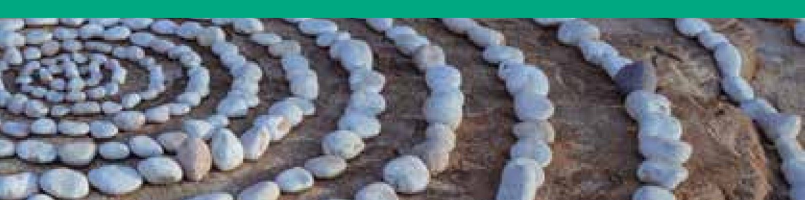
THE ANALYST

CFA Society Toronto

March 2017

WONDER WOMEN:
CFA charterholders on Bay Street

INVESTMENTS THAT HAVE AN IMPACT



DOES YOUR COMPANY HAVE A SUCCESSION PLAN?

PM # 43003032

Setting a higher standard for the Toronto investment community

March 2017
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THE CEILING DOESN'T STOP WITH WOMEN

Last year, in our diversity and inclusion issue, I addressed the women in the room—or rather, the lack of women in the boardroom. And while this is an important issue—after all, the glass ceiling is still firmly installed in many business environments—questions around diversity and inclusion are, of course, not limited to gender issues.

I'm thinking about the LGBT community. Here in Ontario, a 2010 survey by the Trans PULSE Project showed that, out of just over 400 transgender respondents, 18 percent said they'd been turned down for a job because of being trans, and 13 percent said they'd been fired.

Not encouraging statistics, but society is taking positive steps. Think Caitlyn Jenner or the TV comedy-drama *Transparent*, for example. And don't forget our own Bill C-16 (currently in its second reading), which will amend the Canadian Human Rights Act to add gender identity and gender expression to the list of prohibited grounds of discrimination.

In the business world, OUTstanding (an LGBT professional network) and the *Financial Times* produce a list of the top 100 LGBT executives each year. At the top of the list for 2016 was Gigi Chao, executive vice-chairman of Cheuk Nang Holdings Ltd. Vocal in her fight for LGBT rights, Chao rejected her father's attempt to find her a husband; her father had offered $65 million to any man who would marry her. Martine Rothblatt, founder of Sirius XM satellite radio and now chief executive of United Therapeutics Corp., was No. 4. Rothblatt is transgender.

While some execs have broken the LGBT ceiling, it hasn't been smooth sailing for all emerging business leaders. According to the U.S.-based LGBT advocacy group Reaching Out MBA (ROMBA), 50 percent to 80 percent of LGBT individuals in business school return to the closet when they begin working. Either they're not comfortable or they're worried their careers will be sidelined, particularly if they're targeting the C-suite.

As depressing as that is, there is hope through mentoring and leader development. In 2015, the Rotman School of Business became the first Canadian school to formally partner with ROMBA. As part of its commitment, Rotman created two new fellowships for Rotman students (each individual receives a minimum $10,000 scholarship per academic year, or a total scholarship of $20,000), as well as access to exclusive mentorship and leadership development programming through Reaching Out.

It's a good start.

MARCH 8 MARKS INTERNATIONAL WOMEN'S DAY, and from March to May we'll be celebrating and reflecting on all the progress women, and other under-represented groups, have made—not only in our local financial community but internationally—across disciplines, industries, and cultures. CFA Society Toronto has proudly held its position as a champion of positive change since its establishment in 1936, when it was founded on the principle of supporting the professional development and advancement of CFA charterholders, free of discrimination and biases. Our efforts to build a fair and flexible investment culture—and to challenge conscious and unconscious biases—is not just limited to a day, month, or time of year. It's an ongoing commitment.

Some of the Society's initiatives include the Alpha Project, a gender diversity initiative that pairs mentors, both female and male, from senior financial backgrounds with female protégés. On January 18, the Society hosted its last series of luncheons for the Alpha Project. The project came to be in 2015, after Marg Franklin, one of our most senior and celebrated volunteers, was awarded the Alfred C. "Pete" Morley Distinguished Service Award. She used the reward money to put together and fully fund a project to help young up-and-coming women in the financial industry gain access to the networks required to strengthen their skills by providing the mentorship of seasoned practitioners in our membership. Society mentors work with their protégées for 18 months, and, since the launch of the project, many of the project's protégées have applied the skills they've learned either to take on new opportunities or to advance in their professions. We're currently in the process of creating metrics to document and quantify the efforts of this unique project, and hope to see its continuation and cross-Society adaptation.

Additionally, on September 18 and 19, we'll host CFA Institute's 2017 Alpha and Gender Diversity Conference at the Westin Harbour Castle. The conference is part of CFA Institute's Women in Investment Management Initiative, an ongoing effort to build the business case for diversity in the investment profession. The initiative's goals are to increase the number of women joining the financial profession, to retain women in the profession, and to influence culture from within.

So why is diversity and inclusion—whether gender or cultural—important? What does it mean to investors and the overall financial community? Well, by working in teams reflective of our diverse community, we can, ultimately, understand and serve our clients better. Furthermore, studies have found that diversity helps promote strategic decision-making by bringing in different ideas and exposing organizations to greater opportunities.

These are just a couple of examples of the benefits of diversity and inclusion in the workforce. Visit CFA Institute's website, or connect with the Society, to find more information on upcoming initiatives and how you can get involved.

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THE NEW YEAR WAS KICKED OFF WITH A ROAR at the Society as our staff and volunteers planned and executed a lineup of superb events and initiatives. For many of us, our resolutions include new career goals, as we recognize the competitive environment in which we operate. In response, our staff and volunteers are developing programs designed to provide you, our members, with the tools and knowledge required to gain and maintain that competitive edge. For example, programs such as Career Advice From Recruitment Experts on January 24, and Career Chat – Innovation in Wealth Management on February 15—both sold-out events—provided insights from the investment community's top recruiters and employers on industry trends and how to seek career opportunities strategically, while leveraging the CFA designation as a differentiator.

On January 31, we hosted our 2017 Mentorship/Protégé Reception. Our Mentorship Program, now 10 years old, was developed in 2007 to help members build access to professional networks and gain expertise—critical components for their professional development. Since the program's inception, we've successfully paired up more than 300 mentors and protégés. The program bridges the gap between new and experienced charterholders, where both parties benefit: the protégé from the experienced practitioner's knowledge, and the veteran from the new member's challenges and the talents he or she brings to the industry. Overall, by sharing knowledge with each other and demonstrating high ethical practices, we can ensure future generations of successful leaders while promoting a healthy, long-term investment community.

This year, our Local Ethics Challenge has advanced to become a nationwide competition. Over the next few months, local Societies will host their own events, and each local winning team will advance to the inaugural 2017 Canadian Ethics Challenge, to be held here in Toronto on June 1. This initiative, spearheaded by Toronto volunteers in 2014, was designed to promote the importance and understanding of incorporating high ethical standards into our daily investment practices. It also serves as a vehicle to develop stronger relationships with key academic institutions and future industry leaders. On January 19, we were pleased to announce the Smith School of Business at Queen's University as our Local Ethics Challenge champion. They will represent our Society at the nationals.

I'd also like to congratulate all of our new 2016 CFA charterholders. Last year, we welcomed more than 600 into our Society and, on February 9, I had the pleasure of celebrating this momentous occasion with them and their guests at our CFA Charter Recognition event.

Finally, your membership experience remains our top priority, and we value your feedback. If you have any suggestions on how we can better serve the Society, or if you have any questions or concerns about any of our past or upcoming initiatives, please don't hesitate to connect with us.

THE FINDS OF MARCH

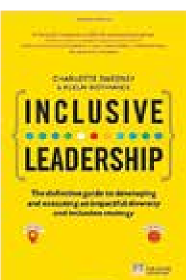
Beware the ides this month, and take time to enjoy these titles from **Books for Business**'s Brenda Bickram.

Inclusive Leadership: The Definitive Guide to Developing and Executing an Impactful Diversity and Inclusion Strategy: Locally and Globally

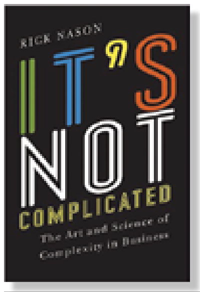
Charlotte Sweeney and Fleur Bothwick

FT Press, November 2016, $43.99

The most successful organizations are those with the most diverse and engaged workforces. Studies show an 80 percent improvement in business performance among those organizations with high diversity levels. When people feel included and able to reach their full potential, they're more engaged, more productive, and often more creative.



Inclusive Leadership will help you drive culture change using organizational development principles. It takes you through the key components of leading change throughout the employee lifecycle and your supply chain, and through product development. Crucially, it will help you make a genuine impact on your business through your people, both now and in the future.



