Friday, April 26th, 2024

Weekly Wrap

After a tough last week, markets bounced back a bit despite a poor US GDP Report that was made worse by some disappointing inflation data contained in the same report. Expectations for rate cuts continue to grind down with the markets now pricing in just one rate cut in the US and two in Canada for 2024. Interest rates, which have already jumped a lot so far in April, rose another 0.05% this past week in North American bond markets. The TSX, which has held up much better than other markets thus far in April, rose 0.75% this week. After a drubbing in the tech sector last week, US markets recouped some of their losses this week, advancing over 2%. Strong earnings from Microsoft and Google offset a weak earnings report from Meta. European Markets continue to shine, gaining 2.5% this week, while news of improved Chinese growth helped the Emerging Markets rise about 2.5% also.

Market Insights

Canada’s GDP per capita slips to 7% below long-term trend. According to Statistics Canada, Canada’s economic output per capita, widely recognized as a measure for a country's standard of living, has declined in five of the past six quarters and is currently 7% below its long-term trend. This amounts to a decline of about $4,200 per person. Households and businesses continue to adjust to higher interest rates which partly explains the slowing pace of economic activity. Moreover, Canada's population continues to rapidly expand, adding nearly 1.3 million people in 2023, and with population growth outpacing output growth, GDP per capita has now dipped to 2.5% below pre-pandemic levels. The federal government recently pushed back on some of the pessimism surrounding the decline in per capita output, suggesting newcomers typically earn less than the average Canadian and that should not be misinterpreted to imply those already in the country are becoming worse off. There is some validity to the Fed's spin on that, however, there is no doubt a widening gulf in wealth in Canada. In their latest projections, the Bank of Canada expects GDP per capita to pick up in the second half of the year and into early 2025, as the bank is widely expected to lower its policy interest rate this summer.

Calling for Prefs. After last week's somewhat surprising announcement from RBC to call a preferred share that few felt would be redeemed (I certainly didn't and I'm about the most optimistic pref investor in Canada), there appears to be a tidal wave of redemption in the bank pref share space. This week Bank of Montreal called two more pref shares (BMO F and BMO S). Tuesday's redemption announcement brings the total tally of 2024 Canadian bank pref redemptions to $2.3 billion and to about $12.5 billion since Limited Recourse Capital Note (LRCN) bonds became an option for banks to satisfy their capital requirements in 2020. Essentially, banks can issue tax deductible LRCN bonds and use those proceeds to redeem prefs, lowering their financing costs. Pref shares are the only fixed income instrument whose attractive features for investors is leading them to be in such short supply that they may one day be extinct. Get 'em before they're gone I say! RBC expects a total of $5 Billion in pref share redemptions this year in a market where there are only about $60 Billion available. In addition, most of this $5 Billion in redeemed prefs is likely to be plowed right back into buying more prefs (pref ETF's are mandated to do so) which increases the likelihood of further redemptions. With pref shares it's likely that one of three things will happen going forward: they get reset and pay dividends of 7-9%, they get redeemed at prices that are 10-25% higher than they are today or a combination of both.

Portfolio Update*

Our efforts remain focused on the fixed income portion of your portfolios as opportunities remain unusually attractive there. The preferred share market continues to ride a wave of positivity with one of the reasons being the substantial pickup in redemptions (RBC was the latest to redeem). With virtually the entire pref share market trading below their redemption price, news of a redemption sends the price of the soon to be redeemed share up to the redemption price. This has a knock on effect for the rest of the pref share market as the announcement of one redemption leads investors to look for another redemption candidate with similar or more attractive features for the issuer to redeem them. We believe we have found another opportunity and have sold an Intact Financial pref share which is trading near redemption price for a Brookfield Corp pref share which, for more attractive terms, trades at a discount of 20% to the Intact pref share.

***Please note any changes apply to our PIM Portfolios Only, subject to restrictions. Please call to clarify if you have any questions.**

Planning On

The 2024 Federal Budget – Capital Gains Inclusion Rate

If you received (and read) our reminder email about Nick's upcoming conference call next week you will know that we plan on spending a lot of time and work on ensuring our clients are well-informed about the proposed increase in the capital gains inclusion rate. We have attached a comprehensive article produced by RBC Wealth Management Canada that we invite you to read.

