Investment Insights

Spring 2023

Change — The Only Constant

"It is up to humans to decide how AI technology is used and the extent to which it affects society." — ChatGPT, when asked: "Will ChatGPT change the world?"

Much continues to be made of the artificial intelligence algorithm (AI) ChatGPT and its potential to disrupt on many levels — we've already seen its substantial competence in writing college essays, prompting questions over whether it will change education as we know it. It has also ignited a debate about the deeper threat of our technological advances.

Change can come thick and fast, and the investing world is no exception. Respected investor Howard Marks believes that we are in the midst of a radical change in direction for the financial markets — a "sea change." With inflation and interest rates rising substantially over the past year, he sees this as a permanent departure from the "easy money" days of recent times. In his view, declining interest rates provided a tailwind for investing success over the past 40 years: growing the economy, reducing businesses' cost of capital while increasing profitability and providing a subsidy to borrowers. He suggests that inflation and interest rates are likely to remain more elevated than in previous decades, providing headwinds for the years immediately ahead.[1]

Where is this financial cycle headed? Only time will tell. Whether or not you agree with Marks' assessment, one thing is certain: Change is imminent. Every financial cycle differs from those that came before. The world is a far different place than 10 or 20 years ago — and, arguably, than even just a couple of years ago. But, changing conditions don't preclude the prospect of continuing to build wealth.

This is because change can also bring opportunity. Beyond its existential debate, ChatGPT exemplifies the human pursuit to advance. Let's not forget that within our generation, a shift to modern commerce, enabled by the Internet, has revolutionized the way we work, communicate and play — the benefits we may take for granted. Earlier innovations, such as those sparked by the development of railroads, electricity and the automobile ignited upwaves of economic growth that lasted for many decades. Consider the impact of the global petroleum industry or the assembly line introduced by Henry Ford — the latter changed global manufacturing processes forever.

As we navigate the changing times, investors should not overlook the value of thoughtful analysis and evaluation. These skills should be trusted to guide us through the longer term. This is because change is the only constant. Do you remember Wang or Commodore, the "high-tech leaders" of the 1980s? Or BlackBerry, the dominant "smartphone" in 2010? Sound portfolio management involves assessing the changing landscape and the potential opportunities to come, all while balancing the risks involved. This is one of my roles as an advisor: to distill the key factors influencing the financial markets from the mountain of available fact and opinion, and make informed decisions and recommendations that are tailored to support my clients in reaching their wealth and investment goals. Continue looking forward.

1. https://www.oaktreecapital.com/insights/memo/sea-change

In This Issue

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To My Clients:

Spring is here, with the promise of longer days and warmer weather. The winter months may have felt particularly long this year, especially as inflation continues to put pressure on many budgets and the financial markets continue to be volatile. We may all be looking forward to a bit of spring's revival.

As we enter a new season and you consider your finances, please let me know how I can be a resource. This may be as simple as a quick spring cleaning, such as updating registered plan beneficiaries. Or, as we deal with 2022 tax receipts and returns, it may be a reminder to review tax-planning opportunities in your investment strategy for 2023.

As we strive to make progress, whether it be with our investments or in other aspects of our lives, I hope that spring brings renewal, growth and expansion.

I Don't Want to Act as Estate Executor/Liquidator

It can be an honour to be named as estate executor (liquidator in Quebec),* as it signifies a person's trust that you will carry out their wishes as intended. But what happens if you decide you aren't able to carry out the duties or no longer want to?

Sometimes individuals accept the position without fully understanding the duties or responsibilities that come with the role. Or, circumstances can change and the person may no longer be able to assume the role, perhaps due to health issues, incapacity, job change or a move to another province or country, which can make the role challenging or difficult.

What happens if the named executor decides that they aren't able to carry out the duties — or maybe that they no longer want to? It is possible to step down from the position. If the executor hasn't yet applied for probate, they are generally able to renounce the role as executor by providing formal documentation to the courts.**

However, if the executor has applied for probate and started administering the estate (called "intermeddling"), renouncing the role may be more difficult. They may need to apply to the courts and provide an explanation of why they wish to step down. Since the estate administration has begun, they may be held liable by the beneficiaries for any loss in value to the estate. It is also possible that the court could refuse this request, especially if the executor is well into administering the estate.

This is why it's important to think carefully from the outset about the role.

As you consider your own estate's executor...

- Make sure the person you ask is comfortable in the role;
- Consider naming an alternate executor within the Will;
- Periodically review your named executor's circumstances to account for changes. Reach out to them to discuss their current capacity to ensure they are still willing and able;
- Don't be afraid to consider the support of a corporate executor, to act alongside an appointed executor or as sole executor.

If you are asked to be someone's executor...

- Recognize that the role can be difficult and may involve many hours of work, emotions and potentially complex family dynamics;
- Don't be afraid to ask questions. Is it a complex estate? Are there any potential surprises that may emerge?
- Remember that this is a fiduciary role with legal obligations and liabilities;
- If your circumstances change, make sure to let the person know. This includes if you plan on moving jurisdictions, face health issues or have a change in responsibilities that make it difficult to assume the role.
- Don't be afraid to say no if you don't think you can handle the obligation.

