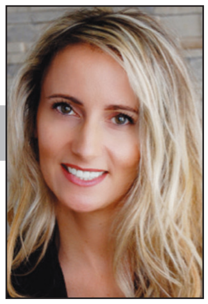
What to expect for 2023

"When all is said and done – make sure you're properly diversified!"

Managing Your Money

LYNN MacNEIL



Good riddance 2022! It may have been a good year in other ways, but from an investment perspective, it was horrible. 2022 was the worst outlier year since 1872 when we look at a combination of stocks and bonds. What can we expect in 2023?

We're not out of the woods yet, but we're starting to see the light at the end of the tunnel. Imagine your doctor telling you that you have high blood pressure, and you need to change your lifestyle habits, while you're told to lose weight, exercise regularly, eat a healthy diet, reduce stress, limit alcohol, and quit smoking. Let's be honest here, it's not a week or a month of these lifestyle changes that are going to reduce your blood pressure. It will take many months to experience improvement from the changes.

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Arguably, It's the same situation with inflation and interest rates. Governments have been increasing interest rates for many months with only minimal impact on curbing inflation. For instance, blood pressure, inflation doesn't come down overnight. But we are starting to see signs that the interest rate policies are working. We may see more small increases in rates but that should taper off soon. In fact, the Bank of Canada is predicting inflation will fall quickly, from 6.3% to about 3% by midyear, with a mild economic contraction at worst. Along with that, we continue to monitor and deal with geopolitical issues and lingering effects from the Covid pandemic. But all-in-all, things seem to be on the mend.

What does this mean for investors? After being in a very low-interest rate environment for two decades, fixed-income investments are now looking more attractive than ever. Bonds, fixed-income mutual funds and ETFs, structured notes, and even GICs are all offering interesting rates. That being said, it's important for fixed-income investors to recognize that these investments are not without risk (as is often believed). This was seen clearly in 2022 when bonds dropped into the negative double digits, something not seen in decades. Conservative investors were hit hard. This is where quality and time horizon become very important. High quality bonds or fixed income may be volatile, but if buying high quality with a reasonable time horizon the risk is significantly reduced.

Fixed Income investments are not all created equal. There are short-term bonds, medium-term bonds, and long-term bonds. There are municipal, provincial, and federal bonds. There are corporate and high-yield bonds. There is an equally wide range of fixed-income mutual funds and ETFs. There are principal-protected notes and structured notes. There are mortgage-backed securities and GICs. And each of these comes with its own benefits and risks. So how do you choose what's best for you? It comes back to a clear assessment of your goals, concerns, and appetite for risk, but as usual, when it comes to investing, diversification among these is key.

On the equity side, there are attractive opportunities as well. High dividend-paying investments and undervalued investments present good opportunities for investors. Stock markets have not likely stabilized yet, and the bumpy ride will continue in 2023. Again here, diversification is key. The "safe", higher-paying dividend stocks tend to mostly fall into the same few sectors, so we often see those investors highly concentrated and lacking in diversification, especially when those sectors get hit.

Alternative investments can include private equity and debt, real estate and infrastructure, and commodities, among other things. 95% of people who come to us for advice or for a 2nd opinion are either completely lacking or falling short on this category of investments. This is particularly unfortunate, as it is one of the few sectors of the market that saw either stable or positive returns in 2022. Most investors, regardless of whether they are institutional or retail investors, are looking for the biggest bang for their buck – or the highest return for the lowest amount of risk. This is what has pushed most pension funds and institutional investors to broaden their portfolios away from the traditional bonds and stocks and include alternative investments into their investment mix, however, most retail investors haven't caught on yet.

So, what's my take for 2023? Some equities are very interesting but don't bank everything on them. They're not what they used to be. Be open-minded to fixed income again. Almost a whole generation has passed since fixed income investments were attractive. Their risk/return profile is looking good, so keep an eye on them. There are some particularly impressive opportunities right now in hybrid-style investments, so explore your options there. And if you're not exposed to alternatives, at least learn how they could reduce the risk and increase the return of your overall portfolio.

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It's a lesser-understood area of investments so ensure you speak with someone with knowledge and experience in this area. And when all is said and done – make sure you're properly diversified! That doesn't mean that you have "a lot" of positions in your portfolio, it means that you have the "right" positions in your portfolio.

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Lynn MacNeil, F.PL., CIM®, is an Associate Portfolio Manager and Financial Planner with Richardson Wealth Limited in Montreal, with over 27 years of experience working with retirees and pre-retirees. For a second opinion, private financial consultation, or more information on this topic or on any other investment or financial matter, please contact Lynn MacNeil at 514.981.5796 or Lynn.MacNeil@RichardsonWealth.com. Or visit our website at www.EphtimiosMacNeil.com.