Recap of proposal:

- FOR INDIVIDUALS: Any capital gains realized prior to June 25th this year will have an inclusion rate of 50%. Any realized after that will have an inclusion rate of 50% up to $250,000 of realized gains and then a rate of 66.67% on any portion above that.
- FOR CORPORATIONS AND TRUSTS: Like above, all gains realized prior to June 25th will have an inclusion rate of 50%. Any gains realized after will not benefit from the $250,000 threshold and lower inclusion rate. The inclusion rate on all gains after June 25th, will have an inclusion rate of 66.67%

Things to consider:

- For individuals with joint property (investments, real estate, etc.), as long as there are no attribution issues then all holders of the property would be able to benefit from their own individual $250,000 threshold. So for a classic spouse/common-law situation, if you were to sell anything for a total capital gain of $500,000, you would have the ability to split that gain between the two of you.
- The advantage of tax-deferral cannot be overstated. If you have a longer holding period for your investment, it may still make sense to avoid realizing any gains now and continue to hold. We can assist to some degree with these conversations through a break-even analysis. Examples can be found within the attached article.
- If you are going to need funds in the next year or two then realizing the gains most likely makes sense (if selling would put you over the $250,000 total capital gain).
- For business owners and the incorporated professionals, this proposed increase likely increases the advantage of the Individual Pension Plan which is registered pension plan held within your corporation. It also strengthens the argument for corporate life insurance.

Some context:

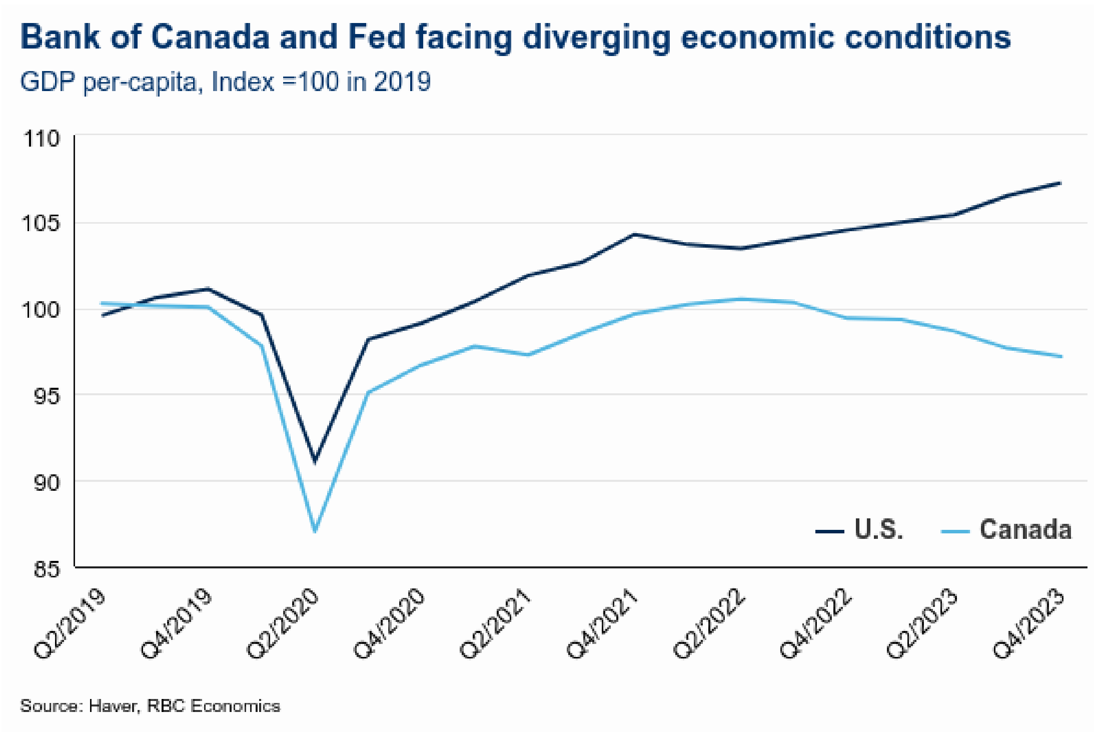
As the article shares, while we have been benefiting from this lowish inclusion rate for over 20 years, historically it has been even higher than the proposed increase. And at those times it was not a 2-tiered system. All capital gains had the higher inclusion rate unlike the proposed budget change. The history of the inclusion rate is below:

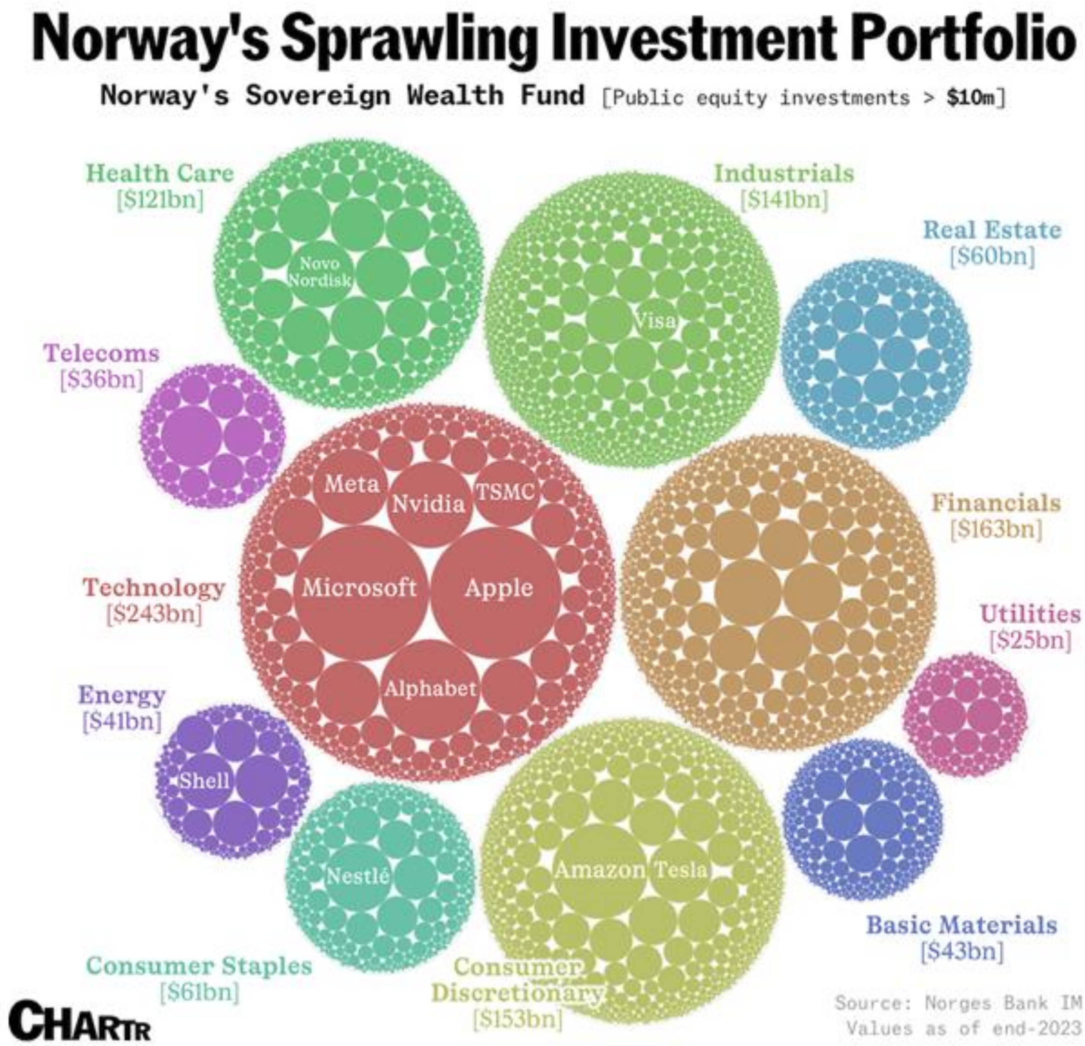
Capital gains inclusion rate changes over time[2]	
Time period	**Inclusion rate**
1972 to 1987	50%
1988 to 1989	66.67%
1990 to February 27, 2000	75%
February 28 to October 17, 2000	66.67%
After October 17, 2000	50%
On or after June 25, 2024 (proposed)	66.67%

To understand how this proposed change may affect you and your family, please reach out to Nick and Justin.

This information is not intended to provide legal, tax, or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified lawyer or accountant, as applicable, before acting on any of the information.

Charts of the Week





Spare Time Updates

[Quiz: Is this an Olympic Sport?]

What is new this year for the Summer Olympics in Paris this year or in the lineup at Los Angeles 2028? All kinds of different ‘sports’ have come and gone and occasionally come back.

[Food Photographer of the Year 2024 Shortlist]

Check out all the food related photos that made the shortlist for the Pink Lady Food Photographer of the year.

Financial Term(s) of the Week

Hedge Fund: Pool of money often favoured by more sophisticated/wealthier investors that is invested in stocks and other assets. The mangers tend to be generally more aggressive than a traditional mutual fund manager. They often employ bold and varied strategies as they pursue higher profits.

Feel free to pass on this email to anyone you think would benefit from its information or see some value in it.

Thank you very much for reading through our commentary.

Feedback is welcome!

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