It's Not Complicated: The Art and Science of Complexity in Business

Richard Ronald Nason

Rotman-UTP Publishing, May 2017, $32.95

In the new knowledge economy, traditional modes of thinking are no longer effective. Compartmentalizing problems and solutions and assuming everything can be solved with the right formula can no longer keep pace with the radical changes occurring daily in the modern business world.

It's Not Complicated offers a paradigm shift for business professionals looking for simplified solutions to complex problems. Richard Ronald Nason introduces the principles of "complexity thinking," which empower managers to understand, correlate, and explain a diverse range of business phenomena—for example, why some new products go viral while others remain unnoticed, how office cliques develop despite collaborative work policies and spaces, and how economic bubbles form. Rather than consider complicated and complex as interchangeable terms, Nason explains what complexity is and how it arises, and the errors in solving complex situations with complicated thinking.

Gen Z @ Work: How the Next Generation Is Transforming the Workplace

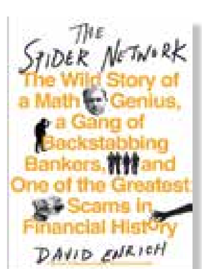
David Stillman and Jonah Stillman

Harper Business, March 2017, $35.99

A generations expert and author of *When Generations Collide* and *The M-Factor* teams up with his 17-year-old son to introduce the next influential demographic group to join the workforce: Generation Z.

Based on the first national studies of Gen Z's workplace attitudes; interviews with hundreds of CEOs, celebrities, and thought leaders on generational issues; cutting-edge case studies; and insights from Gen Zers themselves, *Gen Z @ Work* offers the knowledge today's leaders need to get ahead of the next gaps in the workplace and how best to recruit, retain, motivate, and manage Gen Zers.

The Spider Network: The Wild Story of a Math Genius, a Gang of Backstabbing Bankers and One of the Greatest Scams in Financial History



David Enrich

HarperCollins, March 2017, $36.99

The Wall Street Journal's award-winning business reporter unveils the bizarre and sinister story of how a math genius named Tom Hayes, a handful of outrageous confederates, and a deeply corrupt banking system ignited one of the greatest financial scandals in history.

In 2006, an oddball group of bankers, traders, and brokers from some of the world's largest financial institutions made a startling realization: Libor—the London interbank offered rate, which determines the interest rates on trillions in loans worldwide—was set daily by a small group of easily manipulated functionaries, and they could reap huge profits by nudging it to suit their trading portfolios. Hayes, a brilliant but troubled mathematician, became the lynchpin of a wild alliance. Eventually known as the Spider Network, Hayes's circle generated untold riches—until it all unravelled in spectacularly vicious, backstabbing fashion.

The Spider Network is not only a rollicking account of the scam but also a provocative examination of a financial system that was crooked throughout, designed to promote envelope-pushing behaviour while shielding higher-ups from the consequences of their subordinates' rapacious actions.

The Thoughtful Leader: A Model of Integrative Leadership

Jim Fisher

Rotman-UTP Publishing, July 2016, $32.95

Leadership is a quality that's difficult to define. Some believe it's innate, the gift of a selected few. Others believe it's a skill that can be learned but don't agree on what, exactly, should be taught.

Jim Fisher has incorporated various apparently opposing leadership ideas into an integrated model. In order to successfully meet the challenges of a fast-changing world, leaders can no longer choose between managing, directing, or engaging. The thoughtful leader is someone who simultaneously, consistently, and coherently manages, directs, and engages their followers. The framework provides a way for anyone who is motivated to lead, has the courage to act, and is willing to think about their actions to become more effective.

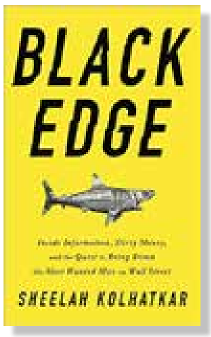
Making Monte Carlo: A History of Speculation and Spectacle

Mark Braude

Simon & Schuster, April 2017, $23.00 (now in paperback)

Monte Carlo has long been known as a dazzling playground for the rich and famous. Less well known are the shrewd and often ruthless strategies that went into creating such a potent symbol of luxury and cosmopolitan glamour. As historian Mark Braude reveals, the world's first modern casino-resort started as an unlikely prospect—with the legalization of gambling in tiny Monaco in 1855—and eventually emerged as the most glamorous gambling destination of the Victorian era. The resort declined in the wake of WWI and was reinvented, again, to suit the styles and desires of the new Jazz Age tastemakers, such as F. Scott and Zelda Fitzgerald, Gerald and Sarah Murphy, and Coco Chanel.

A rollercoaster history of how a small rural town grew into the prosperous resort epicentre of the late 19th century and rose again to greatness out of the ashes of WWI, *Making Monte Carlo* is a classic rags-to-riches tale.



Black Edge: Inside Information, Dirty Money, and the Quest to Bring Down the Most Wanted Man on Wall Street

Sheelah Kolhatkar

Random House, February 2017, $37.00

Black Edge offers a revelatory look at the grey zone in which so much of Wall Street functions. It's a riveting, true-life legal thriller that takes readers inside the government's pursuit of Steven A. Cohen and his employees, and raises urgent and troubling questions about the power and wealth of those who sit at the pinnacle of modern Wall Street.

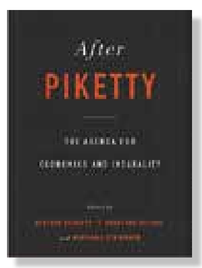
Cohen changed Wall Street. He and his fellow pioneers made their billions through speculation, by placing bets in the market that turned out to be right more often than wrong—and for this, they gained not only extreme personal wealth but also formidable influence throughout society.

Cohen was one of the industry's biggest success stories, the person everyone else in the business wanted to be. On Wall Street, Cohen was revered as a genius: one of the greatest traders who ever lived.

That image was shattered when SAC Capital became the target of a sprawling seven-year investigation, led by a determined group of FBI agents, prosecutors, and SEC enforcement attorneys. SAC Capital was indicted and pleaded guilty to charges of securities and wire fraud in connection with a vast insider trading scheme, even as Cohen himself was never charged.

After Piketty: The Agenda for Economics and Inequality

Heather Boushey, J. Bradford DeLong and Marshall Steinbaum



Harvard University Press, May 2017, $47.50

Thomas Piketty's *Capital in the Twenty-First Century* is the most widely discussed work of economics in recent history, selling millions of copies in dozens of languages.

But are its analyses of inequality and economic growth on target? Where should researchers go from here in exploring the ideas Piketty pushed to the forefront of global conversation?

A cast of economists and other social scientists tackles these questions in dialogue with Piketty, in what is sure to be a much-debated book in its own right.

After Piketty opens with a discussion by Arthur Goldhammer, the book's translator, of the reasons for *Capital*'s phenomenal success, followed by the published reviews of Nobel laureates Paul Krugman and Robert Solow. The rest of the book is devoted to newly commissioned essays that interrogate Piketty's arguments. Suresh Naidu and other contributors ask whether Piketty said enough about power, slavery, and the complex nature of capital. Laura Tyson and Michael Spence consider the impact of technology on inequality. Heather Boushey, Branko Milanovic, and others consider topics ranging from gender to trends in the global south. Emmanuel Saez lays out an agenda for future research on inequality, while a variety of essayists examine the book's implications for the social sciences more broadly. Piketty replies to these questions in a substantial concluding chapter.

After Piketty does not shy away from the seemingly intractable problems that made *Capital in the Twenty-First Century* so compelling for so many.

Brenda Bickram is the manager responsible for special orders and corporate sales at Books for Business online store.

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WOMEN WARRIORS ON BAY

Five women open up about careers, mentors, and myths about females in capital markets.

Camilla Sutton, CFA

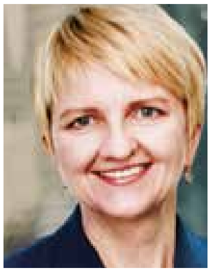
To mark International Women's Day, *The Analyst* is proud to profile five impressive Bay Street CFA charterholders. These women, all awarded their charters at various points over the last three decades, talked with us about their careers, mentors, and advice, and about what's critical in delivering on the industry's goals for diversity. We learned that there are many myths about women in capital markets, and that much has changed over 30 years, but the exceptional quality, intelligence, and dedication these women bring to their clients, firms, and the industry has been impressive, and unwavering.

