Advice **Matters**

SPRING 2019

Investing in Mutual Funds

A primer for investors of all experience levels

Although Canada's investment landscape keeps evolving to offer new products, mutual funds remain the most popular option for Canadian investors, with mutual fund assets totalling $1.51 trillion at the end of February 2019[1].

And for good reason—mutual funds as opposed to investing in an individual stock, deliver instant diversification (more about that later) and professional money management in a cost-effective vehicle that's easy to access. You'll find mutual funds are widely available for sale through banks, financial planning firms, brokerages, credit unions and other investment firms.

So what exactly is a mutual fund?

A mutual fund is an investment vehicle made up of a pool of money provided by individual investors for the purpose of investing in securities such as stocks, bonds and other assets. Actively managed mutual funds are operated by professional portfolio managers, who buy and sell investments in order to deliver gains for the fund's investors. Supported by a team of analysts, the portfolio manager's primary goal is to identify investment opportunities that help enable the fund to outperform its corresponding benchmark, such as the S&P TSX Composite Index, Canada's most widely followed stock index. The following are just some of the benefits provided by mutual funds.

Key benefits: The case for mutual funds

Diversification

1 By investing in a range of different securities, mutual funds help diversify risk, which is really another way of saying that you won't be putting all your eggs in one basket. Most mutual funds hold well over 50 securities to help spread risk throughout the fund and provide a variety of return streams. If one investment is down, those losses can potentially be offset by another of the fund's holding. Strong diversification also helps reduce wild swings in the value of your investment (which may help you sleep better at night). This is a much less riskier proposition than investing all of your money into the stock of a single company.

Cost-effectiveness

2 Imagine if you had to go out and buy each individual stock for your own portfolio. The time and money spent on commissions would be significant. Thankfully, mutual funds deliver access to a diversified basket of securities in one single, cost-effective transaction. Another cost-effective aspect of mutual funds are the low investment minimums, which means new investors can get started with an initial investment as little as $500–or even less in many cases.

Professional money management

3 Mutual fund investors get the benefit of having a professional manager reviewing the portfolio on an ongoing basis. Their investment knowledge can be an invaluable resource, especially for many investors, who simply don't have the time or investment expertise to micro-manage their investments.

[1] The Investment Funds Institute of Canada (IFIC) Monthly Investment Fund Statistics, February 2019.

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Access and convenience

4 All mutual funds allow you to buy or sell your fund units once a day at the close of the market. Mutual funds also conveniently allow you to automatically reinvest income from dividends and use dollar-cost averaging, a simple process that allows you to automatically invest a pre-determined amount of money on a regular basis (usually taken from your bank account, timed with your paycheque). Mutual funds also deliver access to a wide array of markets across the world, which would not be accessible to everyday investors.

Understanding fees

It's important to have a clear understanding of all fees associated with an investment. There are usually two key fees that may be associated with mutual funds.

Sales charges

- Sales charges are the commissions that you may have to pay when you buy or sell a fund (also known as "the load" of a fund). If you pay this charge when you buy the fund, it's called a front-end load. If the charge is levied when you sell, it's called a back-end load. Today many mutual funds–including those sold by Scotiabank–are sold on a "no-load" basis, which means there is no sales charge when you buy or sell. It's important to speak to your advisor to have a full understanding of all fees, if any, that are associated with your investment.

Management Expense Ratios (MERs)

- Each mutual fund pays an annual fee to its management company for overseeing the fund and its investments. The management expense ratio (MER) is the total of the management fee and Fixed Administration Fee (or operating expenses) and is shown as a percentage of the fund's assets, usually ranging from 1% to 3%.

To find out more about fees, fund performance and the difference advice can make, check out Scotiabank's helpful investor resources.

A word about risk

Although they are a diversified investment, mutual funds have risk and are not covered by the Canada Deposit Insurance Corporation, the Autorité des marchés financiers' fonds d'assurance-dépôts (Québec) or other deposit insurance. The level of risk in a mutual fund largely depends on what it invests in. Stocks are usually riskier than bonds, so you would generally expect an equity fund to be riskier than a fixed-income fund–although this is certainly not always the case. Take time to learn about a particular fund's risk rating by reading its Fund Facts and simplified prospectus.

So, which mutual funds are right for you? The short answer is that much depends on your unique investment goals and preferences.

