Nexus Notes

March 2021
Vol. 26, No. 1

Featuring:

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Thoughtfully™

NEXUS

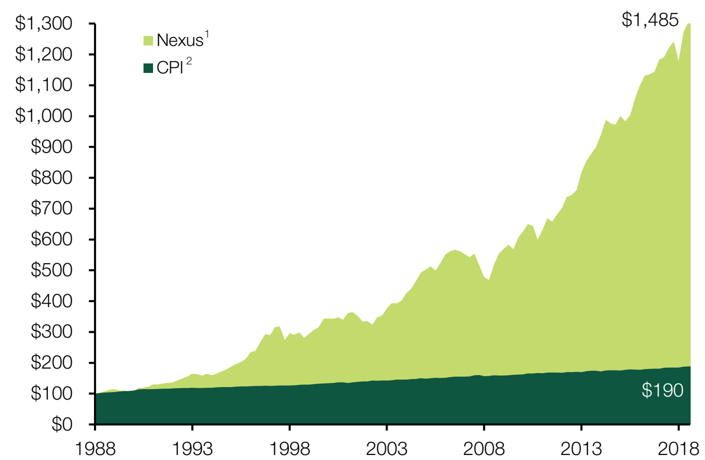
Our market-resilient investment strategy focuses on long-term results, providing investors with peace of mind through all stages of life.

Building Value for Clients

Since its establishment in 1988, Nexus has pursued an investment approach which concentrates on real growth in client wealth over the long term.

The chart illustrates the impact of this long-term investment thinking – a $100 investment in a balanced portfolio in 1989 has grown to $1,485 at December 31, 2020.

$100 Investment with Nexus in 1989



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1 "Nexus" reflects the performance of a composite of Nexus accounts managed to a balanced mandate (until September 30,1997) and the Nexus North American Balanced Fund (thereafter). Returns shown prior to the deduction of investment management fees.

2 CPI is the "all-items" Consumer Price Index for Canada, not seasonally adjusted.

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FROM THE EDITOR

Springtime

It's official: it's spring! Ever since people have been telling each other stories, they've used the different seasons as metaphors, and spring evokes the start of something new. This feels appropriate as this is the beginning of my role as the Editor of *Nexus Notes*. I take over these duties from Dianne White, who served as Editor for the past 20 years.

I joined Nexus a little over a year and a half ago, and while I have had a chance to meet many clients, the pandemic has slowed my introduction to everyone. So, let me share with you a bit about myself. I help deliver wealth planning here at Nexus and provide relationship management to some of our clients. Before joining the Nexus team, I worked for one of the big banks for 15 years. Before that, I had a stint in public accounting, earning my accounting designation.

Thinking of new starts also fits with changes going on at Nexus. We launched our refreshed website, building on our rebranding from last year. The Nexus team continues to evolve too. We recently announced Jorjan Mead's retirement. While it's always sad to see someone move on, I can't help but be happy for Jorjan as she starts a new stage of her life in retirement. As it is often said, every end is just a new beginning. We also welcomed Lily Lucacescu as a new addition to the team.

Earlier this month marked the first anniversary of the beginning of the pandemic; the World Health Organization made the official declaration on March 11th, 2020. Most of us still find ourselves in some state of lockdown one year later, but we do see the world is in a different place. In Canada, we have four approved vaccines (for now). The road to getting people vaccinated has been bumpy, but progress is underway, making discussions on what the post-pandemic world will look like more relevant.

Yet, when any debate turns to what tomorrow will bring, there's always an element of uncertainty. So, while springtime might represent the start of things, it doesn't give any clearer picture of what the future might hold. However, one thing that doesn't change is Nexus's investment approach and our philosophy of taking a long-term view, even in the face of extreme market pressures. In February we held a webinar hosted by (another!) new team member, Tom Wilson, and featured guest speaker and award-winning author, Morgan Housel, who shared stories on how investors should think about risk. If you didn't have a chance to join the live event, I recommend setting aside some time to listen to the recorded version available on our website. Our own John Stevenson shares some of his thoughts on Morgan Housel's work in this issue of *Nexus Notes*.

Lastly, whether it's springtime, winter, or anytime in between, it's a good idea to be thinking about your goals and putting in place a wealth plan to help you prepare for the long-term. And just how long-term your needs are is likely changing as well. I highlight the prospects of living to age 100 in a wealth planning article in this issue.

I am looking forward to serving as Editor and carrying the torch for many more editions of *Nexus Notes* to come.

Brad

Brad Weber
CPA, CA, CFP

The Tail That Wags the Dog

by
John C.A. Stevenson, CFA

We thank our friends at Northwood Family Office for having brought to our attention a fantastic book called, *The Psychology of Money*, written by former Wall Street Journal and Motley Fool journalist, Morgan Housel. We strongly recommend it! In fact, reading this book inspired us to recruit Morgan for a virtual event in February, hosted by Nexus's Tom Wilson.