Deborah Leckman, commissioner and director, Ontario Securities Commission, CFA 1990

A range of experience like Deborah Leckman's is rare; in the past, she has both run global equities at a major Canadian pension plan, and headed a Canadian bank's retail sell-side investment research group. Currently, she serves as an OSC commissioner—a role she describes as the highlight of her career, mainly because it "is a tremendous challenge to balance investor protection issues and maintain vibrant and healthy capital markets given how quickly the industry is evolving." Her experiences have enabled her to bring tremendous perspective to how she views regulatory oversight and policy-making, which, in turn, serves the entire industry.

Leckman's advice to those early in their careers is to have "a desire to continually learn, an openness to ideas that are different than your own, a sense of humility, and the ability to not take yourself too seriously." The best advice she herself ever received was to understand the importance of her own integrity and reputation—something she has done very well at.

Leckman recognizes that, when it comes to delivering on the industry's goals for diversity, many steps are needed to add up to significant change. These steps include finding ways to encourage girls to consider careers in the investment industry, having more women in decision-making roles in portfolio management and research, and gaining a better understanding of why women self-select out of the industry, so that change can take place.



Dagmara Fijalkowski, head, global fixed income and currencies, RBC Global Asset Management, CFA 1997

In November 2016, Dagmara Fijalkowski was appointed to RBC Global Asset Management's most senior decision-making group: the executive committee. In its announcement, the firm highlighted that it would "benefit from her energy and clear view," and praised her long-standing commitment to being a champion of change.

Fijalkowski's success is rooted in her knowledge, commitment, and drive. One of the characteristics she likes most about the financial industry is how one is able to measure success through performance. She is also excited by "the challenge of figuring out what lies ahead."

To date, Fijalkowski's career highlight has been managing the fixed income and currencies teams. She has found leading people to be incredibly rewarding; in part because it requires one to think ahead and focus on removing potential road blocks to people's peak performance.

When it comes to critical next steps for delivering on the industry's diversity goals, she suggests that diversity attracts diversity. "It's up to those of us already in the industry to become active ambassadors for our profession," she says.

Jaqui Parchment, senior partner, Toronto office leader, Mercer Canada, CFA 2000

Jaqui Parchment has built an impressive career on Bay Street, where she leads a large team and is a driving force behind securing the financial well-being of her clients. One of the most influential people in her life has been her mother, from whom she learned the importance of approaching a career with courage and resiliency, and how to balance being a firm but caring leader.

What advice does she have? It's about delegation, Parchment says. "Effective delegation allows you to have personal career success and balance at the same time, and it allows you to mentor and groom others for success."

Parchment has firm views on how to deliver on the finance industry's diversity goals. The industry needs "leaders who passionately believe diversity is a business imperative and recognize the power of data and analytical tools," she says. "Mercer research shows that leaders who are willing to personally engage and promote diversity have a greater impact than those who are trying to meet quotas or check the box."

Marian Hoffmann,
portfolio manager,
Sionna Investment Managers, CFA 2006

Marian Hoffman finds her role as a portfolio manager rewarding for both the client work and the continuous learning, which includes meeting business leaders who inspire and deliver on critical business models. Part of Hoffman's success has been due to her philosophy of having strong convictions, weakly held, allowing her to take decisive action on good ideas, but not leaving her too boxed in if underlying facts shift.

Hoffman has spent most of her career at Sionna, a company built around the belief that diversity in perspective, experience, gender, education, and background leads to stronger results. She speaks highly of her work environment and its culture of diversity, and encourages those who are starting out in the industry to be curious and ask boundless questions. She also notes the significant influence her husband and parents have had on her and the critical role mentors have played, particularly when they've questioned and challenged her.

Eileen Jurczak,
director, trading products,
BMO Capital Markets, CFA 2013

Eileen Jurczak is breaking myths and educating a whole generation of young women on the capital markets industry, all while achieving success in her day job.

To start with the myths, when I ask her what she finds most rewarding in capital markets she says "the culture" and then elaborates that "trading products fosters an entrepreneurial atmosphere, with a balance between autonomy and teamwork that allows each employee to add value while developing skills and leadership abilities."

Jurczak is making big contributions to education, a critical component of driving the industry's diversity goals. In 2015, she successfully started Bay Street Deconstructed, a not-for-profit organization that provides an interactive educational program on Bay Street and capital markets for Grade 10 students.

As for best advice she's received in her career? "Focus on skills, not your job title, and be open to different career opportunities that develop your skills."

Camilla Sutton, CFA, is managing director and global head, foreign exchange, with Scotiabank.

International Women's Day is March 8, 2017

CFA Society Toronto

TO BUY OR RENT

A leading analyst offers advice on one of life's most important financial and investment decisions.

Rossa O'Reilly, CFA

Alex Avery CFA, a long-standing member of CFA Society Toronto, is a managing director and real estate analyst at CIBC World Markets. He has recently published a book, on the role that housing plays in people's financial planning and investment decision-making, that has risen to the Canadian national bestseller lists. *The Wealthy Renter* (Dundurn Press, 2016) offers an unbiased analysis of the biggest investment most people will ever make: their housing. Public debate on the own-versus-rent question tends to be dominated by powerful pro-ownership biases that exist among many commentators on the topic, including real estate brokers, mortgage lenders, and financial planners. Avery's book brings balance to the public debate and, through rigorous analysis of both financial and behavioural considerations, puts the topic in the context of thoughtful and prudent financial planning and investment decision-making. The book presents sound advice to people who are thinking of buying a house, or who are planning their financial future. *The Analyst* interviewed him about his book.

How would you summarize the analysis and advice in *The Wealthy Renter?*

The book challenges conventional wisdom about Canadian housing. Its goal is to debunk common misconceptions, including the fallacies that renting is throwing away your money, that home ownership has provided better returns than other common investments, and that home ownership is the best and only practical path to wealth. It explores the financial and non-financial benefits provided by renting, looks at the current state of the Canadian housing market and what really drives housing markets, and helps Canadians better understand housing as an investment and as a lifestyle choice.

What prompted you to write the book?

More than a decade ago, I began writing down my findings from everyday conversations I had with friends and strangers alike about housing. Over the years, what emerged was a clear picture of home ownership as a heavily subsidized, mass-marketed lifestyle choice, promoted on a nearly universal basis by everyone from parents, friends, and neighbours to lenders, brokers, and the government. I decided to publish the book now because of the risks associated with the current state of the Canadian housing market, including record-low interest rates, record-high price-to-income ratios in certain markets, and record-high debt levels among Canadians. Right now is the most important time for Canadians to know as much as possible about housing to ensure they don't receive and act on bad, biased advice.

Should your analysis be undertaken by financial advisors and individuals? If so, how should they conduct it?

The Wealthy Renter includes simple, quick exercises to help readers understand the true costs of housing and how housing fits into their financial situations. Financial advisors are well positioned to help their clients better understand housing, which, in most cases, represents Canadians' largest single investment. Since homes are the largest, and typically most leveraged, investment most Canadians will ever make, gaining a better understanding of the housing market is likely to be the most important factor in personal financial success.

What kind of long-term relative returns have house prices in Toronto generated compared with the stock market?

Contrary to popular belief, house prices in Toronto have not outpaced the stock market, as represented by the S&P/TSX Composite Index. Over the past 25 years, Toronto home prices have delivered a compound annual return of just 2.9 percent, versus a return on the S&P/TSX Composite Index of 8.0 percent (taking into account standard transaction costs of 5 percent for homes; a very conservative 1 percent combined cost for annual property taxes and maintenance; and standard equity transaction costs). This represents a 5.1 percent (510 basis point) annual average difference in favour of the stock market.

What do the numbers look like over different time periods?

Even cherry-picking the time frame for the most flattering comparison—which turns out to be the 20 years since the end of 1995—Toronto homes delivered 5.2 percent annually, on average, over the 20-year period, while the TSX delivered 7.4 percent. Much of the belief in high home price performance is more likely associated with the high leverage used to finance homes and the forced savings of monthly mortgage payments. However, high leverage also brings increased exposure to declines in house prices.

How is the comparison affected by taking into account the cost of renting?

Using the Toronto Real Estate Board's current average house price of $706,000, and the Canada Mortgage and Housing Corporation's [CMHC] current average two-bedroom unit rent of $1,325 per month, the average annual return on stock market investment would be reduced by 2.25 percent (225 bps) going forward, still leaving a 2.85 percent (285 bps) differential in favour of renting, based on the past 25 years' relative returns.

Should the involvement of foreign investors in Canadian real estate be factored into people's thinking about future housing prices today?

The influence of foreign investors is easy to see and understand but hard to prove and measure. Homes are no different from virtually every other asset class in the world, and as low interest rates have pushed the valuations of many assets around the world higher over the last several years, home prices in the internationally attractive cities of Vancouver and Toronto were further boosted by land constraints and one of the most open immigration stances in the world (one of Canada's greatest assets).