A Scotiabank® advisor can work with you to create a customized financial plan complete with investment recommendations that include mutual funds that help you manage today's priorities while preparing for your future needs – whether that's retirement, buying a home or funding your child's education. ■

QUICK FACT

Canada had 106 investment fund companies offering more than 3,400 mutual fund products at the end of 2018.[2]

[2] The Investment Funds Institute of Canada (IFIC), 2018 Investment Funds Report.

TYPES OF MUTUAL FUNDS

Although there are a seemingly endless variety of mutual funds, here are four of the most basic mutual fund categories.

1. Equity Funds

The largest category within mutual funds, equity funds invest primarily in stocks. These funds accept a higher level of risk to deliver a higher level of return. The range of equity funds is extremely broad, but common sub-categories include geography (for example, Canadian, U.S. or global equity funds), company size or investment style (for example, growth or value), to name just a few.

Investor Outcome:
Long-term growth

2. Fixed-Income Funds

These funds focus on purchasing debt instruments, such as government and corporate bonds, which generate interest income that can be passed onto unitholders. These funds look to provide less risk and higher income.

Investor Outcome:
Regular income

3. Balanced Funds

A very popular type of mutual fund focused on long-term growth, balanced funds invest in a mix of stocks and bonds.

Investor Outcome:
Growth and income

4. Index Funds

Designed for cost-sensitive investors, index funds are passively managed funds whose holdings are designed to track the performance of a specific index, such as the S&P/TSX Composite Index. This is in stark contrast to an actively managed fund, which relies on a portfolio manager to select securities in an effort to outperform the market or a benchmark index.

Investor outcome: *Varies according to type of fund (equity, fixed-income etc.)*

INVESTOR INSIGHTS

RRSPs: No parking zone

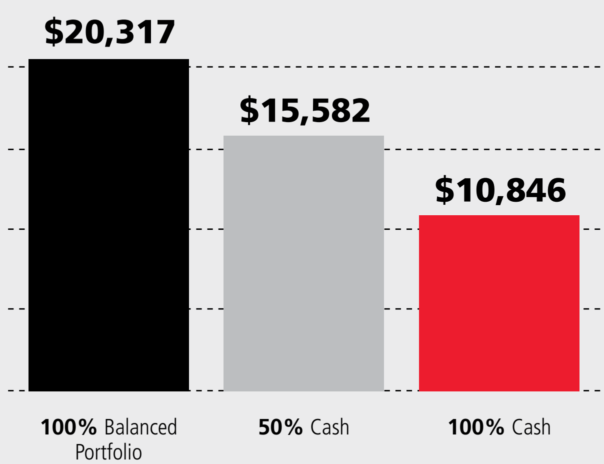
Congratulations. You beat the March 1 deadline to contribute to your RRSP and helped reduce your tax burden in the process. While it's great that you're saving for retirement, it's important to remember not to leave your contribution just sitting there parked in cash.

In the following scenario, we invested $10,000 in three different ways over a 10-year period: fully invested in a balanced portfolio; 50% in a balanced portfolio and 50% cash; and 100% parked in cash.

As the graphic below clearly shows, cash can be a real drag when it comes to your retirement portfolio. Not only will you be missing out on investment opportunities to generate greater returns, your cash holdings may not even keep pace with inflation, leaving you with a negative real return.

Cash and its long-term impact on your Portfolio[1]

Based on a 10-year period
(January 2009 to December 2018)



Source: Bloomberg.

[1] The example is hypothetical and for illustrative purposes only. It is not possible to invest directly in an index. Assumes reinvestment of all income and no transaction costs or taxes. Value of investment calculated using annual compounded returns from January 2009 – December 2018. Assumes investment in a balanced portfolio weighted 25% S&P/TSX Composite TR Index, 50% FTSE Canada Universe Bond Index, and 25% MSCI World GR Index. Cash is assumed to have been invested in FTSE Canada 91 Day T-Bill Index.

What is "cash drag"?

Investment portfolios holding a portion of assets in cash for a considerable amount of time can suffer from "cash drag", so named because the minimal returns provided by cash actually drag down overall performance.

> **Remember: Saving for retirement is good. Investing for retirement is even better.**

And why not avoid last-minute contributions once and for all?

