**Chairman’s Message:**

**50 Quarters of Perspective**

*Tom McCullough*

This is the 50th edition of *The Northwood Perspective* newsletter. Since our first edition in the summer of 2006, we have published one every single quarter. Our goal has been to bring perspective to the complex and often-confusing issues that families of wealth face every day.

Some of you will remember the three things Northwood strives to deliver to our client families – Direction (knowing what ‘north’ is for you and your family), Perspective (seeing ‘the forest’ and not just ‘the trees’), and Confidence (knowing that everything is well-planned, sensibly-managed and on-track). These have been our goals since we started the firm in 2003, and this newsletter has been one of the tools that helps bring critical perspective.

We also wanted to be positive contributors to the general level of debate, discussion and insight in the field of family wealth and in the lives of all families and advisors. We hope that the last 50 editions of our newsletter have helped to accomplish that.

We have been very gratified by the amazing responses we receive from the thousands of readers of the newsletter. So many of you have taken the time to comment on an article, express support or challenge, add to the discussion from your own experience, or just say thanks. Countless numbers of you have said that it is the one newsletter you read regularly.

Some of the reasons you said you appreciate *The Northwood Perspective* are that it is personal (it comes from the experiences of real people doing real things), relevant (it covers actual issues that families are facing, not just technical investment topics) and speaks in plain language (it is written in a way that is accessible and not overly complicated). So, thanks for your support, feedback and encouragement over the past 50 quarters.

There have also been a few interesting spinoffs from the newsletter. One of them is our *Northwood Quarterly Reading List* of articles that bring further perspective on the world around us and how we can think wisely about it. The feedback on this list has been amazing as well. Please continue to send us your comments.

If you are not signed up for the newsletter and reading list, you can do so on the home page of the Northwood website. ([www.northwoodfamilyoffice.com](http://www.northwoodfamilyoffice.com))

The other spin-off is my recent book, *Wealth of Wisdom: The Top 50 Questions Wealthy Families Ask*, co-authored with my colleague Keith Whitaker. (It seems like the number ‘50’ is today’s theme!) The motivation for the book comes from the same place as the newsletter. We wanted to help families address the important issues that they face every day, and bring practical expertise from around the globe, right to their doorstep.

The book answers questions like:

- How do we raise responsible, independent, and productive children?
- How can we manage conflict in our family?
- How can we ensure the success of our successors?
- What return should we actually expect from our investments?
- How should we think about risk?
- How can we find a good advisor? A good trustee?

At the end of each chapter, there are questions for further reflection and additional readings and resources so families can continue the discussions on their own. We have also created the *Wealth of Wisdom Podcast*, a series of fascinating interviews with our contributing authors (see the image of the mobile podcast studio on the right). The podcasts, chapter summaries and bios of the contributing authors are all available on the book’s website ([www.wealthofwisdombook.com](http://www.wealthofwisdombook.com)). Be sure to click on the link to check it out.

We really hope that the newsletter, reading lists, and our new book bring valuable perspective to all families.
Q&A With Our First Client Family

Scott Hayman, CPA, CA, CFP, TEP

Northwood Family Office was incorporated in February 2003, which means that 2018 marked our 15th anniversary. To celebrate this milestone (and the 50th edition of The Northwood Perspective), we decided to ask our first client family to participate in a Q&A on their 15 year relationship with Northwood.

The Smith family started working with Northwood in 2003 after concluding the sale of their family business the previous year. Northwood’s relationship with the family has grown over the years, and we now maintain accounts for many members of their extended families. For this 50th edition of The Northwood Perspective, we interviewed brothers Allen and Bob Smith, and their cousin Chris Smith. All three were owners of the family business that was sold in 2002.

[The questions and answers below have been edited and condensed for clarity. All names have been changed for the sake of client confidentiality.]

1. You were our very first clients. That was a big step. Did you have any hesitation about that?

Chris: No. The professionalism that was exhibited from both Scott and Tom made us feel comfortable that you would guide us through what we needed to know and to prioritize this.

Allen: Simply the answer is no. Both Tom and Scott came highly recommended by a person I trusted. I felt I was still in control and there were enough checks in balances in the system to ensure my money was safe. I also was very attracted to the vision they had for their company and the services they offered.