What house price return can Canadians expect in the future in light of demographics, the recent housing price boom, and the tightening regulations on mortgage lending?

I won't give you a single number, or even a range. But, if Canadian house prices compounded at just 3.7 percent over the past 25-year period—in which Government of Canada 10-year bond yields dropped from over 10 percent to barely over 1 percent, average price to income rose from four to seven times, and Canadian household debt as a percentage of income rose from 70 percent to 170 percent—I'm inclined to think it could be lower than 3.7 percent.

That doesn't sound encouraging, for either the future or the past. Yet most Canadians continue to choose home ownership over renting. Why?

I think it's equal parts the broad-based promotion of home ownership and the success of its forced savings element. The promotion of home ownership is often inaccurate or includes intuitive, difficult-to-understand representations of returns, such as "I bought in 1990 for $100,000, and today it's worth $300,000," which sounds very good but is actually a compound annual growth rate of only 4.5 percent. Promotions include TV shows about all aspects of home ownership, government incentives like subsidized borrowing rates via CMHC, and tax incentives such as capital gains exemptions, land transfer tax rebates, and RRSP homebuyer plans. Forced savings programs, like the one built into home ownership through mortgage payments, are a critical tool for personal financial planning, providing a path to wealth not reliant on self-discipline. Fortunately, as discussed in *The Wealthy Renter,* there are several alternative investment plans, such as employer share loans, employer RRSP matching programs, Government of Canada bond purchase programs, automatic payroll deductions, and premium term life insurance policies, that also offer forced saving and can deliver potentially superior returns.

Your book discusses some of the behavioural effects of home ownership.

Yes. Owning a home with a substantial mortgage can limit mobility in the job market, as it can be financially costly to sell a house in an area of high unemployment to move to a region that offers better job prospects. It can be a source of additional worry and concern to families during times of economic recession and falling house prices. Homeowners often succumb to the desire to make costly renovations and improvements, justifying them as an investment, when they're really more of a consumption item. Home ownership can also be inflexible and costly as people's needs change in life. Young families often extend themselves financially to buy houses that can accommodate their future family requirements, but are too big for their near-term needs. Later in life, empty nesters often maintain their overly large dwellings due to the complications and costs of selling a house.

What was your motivation and experience as a CFA in writing the book while continuing to be a real estate equities analyst at a chartered bank that provides a substantial percentage of the residential mortgage loans made in Canada?

On the surface, there might seem to be a contradiction between promoting the virtues of renting and offering Canadians mortgages, but the underlying message and goal of the book is to help Canadians make good decisions about housing and promote a healthy housing market. Those are goals all Canadians can support!

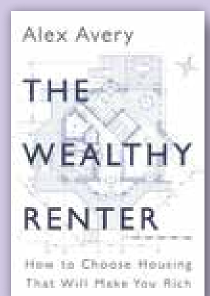
How has your role as a bestselling author affected your professional career? Should we all think outside the box sometimes about how we use our professional skills and knowledge as CFAs?

Researching and writing *The Wealthy Renter* has broadened and deepened my understanding and appreciation of the importance of the housing market to the Canadian economy. The book is also an interesting channel through which to connect with a much broader audience than institutional equity research reaches.

What's the most important thing you hope readers will take away from the book?

Advice on housing is very heavily biased by parties who have incentives to see more homeowners. The best defence against biased advice is knowledge. I hope *The Wealthy Renter* helps Canadians make the best housing decisions for their own needs and wants, with the best understanding of the implications of those decisions.

Rossa O'Reilly, CFA, is a past chair of CFA Institute and a former managing director, institutional equities research, with CIBC World Markets.



CFA Society Toronto members can receive a 20 percent discount on *The Wealthy Renter* (ISBN: 9781459736467) until May 31, 2017. Promo code: WRFA.

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MAKING AN IMPACT

Think investing is only a force for profit? Think again. It's also a force for good.

Vanja Perić, CFA

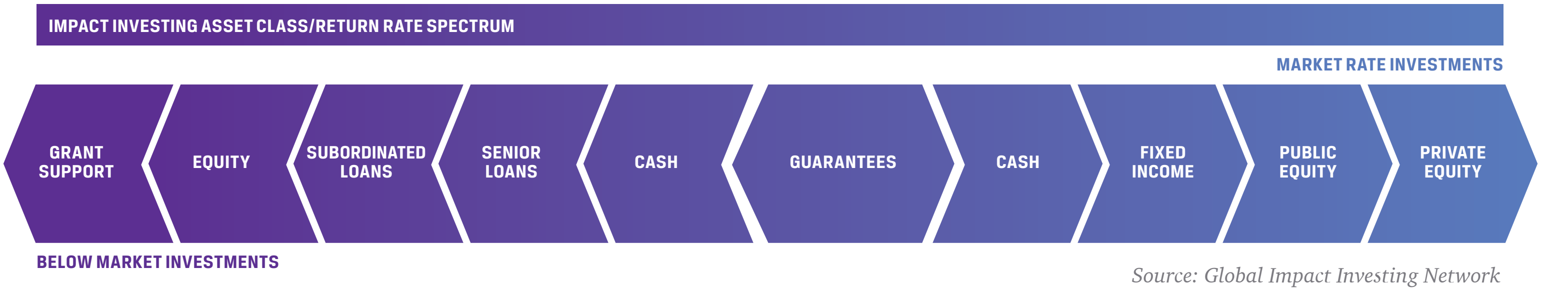
Investing is about returns, but it doesn't have to be about returns only. Consider impact investing, which has been referred to as "investing with purpose." Impact investing marries financial profit with social and environmental benefit, while impact investors seek to align their investments and their values, but not through philanthropy. They're investors, first and foremost, who believe financial profit and social progress aren't mutually exclusive. Impact investments are profit-seeking investments made in companies that have the power to make a social or environmental change for the better.

But don't get impact investing confused with socially responsible investing (SRI)—SRI strategies apply a number of negative and positive screens to a list of publicly traded companies. They're generally passive, and adopt a "do no harm" approach by excluding investments such as tobacco, alcohol, and firearms. Impact investing strategies actively seek investments with potential to create a positive social or environmental impact. In addition to their main objective, these strategies take into account the environmental, social, and governance (ESG) characteristics of the target company's business operations.

While the term "impact investing" has gained broader recognition recently, it has been in practice for some time, in various forms. Government-funded development finance institutions such as the International Finance Corp. (IFC)—the private investment arm of the World Bank—have been making impact investments, primarily through private equity and debt, in developing countries since the 1960s. Foundations have also been early adopters. Impact investing strategies have provided foundations with the opportunity to align their investment capital with their philanthropic objectives, and increase their overall impact.

The field of impact investing is no longer sitting on the fringes of investment management. It's growing across the globe, and quickly. At the end of 2015, the global impact investment market was worth at least US$77 billion,[1] with some experts estimating this figure could grow to US$500 billion[2] in the next few years. There is momentum. Globally, many of the largest asset managers and advisors have entered the impact investment market, recognizing the changing preferences of investors. Today, impact investing attracts a wide range of investors, both individual and institutional. David Chen, program director of impact investing at the Kellogg School of Management at Northwestern University in Illinois, noted the following in a recent interview with *Kellogg Insight:* "We're finding that mainstream investment firms are responding to two primary catalysts. Their clients are looking for impact investing strategies. You have one group of investors asking for impact products who tend to think, 'My money should do more than bring returns.' Then you have institutional investors who have a slightly different focus. They are thinking about sustainability affected by global demographics, resource consumption, asset productivity, and climate change. Institutions examine their portfolios from a risk management standpoint."[3]

One of the concerns around impact investing is the perception that it's not profitable. However, the data suggest otherwise. Of the world's leading impact investors surveyed in the Annual Impact Investor Survey, conducted by JP Morgan and the Global Impact Investing Network, 90 percent of respondents said financial performance of their investments was in line with or above expectations. It's important to remember that, just like conventional investments, impact investing encompasses a broad universe of approaches, asset classes, and products providing a range of returns.



Source: Global Impact Investing Network

While millennials are often discussed as influencers of the future of finance, another demographic that's not mentioned as often, but also will have a significant impact, is women. According to the Responsible Investment Association's report "Millennials, Women, and the Future of Responsible Investment," millennials and women are increasingly important demographics for Canada's investment industry and drivers of demand for responsible investments that incorporate ESG criteria. A Bank of America study found that two-thirds of millennial investors (double their baby boomer counterparts) saw their investments as an expression of their values.

