Investment Insights

Autumn 2022

Time: The Investor's Great Ally

"Time is the exponent that does the heavy lifting. The common denominator of almost all fortunes isn't returns; it's endurance and longevity." — Morgan Housel

We are living in a world where instant gratification has become a way of life. We've been conditioned to expect instantaneous results through on-demand television and one-click internet shopping. Many of us aren't willing to wait more than two seconds for a website to load[1] (*how about you?*); yet, we may forget that just 20 years ago most of us couldn't access high-speed internet.[2]

The need for immediate outcomes can also translate to investing. Excess market exuberance in 2021 may have convinced "day traders" on internet forums that instantaneous wealth was well within reach. Indeed, market performance in 2022 has been a reminder that there are often no shortcuts to investing success. For most investors, creating wealth involves enduring the inevitable up and down cycles.

This involves navigating through times like today. The aggressive actions by central banks in raising interest rates to curb inflation continue to create significant jitters in the markets. Many market observers point to the current outlook for the economy and financial markets as being uncertain: Is a recession imminent? With the days of easy credit and low-cost capital behind us, we have undoubtedly entered a period of slowing economic activity.

Uncertainties tend to raise fears, which can be a driving factor in short-term market behaviour and one that appears to dominate today. With all the volatility, investor confidence remains at fragile levels. Yet, uncertainties will always be with us and concerns over things like a potential recession are no reason to avoid the investment markets altogether. Economies will experience downturns. And, bull markets, as often as not, have started in the middle of recessions, sometimes quickly or unexpectedly when sentiment appears at its worst.

Investing is never a smooth road, even for the best of us. Some of the most respected investors who have delivered outstanding long-term returns have managed through similar periods of uncertainty and down markets, even routinely underperforming the markets. Would you be surprised to know that over the life of their investing, the annual performance of Warren Buffett, John Templeton and Charlie Munger fell short of the markets at least 33 percent of the time?[3] Yet, they endured the short-term bumps and stuck to their approach to outperform the markets over time. The common denominator? Endurance and longevity.

Just as setbacks can happen too quickly to ignore, progress often happens too slowly to notice. This is why investing has sometimes been compared to the growth of a tree: a month's progress may show nothing; a few years' progress may show a little; but long-term progress can create something significant — and this can only happen with time, the investor's great ally.

1. 2014 Consumer Web Performance Expectations Survey, Akamai; 2. www150.statcan.gc.ca/n1/daily-quotidien/030923/dq030923b-eng.htm; 3. Compared to the S&P 500 Index. Tweedy Browne Co., "10 Ways to Beat an Index," 1988. BRK-A data has been updated to 1965-2021.

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To Our Clients:

As the cooler months approach, investment decisions may need to be made before year end, such as maturing your RRSP if you've turned 71, RESP contributions or tax-loss selling, to name a few. Think about them now and let's talk soon about any needs you may have.

At the time of writing, the markets continue to be dominated by bearish sentiment. Over the summer, there was good news as inflation showed signs of slowing; yet, this has been overshadowed by recent U.S. inflation data that was higher than expected. Excessive pessimism can often make room for renewed strength. For longer-term investors, an emphasis on quality and patience may be our greatest allies to see us through these times. Over extended periods, sound investment plans have done well. Keep your sights on the longer term.

Matt, J.D., Aimée & Emma

In This Issue

Consider These Ways to Gain From Your Losses

With market declines in 2022, if you're looking to make portfolio adjustments, there may be ways to gain from your losses.

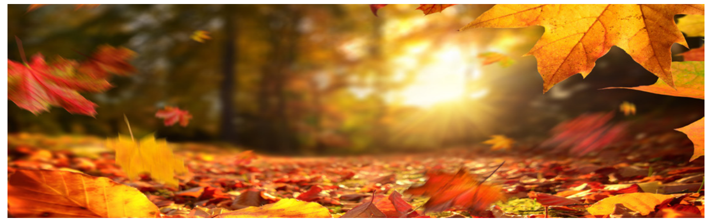
In general, when an investment held in a non-registered account is sold for less than its original cost, the result is a capital loss. For tax purposes, 50 percent of the capital loss can be used to offset any taxable capital gains realized during the year to reduce your current tax liability. If you do not have sufficient taxable capital gains to offset the losses, you can carry the net capital loss back for three taxation years to recover taxes paid on eligible capital gains. Or, you can carry the net capital losses forward indefinitely to use against future taxable capital gains.

