Mark Noble
Hi, it's Mark Noble, Executive Vice President of ETF Strategy at Horizons ETFs. And today, we're going to talk about balanced ETFs. Now, it may seem like a sort of a boring ETF topic to discuss, how do balanced ETFs fit with a larger portfolio?

Mark Noble
There's nothing really exciting about balanced ETFs, but what's astounding is the amount of money in balanced ETFs, not just on the ETF side, but you're looking at roughly about 40 to 50% of the mutual fund side in Canada, probably almost one out of every $2 in the larger fund complex in Canada is invested in balanced funds. It's really the go-to for the vast majority of Canadian investors.

Mark Noble
And so, here to discuss this topic with me today is Dale Roberts, the primary author at cutthecrapinvesting.com, a well-known Twitter aficionado and blogger, as well as a weekly MoneySense commentator. It's always fun to be following Dale on social media. And of course, he's a big conduit to this massive growth of large self-directed investors that we've seen this year.

Mark Noble
And I want to give a little bit of context, Dale, before we begin about how big this trend is. We look at the number of self-directed investing accounts that opened last year, and it was roughly about 1.7 million new Canadian investors entered the Canadian marketplace opening self-directed accounts according to data from Investor Economics.

Mark Noble
Now, this is an astounding number because we now are looking roughly at total accounts as of December 2020, roughly 9.1 million Canadians. And that number actually then would be not quite above both financial advisers and full-scale brokerages, but it's certainly catching up, and it's bigger than any one of those individual, whether it's the bank planners or the IIROC advisors, it's bigger than any one of those individual distribution networks.

Mark Noble
So very quickly we're seeing this moment where there's a big movement of investors towards self-directed investors. And I think it's fair to say that many of them are gravitating towards these balanced ETFs. So Dale, as somebody who really follows the self-directed space and is a well-known self-directed investor yourself, what makes these balanced ETFs so popular?

Dale Roberts
Well, and thanks for having me on, Mark, always a pleasure. I guess, it's just, as you said, it's the boringness of it because most investors really... I mean, there's a segment of us that love to play around and get our own assets. A lot of people will mix stocks with ETFs and create that kind of hybrid portfolio, but a larger segment, really, they just want a managed portfolio. They want it done for them. They don't want to have to have their fingers in the pie. They don't want to rebalance. They just want to set it and forget it. They can add monies on a regular schedule, even better, you can automate it. Again, they just want it on autopilot.

Dale Roberts
And it's a good thing for many too because in that category and they recognize that, if they start playing around, we know that they can can make mistakes. So it really is the boringness of it all that makes them wonderful and great. And again, as we often say on my site or on MoneySense, the one ticket, the asset allocation, they're game-changers in Canada, absolutely.

Mark Noble
And we've seen a lot of money move in towards these products. But ultimately, what kind of investor are these geared to when you're looking at, if someone asks you, "I'm looking at getting into ETF investing," or, "I'm looking at getting into investing," what are some of the key kind of pillars that you would talk to them about? And which case would you probably suggest that they use a balanced or one ticket ETF solution?

Dale Roberts
Well, I guess, I mean, they are hybrid in a sense because while they aren't managed portfolios and are really simple, and they're really boring, the really important distinction here is you still, you have to press that button. It is self-directed, right?

Mark Noble
Right.

Dale Roberts
And it's crazy how hard it is, even for folks who understand what it is and know what's in it, have a good degree of knowledge about it all, but for them to get over that hump and just press that button, it's a real challenge for many.

Dale Roberts
And I've had a lot of, again, my site's not about advice and I'm not a planner. I don't take portfolios, but if I have someone that's a friend or I'm close enough to, I mean, I'll get on the phone with them and have to get them over the hump to go, "Okay, you can, you're looking at the screen, you know what you're buying. Go ahead, hit it. You know what you're buying." But for others, again, it's just that big leap.