As always, consult an estate planning professional as it relates to your particular situation.

*For the purposes of this article, we refer to the person appointed to settle the estate as the executor, also called the liquidator in Quebec and may go by other terms based on province of residence. **In QC, the liquidator cannot refuse the role if they are sole heir.

Spring Cleaning? Check Your Credit Score

When was the last time you checked your credit score? It may be important for young and old people alike, for benefits beyond just understanding your credit position.

As advisors, one common problem we have seen with older couples is that one spouse will have a good credit rating, but the other will have none. If the spouse with the good credit rating passes away, the other may have difficulty qualifying for a loan or even a credit card.

Establishing a good credit score can take time. It involves creating a credit history and showing that you are able to pay bills on time and in full. The two main Canadian credit bureaus, Equifax and TransUnion, keep track of your credit through public records of lenders like banks, collection agencies and credit card companies. Credit scores are usually based on a range between 300 and 900, with a score of over 700 considered very good.

Help Younger Folks Understand the Importance of Building Credit

Many young people may have limited experience with credit and do not realize that having a good credit history can make life easier. It is important because your score determines how lenders assess your credit capacity — the higher the score, the greater the likelihood that you'll be approved for loans or credit. It is often checked when applying to rent a property or even for certain jobs.

Identify Possible Fraud

For both young and old alike, periodically accessing a credit report may be valuable not just to check your credit score standing, but also to help guard against identity theft. A credit report may list accounts that you may not have opened, which can uncover possible fraud. The credit bureaus also offer monitoring services that can notify you if there are changes to your credit position. You can also request to add extra security measures, such as a fraud alert, when financial providers issue new credit in your name. Some of these services have associated fees, but the cost may be worthwhile to act as a safeguard as new scams become increasingly sophisticated.

Surviving (and Thriving) in Challenging Economic Times

Are we in for a hard or soft landing...or no landing at all? While we can never control the timing of challenging economic times, there may be ways to better survive and even thrive!

This was the conclusion of a Harvard study that looked at the performance of 4,700 public companies through three recent recessions. While 17 percent fared particularly badly, almost 10 percent did the opposite: they flourished, outperforming competitors by at least 10 percent in sales and profit growth.[1] What made the difference? Preparation. When a downturn eventually hit, companies with contingency plans that had thought through alternative scenarios could switch to survival mode and react defensively.

This may be equally applicable to our personal financial positions. How we survive — and possibly thrive — through a downturn may come down to how well we prepare. In this regard, here are some personal finance ideas that may be valuable regardless of the prevailing economic conditions:

1. Maintain an Emergency Fund — This typically consists of the equivalent of three to six months of living expenses set aside in the event of an unforeseen financial situation, such as job loss, illness or damage to your home. While the obvious benefit is to help buffer against financial hardship, it can help to avoid taking on debt. For high-net-worth individuals, an emergency fund may be useful to prevent the need to liquidate investments on short notice.

2. Take Stock of Your Cash Flows — Having visibility over your cash inflows and outflows can help better plan your finances. A personal cash flow statement provides a snapshot of your sources of income, as well as what you're spending and saving. Many of us have good visibility over our income, but we may not have as clear a picture of where our funds are going. Often, when our clients undertake this exercise, they discover their expenses aren't exactly what they thought. Once you determine how much you are spending, you can incorporate different rules for managing money. For instance, some set goals like the "50/30/20 Rule," which budgets 50 percent of inflows for needs, 30 percent for wants and 20 percent for saving and investing.

3. Prioritize Your Spending — There may be an opportunity to increase savings by cutting back on non-essential spending. Debt-relief experts suggest that there are common ways we can all reduce expenses, such as focusing on insurance, unused memberships or subscriptions and "unconscious spending."[2] For instance, consider revisiting insurance coverage to negotiate better rates through bundling (i.e., home and auto insurance), raising a deductible or dropping non-essential add-ons. Or, you may be unknowingly paying for unused subscriptions, especially if you signed up for a free trial that you have since forgotten. There may be areas to reduce unconscious spending: thoughtless purchases made out of convenience, such as one-click online purchases, expensive coffees or food delivery that can add up over time.

4. Pay Down Debt — Historically low interest rates made it easy and affordable to assume debt. With rising rates, the cost of debt has increased. If you hold debt, it may be beneficial to focus on paying it down. Consider prioritizing debt subject to the highest interest rates first, such as credit card debt, to reduce the interest paid and allow the principal to be paid down. If you hold a mortgage that will be renewing, shop around to get the best rate possible.

5. Review Your Goals — One way to help keep on track is to review your wealth plan to see how you are tracking to your goals. Wealth management can consist of many elements, not just your investments. Tax strategies, insurance planning, risk management/contingency planning, retirement planning, business succession planning and estate planning can all contribute to building wealth. Remember that we are here to assist.