Be aware of the superficial loss rules, which deny the capital loss if you or an affiliated entity (i.e., spouse/partner, RRSP, TFSA) acquires the same security 30 days before or after the date of the loss transaction. If so, you will not be allowed to use the capital loss in the current tax year to offset capital gains; it will be added to the adjusted cost base (ACB) of the identical property.

Beyond the benefit of offsetting realized capital gains with capital losses, here are some opportunities to gain from your losses:

Gifting to Adult Children — Gifting investments that have declined in value to an adult child can put subsequent capital gains/income in the hands of someone in a lower tax bracket, resulting in less taxes payable for the family unit. This will also trigger a capital loss in your hands, which can help to offset realized capital gains. For estate planning, transferring assets to your children while alive can reduce the value of your estate and the eventual taxes or probate fees (where applicable) on your estate at death.

Charitable Gifting — Donating publicly-traded securities "in kind" that have appreciated in value from a non-registered account will eliminate the tax liability on the capital gains triggered and allow for a donation tax credit for the fair market value of the securities. However, if securities have declined in value, you may wish to simply sell the securities to claim the capital loss and donate cash, which will entitle you to a donation tax credit. Unlike appreciated securities, where the additional tax benefit (that eliminates the tax liability on the capital gains) will only occur if you donate shares "in kind," you will still be able to claim the capital loss. Make charitable donations in advance of the December 31, 2022 deadline to count towards your 2022 taxes. Seek the support of tax professionals for your situation.



Before Year End: Consider These Actions To Save Tax

- **Realize capital losses to offset capital gains.**
- **Split income.** This may include electing to split eligible pension income with a spouse or paying reasonable salaries to family members for services provided to your self-employed business.
- **Contribute to your RRSP** for the 2022 year. You still have 60 days after the calendar year end to make contributions.
- **Convert your RRSP if you turned 71 in 2022.**
- **Don't forget the pension income tax credit.** If you are 65 years or older and don't have eligible pension income, consider opening a small RRIF or purchasing an annuity.
- **Consider charitable donations.** Gifting publicly-traded securities to a registered charity can offer tax benefits.
- **Make RESP contributions.** While this won't impact taxes, you may benefit from the Canada Education Savings Grant for 2022.

Inflation & Interest Rates: Has Inflation Peaked?

We are in one of the most aggressive tightening cycles in more than 40 years. Are higher rates curbing inflation?

There have been positive disinflationary signals: commodities prices, notably energy, have been moderating, supply chains are being fixed and consumer spending is flattening. While higher inflation rates continue to put a strain on many, consider that we aren't alone. Most of the world has been troubled by inflation; countries like Turkey and Argentina have had unprecedented rates, in excess of 70 percent! Only a handful of nations, such as South Sudan and Bolivia, have been able to escape inflation.

Canada continues to be in a comparatively favourable position due to our vast domestic resources production and as a net exporter of both food and energy. Many European countries continue to suffer from high energy and food prices due to their dependence on imports.

For investors, talk of slowing inflation is welcome because this may slow the pace of future rate hikes. Rising interest rates have been a key driver of the volatile markets in 2022. For fixed income, the inverse relationship between bond prices and interest rates meant a significant decline in the bond markets this year. For equities, valuations often go down as the future value of cashflows is lower when a higher discount rate is used. Company profitability may also be hampered by slower economic growth.

Inflationary pressures are expected to continue, so it's too soon to say if the central banks will ease their practices. Yet, consider that our monetary policy practices appear relatively benign compared to others: In August, Argentina's central bank raised its key interest rate to a whopping 69.5 percent!

