

Guaranteed returns a calming concept

Rudy Luukko – Toronto Star, March 21, 2009

Maturity guarantees have long been part of the investment landscape, mostly through segregated funds sponsored by life insurers. A new twist on this theme comes from mutual fund sponsor IA Clarington Investments. It's promoting its four-year-old Target Click product line that – at current prices – features guaranteed positive returns if held to maturity.

The Target Click products are target-date funds, meaning they reduce their equity exposure as they near their fixed maturity dates.

Most target-date mutuals don't provide maturity guarantees, relying on asset allocation to manage risk for their unitholders. Non-guaranteed products include the Ethical Advantage, Fidelity ClearPath, RBC Target, Russell LifePoints and Scotia Vision offerings.

With IA Clarington Target Click, investors can lock in the highest month-end net asset value, even if they weren't aboard at the time the high point was reached.

The company has a calculator on its website at iaclarington.com that illustrates the relationship between current market value and guaranteed value at maturity.

For example, a \$10,000 investment made on March 16 in IA Clarington Target Click 2020 would have a guaranteed value of \$12,183 on the maturity date of June 30, 2020. That works out to an annualized return of 1.7 per cent.

The guaranteed annualized returns to maturity for the four other Target Click funds range from a high of 2 per cent for the fund maturing in June 2025, to a very slight 0.1 per cent for the fund that matures in June of next year. These guaranteed returns are possible only because the funds have fallen from previous month-end highs.

Actual returns are likely to be significantly higher. Each Target Click fund has three components. The largest is a strip bond designed to provide a guaranteed return. The other components are cash and, more importantly, an equity component that provides exposure to major market indices in the United States, Europe and Asia.

Target date funds have been hit by the market crash like other equity-exposed investments, though the IA Clarington funds have fared better than most. Despite having generally higher management-expense ratios than non-guaranteed funds, the four Target Click funds with three-year track records have all performed in the top 25 per cent of their peer groups, with either modest compound annual returns or single-digit losses.

The Target Click funds also have more growth potential than some competing funds with capital-guarantee provisions, offered under the BMO LifeStage and Mackenzie Destinations brands. Most of these target-date funds have shifted entirely to fixed income and cash to ensure they'll return at least the guaranteed amounts.

Guarantees are only as good as the credit quality of the guarantor, which in the case of the Target Click funds is Belgium's Fortis Bank, taken over by the Belgian government and considered by rating agencies to be a high-quality credit. But the chances of requiring the bank to make good on the shortfall are remote. "The funds hold the strip bonds, which are really what is providing the foundation for the guarantee," says Eric Frape, senior vice-president at IA Clarington.

Few if any investors would be satisfied with a guaranteed long-term return of 2 per cent, since even in today's low-rate environment you could earn higher returns with a five-year GIC. But the Target Click guarantees provide a measure of security for risk-averse equity investors. Given the carnage of the past year, no one can argue that such guarantees are worthless.

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