a specific stock, industry or the total market. While they may be able to predict short-term direction they should not be expected to provide long-term forecasting. Based on this we have a very strong preference for passive investing. To get you started here are some references that have influenced our thinking.

- In his best-selling book, *The Myth of the Rational Market***,** Justin Fox chronicles how leading economists and academics from Harvard, Yale, Michigan, and parts of Europe have debated this question with no winner. In his last chapter he writes **"First, it is hard to beat the market. If you have money to invest, the only sensible place to start is with the assumption that the market is smarter than you. …"**
- Warren Buffet is considered to be the best investor in the world. *Think, Act and Invest like Warren Buffet* is a small, highly recommended book. Here are some Buffet quotes from this book:
  - "By periodically investing in an index fund, the know-nothing investor can actually outperform most investment professionals."
  - "Most investors, both institutional and individual, will find that the best way is to own common stocks through index funds that charge minimal fees. Those following this path are sure to beat the net results delivered by the great majority of investment professionals."
  - "We have long felt the only value of stock forecasters is to make fortune-tellers look good. Even now I continue to believe that short-term market forecasts are the poison that should be locked up in a safe place away from children and also grownups who behave in the market like children."
  - "A prediction about the direction of the stock market tells you nothing about where the market is going but a whole lot about the person doing the prediction."
- **What the Standard and Poor Say.** The Standard and Poor rating agency publishes a periodic scorecard that compares the performance of actively managed mutual funds to their benchmark index by country. Almost every year their comparison reports confirm that active investment management cannot consistently over the long term outperform its related index. In other words, if you take a basket of stocks with the same risk attributes the market will most surely outperform the active fund manager. You can examine one of their report findings here: https://www.ifa.com/articles/despite_brief_reprieve_2018_spiva_report_reveals_active_funds_fail_dent_indexing_lead_-_works/
- **From an honest Active Manager?** A few years ago we were in discussion with an active management firm who were interested in having us move our retirement funds to their management team. At the end of our last meeting, they concluded by saying *"Our managers do not seek to beat the market in the long term.* ***They cannot.*** *Their primary objective is to reduce volatility. When the markets go up, they do not do as well but when the markets go down, they do not do as poorly and recover a bit faster. So while active managers may not add much value in good times, they offer value in protecting the investment in bad times and help accelerate recovery from a down market."*

In summary "Forecasting The Stock Market: A Fool's Game." While a very, very small percentage of active fund managers may outperform the index in any given year. There are seldom, **if any**, who consistently outperform the market on a long-term basis.

How About You...?

How Do You Describe Your Investment Philosophy

What Is Your Risk Tolerance?

Your risk tolerance is the degree of uncertainty you are willing to take to achieve desired rewards. Everything you do or do not do regarding your finances brings some level of risk. The risk level you are prepared to take could be one of the most important factors that impact the investment returns you seek. While risk tolerance is mostly subjective and cannot be accurately measured, most professional advisors will engage with you based on a risk tolerance survey. Similar surveys can be found online as well. The key elements of this survey consider:

- **Risk capacity** is expressed by your ability to take certain risks. This is often impacted by age, available funds, and expected needs.
- **Your knowledge** or understanding of the investment market.
- **The experience** you have gained through life and investing.
- **Willingness to take risks** is an added factor that varies from one person to another based on personality type, temperament, and personal and family history.

How Do You Manage Risks?

It was wisely said, "*Do not put all your eggs in one basket*." Investment Risk can be mitigated by diversifying your investment using a wise Asset Mix Allocation Strategies.

Professor Harry Marchoviz won the Nobel Prize in economics for his Efficient Market Theory (EMT). Simply put, it says that asset mix allocation is the most important factor in determining portfolio return. Having a well-diversified portfolio is the best hedge against risk and investment volatility.

Investments can be broken down into a variety of asset types and categories. Each has certain qualities and risk-related attributes. Because of the inherent risk level, each defines its expected returns based on historical performance indicators. When buying an investment, you should always think of the purpose for which it is bought and when you may need to sell it as well as the reasonable returns and risks you expect to get from it.

How We Did It...

After being extremely disappointed in an active adviser and active mutual funds, we read a lot of books, talked to a lot of advisors, and attended many financial conferences. Based on this, we are **very** passive investors. We seek maximum diversification using low-cost Exchange Traded Funds.

While we are not offering professional advice, this paper reflects our belief and will be most helpful to those who agree with our investment philosophy.

What is Asset Class Diversification?

This is the most traditional type of investment diversification. It assumes that there is less risk in holding cash or bonds (income class) than holding stocks. While this assumption is often challenged, it is the way most investments are reported and classified.

- **Income Class of Investments:** Think of this type of investment like you are lending money to someone based on predefined terms of time and rate of return or **yield**. The yield is the interest you expect divided by the amount owed per unit. This asset class includes:
  - **Cash:** This includes bank saving accounts, GICs, and Money Market mutual funds
  - **Bonds:** These are commitments to pay at a predefined target date. There are varieties of bonds such as government bonds, corporate bonds, high yield bonds, and junk bonds. The quality of the bond is based on the stability and the

trustworthiness of the organization issuing it.