Developed Countries With the Highest Inflation Rates: July 2022

Country	Inflation Rate	Change*	Country	Inflation Rate	Change*
1. Turkey	79.6%	▲	4. Spain	10.8%	▲
2. Argentina	71.0%	▲	5. Netherlands	10.3%	▲
3. Russia	15.1%	▼	6. Brazil	10.1%	▼

https://tradingeconomics.com/country-list/inflation-rate; *▲ Increase or ▼ decrease from previous month.

Not Just for Estate Planning: Do You Have a Financial Inventory?

If an unexpected event were to happen, would you, or others, be able to find important documents to handle your finances?

A financial inventory is a list of all of your finances and other important financially-related information. While we often suggest that an inventory be created as part of an estate plan, there may be other situations in which having this inventory can be invaluable, such as in the event of:

- Damage to your home, such as a fire, flood or natural disaster;
- Divorce or separation;
- Incapacity or illness of you or your spouse/partner; and
- Theft.

The Benefits: A Big Picture View...and No Lost Funds!

A financial inventory is not only important to ensure continuity in managing your finances in the event of unforeseen circumstances, but it can also provide a big picture view of your financial accounts and your overall financial situation. It should be reviewed periodically and updated to account for changes, including major life events.

Another reason why this can be important? By keeping track of your financial documents, there is a better chance that your assets will not be lost or forgotten. The latest reports suggest that there are $888 million in unclaimed balances held by the Bank of Canada and the Canada Revenue Agency has around 7.6 million uncashed cheques valued at $1 billion.[1]

Creating Your Financial Inventory

Putting together the initial inventory can be time consuming, but once it is created it can more easily be maintained. In the process, you may also determine that there are areas that can be streamlined to simplify your finances, such as consolidating or eliminating accounts.

The financial inventory should include all assets and debts. Assets include savings, chequing, brokerage and investment accounts, retirement and education savings accounts, real estate holdings and insurance policies (e.g., health, home, life, car, disability, long-term care, etc.). Debts may include credit card accounts, mortgage accounts and other personal loans. The inventory should also include legal documents such as a Will, trusts and power of attorney documents, as well as titles, deeds and business documents. Any valuable property, such as artwork or jewelry, should be documented. Finally, the list should include the contact details of professionals involved in your finances, such as accountants, investment advisors and lawyers.

A detailed inventory should include contact information, account numbers, user name/password information and other account access details. Other information may also be included, such as social insurance numbers, automobile VIN/licensing details, cell phone providers and loyalty rewards programs. Given the abundance of sensitive information, you will need to ensure that this document is kept in a safe place, yet one that can be accessed by others if needed. It may also be beneficial to keep account number/password information in a separate location for greater security. For a copy of our *Estate Information Organizer* to help document this information, please call the office.

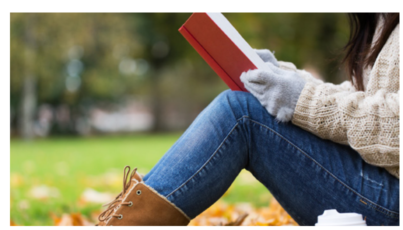
1. At the start of 2020. nationalpost.com/news/heres-how-to-see-if-you-have-any-of-the-888m-in-unclaimed-bank-accounts-the-bank-of-canada-is-holding; nationalpost.com/news/canada/canada-revenue-agency-1-billion-uncashed-cheques

In Brief: Financing Education in a Time of Uncertainty

Given the difficult markets, those considering accessing funds from the Registered Education Savings Plan (RESP) may be wondering if they should wait for equity values to rebound.

Having patience is certainly never a bad thing when it comes to investing through the inevitable cycles, and for those with sufficient funds to cover short-term education needs this may be an option. However, there may be reasons not to delay withdrawing RESP funds.

Remember that educational assistance payments (EAPs) — the withdrawal of income, capital gains and grants that have accumulated in the plan — are taxable in the hands of the beneficiary. The return of capital, the original contributions made to the RESP, are not taxable. If you are considering withdrawing EAPs, there may be a benefit to doing so before year end to use a student's tax credits. Consider that the basic personal amount for the 2022 tax year is $14,398. Assuming a federal tuition credit of $6,700, this combined would total a federal tax credit of $21,098, meaning that a student with no other income could potentially receive $21,098 of EAPs in 2022 and pay no tax.