1. http://hbr.org/2019/05/how-to-survive-a-recession-and-thrive-afterward; 2. https://www.cnbc.com/select/ways-people-waste-money/

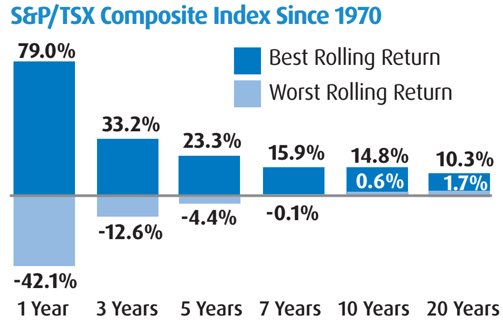
Perspectives on Market Volatility: Extend Your Time Horizon

It has been said that, "*Life can only be understood by looking backward, and yet it must be lived by looking forward.*"

One of the tradeoffs that equity investors have to endure is the volatility that comes with the stock markets. We could choose to invest in other assets like low-risk, fixed income investments to avoid the volatility, but then, of course, we would forego the potential returns.

During volatile times, it may be prudent to remind ourselves that the variability of equity market performance smooths out substantially as the investing period grows. The chart on the right shows the range of outcomes for the best and worst annualized returns of the S&P/TSX Composite Index (not including dividends reinvested) from 1970 to the start of 2023. These figures were calculated using rolling monthly returns. Over one-year periods, the variability is substantial: historically, you could have experienced a variation in annual returns of between -42.1 percent and +79.0 percent! However, as the holding period extends to decades, the range of outcomes narrows significantly and the likelihood of negative returns also diminishes.

Range of Annualized Returns By Holding Period: S&P/TSX Composite Index Since 1970



S&P/TSX Composite Index monthly returns (not including dividends reinvested), 12/69 to 1/23.

As longer-term investors, a look back in time reminds us that we will always have a higher probability of success than short-term investors. As we look forward, patience is often rewarded if you are able to endure the many bumps that inevitably come in the short term.

Start Thinking About Your 2023 Tax Position

Personal income tax season is here again, and while there is little we can do to impact our 2022 tax position, we can act now to impact our 2023 tax position.

Of particular note, due to high inflation, the annual index adjustment for personal income tax and benefit amounts in 2023 is significant, at 6.3 percent. This may provide tax-planning opportunities. For instance, the adjustment will push the federal tax brackets notably higher in 2023. As one example, the top federal bracket (subject to 33 percent tax) will increase to $235,676, from $221,709 in 2022. This may impact those who choose to defer income to stay within certain tax brackets. The adjustment may also change the way we plan for certain benefits, such as income-tested benefits like Old Age Security (OAS) — for 2023, the clawback begins when income exceeds $86,912. If you plan around this clawback, you will be able to have an additional $5,151 of taxable income in 2023 before it kicks in (the clawback starts when net world income exceeds $81,761 in 2022). Or, perhaps there is an opportunity to consider the decision to defer the start of CPP or OAS benefits to take advantage of the enhanced amount by waiting.

There may also be opportunities to lower your taxable income by contributing to a Registered Retirement Savings Plan (RRSP) or splitting income with a spouse/partner. If you are in need of income-splitting ideas, please let us know.

As we consider tax-planning opportunities for 2023, in brief, here are some select tax changes that have been implemented since the last newsletter as a result of the passing of the Fall Economic Statement bill in December 2022:

FHSA — If you have kids or grandkids who have yet to purchase their first home, this may be a great planning opportunity. The First Home Savings Account (FHSA) will be effective April 1, 2023, for eligible first-time home buyers. Similar to the RRSP, contributions will be tax-deductible and, like the TFSA, withdrawals will be non-taxable. The annual contribution limit will be $8,000, with a lifetime limit of $40,000, and the plan can remain open for 15 years. A notable change is that recent legislation now allows qualifying purchasers to access both the FHSA and Home Buyer's Plan (HBP) under the RRSP. For more information, please contact the office.

Residential Property Anti-Flipping Rule — If you've benefitted from the strong real estate market, be aware that effective January 1, 2023, if an individual sells a residence that has not been held for at least 12 months since acquiring it, the residence will be deemed to have been "flipped," subject to certain exemptions, including life events like divorce, death, job relocation and others. Profits from the sale of the property will be subject to tax as business income and ineligible for the capital gains rate or principal residence exemption.

Multi-Generational Home Renovation Tax Credit — A new tax credit, effective January 1, 2023, allows families to claim 15 percent of up to $50,000 in eligible renovation and construction costs for a secondary unit that has a private entrance, kitchen, bathroom and sleeping area in an existing home. The self-contained unit must be for a senior or a family member who is disabled.

Enhanced Reporting Requirement for Trusts — All non-resident trusts that currently file a T3 return and express trusts that are resident in Canada, with some exceptions, will be required to file a T3 return and report additional information (including on trustees, beneficiaries, settlors), for taxation years that end after December 30, 2023. This now includes bare trusts commonly used to efficiently transfer property to a beneficiary. Penalties will apply for failing to file a return, so if you hold a trust, it may be beneficial to seek assistance from an accountant regarding the reporting requirements.

With the compliments of...

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