- **Equity Class of Investments:** This asset class often reflects the risk associated with shares in company stock. Unlike income stocks, they may generate dividends and possible capital gain or a capital loss. Equity classes are subdivided based on the size of the company**,** payment of dividends to its shareholders or not, and/or location geographically.
    - **Large Companies (Large Cap):** Large capital companies like IBM, BCE, and TD are well established. Often these companies pay dividends to shareholders and may be considered Large-Cap/value stocks. There are also large companies that do not pay dividends but invest heavily to grow the business. Companies such as Microsoft, RIM and are called Large Cap Growth.
    - **Small and Medium (Small-Cap and Medium Cap):** The same applies to smaller and medium-sized companies; there are value and growth companies.

What is Geographical Diversification?

In addition to the large and small value and growth, equities are classified by their geographical distribution. Regional diversity impacts domestic growth rates, risk and returns, as well as industry or sector distribution and currency fluctuation.

What is Sector Diversification?

Sector diversification is becoming more important than geographical distribution. The global economy is highly influenced by large corporations that operate globally. The world wide web has brought the ability to operate globally to small and medium enterprises. Along with other trends, this has made sector diversification more important than ever.

Different industry sectors have emerged to present different risk and volatility characteristics.

Index providers such as MSCI and Standard and Poor have adopted sector allocation based on a hierarchy that begins with the following 11 sectors:

- Consumer Discretionary
- Consumer Staples
- Energy
- Financials
- Health Care
- Industrials
- Information Technology
- Materials
- Real Estate
- Telecommunication Services
- Utilities

What Is the Purpose of The Different Investment Classes?

Trying to accommodate all of these variations can be confusing so it is important to simplify your process by examining the purpose of each asset class. When building a portfolio of different income and equities keep in mind the purpose and the volatility level of each asset class. The volatility level impacts the time horizon that each class can be used for; for example, if funds are held to provide a near-term event such as buying a house or going on a vacation you should not use an investment class that has high volatility. On the other hand, if the purpose of your investment is retirement income 30 years from now, investing in growth-type asset classes with high volatility would be a very good option. The following table seeks to provide some guidance.

Asset Class	Purpose	Volatility
• Canadian Equity Value (Large, medium, and small)	Generate some growth and Canadian Dividends which receive preferred Canadian tax advantage.	Low to Medium
• Canadian Equity Growth (Large, medium and small)	Generate higher growth and potential tax-advantaged capital gain	Medium to High
• US Equity Value (Large, medium, and small)	Access to a stable and profitable side of the US market which represents about 30% of the global economy with high industry diversification	Low to Medium
• US Equity Growth (Large, medium and small)	Same as above providing access to innovative US market generating tax-advantaged capital gain with higher industry and global diversification than Canada	Medium to High
• International Developed Markets	Same as US and Canada and includes Europe, Japan, Australia, and Hong Kong	Medium to High
• Developing Markets	Provide aggressive growth potential and higher volatility including Brazil, Russia, India, and China	High to Very High
• Government and Corporate Bonds	Provide interest income and protection of capital	Low
• High yield and junk bonds	Provide higher interest income with some capital volatility	High
• Short term bonds	Provide capital preservation and modest interest income	Medium
• Real return bonds	Provide income that is inflation-protected and adjusted to the changes in interest rates and consumer price index	Medium to Low
• Money Market and GICs	Provide guaranteed interest income	

How Do You Pick A Winning Investment?

A winning investment comes in the form of a mix of products that collectively match your **investment philosophy, desired returns, and volatility that is compatible with your risk tolerance.**

Volatility can be viewed as the **highest and lowest return of an investment product over specific periods**. Standard deviation is the most common way to measure market volatility. This indicator can be easily found online in places like https://www.morningstar.ca/ca/ It is expected that over the coming few years returns will be lower and volatility higher than average.

Morningstar is one of the most used places for data and analytics on volatility and returns.

Having defined your risk tolerance and your target returns, you can then select the products that can give you an asset allocation model that delivers your risk and return objectives. In the absence of a good financial adviser, tools and screeners such as those offered by https://www.morningstar.ca/ca/ are helpful.

With this Morningstar screener, the following steps can get you started:

1. Define the criteria that you will use to select your investment products. For simplicity, we use ETF funds with the lowest MER and the largest size possible. You may note that funds that have the

lowest MER are likely to be large, more liquid, and/or have the least human or management intervention.

2. Using the screening tool, select funds by asset class that meet your criteria.
3. Take time to understand the attributes of main indexes and the benchmarks in each of these asset categories.
4. Select only one product from each of these categories.
5. Allocate an appropriate percentage of your total portfolio to each of these products.

Returns And Volatility - What Can You Expect?

Pick up any investment paper, prospectus, or recommendation by a financial advisor and you will find a strong disclaimer that says something like this, ***"Historical and past performance does not reflect or guarantee future results…" The*** truth is that no one can time the market to guarantee future returns or predict volatility. As a result, there are only two factors that a rational investor can control.