Bob: I was a little apprehensive as I had just severed a less than satisfactory relationship with my prior advisor.

2. How did you decide to work with Northwood vs. the other options available to you?

Chris: Northwood offered the most complete package of services. We felt a sense of trust that was important.

Allen: Northwood was unique in the services they offered. There were plenty of financial planners, tax experts, lawyers and bankers, but Northwood brought to the table a collective approach which was very valuable to me.

Bob: I was looking for an advisor that provided a comprehensive list of services. Northwood provided all of that and more, on a very personal basis.

3. What are the three most important things you receive from your relationship with Northwood?

Chris:
- Expert advice and implementation on a wide range of estate planning tools
- Tax planning advice, and
- Lifestyle balancing

Allen:
- Forward thinking and planning
- A collective approach, and
- Professional people (with long tenure at Northwood)

Bob:
- Regular contact with an experienced and senior partner of the firm
- They are continually offering new ideas to enhance my portfolio, and
- They look after the details for me (i.e. tax issues)

4. How do you explain to others what Northwood does for you?

Chris: Northwood provides peace of mind and confidence for my family in the following areas; estate planning, tax planning, insurance needs, financial management, investment planning and succession planning.

Allen: I describe Northwood as my team of professionals who oversee the financial, legal, strategic planning needs of both my personal and business lives. They manage all the professional services I require to ensure the execution of a prescribed plan.

Bob: A full service at a very personal level. They are always coming up with new ideas. I feel very confident with my financial progress.

“I describe Northwood as my team of professionals who oversee the financial, legal, strategic planning needs of both my personal and business lives. They manage all the professional services I require to ensure the execution of a prescribed plan.”
5. When we started working together, your kids were younger. It’s now 15 years later, and they are all young adults, in some cases, starting families of their own. How has your view of your children’s involvement in your financial affairs changed over that timeframe?

**Chris:** My view is always evolving. We were very cautious initially because we didn’t want our children to feel an inordinate sense of privilege. Over the years, we have relied on Northwood to help us bring a well-rounded education to our children around financial management. This continues to this day. We really count on Northwood to help us in family meetings as we gradually educate our girls about our estate planning.

Additionally, all three of our daughters have been meeting regularly for a number of years with the Northwood team. The assistance that Northwood has helped them with ranges from planning family meetings, educating them about investing and assisting them with picking companies for their portfolios, working with them on budget planning as they entered university, helping them determine financing strategies as they purchased businesses, and most recently guiding one daughter and fiancé on home ownership options.

“My relationship with Northwood has only grown stronger over the years. I trust them, as I know that they sincerely have my family’s best interests at heart.”

**Allen:** My kids need to have their own lives and their own successes and failures, but they also need to be prepared for what lies ahead when they will need to manage their family’s wealth. Northwood has been very valuable in starting to prepare them for that time. This way they are able to learn today about investments, tax, and the value of a plan.

**Bob:** Northwood has been very helpful in educating my family in financial planning. We have started a series of family meetings that assist with important issues such as the sharing of the family cottage and the purchase of their first home.

6. Can you name one specific example where Northwood helped you out with an important problem you had?

**Chris:** I can think of many examples ranging from fairly complex tax planning to advice and analysis on private equity opportunities.

**Allen:** When I stopped earning US income and stopped filing income tax with the IRS – the IRS still wanted to assess me tax – Northwood led the process of coordinating our accountants and lawyers to ensure the IRS finally shut down my file – which was easier said than done.

**Bob:** There have been many activities that they have assisted with. A very important one was the purchase of our home in Florida. A trust was created to protect our assets from unnecessary probate charges.

7. How has Northwood changed over the past 15 years, and how has your relationship with the firm changed over that timeframe?

**Chris:** Northwood’s success has been directly attributable to their listening skills. They have grown as a result of treating every client like they are the only client. My relationship with Northwood has only grown stronger over the years. I trust them, as I know that they sincerely have my family’s best interests at heart. Every interaction that I have had with all associates has been positive!