By all indications, impact investing is still in its infancy. The need for impact investment expertise is growing, and CFA charterholders have an opportunity to lead the way. Adam Camenzuli, CFA, and member of CFA Society Toronto, has seized the opportunity. He is the executive director of KARIBU Solar Power, a social enterprise that designs, manufactures, and distributes solar-powered "hockey pucks" for off-grid communities in Tanzania. KARIBU's product is an income-producing asset for an entrepreneur (just like a chicken or goat) but also an affordable way to buy light (and electricity for cellphone charging) for end consumers. The company reduces CO_2 emissions, saves families money, increases study time for children, and cuts toxic kerosene smoke from the home. *The Analyst* spoke with Camenzuli about this growing field.

How did you become involved in social entrepreneurship?

My interest started in my last year of studies at York University. A few friends and I submitted an idea to the Harvard Social Enterprise Conference; we ended up winning the Audience Choice Award and third place. I also lived in Tanzania, working with street youth in 2010 and 2011, and saw the need for solar power.

What skills can a CFA charterholder contribute to the success of a social enterprise? How did the knowledge you gained through the CFA program help you in building the business?

In my experience, many people who start a social enterprise lack an understanding of how business and finance works. Quantitative skills are super important in running a data-driven business, which is where social enterprise is going. I used the accounting knowledge I gained in doing the bookkeeping. Also, the corporate finance portion was very helpful when we were raising capital for the business.

How have investors reacted to social enterprises? How difficult or easy is it to raise capital?

People are interested and excited to invest in social enterprises. Our problem was that the amount of money we needed to get started was a lot smaller than what investors were looking to invest. It was extremely difficult to raise the initial capital, but we were confident in our product and kept pushing. The end result was positive, and we were very fortunate to get a great group of supportive investors.

There's a myth that social enterprises don't make a profit and investors are basically "donating" their money to a social cause. What has been your experience?

That can be the case for a lot of enterprises, but what any enterprise does is solve a problem. Social enterprise happens to solve a social problem. For those who truly combine the efficiency of business with the impact of charity, social enterprise can truly be a force for good. What better use of one's money is there?

Vanja Perić, CFA, is an investment consultant in Toronto.

1 *Global Impact Investment Network, Annual Impact Investor Survey 2016*

2 *Monitor Institute, "Investing for Social & Environmental Impact"*

3 *Kellogg Insight (the publication of the Kellogg School of Management): https://insight.kellogg.northwestern.edu/article/what-is-the-future-of-impact-investing*

VOLUNTEER SPOTLIGHT

KEVIN VEENSTRA, CPA, CFA

Kevin Veenstra was very busy this past January getting trained by CFA Institute to facilitate its ethical decision-making interactive presentation. Soon after completing the training, he volunteered to present at the 2017 Canadian Ethics Challenge: Local Competition on January 19. In March, Kevin will begin presenting to universities across Ontario. CFA Society Toronto would like to thank Kevin for his hard work as a volunteer with the Society's finance committee and now as a volunteer outreach representative.

Kevin Veenstra is a chartered professional accountant (Ontario) and a CFA charterholder. He earned his CA/CMA designations while working in the audit practice at Ernst & Young LLP (Kitchener). Subsequent to leaving Ernst & Young LLP, he worked in the internal audit department at Walmart Canada and in the corporate accounting department at Canadian Tire. Kevin earned his PhD in accounting at the Rotman School of Management (University of Toronto) in 2013. Currently, he is an assistant professor of accounting at DeGroote School of Business (McMaster University). His research interests, broadly speaking, encompass the impact of social and cultural influences on decision-making and financial performance. He also serves as a volunteer on CFA Society Toronto's finance committee.

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TORONTO INVESTMENT ANALYSTS ROUNDTABLE

Got a stock pitch or a market update? Share it at the TIAR.

James Barry, CFA

CFA candidates must command a wide range of knowledge to earn their charters, ensuring that new members will be able to add value in a diverse range of jobs throughout the finance industry. Although a large number of CFA charterholders work directly in equities, many choose a different focus while still maintaining a keen interest in equity markets—and in individual securities.

The Toronto Investment Analysts Roundtable (TIAR) was founded in September 2014 by members of CFA Society Toronto to create a forum for charterholders to meet and discuss equity markets and individual investment ideas. Although the group is predominantly composed of members working directly in equities, research, and portfolio management, it's open to Toronto CFA members interested in networking, enhancing their stock-pitching skills, and exchanging investment ideas. All TIAR members share the same passion for capital markets and investing.

TIAR meetings are held twice every month, with a typical attendance of about 12 to 18 individuals, and sessions alternate between industry speaker presentations and stock pitches. Industry speakers are invited to share their experiences working in equities or investment management to give members insight into potential career paths and emerging industry trends. At a recent meeting on Nov. 28, for example, Dale Powell from Citi Private Bank spoke about his 30-plus-year investment career, which has focused primarily on asset allocation and portfolio construction. It was a broad-based discussion, but centred on those ultra-high net worth individuals who can generate significant revenue for a wealth management platform, but who also require deeper expertise and a wider array of services.

"Although the group is predominantly composed of members working directly in equities, research, and portfolio management, it's open to Toronto CFA members interested in networking, enhancing their stock-picking skills, and exchanging investment ideas."

Stock-pitch sessions begin with a general market update, covering some of the key recent developments. A volunteer is appointed ahead of time to prepare a short presentation that will lead discussion. The session structure is fairly informal, and other members are invited to contribute and challenge prevailing views. A recent meeting on December 12 for instance, was focused on small cap outperformance, OPEC's new production quota, and seasonal trends in historical equity market performance. After a brief review of the recent performance of global indices, commodities, bonds, and currencies, the focus then turned to economic data due to be released in the coming weeks and to other notable items the group is watching.

After the market update, a member is invited to present a stock pitch for the group to review. The scope is very comprehensive, but the purpose is simple: Should this investment be included in a simulated portfolio managed by TIAR? Each pitch requires an extensive amount of research, but members have flexibility to choose their investment idea, which can be either a long or a short equity position.

The December 12 pitch was a long position in Home Depot. In addition to presenting the customary business overview of the company and valuation work (a discounted cash flow was performed), the member focused on four key fundamental drivers: nascent e-commerce business, an opportunity to expand to non-traditional customers (professionals), the company's recent data breach in 2014, and the broader recovery taking place in the U.S. economy. When a presentation is over, other members are encouraged to challenge the pitch before the group votes on whether or not to include it in the portfolio. (In this instance, the group decided to add Home Depot to the portfolio, with a 10 percent allocation.)

If you're looking to discuss individual equity investments and economic events and develop skills in research and analysis, TIAR presents a great opportunity to do so. If you wish to participate in future meetings or are interested in presenting an investment idea, discussing a financial topic, or providing a market update, RSVP to TOINVAR@gmail.com to confirm your attendance.

James Barry, CFA, is an associate at ECN Capital Corp.


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DEPARTURES

Will your investment management practice survive when you leave the firm?

Lisa Hui

The Analyst interviewed Eric Leeper, vice-president of research and analysis at FP Transitions, to find out.

What is FP Transitions, and what is your role at the firm?

FP Transitions provides equity management, valuation, and succession planning services for the financial services industry in North America. Based in Oregon, the 30-plus person firm supports the annual transition of more than $20 billion in assets from current business owners and founders to next-generation advisors. I currently oversee new product development, financial modelling, and benchmarking, as well as many other analytical issues that financial professionals face today. We focus on systematic business transition, and sustainable wealth management and advisory practices.

What one issue is currently facing the wealth management industry in North America?

Aging demographics. Today, top advisors have around 10 to 15 years of experience in the industry, with an average of $50 million to $65 million of assets under management and advisory. The average age of advisors is 58. However, as advisors are getting older, there aren't a lot of young professionals entering this field, further complicating the issue.

How does this issue relate to succession planning?

In today's environment, attrition is the most common trajectory for advisory firms. Too many advisors are working for as long as they possibly can and then finally stepping away from their businesses without a plan as they head into retirement. Eighty percent of the industry currently have no succession plan for after their departure. Many advisors are simply assuming they'll work into perpetuity, which isn't a practical mindset to have in the interest of continuity of their businesses. The challenge is to create and build robust, sustainable firms; they don't simply emerge.

What's the importance of sustainability in the wealth management industry?

It's important to plan for the continuation of a wealth management business beyond the longevity of the founder's career. In all relationships between wealth managers and clients, there's an implied covenant that the firm will be around to execute clients' long-term plans. Unfortunately, many businesses aren't capable of this, even though they believe it's possible. In order to create a sustainable firm, the business must have multi-generational owners and be value-driven and equity-centric.

What are your views on the future of the wealth management industry? How do you see the issue of fewer young people entering the field being addressed?