- **Having the Right Asset Mix Allocation:** As discussed earlier, returns are directly related to risk and volatility. The more risk or volatility you are willing to take, the higher the potential return. This is the role of a well-thought asset mix allocation.
- **Keeping Expenses and Fees as low as possible:** Whether they are imbedded in mutual funds, spent to execute trades or paid directly as a fee to fund managers or financial advisers, expenses have a very high impact on your return.

For example, suppose you are invested in a Canadian equity mutual fund that tracks the S&P/TSX Composite Index. According to the S&P scorecard, that index generated a 5-year annualized return of **6.5%.** If a mutual fund has a Management Expenses Ratio (MER) of **2%** you will be left with only **4.5%**; that is a loss of **31%** of your potential return. If you have an investment advisor that charges **1.5%** fees for services and you buy an ETF you will lose **23%** of your return. If that advisor sells you that fund your combined EMR is **3.5%. You are left with only 3.01%.**

When considering returns it is always important to focus on the real rate of return. The real rate of return represents the buying power of every dollar you get from your investment. It is what is left after you deduct all fees, management expenses, taxes, and inflation. Using the example above, if the inflation rate is **2% your pre-tax real return will drop from 3.01% to only 1.5%.**

How Do You Select A Financial Advisor?

"If you do manage your own investments, no one else will."

Finding the right financial advisor is critical. Like most people, I often selected advisors based **ONLY** on advice from friends or based on market reputation. **This was my big mistake.** I ignored having the right fit or defining the role I expected the advisor to play. **Further, I did not manage his performance to that expected role**.

We believe most financial advisors are ethical and try to act professionally. But we also realize as human beings they are influenced by their investment philosophy, culture, personal biases, personality type, experiences, risk tolerance, knowledge, skills, the priorities of the corporate leaders who employ them as well as what motivates them as individuals.

Financial advisors are not God's and can never predict the future or "time the market". No one can. Keeping all this in mind will help you define the role and the expectations you may have of the financial advisor you may like to work with.

It is your responsibility to find the advisor that best meets your investment philosophy and can professionally play the key roles that you want him or her to play. To help you, let us consider the 4 key success factors in your relationship with the financial advisor.

Key Success Factor

- **Culture:** Culture is reflected in the mission statements and core values of the advisor and the firm he is associated with. This is also reflected in the reputation of the firm and the references that you can check. Is there compatibility between your values and the firm's investment philosophy?
- **Chemistry:** How do you feel when you communicate with this advisor?
- **Competencies:** Does the financial advisor have the knowledge, skill, experience and tools for the role you expect her to play?
- **Compensation:** This is often a challenging part of the conversation. It is your responsibility to ensure that the financial advisor is fairly compensated for the role you expect. More on this later.

Key Roles the Financial Advisor Plays

There are many roles embedded with the title of a "Financial Advisor." It is your responsibility to prioritize these roles and communicate them clearly as you interview prospective advisors:

- **Life Coach** helping link the dots of life priorities and financial stewardship in good and emotionally volatile times. This role is critical especially in light of emotional volatility that often results from financial stress.
- **Financial Planners** develop long-term and life plans. He demonstrates knowledge, skills, and experience but more importantly, **the right tools** to craft an easy-to-understand plan that is easy to update. We believe this is the most important and often most neglected role.
- **Financial Analysts** do not project or forecast the market. They simply analyze various options and tax implications for your various investment plans.
- **Advisors** should be wise enough to provide an educated answer to questions that you can bring that impact your financial wellbeing.
- **Product Providers** provides knowledge and ability to acquire or facilitate the acquisition of financial products.
- **Portfolio Managers** can manage your investment portfolio on your behalf. Based on a well-defined fee structure. The portfolio manager assumes a "fiduciary duty" to act in your best interest without seeking your permission.
- **Teacher Educators** will help you learn what you need to know to become less dependant on his knowledge and services.
- **Robo Advisor** is a new model or service that seeks to automate the process of planning, selecting investing and managing funds.[5]

How We Did It...

After being disappointed in our last financial advisor in March 2000 we decided to become a Do-It-Yourself Passive Investors. We are grateful that by God's grace we did reasonably well.

Turning 70 years old, with diminishing mental capacities, we felt that we may need help in managing our investment. In the process we met and interviewed 12 different advisors. The following thoughts are based on this experience. Please modify them to create your personal search plan.

Ultimately you are the only one who can manage your money. Finding the right advisor simply assists you in achieving your goals. With this in view, you must first define your core values, life goals, and priorities as well as the kind of help you

[5] See Video https://youtu.be/PYdgqfxGcWI

need. You also must commit to being the ultimate overseer of all your investments.

Commit to meet with your advisor at least every six months. Before each meeting, prepare the questions that you wish to discuss. A good advisor will value a client who asks a lot of good questions. No question is a bad or poor question.

Advisor Selection Process:

A. **Define your core values and what is most important to you.** What you believe about money and how you use it is a reflection of your worldview and your core values. If you do not define this, you leave it to the assumptions of others and they will define your priorities for you.

