FIRST CAPITAL FINANCIAL

WORLDSOURCE FINANCIAL MANAGEMENT INC.
Sponsoring Mutual Fund Dealer

Welcome back and I hope everyone had a wonderful (and wonderfully filling) Thanksgiving weekend! My sides are still groaning from (over) indulging like a Roman Emperor, and my fridge is packed to the gills with enough leftovers to carry me through to Christmas. All-in-all a well-deserved break from the routine and, best of all, we're almost half way to next weekend! But down to business and today's Daily Report looks at the role of fixed-income investments in your portfolio. Traditionally, government bonds have served to protect capital while delivering steady, predictable returns in the form of monthly interest distributions. And thanks for declining interest rates, holders of sovereign debt have enjoyed capital gains as well, giving a total return over the past 40 years of more than 5.5% annually. Pretty good for a low risk asset class and what's more, it enabled investors to construct balanced portfolios holding a 60/40 equity/bond weightings while enjoying solid, risk-adjusted returns. The question though is whether investors need to revisit this investment thesis, given that interest rates are at historic lows. Record low interest rates mean that:

*yields from government bonds are less than one-quarter of their historical average
*capital gains on the par value of bonds have already been earned
*a rise in interest rates will negatively affect bond prices and total portfolio returns
*longer term duration government bonds are likely to deliver ***negative*** future returns
*a 60/40 equity/bond portfolio has a high probability of underperforming compared to returns from a similar allocation over the past several decades

I know what you're thinking -all that rest and relaxation over Thanksgiving has now been replaced with a feeling of indigestion. After all, what's a bond holder to do? Well, the article from Edgepoint <here> speaks directly to this issue and offers a path forward for investors who cannot stomach a pure equity portfolio, because of the higher volatility that accompanies such an allocation. Their position is that corporate bonds are a more attractive alternative, and a shorter term duration is prudent given that higher interest rates are more likely than not over the next 10 years. Unit holders of the flagship Edgepoint Global Growth & Income fund can look to the bond component of the fund for almost 4% from the coupon yield. This compares favourably with less than 1% for government bonds. The shorter weighted duration of only 2.4 years also lowers the risk of rising interest rates. Now there's the bromide we need to feel better!

In summary, it is our position that bonds remain a core component of client portfolios, and that the challenges of the current low interest rate environment can be managed effectively through high-yield, low-duration corporate bonds. More, bonds remain an important portfolio diversifier which serves to lower overall volatility and provide a higher degree of capital protection. In turn, both of these are expected to contribute to a better investment experience over time -something we are deeply committed to.

Be safe, be well!

Martin
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