The wealth management industry has been in a structural transition for a number of years. Most noticeably, advisory practices are moving away from commission-based models into fee-based advisory businesses. The recent Department of Labor legislation has accelerated this change in the U.S.; however, other countries such as Australia and Great Britain have already adopted similar regulations. This has a couple of apparent impacts on the industry. Most prominently, compensation models are being rethought to reflect this new form of client engagement, and roles and responsibilities within these firms are changing in reaction to a more complex investment and wealth management landscape.

Advisors are also facing challenges from a personnel standpoint—if young talent is not properly engaged, recruited, and trained, then advisors' practices are at risk of being consolidated to firms that have these elements. In fact, we view consolidation as a major factor in addressing succession issues for advisors—if you have no one selected to take over operations and client relationships, then the most logical step is to find a much larger and more integrated firm to assume these duties. A succession plan forms a sustainable base for addressing this problem, and offers strong incentives for talented advisors to stay with their practices.

What's your strategy for educating advisors about the importance of implementing a succession plan and building a sustainable business across generations?

The most important part of educating advisors about succession issues is to remove the notion that a succession plan is about retiring. The benefit of a properly structured succession plan really has little to do with actual succession. It's about building a stronger, more robust platform for meeting the needs of clients for generations to come.

It also involves centralizing the value of the client relationship to the firm so it can be invested in and built upon. Without a team of next-generation advisors who are qualified and empowered to manage a client base that's growing in size and complexity, the advisory practice is subject to the energy of the practice owner—which, over time, will decrease until retirement.

Properly structuring a business creates a sustainable platform that works for both the business owners and the clients, and is far more durable than the single-owner model that's so prevalent in the wealth management industry today. Therefore, succession, as a concept, is an outcome of a properly structured business rather than a single transaction. Advisors must start early in the planning process to maximize their options when it comes to business structuring and succession. All too often we hear that advisors started too late in their planning process, which greatly limits their options for passing on the business.

How would you advise wealth managers to communicate succession plans with their clients, and what should advisors keep in mind for managing client relationships into the future?

Communicating the plan for your advisory practice should be something that's reviewed with clients regularly. It's far easier to explain to clients that you're bringing on young talent to assist in the management of their plans than it is to explain to them you'll be retiring on a certain date. These types of internal transitions to a younger generation over a long period of time result in lower client attrition and a better overall client experience. We also know that clients' ages tend to be centred around the age of the advisor; thus, a multi-generation workforce inside of your practice can open up additional opportunities for client engagement, retention, and growth.

Lisa Hui is a member of CFA Society Toronto's Communications Committee.

2016 INSTITUTIONAL INVESTMENT MANAGEMENT FORUM

Salman Amin, CFA

CFA Society Toronto held its annual Institutional Investment Management Forum on November 9, 2016. It was also the day everyone woke up to realize Donald Trump would be the next U.S. president.

In hindsight, there couldn't have been a better time for the forum, as industry professionals engaged in lively discussions trying to digest the news and grapple with its implications. Market volatility was off the charts that day, and no one had a clear perspective on how the unexpected regime change would impact their investment decisions.

In the end, forum presenters helped to establish an atmosphere in the room of greater serenity, with their objective and logical analyses of what really matters: the fundamentals.

Leading off was Brian Johnston, chief operating officer of Mattamy Homes, the largest private homebuilder in North America, with a discussion of the factors underscoring the strength of the U.S. and Canadian markets. As different as these two economies are, the facts he presented clearly illustrated bright long-term prospects not only for Mattamy, but for the entire homebuilding industry in North America. Johnston addressed the growing concerns of the Canadian market by highlighting regional differences in home prices. He also explained how supply constraints, particularly in Ontario, are supporting price appreciation, despite efforts by the federal government to tighten lending standards.

South of the border, Johnson said, the growth looks more robust, with the housing market in the U.S. is coming off cyclical lows with rising sales, and most markets still well below their peaks. Johnson certainly infused some optimism into the audience, creating a calmer atmosphere that remained through a discussion of alternative assets by Robert Boston, a partner in the investment consulting practice at Morneau Shepell.

Remembering the lessons from the 2008 financial crisis, Boston stressed the importance of downside protection, risk management, matching assets to liabilities, and diversification. But, to meet all those needs, should institutional investors just pile into bonds? Not according to Boston. Given the current interest rate environment, and with yields at historical lows, traditional fixed investments have failed to meet the requirements of institutional investors. This failure becomes more pronounced considering the upward trajectory of future interest rates.

Instead of piling into riskier debt and other volatile assets in search for yield, institutional investors should consider certain types of alternative investments, Boston said. Although alternatives carry a liquidity risk premium, they generally have a lower correlation relative to traditional asset classes and chase absolute return targets rather than trying to beat a benchmark. On the flip side, funds specializing in alternative assets tend to charge higher fees and use more leverage. Nevertheless, Boston pointed to the results of a recent Preqin survey as evidence that large institutional investors are increasing their allocations to alternative assets.

The Preqin survey also highlighted the growing importance of private equity, private debt, real estate, infrastructure, and natural resources. These asset classes are widely established, but Boston made the case for two other types of investments that don't get much attention: water entitlements, or perpetual water rights, that generate income based on the volume of water allocation; and agricultural space opportunities, either with a focus on infrastructure in the agricultural supply chain or with a private equity-type structure to support agricultural-based businesses. Overall, for institutional investors, these types of illiquid investments all provide a higher risk-adjusted return profile than traditional investments.

By the end of the forum, attendees clearly had a better appreciation and understanding of these illiquid investments. More importantly, however, presenters were echoing the tone of optimism set by Warren Buffett after the results of the U.S. election, with his focus on the long-term growth prospects of the U.S. economy. In essence, the forum provided a much-needed perspective to clear the fog of doom and gloom, and to shift attention back to the objective analysis that industry professionals are known for—regardless of the transient forces that may cloud their judgment.

Salman Amin, CFA, is a consultant specializing in wealth management and capital markets.

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2016 ETF CONFERENCE FOR INSTITUTIONAL PORTFOLIO MANAGERS AND TRADERS

Victoria Barclay, CFA

Exchange-traded funds (ETFs) are well on track to overtake mutual funds. That was the sentiment at the fifth annual ETF Conference for Institutional Portfolio Managers and Traders in September 2016. "Canada is a test bed of ETF innovation," said Daniel Straus, citing currency hedges and dynamic hedging as recent examples.

"Due to dramatic declines in energy prices, Canada has been for sale," continued Straus, an analyst for ETFs and financial products at National Bank Financial. He noted that the July 2016 outflow from Canadian ETFs hit $1 billion, and that low-volatility ETFs are attracting interest. "In 2013, we had a calm bull market, and then low volatility came roaring back in 2015."

Nowadays, Straus said, the most popular ETFs have options in them. Options and ETFs have a "symbiotic relationship" because they have similar high liquidity, so have become a "favourite tool" of institutional investors.

"ETFs are the democratization of OTC products," said Camilo Gil, executive director of ETF services at CIBC Capital Markets, in a look at the current market structure. "Setting up a basket of emerging markets currencies on your own would be virtually impossible."

Not surprisingly, technology investment in ETFs has been significant in the last three to five years, according to Gil. In order to manage volatility in ETFs, he said, single-stock security breakers were brought into place for Brexit. Any volatility in markets after the U.S. election would be handled in a similar fashion.

"The relationship between the market maker and the issuer starts well before the ETFs get to market," added Frederic Viger, managing director at National Bank Financial.

The operational risk for ETFs is relatively low: "There's redundancy throughout the system," said Paris Smith, a principal at Wolverine Trading. Model risk is low, too, she adds. "We try to have multiple models because we know others in the market have them."

Operational risk links to workflow, which Bloomberg has been working on. "Two initiatives streamline fixed income ETFs," said Dave Mullen, senior business manager of fixed income ETF products at Bloomberg LLP, who discussed creating standardization and efficiencies in tracking ETFs. The first initiative is Bloomberg's yield and spread analysis (YAS) function, which aggregates cash flow within the fund. The second is the virtual basket (BSKT) function, which streamlines the creation and redemption workflows. (YAS is in use; BSKT 2.0, scheduled to come on stream last November, is now in use.)

Good Returns

There are three reasons for excess returns, according to Brad Zucker, senior product manager at FTSE Russell: rewarded risk, behavioural bias (such as following high-profile investors), and structural impediments (such as mandates against leverage that institutional investors have). Then there are two key questions that factor investors need to ask, he added: What are the factors, and how can they be evaluated? A "factor" in a multi-factor model is a stock characteristic, such as value or quality or momentum. About 330 factors have been suggested in the academic literature, Zucker said. Even the renowned financial experts Eugene Fama and Kenneth French didn't have a clear understanding why certain factors worked, "but they do," Zucker said. As for evaluation, "based on historical back-tested data, our comprehensive factor methodology displayed improved risk-adjusted index returns."