B. **Define Your Investment Philosophy.** As we discussed, this will help guide your next steps.

C. **Define your needs.** A Financial Post article groups investors in three categories based on their needs and emotional capacity:

- **Do It Your Self Investor (DYI):** If you are simply leaving your money unsupervised in some kind of an investment account, you are among the majority who are doing it wrong. To be a good DYI you must be willing to invest the time to learn and manage your money. You must educate yourself in the fundamentals of investing as well as the mechanics, processes, and disciplines of investing. You must be prepared to make the discipline of investment bookkeeping a top priority.
- **An Advised Investor:** Here you are a DYI investor who is too busy or unable to stay on top of the changing world of investing. While you are not prepared to give total control of this important part of your life, you are willing to pay for the complementing services of an investment or financial advisor, or counsellor. The advisor you engage and the fees you pay depend on your selection from a menu of services.
- **A Delegating Investor:** This investor gives the total and discretionary responsibility of portfolio management to a third party. In its purest sense, this is an outsourced relationship where the advisor and his firm must act only in the best interests of the client based on a well-defined investment policy statement.

D. **Understand Advisor Compensation:** Advisors are professionals **and should be compensated fairly**. They sell their time knowledge, skills, and experience. The more they do for you, the more they should get paid. Do your best to be an educated, low-maintenance client. It is your responsibility to understand the compensation preferred by your advisor and how this will contribute to a fair relationship. Organizational and corporate structures also impact how your advisor and his corporate bosses are compensated. Compensation models include:

- Commissions and trailers are paid on products they sell such as insurance, mutual funds, bonds etc. This is the most common model. Regretfully, this often results in a significant conflict of interest.
- Fee for services as a percentage of total portfolio value or Assets under Management (AUM). This is in the range of 0.5% - 2.0% based on portfolio size.
- Hourly based fees. Very few advisors offer this option but we think the market will demand more and more of this kind of service. This fee is in the range of $200.00 - $500.00 per hour.
- A mix of the above three compensation models.

It is your responsibility to gain clear disclosure of what is included and how to avoid conflict of interest between what you need and what is offered.

E. **Prioritize your needs:** Good advisors tend to prioritize their sweet spots and the services they prefer to provide. You need to prioritize the functions where you need the most help. These may include:

- Budgeting, personal finance, or cash and debt management. While an advisor may help you set a budget they cannot help you control your spending.
- Building a long-term financial plan. If he/she has the right tools, this could be the most valuable service the advisor can offer.
- Coaching and keeping emotions in check. This is especially important during market volatility.
- Defining your risk tolerance model using appropriate tools and conversations.
- Creating an **Investment Policy Statement** (IPS). The IPS is a very important document that reflects all of the above-stated points. As an example, our Financial Stewardship Charter includes our Investment Policy Statement.
- Buying products or services, such as insurance
- Creating a model investment portfolio that merges your short and long-term financial plan and your risk tolerance model
- Building the investment portfolio by executing actual purchases or trades on your behalf
- Managing your portfolio based on the IPS and providing a periodic review. You need to decide how much discretionary freedom you will give to the advisor.

F. **Seek credible references** from friends and people you trust to build a long list of potential candidates.

G. Interview as many advisors as you can. In the interview ask the advisor about:

- his or her investment philosophy, the resources used to give advice, and what decision support tools he or she can access
- fees and how he or she is compensated for the work done
- the type of clients he or she enjoys working with.
- The percentage of clients that are similar to you
- The process used to engage with you
- The process used for the periodic review of your portfolio

Gauge your feel for culture compatibility and communication quality. Always ask yourself, "**Can I trust this person? Can I communicate with him or her easily and do I like him or her?"**

H. Select a shortlist of two or three advisors with whom you can share more of your story, financial detail, and financial plan if you have one. Ask them to provide you with:

- A sample Investment Policy Statement which reflects their understanding of your needs
- Two or three references of clients similar to you
- Sample copies of a financial plan as well as the reports and what they will use to discuss your periodic portfolio performance. Make sure that these are simple and in easy-to-understand language and format.

I. Check references carefully.

J. Engage with an adviser based on a letter of engagement that explains clear roles, responsibilities, and fees.

K. Monitor your account performance quarterly. Make sure your brokerage statements are correct.

L. Insist on meeting with your advisor at least twice a year.

WHAT IS A STEWARDSHIP CHARTER?

How We Did It...

As example we are providing you with our charter. Use it as an example, not as a prescription. Prayerfully with God's help create your own.

Our Vision:

Should God allow us to live to age 100, our vision is to serve and live life to the fullest. We want to enjoy the finances He provides without excess and be generous with all that we do not need.

We will never seek financial support from the government or the next generations. We will be good stewards so we can leave what we do not need for those who follow us and the kingdom of God.

Our Objectives:

- Be good stewards and take personal responsibility for our cash management and investments.
- Maintain our present financial quality of life to age 100 and leave a small estate for the next generation and the kingdom of God.
- In our retirement investments, we seek to deliver an inflation-adjusted, real return that complements our Canada Pension (CPP) and Old Age Security (OAS).
- In our asset mix allocation with a risk-adjusted return we need to deliver:
  - Annual investment income of about $XX, XXX before taxes in today's Dollars
  - Investment growth of about 4% real return after inflation
  - Moderate risk tolerance in our 5-year horizon.

