Investing with confidence

A closer look

Take a closer look at managing the investments in your plan, and how you can build upon the essentials of Investing with confidence.
This brochure is a helpful reminder of what you’ve learned in the Investing with confidence session you attended, including:

- What risks affect your investments
- What active and passive investment approaches are
- Investing at home, versus globally
- How Morningstar® can help you to better understand the investment options offered in your plan
- Where to find more insights to help you invest with confidence
The Risk Factor

Most common investment risks

Many market risks can affect the value of your investments.

These are the most common categories of investment risk:

<table>
<thead>
<tr>
<th>Risk Factor</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Economic/Political</td>
<td>A steady economic and political environment helps to keep the investments in that region more stable. But when a local or regional economy or political environment is unstable, typically the value of markets and investments in the area is too.</td>
</tr>
<tr>
<td>Inflation</td>
<td>If inflation is high, it means your rate of return has to be much higher – otherwise your savings won’t buy you as much down the road. Guaranteed investments don’t perform as well when inflation is high, because they don’t adjust for inflation. See Inflation (and your real rate of return) for more information about this important topic.</td>
</tr>
<tr>
<td>Interest rate</td>
<td>When interest rates rise, bond value goes down and vice versa. Bond managers watch for potential interest rate changes to decide which types of bonds to invest in. Check out Bonds and bond risks for more information.</td>
</tr>
<tr>
<td>Sector</td>
<td>An economy is made up of sectors (like financials, health care or information technology). Each sector performs differently in the market depending on economic conditions. The value of a fund, market or portfolio that invests in few sectors rises and falls along with the prices of the stocks in only those sectors – rather like the old adage about having all your eggs in one basket. See Get to know the S&amp;P/TSX for the impact of sector risk.</td>
</tr>
<tr>
<td>Currency</td>
<td>The value of your investments in other countries could benefit or be negatively impacted depending on the value of the Canadian dollar. Some funds are “hedged” against currency risk, meaning that the fund is structured in such a way that a change in the currency exchange value won’t affect the value of foreign holdings. For more details, see Currency: How important is the exchange rate?</td>
</tr>
</tbody>
</table>
Inflation doesn’t just affect the cost of products and services you buy.

In Canada, the official measure of inflation is the Consumer Price Index, or CPI. As the official measure, it is used to calculate annual increases to the Canada Pension Plan and Old Age Security.

Plus, inflation affects your investments.

You’ll find the rate of return on your investment(s) on your statements, but it’s important to understand your real rate of return – that is, your rate of return when you subtract the value of inflation.

What’s your real rate of return?

Let’s assume your statement says your investment grew by 5%.

If inflation was 2%, your real return is 3% (5%−2%=3%).
Bonds and bond risks

What are the risks?

There are two types of bonds: government bonds and corporate bonds. Neither is risk-free.

<table>
<thead>
<tr>
<th>There are two main risks to bond values:</th>
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<tbody>
<tr>
<td>• Credit risk (the ability of the bond’s issuer to repay their debt to the bondholder)</td>
</tr>
<tr>
<td>• Interest rate risk (dependent on whether the Central Bank increases or decreases interest rates)</td>
</tr>
</tbody>
</table>

Credit risk

In practice, there are three categories of credit qualities (low, medium and high) and you can find out how your bond fund invests across these three types from the Morningstar® fund page (see Take a closer look at funds and fees). Some bonds do not have their credit quality rated by an official ratings agency and they fall under the “Not rated” category. This does not mean they are low quality. It means that the fund manager has to make a judgment about their quality.

Interest rate risk

There’s an opposite, or inverse, relationship between interest rates and bond values. As interest rates go up, bond values go down (and vice versa).

Why does this happen?

When interest rates rise, new issues come to market with higher yields than older securities, making those older ones worth less. Hence, their prices go down.

Fund managers try to manage interest rate risk by diversifying across public and private debt and holding bonds with different maturity dates.
You may have heard about actively and passively managed funds. They each have advantages and disadvantages.