**Allen:** Fortunately the relationship has not changed – I am still dealing with the same people I started with. They delivered what they promised day one and continue to enhance their offerings – It is very difficult for a company to grow like Northwood has grown and still deliver – Northwood has done that well.

**Bob:** I am very impressed with how they continue to look for new opportunities and services for us to consider. Even though they have continued to grow, I feel that there is still a great amount of stability and progress in their service offerings. I always feel like a valued client.

8. Chris, this last question is specifically for you. When we were discussing working together back in 2003, you said you understood what we would do for your family for the first two years, but weren’t sure what we could do for you after that. Seeing as you’re still a client 15 years later, how has that view changed over time?

**Chris:** Hindsight is 20/20. I could not have imagined 15 years ago the extent of the value that Northwood would still be providing myself and my family today! Nor can I imagine not having them by my side. Life changes, and it’s nice to know that Scott and Tom and their team are right there with us helping guide us appropriately.

9. Any closing comments?

**Bob:** It has been a great partnership. They are always there making sure everything is working well in my financial world. I appreciate their efforts in support of my family as a whole. They have been helpful in my guidance through the ups and downs of financial planning.

Congratulations to Tom and Scott and the Northwood family for 15 great years.

*We want to express our thanks to the Smith family for taking a chance on a brand new firm with zero clients 15 years ago, and for their continued faith in us. Thank you for participating in this Q&A. We look forward to working with all of you over the next 15 years.*
Roller Coaster Markets Require Perspective and Discipline
Russ Rodrigues, CFA, CIM, MBA

In light of recent market volatility, this quarter we have decided to replace our Investing 101 quarterly feature, with a market update from Northwood’s Director of Investments, Russ Rodrigues.

Looking back at 2018, stock market investors experienced quite a roller-coaster ride. Canadian and US markets crept slowly higher in a relentless ascent for the first three quarters of the year. Then in early October, they abruptly tipped over into a free-fall descent, followed by several more ups and downs for the remainder of the fourth quarter. The wild ride wasn’t limited to stocks. Nearly all risky assets sold off as investors sought safety in cash and high quality bonds.

While the size and timing of descents can be fully anticipated on actual roller-coasters, predicting the timing or magnitude of investment market downturns isn’t nearly as easy.

At Northwood, we make no attempt to guess at when or how far the markets will decline, or what path of ups and downs they might take along the way. We will not suggest “buying the dips” or “selling the rallies”, or any other tactical approach to trading the market’s movements. Instead, you’ll see a patient, disciplined, long-term approach to managing risk and liquidity, which is aimed at helping our clients achieve their goals regardless of the gyrations of the markets.

Even though no one can anticipate the timing of market reversals with any degree of precision, this current sell-off is not entirely unexpected. We are in a contractionary phase of the credit cycle, and valuation multiple contraction is exactly what is supposed to happen. All else being equal, when interest rates rise, the fair market values of capital assets (like stocks) should be expected to fall.

Interest rates have indeed been steadily rising as the US Federal Reserve and the Bank of Canada have ratcheted up their policy rates and withdrawn some of the extraordinary monetary stimulus that has provided highly favourable financial conditions for the last decade.

Though nobody was able to anticipate the date that this looming monetary policy transition would take place, we can confidently say that we are now in the midst of that transition. Asset valuations have begun to contract, but are still high by historical standards (the MSCI All Country World Index is currently valued at 9.4x EBITDA, vs. its 10 year average of 8.5x and a longer term average of around 7x).

Above average valuations during a contractionary phase of the credit cycle suggests that prices could easily fall further. Will they? That’s anyone’s guess. For several years we have anticipated that when the accommodative monetary policy was eventually neutralized, the historically high stock market valuations would inevitably return to more normal levels. As such, we’ve been cautious about keeping equity exposures from rising above target allocations, and Northwood’s roster of equity managers have positioned their portfolios defensively by focusing on ‘quality’ and ‘value’ stocks (which are generally much more resilient in downturns), or by increasing cash weights where permitted within their investment policy.