Our Policy

- We follow a passive, simple investment strategy.
- We believe that asset mix allocation, management expenses ratios (MER), and investment time horizon are the most important determinants of risk-adjusted return.
- We seek to improve the risk-adjusted return by increasing diversification and lowering the correlation of the investment products we choose.
- We do not time the market but we believe in a buy-and-hold strategy.
- We welcome advice in response to macro-political and geo-economical indicators or response to extraordinary life changes.
- At all times we invest only in what we understand and avoid exotic or complex products.
- We see lower MER as a good indicator of product simplicity and lower human and management intervention.
- We favour low-cost Exchange Traded Funds.
- In Income asset classes, while we favour low MER ETFs; we may consider the value of large managed bond funds or specialty products during a period of low returns.

Stewardship System and Tools

System

- **Cash Flow**
  - **Budgeting: Annually**, using Quicken Software we update our budget including expected income, discretionary and non-discretionary spending needs. This will reflect our cash flow requirements. This budget is updated in November of every year for discussion with our financial advisor and accountant for year-end tax planning.
  - **Spending Controls: Monthly** we download and/or input all income and expenses and generate a Year to Date actual to budget comparison.
- **Investment Management:**

- **Annually:** Update our Retirement Financial Plan to refine our risk tolerance, expected rate of return, and updated the Asset Mix Allocation.
- **Quarterly:** Summarize our investment holding in an Excel spreadsheet
  - If needed, update our Asset Mix Allocation (Make changes when variance from the target is +/- 25%)
  - If needed, seek financial advice.

Tools

- **Long Term Planner:** Quicken Retirement Planner
- **Cash Flow:** Quicken Software or www.Mint.com
- **Investment product selection and Analytics:** Morningstar Portfolio X-Ray (www.morningstar.ca)
- **Investment Management** – Use TD Web Broker supported with Excel Workbook for annual summary and performance comparisons.

Investment Construction Process:

1. Define risk tolerance: We have moderate risk tolerance. *(up to 20% drop once in 5 years which is our investment horizon).*
2. Define growth expectations and risk-adjusted asset allocation. (4% real return after tax and inflation)
3. Ensure optimization between in correlation in category/class mixes.
4. Define asset category/subcategory mix allocation.
5. Create/update product watch list. *(Based on advisor input and Morningstar screener: (Category> Style> MER > and fund size > Star Rating). (See appendix)*
6. Select products to use and allocated % of to execute in investment accounts.

Investment Asset Mix allocation

Based on our investment philosophy and risk tolerance, we have chosen the following **Low volatility, low-cost, large-volume ETFs** that we believe will help us achieve our objectives**.**

Equity Asset Allocation	**80%**
▪ **Canadian Equity:** Major Canadian companies (Example **XMV** -60 Companies)	**20%**
▪ **US Equity:** Provides broad sector diversification in global companies. (Example XMU -186 Companies)	**40%**
▪ **International Market Equity:** Provides industrialized Diversification in Europe and Asia. (Example **XMI** 275 Companies)	**20%**
Income Asset Allocation (Always prefer short-term funds. Larger funds have greater liquidity and trading advantages.)	**20%**
▪ **Canadian Bonds:** Provides income and preservation of capital. (Example **ZAG**)	**20%**

NOTE: Wherever possible, simplify by using fewer products and/ or categories

Tax Optimization:

- As much as possible place income type holdings in tax-sheltered instruments.
- Take advantage of the pension tax credit and pension splitting.
- Make RIFF and LIF withdrawals based on younger spouse age.

Estate Planning:

- Our will and property and healthcare Power of Attorney were professionally updated in 2018 with very clear instructions for the distribution of our estate.
- Our Funerals are pre-planned and prepaid.

Insurance:

- In light of our age and present portfolio, we feel no need for life insurance
- We considered long-term care insurance but do not think it is economical at this point.
- Estate insurance may be considered in the future.

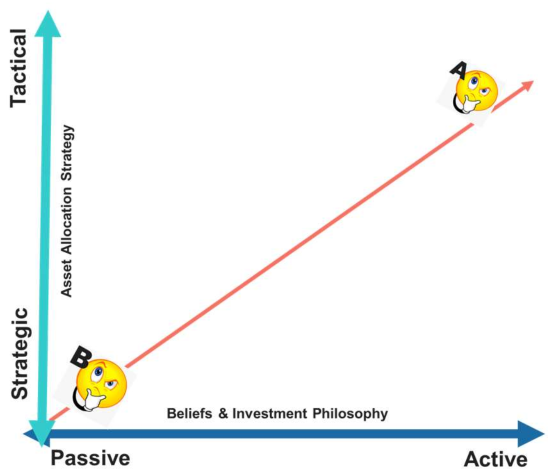
More To Learn

About Asset Allocation Strategies.