**Passive (or “index”) funds try to match the value of a particular market.**

- For example, the value of a Canadian equity index fund will move up and down with the value of its market – the S&P/TSX. You will probably fare as well as the performance of the market.
- Passive/index funds tend to have lower fees compared to active funds.

**Active funds try to do better than the benchmark they are measured against.**

- Fund managers analyze the markets and make active buying and selling decisions to get the best investment returns. For example, an actively managed U.S. equity fund will hold the stocks that the fund manager believes are most likely to rise in value. An active fund may even hold some assets in cash if the manager expects the markets to perform poorly, or they are awaiting buying opportunities.
- Because active fund managers are trying to outperform the market (rather than simply match its value like a passive/index fund), actively managed funds charge higher fees than passive funds.
- If the fund manager makes the right decisions, you could do better than the markets. But if the fund manager misjudges, the fund could underperform the market.

The terms “active” and “passive” refer to a fund manager’s style.

TIP: If the word “index” is in the naming convention of a fund, it will be a passively managed fund.
Invest at home, or abroad?

Get to know the S&P/TSX

Canadian equities are traded on the Toronto Stock Exchange, or S&P/TSX. There are many indices used to track the value of the Canadian equity market, but the key index is the S&P/TSX Composite Index. It consists of over 200 of the largest companies in the Canadian equity market.

There are many sectors in the Canadian equity market, but they are not equally represented or “weighted” in the index. Some sectors have a larger presence than others (like financials, as you can see in the chart below).

Remember our talk about sector risk?
When you hear the S&P/TSX rose in a particular year, or declined in that year, the truth is more nuanced than that. Some sectors may have done well and some not so well. Because the S&P/TSX is heavily concentrated in just a few sectors, its performance is very much affected by performance in those few sectors (like financials, energy and materials).

The S&P/TSX’s closest neighbour: The S&P 500

In the U.S., the S&P 500 Index is the most directly related index to the S&P/TSX Composite Index. But there are some important differences:

- The S&P 500 is more than **10 times larger** than the S&P/TSX.
- There are **fewer sectors** in the S&P/TSX than in the S&P 500. That means if a particular sector that’s a large part of the S&P/TSX performs poorly, the S&P/TSX Composite Index performance is more negatively impacted. In other words, the S&P/TSX has higher sector risk.
- The **sectors are very different**. The S&P 500’s largest sectors are IT, financials and health care; the S&P/TSX’s largest sectors are financials, energy and materials.

![TSX vs S&P 500 chart](chart.png)
**What about farther afield?**

Your group plan may have funds that specialize in markets outside of North America. For example, Europe and Asia have their own active equity markets.

Equity markets outside of North America give fund managers access to companies that are significant on the world stage. Some examples of companies you may see in your Top 10 holdings are Vodafone, Toyota, Michelin or Toshiba.

**Different regions, different risks**

There are three types of national equity markets:

- Developed (e.g. Canada and the U.S.)
- Emerging (e.g. China and India)
- Frontier (e.g. Romania and Sri Lanka)

All three have their advantages but also their own sets of risks. For example, frontier markets are least tied to developed markets. So when a developed market such as Canada experiences a downturn, frontier markets may still do well.

However, in frontier markets, it may not be as easy for a fund manager to pull out when they want because of liquidity and local laws.

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**The two primary types of foreign equity funds are Global and International.**

**Global** funds invest around the world with a significant weighting within North America.

**International** funds have little or no weighting in North America. The markets they most invest in are Europe, Australasia and the Far East. In an international fund, at least 70% of the fund’s assets must be in developed markets.

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**Equities come in all sizes**

You may choose funds based on the size of the companies the fund manager chooses to invest in.

For example, some funds specialize in medium- and large-sized companies whereas other funds (known as Small Cap funds) specialize in companies with a smaller market capitalization.

Medium- and large-sized companies often have more predictable revenues but small companies often have more growth potential, though they can be riskier.