Episodes like this are the reason that we focus on selecting investment managers who have demonstrated a long history of generating above market returns with low “downside capture” (i.e. falling less than the market during downturns), even if this means sacrificing some upside participation during strongly rising markets. In a volatile fourth quarter, our global equity managers performed as expected. While the equity markets were down 8.8% (equally weighted index), our managers’ portfolios declined by an average of only 4.3% (equally weighted composite). For calendar 2018, their combined portfolios increased by 0.7% vs. a 3.6% decline for the markets.

How does this market correction affect our investment strategy? For the most part, it doesn’t. Our strategic asset allocation process remains consistent. For clients’ long term goals (generally those beyond 15 years) where short term volatility isn’t a major concern, equities remain the best asset class for generating capital growth. For nearer term goals (generally those less than 5 years) a mix of lower risk assets, such as cash and fixed income securities, provides greater safety but gives up some expected return. In neither of these cases is any adjustment to exposures necessary.

However, for any intermediate term goals (those between 5 and 15 years), there’s some optimal mix of risky and low risk assets that takes advantage of portfolio diversification and maximizes the probability of achieving that goal for an acceptable level of risk. Determining that optimal asset mix requires some analytical modeling, and is a function of the expected returns of each asset class.

As equity prices have been falling, their expected future return has been rising. As those return expectations rise, our asset allocation model will begin to increase target equity weightings, and our clients’ portfolios will benefit from the downturn by accumulating more equity exposure at lower prices.

It’s normal for investors to look at their statements and perhaps feel some anxiety over short term declines. However, it is important to keep in mind that in the long term, volatility is not necessarily risk, it can be opportunity. But to take advantage of these episodic opportunities investors must maintain perspective, liquidity and discipline. If you have any questions, please don’t hesitate to contact us.
Northwood Staff Profile – Claire Hunt
Claire Hunt, CFA, MBA

In this quarterly feature, we help our readers get to know some of the people who work at Northwood Family Office. In the ‘Northwood Staff Profile’ we interview a key team member at Northwood. This quarter, we introduce Claire Hunt, who works on the client service and investment research teams.

1. What do you do at Northwood Family Office?

At Northwood, I split my time between the client service team and the investment research team. On the client service team, I work directly with our families and foundations on a wide range of projects and help to manage their day-to-day financial needs. On any given day I might be mapping out a will, reviewing insurance options, assessing tax planning strategies, or projecting out cash flow needs. On the investment research team, I spend most of my time analyzing investment managers and strategies.

My background is heavily tilted toward investment research. I completed my MBA with a focus on investment management; I am a CFA (Chartered Financial Analyst) charterholder; and I’m registered with the Ontario Securities Commission as a Portfolio Manager. I’m currently working on my CFP (Certified Financial Planner) designation to help round out my planning knowledge base, as my future goal is to transition into a broader role surrounding client services.

2. What did you do before Northwood?

I started my career with an independent Toronto brokerage firm on their institutional equity trading desk. The experience provided me with an intimate look at the inner workings of research, trading, and investment banking. From there I moved into retail equity trading and then foreign exchange trading. I really enjoyed the fast-pace of the trading desk, especially foreign exchange, but I knew I wanted to eventually interact more with clients and work with them on all their financial needs. With my next step, I moved into investment manager research and portfolio analysis, helping to construct and evaluate client portfolios. This investment research experience led me to Northwood where I now get the best of both worlds – working directly with clients and performing research and analysis.

3. What do you enjoy most about working at Northwood?

There are a lot of things to enjoy about working at Northwood but I will focus on my two favourites. First, I really enjoy the team culture. Northwood has worked very hard at choosing talented people who work well together. At our company offsite in June, we learned that we have a very diverse mix of personalities with a wide variety of strengths. Everyone brings something different to the table. Our day-to-day work is extremely collaborative as we tackle projects and problems together. I’m constantly learning more about tax from my CPA colleagues and I’m happy to help them on investment questions.

Second, I really enjoy working with our clients. I love getting to know our clients and building relationships with them. At Northwood, we are heavily involved in all areas of a family’s wealth. It turns out that the bulk of what we do has nothing to do with numbers. We get the privilege of seeing the entire family situation, which enables us to look at family issues from every angle and help problem-solve. You can see the impact this has on the family, as they are able to untangle complex problems and make informed decisions.