On page 8 of this paper, we tried to explain the difference between active and passive investing as the key to defining what you believe. This is reflected in your **investment philosophy**. With the help of YouTube, we would like you to help you answer the second two most important questions:

- What is Strategic Asset Allocation? See https://youtu.be/7Vh1g5v7H50
- What is Tactical Asset Allocation? See https://youtu.be/dSX3qa2mWCQ

The attached image seeks to illustrate the interplay between investment philosophy and investment strategy presented by two **investors A&B:**



A. At the top right-hand corner, you will find you find investor A. He has high-risk tolerance and lots of time to play the market. As a day trader, he is highly active and believes he can time the market. With tools that he found on the web, he buys and sells individual stocks and bonds. Or maybe he took a course on trading stock options.

B. At the bottom left corner, you will find investor B. He grew up in a very conservative family. His parents are enjoying their retirement through the defined benefit pension they gained as long-term teachers and government workers. He is very busy with his work and his growing family. Like his dad, he is risk-averse. Influenced by his parents he placed his retirement saving into **an annuity account**. This is a contract that will provide him with a series of payments at a future point in time and will last for a predefined number of years or as long as he lives.

> **. HOW ABOUT YOU?.**
>
> **Where do you fit?**
>
> **As you look at the attached diagram and related text, how do you describe your investment philosophy and asset allocation strategy?**

What Is an ETF?

- See https://youtu.be/kqr-h-pmky4

ETF or Exchange-Traded Fund is a type of security that tracks an index, sector, commodity, or other asset and can be purchased or sold on a stock exchange the same as a regular stock. An ETF can be structured to track anything from the price of an individual commodity to a large and diverse collection of securities. ETFs can even be structured to track specific investment strategies.

A well-known example is the SPDR S&P 500 ETF (SPY), which tracks the S&P 500 Index.1 ETFs can contain many types of investments, including stocks, commodities, bonds, or a mixture of investment types. An exchange-traded fund is marketable security; this means it has an associated price that allows it to be easily bought and sold.

How to select an ETF

Select The Right Index:

An index is a collection of investment products created by a respected, independent industry organization. These organizations include Dow Jones, Standard and Poor, EMCI, etc. Choosing the index for your asset groups is like choosing the route you will take going to work as it will define how long you will take to get there as well as the challenges, risks, and opportunities you may encounter. Key questions to consider when selecting the index include:

A. Which asset class does it cover and what is the index tracking? Is the index tracking a total market class or a subsection of it?

B. How representative is the index of the market it tracks? For example, the Dow Jones tracks only the top 30 US companies while the S&P 500 includes the top US 500, the S&P TSX 60 the top 60 Canadian firms while the S&P TSX Composite holds the majority of listed companies.

C. Is the index concentrated in particular sectors, companies, or countries?

D. Is this a total return index? This means that the index tracks return and performance as the sum of growth or capital gain plus dividends if any.

E. What are the index rebalancing rules? To support its philosophy, indexes occasionally change the products they hold. The higher the turnover, the higher the costs to the funds that mimic it.

F. What are the rules that cover the index? Most indexes are market cap-weighted or they are based on the market value of their listed stocks. Some are price-weighted or select stocks and companies based on certain investment fundamental measurements.

G. In seeking proper diversification, it is wise to ensure that the indexes you chose do not significantly overlap and have low levels of correlation.

Choose The Right Product.

Based on your investment philosophy, begin choosing your investment products. For this, you will need a screening tool such as www.morningstar.ca to help you sift through the hundreds of products and choose the investment that is correctly mapped to the indexes you are choosing.

H. **Examine the fund index replication strategy**: How does the fund mimic its index? How closely does it track the index it seeks to emulate?

- **Full Physical Replication:** These funds hold every security in the same index proportion.
- **Sampling/Optimised:** To reduce costs, such funds hold a representative cross-section of the index. This likely results in higher tracking error when compared to a full replication fund.
- **Synthetic:** Synthetic funds use derivatives known as total return swaps to earn returns similar to the index, without having to hold any of its component securities. Swaps are good for tracking errors but they expose the fund to much higher risk and volatility.
- **Tracking Error:** Theoretically, index funds should hug their index or be as close to their performance less the management fee or Management Expense Ratios (MER). In practice, fund returns can deviate from their index for all sorts of reasons. If they do so regularly, then bad fund management may be at work.

- **Portfolio Turnover Rate:** Due to trading costs, the more the fund buys and sells securities, the lower its expected returns. Check a fund's Management Expense Ratio (MER). The lower the better.

I. **Assets under Management:** A large fund with lots of investors is less vulnerable to sudden investor withdrawals. Small funds are more likely to get wounded if investors flee and the fund falls below the critical mass required by its creator. In the case of ETFs, a larger figure can also suggest a more liquid fund that will help keep trading costs down.

J. **Currency Risk:** While using international investment products is an advantage to a well-diversified portfolio it also highlights the currency risk associated with it. Very often the product manufacturer or fund issuers hedge this risk by offering the product in your home currency (Canadian dollar).