In one of the most interesting chapters, Housel writes about "tails". Not the canine kind, but the ones at the outer reaches of a probability distribution. The "dog" in our title is a metaphor for so many things in life, especially investing.

Most will remember probability theory from high school math. If you don't, never fear, the idea is straight-forward. The most common probability distribution is the normal curve, where the high point on the curve is the mean, or average, of the possible outcomes of a certain event. The mean is the value with the highest probability of occurring. As you move away from the centre of the curve the probability of events gets lower and lower. You might recall that the mathematical measure of this is standard deviation. But that is not important here. What is important is that the outer reaches of the curve are the "tails" – the outcomes that are not very likely. Housel argues that the "tails" are critical, because so many things in life and investing depend on what happens in these "tails".

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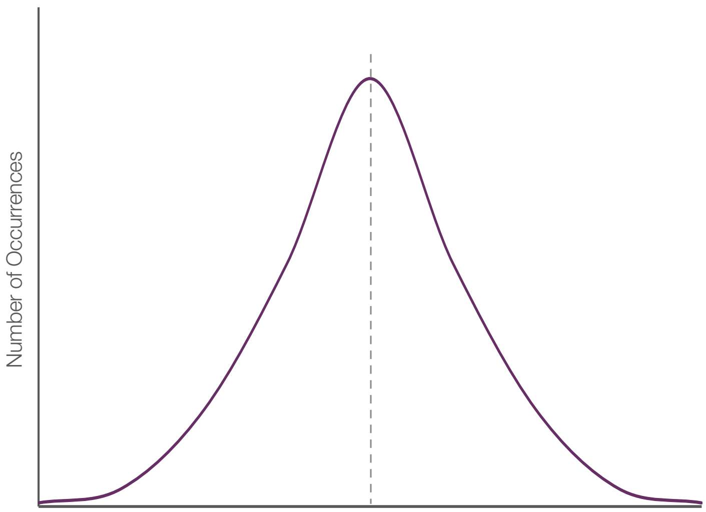
Standard Normal Distribution



It's a fact of life that small probability events can account for a disproportionate outcome. As Housel writes, almost everything in life that "is huge, profitable, famous, or influential, is the result of a tail event – an outlying one-in-thousands or millions event." [1] It's normal for things to fail. An investor or business person can be wrong more than half the time and still make a fortune.

Before shifting to the investment world, Housel gives the example of Walt Disney. In the 1930s, Disney had made more than 400 cartoons. They were expensive, most lost a fortune, and Disney's career seemed financially doomed. Then, in 1938, Disney produced an animated feature called *Snow White and the Seven Dwarfs*. It changed everything. *Snow White* was such an outrageous success it more than compensated for the economic disasters before it. Its profits overwhelmed the losses. The rest is history.

In the investment world, the idea of "tail" outcomes might be familiar to most in the context of venture capital. If a highly successful VC firm makes 50 investments, half or more are likely to fail. A good number of others will produce decent results. Only one or two will be fabulously successful and will drive virtually all of the returns of the successful firm.

This doesn't seem surprising because we view the VC industry as "risky". Most conservative investors stick to the public markets where returns seem more predictable and reliable. Except that they are not. Many public companies fail as well. A J.P. Morgan survey of the Russell 3,000 – the largest 3,000 companies in the U.S. – found that 40% of companies in the 1980 to 2014 period lost at least 70% of their value and never recovered. [2] All the index's returns came from 7% of the companies. Failure is most common in industries like technology (57% failed), but no industry is immune. Even 13% of staid old utilities suffered catastrophic losses during this period.

Even within the companies that are themselves tail events in the market (the top 7%), there are tail events in their business. Apple has been wildly successful over the last decade, largely as a result of a tail event called the iPhone. But Apple has had many failures. Who remembers the Newton? The Lisa? Amazon is another successful company that has suffered more failures than we can ever know. Remember the disastrous Fire phone? CEO, Jeff Bezos, was quoted shortly after launch saying," If you think that is a big failure, we're working on much bigger failures right now. I am not kidding. Some of them are going to make the Fire phone seem like a tiny blip." Sounds like a man who understands tail events.

Many of the greatest investors of our generation are well aware of the phenomenon of the tail. Peter Lynch, the legendary Fidelity manager, remarked that if you are terrific in the investing business you are right six times out of 10. At the 2013 Berkshire Hathaway annual meeting, Warren Buffett observed that he had invested in 400 or 500 stocks in his career. He made all his money on about 10 of them.

What's the moral of the story? Failures, losses or setbacks can make us feel like we are doing something wrong. In fact, they are normal. Don't be discouraged. Even people like Jeff Bezos and Steve Jobs made plenty of bad decisions. Second, accept that you don't know when or where these tail events will occur. We've often said, "it's time in the market, not timing the market." If you are not invested, even when the outlook seems dire (think March 2020), you might miss out on the defining moment of an investing career.

Housel concludes the section on tail events with the following observation: "There are 100 billion planets in our galaxy, and only one, as far as we know, with intelligent life. The fact that you are reading this book is the result of the longest tail you can imagine."