ESG

Emily Ulrich, senior manager, sustainability, at S&P Dow Jones Indices, told attendees that, while ETFs provide good returns, there are global trends and demands for environmental, social, and governance (ESG) funds.

"Sustainable investing is slowly trickling into the mainstream," Ulrich said, noting that many ESG funds will attract the interest of millennials, who want their investments to reflect their values around sustainability and ethical impact.

Ulrich said that some European countries have increased ESG regulation for institutional investors. "North America is a little bit behind," she said. In Ontario, pension plans are required to disclose whether ESG factors are incorporated into their plans' investment policies and procedures.

And there's much thought that goes into designing ESG ETFs, according to Priti Shokeen, vice-president of Index Coverage at MSCI, an ESG index provider. "Where does the strategy fit in, who are you targeting, and what are the distribution channels?" she asked. For example, with COP21, the agreement from the 2015 United Nations Climate Change Conference, carbon is a prominent interest to institutional investors. Rules-based transparent ESG indexes will effectively communicate ETF strategies to clients.

The future for ESG funds is bright, said Toby Heaps, CEO of Corporate Knights, a body that has been ranking sustainability of corporations for 12 years. "There's an explosion of data, interest in fintech is growing, and increasing social awareness means people want to take ESG into account," he said.

"We compile data so people can see [ESG metrics] in a credible way," Heaps said, adding that ETFs provide great transparency. That, in turn, can be used by robo-advisors to customize ETF offerings according to individual investors in a cost-effective way.

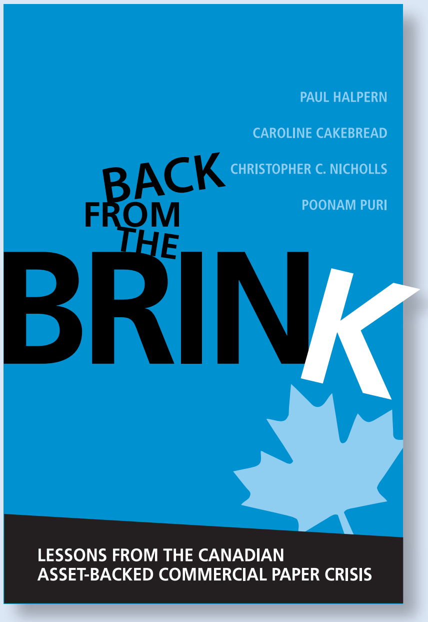
Smart Beta

Dave Nadig, director of ETFs at research firm FactSet, discussed smart beta ETFs, which try to combine the benefits of passive strategies with the advantages of active strategies. He noted that these products do deliver, but investors and analysts need to sort the wheat from the chaff. He described an analytical framework for the "new normal" of the investing world. "Most of the risk comes from the fact you are in the market," he said. "Industry tilts make an enormous difference."

Victoria Barclay, CFA, is a Toronto-based risk manager and has been a charterholder since 2006.

SNAPSHOT OF ETFs IN CANADA

- Largest ETF in Canada: XIU, with C$12 billion in assets
- XIU refers to: iShares S&P/TSX 60 Index ETF from Blackrock, begun in 1990
- Number of ETF providers for Canadian institutional investors: 17
- Global growth of ETFs in the past five years: C$1.4 trillion
- Global CAGR of ETFs in the past five years: 22 percent
- 2015 inflows to ETFs: C$16.5 billion (28 percent year over year)
- 2015 inflows to mutual funds: C$29.8 billion (2.2 percent year over year)
- Number of the past calendar years in which ETFs have outsold mutual funds: 6
- Canadian equity fund outflow, as at September 1, 2016: C$2.8 billion



THE ART OF THE POSSIBLE

Victoria Barclay, CFA

Back From the Brink: Lessons From the Canadian Asset-backed Commercial Paper Crisis

by Paul Halpern, Caroline Cakebread, Christopher C. Nicholls, and Poonam Puri

Hardcover | 251 pages | ISBN 9781442641921

Trying to deal in asset-backed commercial paper (ABCP) during the financial crisis was like trying to fry an egg in a hurricane. Nothing would stay level long enough to cook, and there was a sense that, at any moment, everything could blow up. Now imagine trying to fry 18 eggs in the middle of a hurricane, and you'll get some idea of the challenges faced during Canada's third-party ABCP crisis.

Back From the Brink by Paul Halpern, Caroline Cakebread, Christopher C. Nicholls, and Poonam Puri attempts to give context to, and extract meaning from, those troubled times. The book is compact, ambitious, and clearly written.

In late 2006, the first rumblings of the subprime mortgage crisis were heard in the U.S. markets. In July 2007, Coventree, a leading seller of Canadian third-party ABCP, released a letter intended to reassure its dealers—but it had the opposite effect when some dealers forwarded it to clients. Coventree had an overall exposure to subprime of approximately four percent across all conduits; investors began to panic. Early in August 2007, giant Quebec pension fund the Caisse de dépôt et placement du Québec (the Caisse) decided to reduce its ABCP exposure. The spread between bank and third-party ABCP began to widen.

On August 13, 2007, the National Bank's CEO called Deutsche Bank to request liquidity lines for ABCP, but was denied. "The soft landing had failed," the authors write. At that dreadful point, the CEO "knew the ABCP market would collapse."

Thus began the ABCP crisis in Canada. After many phone calls, the Caisse and others discovered the problem was Canada-wide. (*Back From the Brink* provides a table of the conduits, sponsors, and the amounts eventually determined.) Two days later, the $32-billion third-party ABCP market was at a standstill. Negotiators asked for a moratorium on liquidity and collateral calls until October 15, 2007, in an attempt to stave off huge losses in a forced liquidation. Ten of the biggest buyers and sellers of ABCP signed this moratorium agreement, known as the Montreal Accord.

Liquidity providers Deutsche Bank and Barclays refused to honour their agreements, "relying on the restrictive terms of the Canadian-style liquidity clause."

Purdy Crawford, as chair of the Montreal Accord investors' group, established the Pan-Canadian Investors Committee (PCIC), which grew to 12 members and held about $21 billion of the book value. The court appointed an Ad Hoc Committee Investors' Group from smaller corporate investors. And a third group, calling itself the Ad Hoc Retail Investors Group, formed independently, chiefly made up of affected individuals.

The Montreal Accord wanted to convert third-party ABCP to notes that would mature at the same time as the assets. It also wanted to revise the margin provisions of certain swaps. In the meantime, however, credit default swap (CDS) spreads began to climb and global markets became even more skittish. Specialists working to piece together information on third-party ABCP were shocked to discover more than 2,000 retail investors were also involved.

These retail investors had been sold the product on the claim that it was "just like GICs." One such investor, Brian Hunter, marshalled his forces through social media. Their investments were small, relative to the dollar amounts of the Montreal Accord signatories, but these were the life savings of ordinary people and garnered lots of media attention.

Crawford set to work hammering out a deal. Along the way, one company tried to tempt holders with an offer to buy third-party ABCP at a 30 percent discount.

"The ABCP crisis during the fall of 2007 looked like a house of cards loosely constructed with competing interests: angry investors on the PCIC vied with asset providers, which, in many cases, also acted as liquidity providers. Both groups feared litigation....Standstill agreements were pivotal to the process: everyone...agreed they would not trade ABCP," the authors write.

The standstill agreements, shaky as they were, had to be renewed several times—in the midst of the tumult of the financial crisis.

How did Crawford ensure the final deal would not "fall apart in a barrage of lawsuits"? He turned to the 1985 Companies' Creditors Arrangement Act (CCAA). This law allowed for the reorganization of debt rather than a fire sale of assets—but it needed a supermajority of investors (both in numbers and dollars).

More than 10 proposals for restructuring were submitted to the PCIC and related bodies. *Back From the Brink* approaches these details with precision and clarity, including, for example, a spread-loss trigger matrix for a certain type of note (MAV II). The reader can empathize.

Once the restructuring was concocted, Crawford went on a four-city "road show" to present it to investors. Retail investors turned out to jeer and heckle; meanwhile "some investors were giving in to despair—by now, there had been one suicide and several threats of suicide." Finally, Canaccord and Credential offered a buyback to some retail investors.

After more fine-tuning, the PCIC had to get the new paper rated by DBRS and then take it to court for approval. A battle erupted over the fraud "carve-out."

By August 2008, the liquidity crisis had deepened to a full-blown credit crisis. The fiascos of Fannie Mae, Freddie Mac, Lehman Brothers, and AIG all make cameo appearances in the book. The restructuring that had been so painstakingly crafted started to weaken—again.