Recommended Reading:

In developing our investment philosophy, we have read several books including the following:

- *Holy Bible*
- Burkett, Larry*, Complete Financial Guide for Young Couples: A Lifetime Approach to Spending, Saving and Investing*
- DeGoey, John H., *The Professional Financial Advisor: Ethics, Unbundling & Other Things to Ask Your Financial Adviser*
- Fox, Justin*, The Myth of the Rational Market: A History of Risk, Reward, and Delusion on Wall Street*
- *Mackenzie, Warren, New Rules of Retirement: What Your Financial Advisor Isn't Telling You*
- *Mackenzie, Warren, The Unbiased Advisor*
- *Swedroe, Larry E. and Hempen, Joseph H., The Only Guide to a Winning Bond Strategy You'll Ever Need: The Way Smart Money Preserves Wealth Today*
- *Swedroe, Larry E., The Only Guide to a Winning Investment Strategy*
- *Swedroe, Larry E., The Successful Investor Today: 14 Simple Truths You Must Know When You Invest*
- *Swedroe, Larry E., Think, Act and Invest like Warren Buffett: The Winning Strategy to Achieve Your Financial and Life Goals*

Descriptions of Terms and Other Educational Notes

Copied from MorningStar.com

Category and Description
Canadian Equity
Funds in the Canadian Equity category must invest at least 90% of their equity holdings in securities domiciled in Canada, and their average market capitalization must be greater than the Canadian small/mid-cap threshold.
Canadian Dividend & Income Equity
Funds in the Canadian Dividend & Income Equity category must have a stated mandate to invest primarily in income-generating securities and must invest at least 90% of their equity holdings in securities domiciled in Canada. In addition, these funds must invest at least 50% of their non-cash assets in income-generating securities such that the 3-year weighted average yield on the equity component of the fund's portfolio is at least 1.5 times the average yield of the Canadian Equity Fund benchmark, defined as the S&P/TSX Equity Index. The fund's average capitalization must exceed the Canadian small/mid-cap threshold.
Real Estate Equity
Funds in the Real Estate Equity category must invest at least 90% of their equity holdings in the Real Estate industry group according to S&P Global Industry Classification Standards (GICS®).
US Equity
Funds in the U.S. Equity category must invest at least 90% of their equity holdings in securities domiciled in the United States, and their average market capitalization must be greater than the U.S. small/mid-cap threshold.
US Small/Mid Cap Equity
Funds in the U.S. Small/Mid Cap category must invest at least 90% of their equity holdings in securities domiciled in the United States such that their average market capitalization is within the U.S. small/mid-cap threshold.
European Equity
Funds in the European Equity category must invest at least 90% of their equity holdings in a diversified portfolio of securities domiciled in 2 or more countries in Europe.
Emerging Markets Equity
Funds in the Emerging Markets Equity category must invest at least 90% of their equity holdings in a broadly based portfolio of securities from emerging markets countries. Funds with a consistently narrow focus on a single country, group of countries or single region within the emerging markets will be excluded from the category.

Global Equity

Funds in the Global Equity category must invest in securities domiciled anywhere across the globe such that their average market capitalization is greater than the small/mid-cap threshold, and invest more than 5% and less than 90% of their equity holdings in Canada or the U.S. Funds that do not meet any of the requirements of other geographic equity categories and have no formal restrictions that limit where they can invest will be assigned to this category.

International Equity

Funds in the International Equity category must invest at least 95% of their equity assets in countries other than Canada and the United States and at least 70% of their equity assets in developed countries. Funds that do not meet any of the requirements of the more focused geographic equity categories and that invest less than 90% of their assets in any single country or region will be assigned to the International Equity category.

Canadian Fixed Income

Funds in the Canadian Fixed Income category must invest at least 90% of their fixed income holdings in Canadian dollars with an average duration greater than 3.5 years and less than 9.0 years. In addition, these funds must invest primarily in investment-grade fixed-income securities, such that the average credit quality of the portfolio as a whole is investment grade (BBB or equivalent rating or higher) and not more than 25 % of the portfolio's holdings are invested in high yield fixed income securities. For purposes of the category definition, up to 30% of a Fund's assets may be held in Foreign Fixed Income products which will be treated as Canadian content provided that the currency exposure on those holdings is hedged into Canadian Dollars.

Canadian Inflation-Protected Fixed Income

Funds in the Canadian Inflation-Protected Fixed Income category must invest at least 90% of their fixed income holdings in inflation-protected fixed-income securities denominated in Canadian dollars. In addition, these funds must invest primarily in investment-grade fixed-income securities, such that the average credit quality of the portfolio as a whole is investment grade (BBB or equivalent rating or higher) and not more than 25 % of the portfolio's holdings are invested in high yield fixed income securities. For purposes of the category definition, up to 30% of a Fund's assets may be held in Foreign Fixed Income products which will be treated as Canadian content provided that the currency exposure on those holdings is hedged into Canadian Dollars.

Global Fixed Income

In addition, to maintain a weighting of at least 95% in fixed-income securities, Funds in the Global Fixed Income funds must invest at least 90% of their bond holdings in fixed-income securities denominated in a currency other than Canadian dollars.

Canadian Money Market

Funds assigned to the Canadian Money Market category must be designated as Money Market funds in accordance with National Instrument 81-102 and maintain a minimum weighting of 95% in Canadian dollar-denominated investments.