If you are interested in watching a replay of *Talking Risk: A Virtual Event Featuring Morgan Housel*, please contact your Nexus relationship manager.

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1) This quote and other references in this blog all come from Chapter 6, "Tails, you win", by Morgan Housel, *The Psychology of Money*, Harriman House, 2020.
2) Quoted by Housel. "The Agony and the Ecstacy: The Risks and Rewards of a Concentrated Stock Position," Eye on the Market, J.P. Morgan (2014).

Is 100 the new 80?

by Brad Weber, CPA, CA, CFP

It's a common saying that there are two certainties in life, death and taxes. While we have a pretty good idea when we get taxed, which feels like all the time, we don't really know when our final chapter will come. However, the trend line of history shows us that life expectancy has been increasing.

Look at Canada. Not only is our population growing, but it's getting older at the same time. In 2019 Canada reported 10,000 citizens who were at least 100 years old. According to Statistics Canada, that figure is likely to double in 15 years and could reach almost 80,000 by 2061. Even now, women's life expectancy is age 84, and for men, it's age 80. Those figures are calculated at birth, and the older you get, the longer your probable life expectancy. If you are 65 now, you can tack on another two years to those estimates. And don't forget, those are averages, so we know many people will live beyond that.

While drinking from the fountain of youth sounds good in theory, there are both opportunities and challenges with longevity. If you consider time is precious, then more of it is a good thing: time to spend with family and friends and experience the things you enjoy. But a longer life doesn't necessarily mean they will all be healthy years. Health care over the long term, and the quality of that care, will become important. There are behavioral and social aspects of aging that need to be considered and potentially end-of-life planning. And, of course, there are retirement considerations. You might spend a third of your life in retirement, and you should consider if you'll have the financial resources to support yourself for that long of a time.

A key consideration in any retirement planning exercise is understanding your spending. The first thing to do is at least consider these needs over an extended period. It's common at Nexus for us to review projections out to age 100. That exercise shows that you'll likely see the cost of your lifestyle double simply due to inflation, and that's at today's low inflation rates. Expenses over such a time horizon can add up. Imagine how many roofs or water heaters might need to be replaced on the journey from age 65 to 100. As you age, spending in one area might decline but could be replaced with higher costs elsewhere, particularly for health care. Reviewing health care costs is a topic on its own. But contemplating their potential impact on your retirement planning is a good starting point. A change in your health status or an adverse medical diagnosis should also be a cause to revise your planning.

Any discussion of retirement planning will include the topic of the Canada Pension Plan. In the face of increasing longevity, it's worth delaying when you start your pension, which will increase the amount you'll collect over your lifetime. A recent blog post, *"When Should I Start my CPP Payments?"* covered just this topic.

Portfolio construction going into retirement has traditionally involved reducing your percentage of equities as a form of risk management. But when your time horizon could be measured in thirty or forty years, a new risk becomes important: that you might run out of money before you run out of time. A "safe" investment strategy with more money in fixed income may not allow your assets to keep pace with inflation. This problem is further compounded when you consider the current low interest rates.

The prospect of living to 100, or close to it, might not feel real to some. But we do know it's happening and will happen to more and more people. Determining your longevity is just a guess. But your retirement planning should consider a potentially long life span.

New Year, New *Beginnings*

It is with mixed emotions that we announce the retirement of Jorjan Mead from her position of Administrative Assistant with Nexus.

by Nicole Weiss

Over the last 12 years, Jorjan has played an important role for our clients, many of whom have come to know her friendly face at the Nexus reception – or more recently the "voice" of Nexus in our new virtual world. Her tireless efforts at our events earned her much gratitude from her colleagues, resulting in formal employee recognition. Internally, she also spearheaded the "healthy snack" initiative that we all enjoy!

Jorjan Mead

Lily Lucacescu

Although we were unable to celebrate her many years of service in person, we hope you will all join us in extending our warmest wishes to Jorjan.

While the start of 2021 has seen us bid farewell to Jorjan, it has also brought us the opportunity to introduce Lily Lucacescu, who is taking on a new role as our Junior Office Manager. Lily's focus will be on office management and administration, as well as supporting our client service team. We have seen tremendous growth over the last few years at Nexus, and we are excited to have Lily take on these important responsibilities at the firm.

Lily joins us after nearly a decade as an Executive Assistant to a variety of CEOs across several industries. Outside the office, Lily spends her time staying active as an avid cyclist and barre fitness enthusiast.

We look forward to the end of the pandemic for many reasons, not the least of which is to introduce you to Lily in person. In the meantime, hopefully you will have a chance to meet her virtually. We are excited about Lily becoming a key member of the Nexus team.

Worth a Thousand Words…

Image used with permission: Ali Solomon, The Cartoon Bank/ The New Yorker Collection

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At Nexus, we offer thoughtful wealth planning and investment management with unparalleled personalized service to private clients and foundations.

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