Around this time, the Caisse reported a $40-billion loss, and was itself in a serious bind. Some members of the PCIC clamoured to change the deal yet again. The asset providers, themselves highly leveraged, grew restless. Days before the final extension deadline (December 30, 2008) the restructuring had to be reworked.

Would the feds step in? Mark Carney, soon-to-be governor of the Bank of Canada, said, "Canada can afford to see the failure of a proposed rescue for $32 billion of ABCP." Tough love, indeed.

The parties knew they had to stay focused and complete the restructuring. And they did.

But the story does not stop there; *Back From the Brink* also explores the aftermath of the crisis. Liquidity has returned to the ABCP market, albeit with greater reputational risk. Some market participants have gone on to profit from the restructured notes. The primary sellers are the note holders (pension funds, governments, corporations); the buyers are the market makers, brokers, and hedge funds. The book explains how an unexpected source of liquidity has been the unwinding.

And what about the regulatory fallout? It seems obvious the dealers should not have lumped together the two types of ABCP (bank and third-party); the risk profiles are different. Arguably, the Ontario Securities Commission (OSC) didn't take prompt enough action. The book discusses some big-picture questions that have resulted from the fallout: Is the enforcement of Canadian securities too lax? Should Canada have a single national securities regulator?

The OSC eventually brought four allegations against Coventree regarding public disclosure and a misleading statement to the market; and, ultimately, the penalties against Coventree and its principals were very light. For this, *Back From the Brink* provides explication—if not juicy vindication.

Continued... page 26

Quibbles

As much as I enjoyed the book, I have three quibbles. In addition to the Notes and Index, I would suggest a List of Acronyms. At one point, I was swimming in LSS, MAV, MDE, MFF, and more. Although most terms can be found in the index, some are listed first by the spelled-out form, whereas others are listed by acronym first. The index shows "MFF (margin funding facility)" and "market disruption events (MDEs)."

Second, the index is uneven. The index points to "BGI" on page 28, but it's not there. Topics (such as E*TRADE, GTAA, and suicide) appear in the text but not in the index.

Finally, in the chapter on winners and losers, DBRS mistakenly appears in the "losers" subsection. The authors themselves note that DBRS was "off the hook," despite its misleadingly high ratings, and was recently bought by a private equity company for US$500 million.

Kudos

For a complex topic, the book is a model of clarity. It explores multiple facets of numerous problems and yet does not get bogged down. Devonshire Trust and Barclays, for example, had a lively side dispute due to an agreement "byzantine in its complexity," according to the judge presiding. The authors provide a crisp, readable summary and move on.

The sections are well organized. A statement is made—sometimes a controversial one—and the next few statements dissect the nuances. Consider the exemption from legal liability, for example: one party said, "This exemption must apply across the board." The other party said, "No, we must be able to sue persons engaged in fraud." (This became known as the "fraud carve-out.") The authors are able to explain why, perhaps surprisingly, the fraud carve-out didn't occur.

Five Factors

Overall, the authors point to five factors at play in the negotiated restructuring.

1. The collective interest of saving the assets was the overriding goal.
2. The Canadian solution was a private sector solution that didn't involve direct government intervention.
3. Two entities dominated the negotiations: the Caisse, which had billions invested; and Deutsche Bank, which was the largest asset—and liquidity—provider.
4. Legislation intended to provide a smooth landing for creditors of a single company going bankrupt, the CCAA, was applied to an entire industry: the third-party ABCP.
5. The underlying assets in the trusts were mostly sound.

Back From the Brink has more ups and downs than the Calgary foothills. It gathers together news fragments and the inside stories of participants, from "the day Montreal stood still" until the restructuring of notes was completed and the ABCP market was restarted.

As Crawford often said, all negotiation is "the art of the possible." I often heard news items about the Montreal Accord at the time, and I wondered how it would end. *Back From the Brink* explains and provides context for the compromises that were made. Best of all, it suggests how we may learn from the mistakes.

Victoria Barclay, CFA, is a Toronto-based risk manager and has no relation to Barclays Bank. One of the book's co-authors, Caroline Cakebread, was editor of *The Analyst*.

THE ABCP DEBACLE: FIVE LESSONS LEARNED

Adapted from the final chapter of *Back From the Brink: Lessons From the Canadian Asset-backed Commercial Paper Crisis* by Paul Halpern, Caroline Cakebread, Christopher C. Nicholls, and Poonam Puri.

1. We need a more competitive landscape for credit rating agencies—investors need to check their over-reliance on ratings.
2. Consider the role of the Investment Industry Regulatory Organization of Canada and the question of broker fiduciary standards.
3. Financial companies need a risk management investment framework.
4. Financial companies need board-level risk engagement.
5. Securities regulation must require disclosure and transparency.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THE PRACTITIONER

Mari Jensen, CFA, encourages future charterholders to be self-aware and to accept help when it's offered.

Stephanie Condra, CFA

What attracted you to a career in the finance industry?

I've been interested in finance since taking Finance 101 at Simon Fraser University. None of my extended family is in finance, so I knew very little about careers in [the industry] at the time, but I knew I loved the subject matter. Doing my MBA internship in wealth management at Scotiabank, I knew I'd made the right decision. Careers in finance are so varied, so there are endless opportunities to keep you challenged.

Where do you see yourself in the next five to 10 years?

Within five years, I'll be leading a team within the finance industry. Within 10 years, I'll be on at least one corporate board.

How has the CFA designation and the knowledge you gained in the program helped you in your career?

I wouldn't have my current position if it weren't for my CFA designation. The hiring manager at the time specifically wanted a candidate with the designation, as the role was covering fund managers with their foreign exchange needs. She felt that understanding the process of investment management was critical to understanding their needs, and I'd agree with that. When I was writing Level 3, I was working in institutional investment management sales for Scotiabank. I remember specifically being able to apply the knowledge I learned about investment policy. So much of what you learn in university is theoretical—I loved the practical aspects of the CFA program.

You've held numerous roles at Scotiabank, from institutional investment management sales to foreign exchange. What advice would you give to new charterholders who might want to follow in your footsteps?

It's important to remember that the actual job differs greatly from the theory you learned in school, and that there are so many different jobs in finance—so it's best to keep an open mind. Finding the job that makes you happy also involves strong self-awareness. Do you like working on one project for a long time, with the prospect of a big win? Or do you like smaller but more frequent wins? Do you love to read, write, and research, or are you best when talking to people? Do you love learning about specific companies, or are you more interested in macro events?

Mari Jensen, CFA | **CAREER HIGHLIGHTS**

- First started working at Scotiabank in 1993
- Left Scotiabank in 2002 to complete a full-time MBA
- Rejoined in 2004 and is now director, Institutional FX Sales, with Scotiabank Global Banking and Markets
- Is the current chair of the Women in Capital Markets network
- Completed the MBA program in the same year she earned her CFA designation

"If you're asking whether or not you should write your CFA, just do it. Otherwise, you'll be asking the same question in three years, and you could have finished it by then!"

You're currently the chair of Women in Capital Markets (WCM). Why did you get involved with the group?

I got involved about eight years ago because I wanted to give back to the investment community. I really enjoy mentoring. I was just starting out on the trade floor at the time, so I felt the area I could best contribute to was the High School Liaison Program. It had the added benefit of helping me to develop my public speaking skills. (I once spoke to an audience of 400 high school girls!) I volunteered for a few years, doing presentations on capital markets at high schools, and eventually chaired the committee and joined the board in 2011. Volunteer work is a parallel career, where you can be developing new skills and progressing into roles with greater responsibility. I feel very privileged to be chair. It's a position I worked very hard to attain, and I learn so much from my fellow directors every day.

When it comes to the degree of gender diversity in our industry, what are we getting right and what could be done differently?

In the past few years, we've witnessed a big gain in momentum for gender diversity in finance, with many senior leaders putting their weight behind the cause. This is critical, and this is what we're doing well. What we need to work on is eliminating any systemic barriers to people—both women and men—attaining their potential. Unfortunately, there's no magic bullet, so this involves tremendous institutional will. For example, right now there's a big focus on cognitive bias, and many leaders are taking courses on the subject. This is a great start. Of course, taking a course will not eliminate bias in decision-making. We have to ensure there are processes to review critical decisions—such as promotions—to ensure they're being made optimally and without bias.

You were a single parent when you finished your MBA and CFA. In an issue focused on gender diversity, this is an accomplishment that shouldn't be overlooked.

You don't get any extra points for finishing your degree without accepting any help. I was extremely fortunate as I was finishing both programs to have very supportive classmates, colleagues, friends, and family who offered their help.

Any final words of advice?

If you're asking whether or not you should write your CFA, just do it. Otherwise, you'll be asking the same question in three years, and you could have finished it by then!

Stephanie Condra, CFA, is head of Canadian business with Irish Life Investment Managers.

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