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**What is a…**

**Small cap fund?** It invests in companies worth less than $2 billion.

**Medium cap fund?** It invests in companies worth between $2 billion and $10 billion.

**Large cap fund?** It invests in companies worth more than $10 billion.
**Currency: How important is the exchange rate?**

The value of the Canadian dollar also affects your investments

You’ll regularly hear about the value of the Canadian dollar (most often compared to the value of the U.S. dollar). You know it affects you when you travel or buy imported products. However, the value of the Canadian dollar also affects your investments.

If the value of the U.S. dollar changes significantly compared to the Canadian dollar, the return on any U.S. funds you have that aren’t “hedged” will be affected by the change in the exchange rate.

*When investing outside of Canada, exchange rate movements can have as much impact (positive or negative) as the fund or market performance itself.*

Let’s say you had an S&P 500 index fund that grew in absolute terms about 15% per year over the last three years. Let’s also say the Canadian dollar declined significantly during that period compared to the U.S. dollar – in other words the U.S. dollar strengthened in value. Your investments in the S&P 500 would have had extra growth when you include the effect of the exchange rate movement over that time. In fact, in this real example, the value of your investment would have grown by over 28% per year on average in the last three years up until the end of 2015, in Canadian dollar terms.
Take a closer look: at funds and fees

**Morningstar®**

The Morningstar® fund pages in your mySunLife.ca account will give you a wealth of information about the funds in your group plan. Use Morningstar® for information such as:

- How they’re managed
- The asset classes they’re invested in
- Their top holdings
- The sectors and countries in which they hold their investments
- The credit quality (for bonds)

**Access Morningstar® at mySunLife.ca**

- Sign in to mySunLife.ca
- Select my financial centre
- Under the Accounts menu, choose Investment performance

There is a suite of options on this page:

- You’ll see the **rates of return and unit values** for each fund option available in your plan. You can change the period of time used to measure investment performance.
- The **Fund Report** option will show a list of the funds you’re invested in and all funds available in your plan; by clicking on the fund name, you’ll get a full fund information sheet.
- **Market Indices** show you the index values for major markets around the world.
- **Fund QuickRank** quickly shows you which fund options in your plan are performing best over long- and short-term periods.
- **Instant X-Ray** shows you even more detail about your fund, and allows you to compare it to a benchmark of your choice.
- **Updates** will appear to give you any current news about the funds available in your plan.
Understand your fees

Don’t forget that the fund fees in your group plan are often lower than the fund fees you would pay as an individual investor. This can make a big difference over time. Take a look at this example:

<table>
<thead>
<tr>
<th>YEARS OF CONTRIBUTION</th>
<th>TOTAL CONTRIBUTIONS TO YOUR PLAN ACCOUNT</th>
<th>MANAGEMENT FEE*</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>3%</td>
</tr>
<tr>
<td>10 years</td>
<td>$40,000</td>
<td>$46,132</td>
</tr>
<tr>
<td>20 years</td>
<td>$80,000</td>
<td>$105,634</td>
</tr>
<tr>
<td>30 years</td>
<td>$120,000</td>
<td>$182,379</td>
</tr>
</tbody>
</table>

*Assuming a $4,000 yearly investment to a registered plan at a 5.75% gross rate of return, a 1% difference in fees adds up to $45,158 additional savings over 30 years. That’s a lot of extra money, just for keeping an eye on your fees! Your group plan may also allow for you to transfer in external assets, in which case you could benefit from the lower fees on those savings as well.

You can check the fees you pay in your Sun Life Financial group plan on your annual statement or online:
- Sign in to mySunLife.ca
- Select my financial centre
- Under the Accounts menu, choose Account fees
Useful links

Morningstar® has a wealth of information, but you can also learn a lot more by reviewing market commentary online at:

- Sunlifeglobalinvestments.com
- blackrock.com/investing/insights
- bloomberg.com/markets

For index performance in different markets around the world:

- International
  - msci.com/eafe
- Global
  - msci.com/world
- Canada
  - http://ca.spindices.com/indices/equity/sp-tsx-composite-index
- U.S.
  - http://ca.spindices.com/indices/equity/sp-500

Want to check the Consumer Price Index and the impact of inflation?