BMO Nesbitt Burns | Autumn 2018

Investment **Insight**

Perspective in the Face of Pessimism

With the extended bull run, it seems as though every global event is analyzed for its potential negative effect on the markets: Will this be the start of a bear market?

But think about just how much opportunity would have been missed if you followed the underlying pessimistic narrative over recent times. For years, the media has been claiming that equity markets have reached their peak.

So, why is pessimism so seductive? First, it is innate: Organisms that treat threats as more urgent than opportunities have a better chance to survive and reproduce. A Harvard study showed that pessimism is perceived to be more expert, intellectual and competent. Daniel Kahneman, who won a Nobel Prize for his work on cognitive psychology, showed that people respond more strongly to loss than gain. Optimism often means staying the course, which can appear oblivious to risks. Pessimism requires action, which appeals to human nature because we are more inclined as a species to act than wait.

This is not to say that today's economic headwinds should be ignored. A major shift in global trade continues to be of concern as the U.S. imposes tariffs globally. At home, Canada remained sidelined in NAFTA negotiations over the summer and the Trans Mountain pipeline experienced setbacks. Italy's debt issues, complicated by political change, and Turkey's currency crisis have been in the news; all of which have kept investors on edge.

Being an optimist doesn't mean believing that short-term setbacks won't happen. After all, financial and economic markets are cyclical by nature. But what looks like tomorrow's problem is often not the real issue when tomorrow rolls around. Economies have proven remarkably resilient over time and the future is likely to be no different. We often underestimate our ability to adapt: people, businesses and economies move on from even the toughest setbacks.

How can investors keep perspective in the face of pessimism? One way to do this is to step back from the headlines. Focus on your end goals, not the news of the day. Continue to save and invest steadily for the future. Leave the worry over day-to-day developments to those of us who oversee your investments.

Equally important, invest confidently with your longer-term objectives in mind. Your portfolio is being managed with the expectation that markets will experience both ups and downs. Remember that patience, along with time and the virtues of compounding, are likely to be some of your greatest allies.

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Vice President
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To My Clients:

Welcome to my new quarterly newsletter. It is my hope that you will find it full of useful wealth management information, including perspectives on the many aspects of the markets that impact our portfolios.

I will endeavour to keep each edition relevant and timely. If you have suggestions for future topics, please let me know.

As always, if I can help in any way, please get in touch. Have a wonderful autumn seas

Dilk

In This Issue

Business Owners: Tax-Planning for Year End

Is it too early to think about year end? As a business owner, if you are thinking about tax-planning strategies, not at all. Now is the time to take steps in order to help minimize 2018 corporate taxes and plan ahead for 2019. Here are some ideas to review with your professional advisors:

Consider the new passive income and refundable dividend rules...

- For taxation years starting after 2018, certain passive income earned in the company, and associated companies, in excess of $50,000 will reduce the small business deduction (SBD). If you are at risk of exceeding the threshold in future years, there may be options: defer passive income (i.e., wait to trigger capital gains, etc.), realize capital losses or review options to reduce active business income.
- With the new income sprinkling rules in place restricting the payment of dividends, consider whether family members can be paid a reasonable salary.
- Changes to the company's refundable dividend tax on hand ("RDTOH") account will be effective for taxation years after 2018, so consider whether RDTOH should be refunded in the current year.

Minimize the impact of taxes on bonuses...

- Bonus payments can be deferred up to 179 days after a corporation's year end and the company can still claim the amount as a deduction for tax purposes in the current year. With federal corporate tax rates decreasing in 2019, it may be beneficial to get the deduction at a higher rate. However, consider whether you believe personal tax rates will change in 2019, potentially offsetting the benefit.
- For year-end bonuses, consider having the company contribute directly to the employee's Registered Retirement Savings Plan (RRSP). While this is considered employment income, there are no income tax withholdings required (CPP and EI withholdings will apply if maximums have not been reached in the calendar year).

Evaluate how funds are extracted from the corporation...

- Review your remuneration strategy to determine if it is more tax effective to receive salary or dividends, especially if the company's SBD will be reduced by the amount of passive income earned in the company. Changes to provincial and/or federal tax rates may change "integration", so there may be advantages to paying one over the other.
- Since other-than-eligible dividend tax rates will be increasing in 2019, determine whether it is more advantageous to declare dividends in 2018.
- If you require funds before year end, consider repaying shareholder loans, declaring capital dividends or reducing the paid-up capital of your shares in order to extract funds on a tax-free basis.

Time the purchase of capital assets...

- Consider purchasing fixed assets before the end of the company's tax year. Currently, you can claim one-half the amount of tax depreciation, or capital cost allowance (CCA), to reduce business income in this fiscal year and claim the full amount next year.

As always, please seek professional advice for your situation.

With the compliments of...

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