With Pre-Authorized Contributions (PAC), you can invest automatically and save. It's an easy and convenient way to start building up savings for retirement. You can choose how much money you'd like to save and how often.

How setting up a PAC benefits your investments:

- Eliminate the guesswork of when to invest
- Avoid the RRSP deadline scramble
- Compound growth potential
- Get started with as little as $25 per month

Talk to your Scotiabank advisor about how you can make the most of your RRSP contributions.

INVESTOR EDUCATION

The three Rs: Recognize, Reject and Report

How to protect yourself from financial fraud

At Scotiabank, we're committed to helping you keep your accounts and financial information safe and secure. By helping you recognize, reject and report the most common types of scams, together we can help prevent financial fraud.

Here are three principles to help you be more aware and protect yourself from fraud.

1. RECOGNIZE fraud by knowing the most common scams

Phishing

Fraudsters impersonating government agencies, banks, communication providers or other companies send text messages to potential victims to lure them into providing personal or financial information, such as usernames, passwords, credit/debit card numbers, PINs and other sensitive data that can be used to commit financial crimes. Please be aware that Scotiabank will not send you text messages or emails asking you to validate or restore your account access by asking for your passwords, PINs or account numbers.

Service

Imposters call and identify themselves as a representative of a well-known technology company, such as Microsoft or Windows. They claim that your computer has been hacked and must be serviced for a fee payable by credit card or money transfer. These individuals will remotely access your computer and may run malicious programs, alter settings or steal personal information.

Extortion

Impersonating employees of the Canada Revenue Agency (CRA), fraudsters call unwitting victims to falsely claim that there are discrepancies from past tax returns and that payment is required immediately. They then threaten that failure to do so will result in additional fees and/or jail time.

Bank Investigator

Consumers are contacted by phone and asked for assistance to catch a bank employee who has been stealing money. The victim is instructed to visit their bank branch and to make a cash withdrawal from their account without disclosing the reason, as the teller may be involved in the scam. Finally, the victim is directed either to place the cash in an envelope and meet the "investigator" or send the money through a wire service, such as Western Union.

Mail Scams

Victims receive unsolicited mail advising them that they are either the beneficiary of an inheritance from a distant relative or have won a lottery. In order for funds to be released, the victim is asked to pay one or more upfront fees.

Romance

Unscrupulous individuals will use dating or social networking sites to seek out potential victims and gain their trust over a few months. Once the perpetrator has gained their confidence, they will eventually ask for assistance in paying travel costs to meet them or for money to cover an emergency.

Loan

Consumers seeking loans may stumble upon offers through advertising or websites designed to resemble legitimate lending institutions. Once the victim has provided their personal information and has been approved—all are approved—they are informed their loan will be deposited into their account within 24 hours of sending an upfront fee. Once the fee is received, the fraudster ends communication, and no loan money is provided.

[redacted]

To learn about recent fraudulent activities or scams, and how to protect yourself, visit the Government of Canada Canadian Anti-Fraud Centre website at www.antifraudcentre-centreantifraude.ca.

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2. REJECT fraud by being aware of preventive tips

DOs	DON'Ts
✔ Shred and dispose of all personal and financial documents; receipts, credit card offers, bills etc.	✗ Never provide personal or banking or other account information unless you initiated the call
✔ Keep personal and financial documents, wallets and purses locked safely	✗ Never click on any links received from suspicious senders
✔ Sign up for Scotiabank InfoAlerts through Scotia OnLine or Scotia Mobile Banking	✗ Never respond to any request offering a percentage of a fortune or fees to claim prizes
✔ Always review your banking and other statements for irregularities. Go paperless by signing up for online statements	✗ Never respond to companies offering guaranteed loans or pay upfront fees

3. REPORT fraud by immediately notifying Scotiabank

You can report suspicious activity by:

Emailing phishing@scotiabank.com

Calling the Scotiabank Contact Centre at 1-800-4SCOTIA (1-800-472-6842)

Be wary of those impersonating the bank

Scotiabank will not send you text messages or emails asking you to validate or restore your account access by asking for your:

- Password for Scotia OnLine and Scotia Mobile Banking
- Personal Identification Number (PIN) for either your ScotiaCard or credit cards
- Account numbers, for any type of account

What should you do if this happens to you?

1. Do not respond to any such messages by providing your information.
2. Report incident to Scotiabank by calling 1-800-4SCOTIA.