4. What are your favourite things to do outside of work?

My pastimes have certainly evolved over the years. Growing up in Newfoundland, I played a variety of sports and became quite competitive in hockey and rugby. In fact, hockey brought me to Ontario on a scholarship to a private school which then led to playing varsity hockey at Queen’s University. At the same time, I made the Under 19 Women’s Canada Rugby Team and travelled to Wales for a tournament.

These days I play golf and spend time with my two-year-old daughter Alice, my husband Michael, our adopted nephew Tyler, and our soon-to-be (January 2019) newest addition. Michael certainly shares my passion for sports and Alice (and active baby number two) appear to be following suit. Who knows? Maybe we will enjoy family days on the links and rinks in a few years.

5. What do you think separates Northwood from the typical investment advisory firm?

I was first attracted to working at Northwood when I realized I would get a chance to work directly with clients without any pressure to gather assets or sell a product. I think this objectivity really separates us from other advisory firms, especially having come from that side of the industry. We work with clients and other professionals on every aspect of a client’s wealth and we evaluate products and strategies without any incentive to choose one over the other. Our client-centered approach creates trust with our clients and it also gives our team the freedom to truly tackle a client situation and come up with the best solution we can.
The Elevator Rule
Scott Dickenson, CFA, MBA

I have developed an investing rule of thumb that I like to call the ‘Elevator Rule’. Let me explain how the rule works. I live on one of the higher floors in a condo building in downtown Toronto. People ride this elevator down to reach the lobby, and up to reach the top floor gym. If I time my elevator rides poorly, I often have several different groups of people get on and off the elevator before I reach my floor, which means I hear multiple conversations on the same trip.

The elevator rule works as follows: If I hear two different groups of people have two separate conversations about the same stock, asset class, or sector, there is a good chance that the investment is in bubble territory.

I came up with the rule about a year ago, when I heard two people pitching the virtues of Bitcoin to their elevator riding partners at different times on the same ride. The first was a twenty-something woman trying to convince her Mom that her $10K investment in Bitcoin was the best financial decision she’d ever make (Mom was unconvinced).

After they exited the elevator, two guys around my age came on and proceeded to have a spirited debate about whether Bitcoin or Ethereum was the better investment opportunity. At the time (December 2017), cryptocurrencies were taking the world by storm. In the space of a year, the value of one Bitcoin soared from $789 USD on December 16, 2016 to a peak of $19,783 USD on December 17, 2017. When I overheard the conversations in that elevator, Bitcoin was near the end of an incredible year in which its value increased by more than 2,000%. Bitcoin was the future! How could anyone not be excited about it???

You know how this story ends. Bitcoin ended 2018 at $3,685 USD. This is a drop of 81% from its peak price of one year ago. If you owned $10,000 in Bitcoin at the top of the market (like the woman mentioned above), that investment is worth less than $2,000 today. Now the obvious counterargument is as follows: ‘While Bitcoin is down $17,000 this year, it was up $19,000 in 2017. Therefore it’s still up overall and investors are still in the black over a two year period’. This argument is correct, but it of course depends when you got in. Sadly, it does not reflect the actual experience of the vast majority of cryptocurrency investors, since cryptomania didn’t begin in earnest until September 2017 when the price crept above $5,000 USD for the first time. The moral of the story is that most people don’t actually get the returns that are trumpeted in the press.

In fact, most participants will need Bitcoin to double or quadruple in value from its current price just to get back to a breakeven position. They made the critical mistake of investing in an asset class in the months or weeks before the bubble popped.

So, the crypto bubble popped in December 2017 and has been steadily deflating ever since. But people still needed something to talk about on elevators. So what popped up to take Bitcoin’s place at the top of the list of investments that people couldn’t stop telling their friends about?

Marijuana! In October 2018, Canada became the second country (after Uruguay) to legalize the possession and use of recreational cannabis. In the lead-up to legalization day, Canadian companies involved in the production and distribution of cannabis, saw their values skyrocket on the potential of selling their products into this new legal market.