As you plan ahead to minimize the tax bill, consider that the student could carry forward the federal tuition tax credit to a future year. However, the basic personal amount cannot be carried forward. If you are looking to optimize a family tax bill, you should also consider that a student may transfer a maximum of $5,000 of the current year's federal tuition amount to a parent or grandparent (or their spouse/common-law partner, or their spouse's parent/grandparent).

(Grand)Parents: It May Be a Great Time To Contribute to the RESP!

For parents with young children or grandparents who are looking to help support a child's future education, this may be an opportune time to consider opening and contributing to the RESP. Over recent years, it has been difficult to find quality investments at reasonable prices, but 2022 has certainly presented greater opportunities for longer-term investors and the RESP can benefit.

How Does a Recession Impact My Portfolio?

Over the summer, the U.S. reported its second consecutive quarter of negative GDP. A recession is commonly defined as two successive quarters of declining gross domestic product (GDP), the measure used to gauge economic productivity. However, the National Bureau of Economic Research, the U.S. body that makes the official call on whether the economy is in recession, declared that the economic data suggested otherwise and many economists agreed: low unemployment, solid job growth, stable industrial production, high demand for durable goods and travel, as well as solid corporate earnings.

Regardless of whether the U.S. is in recession, what most economists do agree on is that we have entered a period of slower economic growth, largely due to the path that the central banks have taken to fight inflation. While many are hopeful that aggressive rate hikes will help control inflation, there are concerns this will push economies into recession. Is Canada at risk? Until now, our economy has been comparatively resilient, with robust consumer demand, healthy labour markets and resource production providing support.

How Do Rising Rates Affect Economies and the Markets?

Higher rates raise the cost of borrowing, which can lead consumers to spend less. While decreased demand for goods and services eases inflation, it can also impact a business' profitability. Rising rates also increase the cost for companies to borrow money, along with the cost of holding debt. Sometimes companies pass these costs along to consumers. However, if they cannot, it can potentially impact earnings and lower stock prices. As well, valuations often go down because the future value of cashflows is lower when a higher discount rate is used. With fixed income markets, as interest rates rise, bond prices generally fall. This is why we have seen both stock and bond markets struggle in 2022 as the central banks raised rates.

What Happens to the Markets When There is a Recession?
S&P 500 Returns During Recession, One and Three Years After End

U.S. Recessionary Period	During Recession	One Year After	Three Years After
Nov. '73 to Mar. '75	-17.90%	28.32%	21.99%
Jan. '80 to Jul. '80	16.14%	12.92%	55.89%
Jul. '81 to Nov. '82	14.66%	25.40%	67.24%
Jul. '90 to Mar. '91	7.64%	11.04%	29.84%
Mar. '01 to Nov. '01	-7.18%	-16.51%	8.44%
Dec. '07 to Jun. '09	-35.46%	14.43%	57.70%
Mar. '20 to Apr. '20	-1.12%	45.98%	TBD

awealthofcommonsense.com/2022/06/timing-a-recession-vs-timing-the-stock-market/

Recessions Are a Natural Part of the Economic Cycle

It's not normal for any economy to be in a perpetual expansion and economic contractions, including recessions, occur from time to time. Economies, like financial markets, are cyclical in nature and prone to expanding and contracting. Recessions can also be quite different in their length and intensity. Consider that our most recent recession during the pandemic was the shortest on record, just two months in length.

What About My Portfolio?

The potential for a recession should never be a reason to consider curtailing investment programs. Consider that the stock market and the economy don't always move the same way at the same time. History has shown that the markets can begin an upward climb when economic conditions are at their worst. A look back at the last seven U.S. recessions reminds us that the S&P 500 Index has, as often as not, started to climb during the depths of a recession (chart). After all, equity markets are forward looking in nature. Moreover, periods of retrenchment have always been followed by new growth, expansion and improved equity values. As such, when a recession eventually does arrive, remember that it will be temporary. At the same time, longer-term investors should consider that portfolios have been positioned with the expectation that economies and financial markets will experience both ups and downs. This is a normal part of the investing journey.

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