Dale Roberts
So again, on the other side, again, they might go robo if they want that sort of one ticket in his hand and someone to do it for them. But again, also the other distinction is to know which ones to buy because we know that there are the five or six different stratas, if you will, of risk level.

Dale Roberts
So I have a couple of posts on my site where give them the basics on time horizon, risk level, and the amount that the portfolio, the draw down that could happen in a really serious market correction, just to help steer them towards getting the appropriate portfolio.

Dale Roberts
So that's a major distinction too is, yeah, I want in. I love the concept, but which one do I purchase? And on MoneySense, we're working on some tools as well to help along in that fashion. But again, the main distinction there is that they're simple, but it is a self-directed process to get into them.

Mark Noble
We see that a lot of the ETFs in Canada are kind of bucketed by sort of like a... There's usually a conservative, a balanced, and a growth. If I'm a self-directed investor, what's my decision process in trying to look at which one maybe works best? Intuitively, what do you think investors are looking for on that determining which one of those three buckets make sense?

Dale Roberts
Yeah, again, hopefully they come down to, I mean, two of the main determinants, of course, are your time horizon and really, I mean, start with if you don't have a time horizon of three to four years or more, you're going to be stuck in the GICs and savings accounts where you're probably going to go backwards with that bucket of money. But that's fine because you're just trying to protect it.

Dale Roberts
And from there, if they have the longer time horizon and they have a good risk tolerance... So that is the main thing, of course, is do they have the risk tolerance for a major dip? We know that all stock portfolios can fall by 40, 50, 55%. Start adding more bonds, and again, then we're going to start to lower that level where typically on a major correction course, a balanced portfolio would be 40% bonds or more, might only fall by 20, 25%. A really conservative portfolio could fall, let's say, by 10, 15%.

Dale Roberts
So again, it's knowing themselves, know thyself, and match your risk tolerance level. It's probably the biggest mistake is when you invest outside of your comfort level because that's going to create a permanent loss where markets go down, you don't like what you're seeing, you press that sell button, and you create that permanent loss.

Dale Roberts
So tough to know for a new investor, of course, because if you haven't been through a correction, you don't know what your risk tolerance level is.

Mark Noble
Plus you have time on your side, right?

Dale Roberts
You have the time, yeah. So I always advise folks to say when you're assessing your own self-assessment of your risk tolerance, err on the side of caution. Learn, go through a correction, if you will, because you have to know what it feels like. It's a feeling. And then, once you go through, it's like, "That wasn't too bad. Maybe I can go a little bit higher."

Dale Roberts
Eke your way up the scale, not down, because if you're going the other way, you probably created permanent losses. And I've talked to too many investors, I would say, they started investing right before 2008, 2009, had a terrible experience, and they're gone forever.

Dale Roberts
When I was an advisor at Tangerine, I talked to so many who had all of their monies in cash and would chat with them about why. And they said, "You know what? I had a really bad experience... " Either in 2000 in the .com crash or the financial crisis 2008, 2009, and they're not coming back. So you don't want to make that mistake where you scare yourself away for life because you're giving up so much in potential gains and wealth.

Mark Noble
What are your thoughts on the equity allocation? Because if I look at the flows this year, the vast majority of flows and this even includes Horizons ETFs, the vast majority of our flows in this suite have gone to our HGRO, so HGRO, our growth product, which is 100% equities. And then, a lot of money has been steered towards our competitor ETFs with a grow mandate, which is typically 80/20. I think maybe a couple of them are 70/30, but most of them are 80/20.

Mark Noble
So we're definitely seeing people move towards the heavier equity allocation. Do you think that's a strategic decision where people have abandoned fixed income, or is it related to demographics? Just curious, this is definitely something that I'm seeing that there seems to be a view even amongst the self-directed community in Canada that 60/40 doesn't cut it anymore.