The best example of the Canadian cannabis craze of 2018 was Tilray Inc., a small cannabis producer founded in 2014 and located in Nanaimo, British Columbia. The company went public in July 2018 at a price of $17 per share. Within two months (Sep. 19), the stock reached $214 per share (and traded close to $300 earlier that day), suggesting a market capitalization of $20B. You don’t need to have seen Narcos: Mexico to know that $20B USD represents a HUGE amount of marijuana. On this day, a company with 330 employees, on an island off the western coast of Canada, was worth more than American Airlines, CBS Corp. and Clorox.

Rotman Family Wealth Management Program – May 2nd to 5th, 2019

For the fifth consecutive year, the University of Toronto’s Rotman School of Management is once again pleased to offer the Rotman Family Wealth Management course. This 4-day intensive program for family members and family office staff will be held in Toronto from May 2nd to 5th, 2019, and will be taught by Tom McCullough and other key faculty members and wealth management leaders. For more details on the course (including registration information) please visit:

http://tinyurl.com/od5kr7s
Now I’ll admit that I never heard two separate conversations about investing in marijuana stocks on the same elevator ride, so the ‘Elevator Rule’ doesn’t officially apply. Having said that, I have heard lots of general chatter on this subject on the elevator, listened to friends discuss how much money they were making in the sector, and seen other friends leave the corporate world behind to join marijuana start-ups. In other words, all the ingredients for a bubble seemed to be firmly in place.

You know what happened next. Legalization day came and went, and Tilray ended the year down 67% from its peak price, while Canopy Growth Corp (Canada’s largest marijuana company by market capitalization) dropped 50% from its peak in mid-October. It would appear that another bubble had popped.

The story for cannabis stocks (and Bitcoin) is ongoing, and I have no doubt that there will be peaks and valleys in the years ahead. I am not trying to argue that there is no money to be made in either asset class. What I am suggesting is that money isn’t free. Nine times out of ten, if you’re in an investment that doubles in either asset class, it is probably NOT the time to join the party. In fact, it is usually the time to run in the opposite direction.

You know what people don’t talk about in condo elevators, or brag about at cocktail parties, or try to convince their friends is a great investment opportunity? An 8% per year annual investment return. This is what the TSX (Toronto Stock Exchange) has returned on an annual basis over the last 30 years (1988-2017). The US market has been even stronger, with an average of over 10% per year returns in CAD terms over the same time period. The problem is that 8% or 10% per year doesn’t seem like an exciting number. Doubling your money in the space of a month, or a week, or a day, is much more thrilling than doubling your money over eight years, as it would take with annual returns of 9%.

Here’s the thing though; if your investment returns are similar to the returns you can get spending an evening at a roulette table, you’re not really investing, you’re probably gambling.

I wrote about the power of compounding in the last edition of the newsletter, so I won’t go into great detail on it here. Just one quick calculation; $1 million growing at 9% per year turns into $13.3 million in 30 years. A pretty attractive result without the heart-wrenching volatility of speculative investments. Food for thought as you count the floors on your next elevator ride.

Wealth of Wisdom is Out Now!

Tom McCullough’s new book, Wealth of Wisdom: The Top 50 Questions Wealthy Families Ask is out now. The book includes essays by over 50 of the world’s top thinkers and practitioners in the field of family wealth. For more information on the book, including podcast interviews with contributing authors, please visit www.wealthofwisdombook.com

The book is available for sale at the following Amazon links:
https://www.amazon.ca/Wealth-Wisdom-Questions-Wealthy-Families/dp/1119331536

If you’re interested in the discounts available on bulk book orders (25+) please email Lisa Fabregas at (lf@northwoodfamilyoffice.com)

Who is Northwood Family Office?
Northwood Family Office is an independent, privately-owned boutique family office which provides comprehensive Net Worth Management™ for wealthy Canadian and global families. Northwood clients have significant family net worth, typically $100M+. The firm acts as a Personal CFO or Chief Advisor to client families using a dedicated team of professionals who oversee and manage their integrated financial affairs. Northwood Family Office is Canada’s leading independent multi-family office and has consistently been ranked the ‘#1 family office in Canada’ in the Euromoney Global Private Banking survey. For more information, visit our website or contact Tom McCullough for a confidential conversation.