Is shifting retirement investments into safe havens a good idea?

KELSEY ROLFE
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Selling out of equities can have tax implications. Even if holdings are down in any given year, it doesn't mean clients are facing an overall capital loss.
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Equity market volatility tends to send investors fleeing for fixed income. But with stocks and bonds suffering in tandem this past year, advisors say clients are beginning to ask about long-maligned guaranteed investment certificates (GICs), which have become an appealing proposition as interest rates have risen.

"I haven't been using GICs [for] a long time because rates have been so low. They haven't been attractive," says Ian Calvert, vice-president and principal, wealth planning, at Highview Financial Group in Oakville, Ont. "But now … they've become more attractive for short-term needs."

Jennifer Tozser, senior wealth advisor and portfolio manager with Tozser Wealth Management at National Bank Financial Wealth Management in Calgary, says she has also seen clients' desire for safety lead to inquiries about GICs.

"People are [saying], 'If I own fixed income, I want to own something where I don't have to deal with price fluctuation because the market is volatile,'" she says.

"For people who aren't used to this [volatility], the frustration is that what's supposed to be a stable part of their portfolio has shown price movement."

Rona Birenbaum, certified financial planner and founder of Toronto-based Caring for Clients, says her firm normally gets inquiries from clients looking to reduce their equity exposure and pile into bonds during times of market turbulence. (She counsels them against doing so.)

But this past year, the firm saw fewer of those inquiries as rising interest rates have depressed bond returns.

"That has scared some investors away from bonds," she says.

Ms. Tozser says she has cautioned her bond-wary clients against worrying about price risk – pointing out that governments and companies continue to make their bond payments, and investors will still receive the bond's face value at the end of its term. She also sees opportunities in longer-term bonds as the yield curve has inverted to lock in a higher interest rate before interest rates start to fall again.

Ms. Birenbaum says she also thinks investors are set up for good bond returns in the next couple of years. Any money going into both stocks and bonds is now "generating a much higher yield than it was a year ago" as prices have fallen.

"For new money and new savings, the future looks brighter than it has for the past couple of years," she says.

Approaches to preserving capital

GICs, at current rates, can be "very useful tools" for clients in retirement or those who are approaching that stage of their life, providing capital stability and a reasonable yield, Ms. Birenbaum adds.

She's begun building a laddered portfolio of GICs for retiree clients to fund their next three to four years so they don't need to consider withdrawing from more volatile assets and can benefit from the eventual market recovery.

"That brings some peace of mind to clients and it's also just a smart thing to do," she says. "If we do experience a painful recession next year and stocks fall, these retirees won't be selling equity investments at that time."

They might not be in the position to add equities, she says, which would be the "icing on the cake" if they could, but at least they don't touch them.

Ms. Birenbaum says clients' GIC purchases are being funded by new cash deposits, which might have otherwise gone toward other bond strategies.

She may also move money from clients' existing fixed-income positions, but is "doing that more cautiously, because if we're nearing the end of the interest rate cycle, bond [mutual] funds and [exchange-traded funds] returns could easily outperform GICs. Plus, they have liquidity."

However, she says this may be a worthwhile trade for more anxious clients who want peace of mind.

"The risk is just the opportunity cost if bond strategies outperform GICs, but it's just [an] incremental difference," Ms. Birenbaum says.

When shifting investments makes sense

Ms. Tozser says buying GICs or shifting toward a more conservative asset allocation right now can make sense for clients who are well into retirement and/or have exceeded the financial goals they've set for themselves.

"We've had a lot of good years [recently], and even though we've had a negative year, they might be further ahead in their financial plans than they thought they'd be," she says. "So. if they want to have GICs they can."

However, she says clients should never eliminate stocks as a long-term asset allocation strategy.

For those who are on the cusp of or just entering retirement, Ms. Tozser says she emphasizes their long-term goals and encourages them to stay the course. She also points out that selling out of equities can have tax implications. Even if their holdings are down on any given year, it doesn't mean they're facing an overall capital loss.

Mr. Calvert advises only moving assets that were in savings into GICs, rather than selling out of equities – and potentially locking in losses – to fund those investments.

He notes GICs may do well over the next two years but come with re-investment risk if interest rates are no longer as high.

"It can be a good place to park funds in the short-term, there's no doubt," he says. "But if these are longer-term funds, obviously it's going to be challenging to keep renewing at higher interest rates, and you will absolutely lose out on a market rebound, whenever that happens."

To get around GICs' challenging lack of liquidity, Ms. Birenbaum says she designs clients' portfolios in conjunction with their cash flow projections to ensure they also have some capital that's more liquid.

When GICs mature, putting the funds into a high-interest savings account with set monthly withdrawals works well for clients who have registered accounts like a registered retirement income fund. Those without registered accounts typically receive the full amount, which they can put into their own savings account and withdraw as needed.

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