Dale Roberts
Yeah. Well, I mean, bonds getting a lot of bad press, so there's a lot of stuff out there that the bonds just stink, stay away from them, worst investment you'll ever make. I'm shorting bonds and blah, blah, blah. Whereas the stocks are the rock stars, and they're getting all of the glory.

Dale Roberts
So I think there's still a lot of chasing, and it's fine if, like you said, if they have the time horizon, that's okay. You can recover. I think it might be a bit of a mistake if somebody's really, really heavy equities or they're all equities going, or even what you call in the retirement risk zone within 10 years, personally, I would think that's a mistake. Because a major correction, again, stocks could stay under water for 3, 4, 5 years.

Dale Roberts
We know that even, you look at US stocks and take real returns factoring in inflation, we have the last decade where the US stocks were negative. They delivered no real return for 9, 10, 11 years.

Dale Roberts
And some portfolios are... You look at that global cap weighting where the biggest companies in the biggest countries with the most success get the weight. I think the US is something now ridiculous like 67% or something of a global weighting. And that market is, I mean, there's no other word, but overvalued, if you look at all the metrics that... It's approaching where we were, well, it surpasses the Depression level and it approaches the financial crisis. It doesn't mean that we're going to get a correction tomorrow, but we know that over time, valuation does matter.

Dale Roberts
So anybody, I think, approaching retirement within 10 years or so, I think they could at least go a balanced growth area, whether that be in 70, 80%. And then, you would know as well as I do, if you look historically over many longer periods, that a balanced growth model doesn't give up anything to whole equity. Those market corrections are great equalizers.

Dale Roberts
And yeah, I would think most approaching or certainly in retirement would need bonds. I'm also in the camp, not a popular place, of gold and commodities. I'm also in the Bitcoin camp. A different discussion, but I mean, there's really no little respect for gold or commodities, which are the greatest inflation fighters.

Mark Noble
Well, I think from my perspective, when I look at fixed income, a lot of the modeling on the 60/40, and the reason it's sort of this golden ratio that's used for balanced portfolios is mathematically over the last, let's say 40 years going from like 1978 to now, it's done quite well.

Mark Noble
But it's done quite well because when you look at periods of financial impairment, the high relative yield of bonds historically, particularly if we look at periods like the early 1980s, 1994, even to a degree, 2007, 2008, 2009, the financial crisis, you had a yield offset that kind of off-setted the ability for you to deal with those equity draw downs. I guess the challenge now is your interest rates are so, so low, right?

Dale Roberts
Yeah, they're likely to, on their own make, likely or should make nothing.

Mark Noble
Right, exactly, which means that you need to kind of... It's not that 60/40 is dead, it's just you need to look at the risk dynamics differently. And so, I guess the one thing I will mention, which you highlight is there aren't any risk off asset classes in equities. If equities decline, there's nowhere to hide in the equity market. If I buy emerging market equities during a US equity market correction, historically, statistically, likely they're both declining.

Mark Noble
But you do get some risk off benefits with being in US treasuries. But you may not necessarily get them actually with being in something like corporate credit, like we saw in March of 2020, where corporate credit declined by 15, 16% at the worst of it. And only treasuries, as you highlighted gold and cash, were kind of the only asset classes that allowed you to hide that out.

Mark Noble
So I do wonder if that kind of experience is reframing people's thoughts about how much fixed income exposure do I really need? And is the new normal more like 70/30 or 80/20?

Dale Roberts
Yeah, well, exactly, which is, again, and I've done the post on your balanced portfolio, right?

Mark Noble
Yeah.

Dale Roberts
Which is a great rethink at 70% equity. But I love to look at that because it really aligned with a lot of the writing I've been doing on SeekingAlpha for a long time, which was maybe use less bonds, but use some better bonds. There's the treasuries. And I love that idea. I think that, I mean, obviously that's why your balanced portfolio is kicking you know what out of the other ones, probably and likely to continue. And if you do get that rebalancing, you're going to get a little bit more torque to the other side, right?