Filtering and Selection Criteria Description

Equity Style Box

The Morningstar Equity Style Box is a grid that provides a graphical representation of the investment style of stocks and portfolios. It classifies securities according to market capitalization (the vertical axis) and 10 growth and value factors (the horizontal axis) and allows us to provide analysis on a 5-by-5 Style Box as well as providing the traditional style box assignment, which is the basis for the Morningstar Category. Two of the style categories, value and growth, are common to both stocks and portfolios. However, for stocks, the central column of the style box represents the core style (those stocks for which neither value nor growth characteristics dominate); for portfolios, it represents the blend style (a mixture of growth and value stocks or mostly core stocks). Furthermore, the core style for stocks is wider than the blend style for portfolios. For more see http://www.morningstar.ca/industry/articles/FactSheetfromUSrenewStyleBox04-26-2004.pdf

Fixed Income Style Box

This model is based on the two pillars of fixed-income performance: interest-rate sensitivity and credit quality. The three duration groups are short, intermediate, and long-term and the three credit quality groups are high, medium, and low quality. These groupings display a portfolio's effective duration and credit quality to provide an overall representation of the fund's risk, given the length and quality of bonds in its portfolio. As with equity funds, nine possible combinations exist, ranging from short duration/high quality for the safest funds to long-duration/low quality for the riskiest. For more see

http://corporate.morningstar.com/us/documents/MethodologyDocuments/MethodologyPapers/FixedIncomeStyleBoxMeth.pdf

Management Expense Ratio (MER)

The percentage of fund assets used to pay for operating expenses and management fees, including administrative fees, and all other asset-based costs incurred by the fund, except brokerage costs. Fund expenses are reflected in the fund's NAV. Sales charges are not included in the expense ratio. The expense ratio for funds of funds is the aggregate expense ratio as defined as the sum of the wrap or sponsor fees plus the estimated weighted average of the underlying fund fees.

Price/Book Ratio

The P/B ratio of a company is calculated by dividing the market price of its stock by the company’s per-share book value. Stocks with negative book values are excluded from this calculation. In theory, a high P/B ratio indicates that the price of the stock exceeds the actual worth of the company's assets, while a low P/B ratio indicates that the stock is a bargain. All P/B ratios greater than 75 are capped at 75 for the calculation.

Total Return 3 Yr

A stock, exchange-traded or closed-end fund's total return is based on market prices, as opposed to NAV. Morningstar calculates the market-price return by taking the change in the fund's market price, reinvesting all income and capital-gains distributions during the period, and dividing by the starting market price.

Tax Cost Ratio

The Morningstar Tax Cost Ratio measures how much a fund's annualized return is reduced by the taxes investors pay on distributions. Mutual funds regularly distribute stock dividends, bond dividends and capital gains to their shareholders. Investors then must pay taxes on those distributions during the year they were received.

Yield % (TTM)

Yield is a measure of the fund's income distributions, as a percentage of the fund price. Morningstar calculates this figure by summing the income distributions over the trailing 12 months and dividing that by the sum of the last month's ending NAV plus any capital gains distributed over the 12 months. Morningstar adds back capital gains to estimate what the fund's ending price would have been had it not distributed these gains; this makes the result more comparable to a stock yield because stocks do not distribute gains but rather simply increase in price.

Standard Deviation 3 Yr

Standard deviation is a statistical measure of the range of a fund's performance. When a fund has a high standard deviation, its range of performance has been very wide, indicating that there is a greater potential for volatility. The standard deviation figure provided here is an annualized statistic based on 36 monthly returns. By definition, approximately 67% of the time, the total returns of any given fund are expected to differ from its mean total return by no more than plus or minus the standard deviation figure. Ninety-five percent of the time, a fund's total returns should be within a range of plus or minus two times the standard deviation from its mean. These ranges assume that a fund's returns fall in a normal bell-shaped distribution.

Sharpe Ratio 3 Yr

A risk-adjusted measure developed by Nobel Laureate William Sharpe. It is calculated by using standard deviation and excess return to determine reward per unit of risk. The higher the Sharpe Ratio, the better the fund's historical risk-adjusted performance. The Sharpe ratio is calculated for the past 36-month period by dividing a fund's annualized excess returns by the standard deviation of a fund's annualized excess returns. Since this ratio uses standard deviation as its risk measure, it is most appropriately applied when analyzing a fund that is an investor's sole holding. The Sharpe Ratio can be used to compare two funds directly on how much risk a fund had to bear to earn an excess return over the risk-free rate.

Risk Standard Deviation 3 Yr

Standard deviation is a statistical measure of the range of a fund's performance. When a fund has a high standard deviation, its range of performance has been very wide, indicating that there is a greater potential for volatility. The standard deviation figure provided here is an annualized statistic based on 36 monthly returns. By definition, approximately 67% of the time, the total returns of any given fund are expected to differ from its mean total return by no more than plus or minus the standard deviation figure. Ninety-five percent of the time, a fund's total returns should be within a range of plus or minus two times the standard deviation from its mean. These ranges assume that a fund's returns fall in a normal bell-shaped distribution.