The Top 10 most-used passwords

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Preventing hackers from accessing your bank account is a partnership between you and your financial institution. While your bank has extensive security measures in place to protect you from fraud, there are also important steps you should take like choosing secure Personal Identification Numbers (PINs) and unique passwords.

Choosing a unique password for your online accounts is important. Each bank has its own requirements about choosing secure passwords, so it's best to check with your online access agreement, account agreement or credit cardholder agreements.

Check out the list below for the top 10 most-used passwords according to internet security firm SplashData.

1. 123456
2. password
3. 12345678
4. qwerty
5. 12345
6. 123456789
7. letmein
8. 1234567
9. football
10. iloveyou

If your password is on this list, it's time to think about changing it.

SPOTLIGHT

The *"Know your client"* rule

Securities rules and regulations require investment advisors to make recommendations that are suitable for you in relation to your specific personal circumstances.

To meet this requirement, your investment advisor needs to understand your personal financial situation, investment objectives and your tolerance for risk. This is known as the "Know Your Client" (KYC) rule.

YOUR INVESTMENT ADVISOR will need to know whenever you experience a major life change, such as changing jobs, getting married, buying a house, starting a family or losing a loved one.

Ensuring that your KYC information accurately reflects your current personal situation will help your investment advisor provide you with suitable advice.

This article was provided by The Investment Funds Institute of Canada (IFIC). IFIC members represent all facets of the investment funds industry – fund managers, distributors and the many professional and back office firms that support the sector.

Their principle role is to advocate on behalf of the industry and its investors – ensuring their voices are heard by regulators and public policy makers considering the framework of rules that govern investment funds.

The KYC rule requires your investment advisor to obtain the following information from you:

- **Age** – your date of birth
- **Income** – your annual income from all sources, including employment income and investment income
- **Net Worth** – an estimate of your total assets less your total liabilities
- **Risk Tolerance** – your willingness to accept investment risk and your ability to withstand financial losses
- **Investment Objectives** – why you are investing or what you intend to use your investments for
- **Investment Knowledge** – your level of knowledge about investing, investment products and their associated risks
- **Time Horizon** – how long you expect to keep the majority of your account invested

MARKET INSIGHTS

Market Recap

Stock markets off to a strong start in 2019

After a significant correction in the final months of 2018, global equity markets staged a dramatic rally, posting the strongest quarterly performance in equities markets in almost 10 years. Performance was driven by moderating views on monetary policy and a strong bounce in commodity prices.

Growing signs of a slowing global economy

The first quarter of 2019 featured the release of a variety of economic data reports that showed the growth rate of the global economy is slowing. In Canada fourth quarter GDP growth was 0.1%, the slowest pace since the second quarter of 2016. U.S. GDP growth in Q4 2018 was 2.2%, down from the 2018 annual rate of 2.9%. We also saw indications of slowing growth in China, which can be partially attributed to the effects of the ongoing U.S. – China trade dispute. In addition, growth forecasts were cut by the International Monetary Fund, the Bank of England, and the European Union.

A significant shift to a dovish view by central banks around the world

Central banks have shown their flexibility and responsiveness to the recent slowdown in economic growth with more supportive monetary policy statements. In a reversal from only a few months ago, the U.S. Federal Reserve, the Bank of Canada, the European Central Bank, and others have backed away from planned interest rate hikes later in 2019. They have indicated they are now concerned about risk to the downside, and will have patience with additional rate hikes.

Brexit uncertainty continues to provide an overhang

Brexit was originally scheduled to occur by March 29, 2019, but has been held up by the lack of agreement on the terms and conditions of the new relationship with the EU. During the first quarter the U.K. parliament voted down the deal negotiated by Prime Minister Theresa May with the EU. Parliament also rejected leaving the EU without a deal in place. The current deadline is October 31, 2019. The uncertainty is making it difficult for businesses to make plans for the future, and they are delaying investments pending greater visibility. ■

MARKET PERFORMANCE (YTD Returns in local currency as at March 31, 2019). Source: Bloomberg

FTSE Canada Universe Bond Index	S&P/TSX Composite Index	S&P 500 Index	MSCI World Index	MSCI Emerging Markets Index
▲3.91%	▲13.27%	▲13.65%	▲12.65%	▲9.90%

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