Mark Noble
Right.

Dale Roberts
So, I mean, you guys also have what I was always calling growth kicker with the NASDAQ in there. So actually really closely aligned with a lot of the stuff that I had on SeekingAlpha. So that market, again, that's part of the overvaluation area for sure. But it's going to rely on that counterbalance and rebalancing between the two. So again, I do like the rethink idea. Again, it was great to research and putting that post, very popular post in.

Dale Roberts
I think people look at that too. Again, the risk profile is not that different than a traditional 60/40, you're just getting a little more torque. And again, that's by using some better bonds. And I do think people should look at re-evaluating what is a balanced portfolio?

Mark Noble
Well, and it's interesting because just being completely objective at our products, this year, our bond strategies are in the HTB, which is our US treasury bond ETF, which is a fairly significant component of the fixed income portion that we do have in those portfolios, it's quite a bit down relative to, let's say, an aggregate bond ETF.

Mark Noble
But as we've highlighted, because we have a higher equity allocation, it's offset those losses. But then, at the same time, we have that mathematical term convexity working where if we do get a sell off, that portion of portfolio ideally comes back into play.

Mark Noble
So the reason we have a higher equity allocation on our ETFs is because we're benchmarking it to, or anchoring it to a higher fixed income allocation of much, much more conservative fixed income, which is US treasuries.

Dale Roberts
And again, it's that rebalancing premium, right?

Mark Noble
Right.

Dale Roberts
Again, there's that premium of just looking at all the assets themselves. But if you start rebalancing, you can see you can get some torque even to 1% or more over time. And again, that's why I always say to, I tell folks, don't look at assets in isolation because why would you when it's called balanced portfolio? It's not about the stock, bond, gold, short bonds. No, it's balanced. It's teamwork. It's like a hockey team. You got defense. You got a goalie. You got the forwards. You might have some defensive specialists.

Dale Roberts
But it really is about... And these days with bonds, typically probably not going to do much on total return themselves. I think it's time to look at them, they really are just risk managers, right?

Mark Noble
Right, right.

Dale Roberts
And it's true that if you look at them in isolation, you probably wouldn't buy them because they don't make a lot of sense. It really is just if you want that convexity, you want that torque to the other side.

Dale Roberts
So I think that's a way for investors to look at it is that it's not about in isolation what's it going to earn? What is it going to do when stock markets tank? Now, they've outlawed stock market corrections for now, but it's possible that they come back. I mean, everything's kind of controlled these days, definitely on sort of the economic front or political front.

Dale Roberts
But they may lose control of a few things moving forward, and I wouldn't be surprised this summer if we saw some good corrections. I wrote a post recently, I think the investors will take the summer off. And as you mentioned, all those new folks that came in, right?

Mark Noble
Yeah.

Dale Roberts
There's some evidence already that they're just like, "I'm going to go live instead." I think when they get bored, and we know that they have been... The retail investor became a force in 2020.

Mark Noble
Really did.

Dale Roberts
We have the numbers that we haven't seen in actual... Being that marginal buyer and being able to support stock markets on their own. If they take a break, the corrections might not be violent, but I could see them losing their attention in the summer and en masse maybe just kind of leaving. And yeah, we might get some good corrections, and we'll see how the bonds do when that happens.

Mark Noble
That segues nicely actually into another question I have, which is just how do you manage your psychology, particularly as a new investor? Because I think when you see the number of new entrants in the marketplace, I think there's a level of entertainment and fun with it. Like we see AMC, today's June 2nd, 2021, AMC is up over 100% over the last couple of days. Clearly a speculative investment, but there's also a fun kind of excitement around that.

Mark Noble
And then, we're talking about building diversified, balanced portfolios and historical returns of fixed income. How do I manage that as I'm a self-directed investor? Because this whole investing gamut is at my disposal, and even yourself, I think you've got diversified into things like cryptocurrency and other areas that are a little more speculative, but you have some belief in it. How do you manage the what should I be putting in a balanced sort of core strategy versus how do I maintain my sort of interest level in areas that might be speculative? Do you use a core and explore approach, or is that something that's discussed a lot amongst your community?

Dale Roberts
Yeah, I think I look to the younger folks. I use my son, who's 21 who just started getting into investing and his friends are, and some other readers. I think a lot of them are starting by building quite un-diversified stock portfolios. And it's going to be interesting, I think, once again, you don't want to see a major correction come along and wipe these folks out.

Dale Roberts
I actually think it's a really positive thing for them even to start... As long as they don't have too much at risk, and a lot of them are just playing with a few thousand here and there. Probably, a little more smarts than you would think going on. These younger folks are really curious. They've got that thing called the internet, and they get together as a group. And even on the Canadian Reddit forum is probably a little more sensible than the American side, if you will. So they're helping each other out. They're going on blogs and getting some pretty good information.

Dale Roberts
But they're not really building diversified portfolios as of yet, I hope they get there. And again, the hope is one day that they move to this sort of the one ticket area, or at least build their own ETF portfolio, right?

Mark Noble
Right.

Dale Roberts
But I've tried, you can't get them there. They want to play, and it is play. And actually, I was just talking to my son, and told me about one that his friend gave him, a tip, and it didn't work out that well, and I think he bailed on it. But all his other core stocks, like I say, explore a couple of banks. He got into energy stocks, which I've been telling my readers for quite many, many months to consider the energy producers side, and they're doing well, and I think a US market ETF. But it was the more really exploratory things that for him and his buddies that are going the wrong way.

Dale Roberts
So the hope, I mean, again, you can build a really good, simple stock portfolio. It doesn't take a lot of stocks. I hope they get there. I did a post on, I'm not sure if you're familiar with the Beat the TSX portfolio, which has a ticker, it's BT... It's not a real ticker, but BTSX. Has just 10 stocks of the highest yielding on the TSX 60, and it beats the market by like two-and-a-half percent.

Mark Noble
Over what periods? Like how long time-wise?

Dale Roberts
Oh, this goes back to the early '90s or something.

Mark Noble
Okay.

Dale Roberts
I don't know. Someone else took over the site. And again, there's a lot of other real simple strategies like that. So I'm hoping it's like see what you can do with 10 stocks. And at that point you might agree, well, maybe I can just go buy an ETF at that point, right?

Mark Noble
Yeah.

Dale Roberts
Anyway, the hope is that they don't get trapped as they kind of play around because there's a lot of playing going on. That they get through it and their knowledge level can get to a certain level, and even their comfort level and risk tolerance before we get any major correction. But again, in the end, I mean, you hope they're all going to eventually come to some form of a balanced portfolio, whether it be really aggressive or kind of down the middle.

Mark Noble
Very cool. Listen, I just want to thank you for taking the time today. It's always a pleasure reading your writing on MoneySense and your blog. And I also love the fact, as we see this greater amount of social engagement, it's fun to talk to influencers like yourself and get kind of a mindset because I think here on sort of the Baystreet side of things, we tend to sort of lose sight of this undercurrent of real excitement and intelligence and looking at the investment management industry a little bit different than that portfolio manager who's been doing it for a long time.

Mark Noble
And I think both are valid, but it's interesting to see when you get an intersection with things like asset allocation ETFs. So again, just thank you so much.

Dale Roberts
No, it's exciting. Thanks for, again, I remember talking to some folks that were frustrated too, they'd say like, "Don't underestimate these kids because that's how I came in."

Mark Noble
Exactly.

Dale Roberts
He goes, "No, we see what they're doing." And they go, "It's not that bad. There's obviously, you have little pockets." But he goes, "You can tell they're doing the research and they're picking their spots and building a tight, little portfolio." So again, let's hope that that continues. And great, and thanks for having me on. Always fun to chat.

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