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WEALTH MANAGEMENT

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Personal Newsletter from Wes Ashton, Harbourfront Wealth Management

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For 2021: Continue to Look Forward

Amidst the ups and what seem like mostly downs of the past year, there is light shining from the North. Despite the difficult circumstances we have faced in 2020, there have been bright spots to build optimism for the year ahead.

Unlike previous recessions, the economic effects of the pandemic have been uneven and concentrated to certain sectors. This has resulted in a relatively weak multiplier effect for the overall economy. Sectors that have been able to thrive during the pandemic, such as technology, have helped to drive equity markets, as largely seen south of the border. Canadian equity markets, generally influenced by the energy and resources sectors, have been hindered by lower demand due to the slowdown. In response, many companies have reassessed their business models, cut costs and leaned operations.

After the spring shutdowns, Canada's economy rebounded better than expected as restrictions were relaxed. Employment levels grew faster than anticipated, as did consumer spending. The housing market continued to perform well. Unlike many developed nations, Canada's household incomes grew at a time when the economy contracted; savings rates also increased.¹ Many financial institutions that set aside significant amounts for loan loss provisions in anticipation of mortgage or credit defaults have recently seen reductions in those reserves.

These successes were, in part, due to significant stimulus measures. Canada has been more generous than most nations with its support and, as a result, will have the largest stimulus deficit globally in 2020 (as a percentage of GDP).² While there are likely to be future consequences, the good news is that the current cost of carrying this debt remains low due to near-zero interest rates.

South of the border, the U.S. has chosen a new path forward after a highly contested presidential election. Given considerable and continuing unrest, there is hope that this change will temper tensions and newly passed stimulus efforts will help to support Americans throughout the winter.

Driving optimism for the end to the pandemic has been the remarkable progress made in the race to find a vaccine. This is an exceptional feat, given the typical vaccine time-to-market is 10 to 15 years. The fastest ever has been the mumps vaccine, which took four years.³

Progress in combatting a pandemic takes time. Progress in investing may involve greater endurance. During 2020, while the many ups and downs of equity markets captured attention, they aren't the ones that matter for most longer-term investors. Assuming you can stay the course for long enough, the results can be significant. The *Rule of 72*⁴ provides a good reminder: at an annual rate of return of five percent, an investment will double in around 14 years. For those who may not think they have the benefit of time, consider that 90 percent of renowned investor Warren Buffett's wealth was made after the age of 65.⁵

Most notably, despite the many challenges we faced in 2020, we have seen that equity markets don't wait on the sidelines for recovery to happen. They are, after all, forward looking in nature. Perhaps this is an admirable quality to uphold as we leave 2020 behind and bring in a new year. As we look forward, we would like to thank you for your trust and confidence in our services during what has been an unprecedented time.

1. <https://nationalpost.com/news/canadas-generous-covid-19-income-supports-vastly-outpaced-other-developed-nations-oecd-report>; 2. <https://financialpost.com/opinion/jack-m-mintz-in-government-spending-and-deficits-were-now-no-1-in-the-world>; 3. <http://nationalgeographic.com/science/health-and-human-body/human-diseases/coronavirus-vaccine-tracker-how-they-work-latest-developments-cvdi/>; 4. Rule of 72: It takes approx. 72÷(rate of return) years for investment to double; 5. Based on shares of Berkshire Hathaway (BRK-A). 8/30/95: \$25,300; 10/30/20: \$302,500.

RRSP Season is Here Again!

Registered Retirement Savings Plan (RRSP) season is here again. Here are some questions to ask as you consider using the RRSP to its fullest benefit:

Have you maximized your RRSP contribution? Don't overlook the opportunity to reduce personal tax liabilities or take advantage of tax-deferred growth. The last day to make contributions for the 2020 tax year is **March 1, 2021**. Contribution limits are 18 percent of your previous year's earned income, to a maximum of \$27,230 for the 2020 tax year, less any pension adjustment or past service pension adjustment, plus unused contribution room carried forward.

When was the last time you updated beneficiary designations?

The start of the year may be a good time to review your designations and ensure that they are updated in the plan documentation.* Understand that there may be tax consequences to your estate depending upon who has been named as beneficiary(ies). There may also be considerations to address when designating a minor child (depending on provincial/territorial laws), an individual with a disability, or non-residents.

Will you benefit from a spousal RRSP? Consider the opportunities to split income through the use of a spousal RRSP (or common-law partner). A spousal RRSP is a plan to which you contribute and for which you receive tax deductions based on your available contribution room, similar to a traditional RRSP. However, the difference is that your spouse is the annuitant, so any funds withdrawn are considered that spouse's income and must be included in his/her income tax return. Thus, withdrawn funds will be taxed at a lower rate should your spouse pay tax at a lower rate than you.



Are you turning 71 in 2021? You must convert your RRSP before the end of the calendar year in which you turn 71 years of age. The most common choice is to open a Registered Retirement Income Fund (RRIF), but there are other options to consider, including purchasing an annuity or distributing funds as income. Please call to discuss.

Do you have (grand)children who may benefit from a RRSP?

If you have (grand)children who have a part-time job, they may benefit by holding an RRSP. Often, when earned income is less than the basic personal tax amount, an income tax return is not filed. However, by not reporting this income, the opportunity to generate RRSP contribution room is foregone. As such, the chance to compound savings for additional years on a tax-deferred basis or reduce future personal income tax liabilities through annual tax deductions is also lost. Even if a child does not contribute in the current year, the unused RRSP contribution room carries forward.

Some of these actions may benefit from the support of a tax advisor. Please call for assistance with any RRSP matters.

*Note: in Quebec, this designation must be made in your will.

Interest Rates, Inflation & the Risk of Doing Nothing

For those old enough to remember, the late 1970s and early 1980s were periods rife with high inflation and interest rates. In 1981, inflation rates reached over 12 percent and the now defunct Canada Savings Bond returned 19.5 percent interest.¹ While high interest rates meant great returns on low-risk assets like guaranteed investment certificates, it also meant unaffordable mortgages!

Since that time, it has been widely recognized that the central banks are responsible for keeping inflation in check as part of their policy objectives. For many years, the Bank of Canada and U.S. Federal Reserve (Fed) have targeted a two percent core inflation rate. Over the last decade, inflation has generally hovered close to this target, due to monetary policy actions as well as persistently low price and wage increases. It should be noted that the measure of core inflation doesn't include some of the more volatile components of our goods and services, such as food and gas — everyday costs incurred by most individuals. Many Canadians would argue that food costs have largely outpaced core inflation rates!

Today's Realities: Low Interest Rates, Low Inflation

Of course, it is unlikely that we will see the return of the inflation rates experienced in the 1970s. However, even moderate inflation can have a significant impact over time. The chart shows the erosion of purchasing power of \$100 with just moderate inflation rates.

Chart: Even Moderate Inflation Can Erode Purchasing Power

Year	Inflation Rate		
	1%	2%	3%
0	\$100	\$100	\$100
10	\$90.53	\$82.03	\$74.41
20	\$81.95	\$67.30	\$55.37
30	\$74.19	\$55.21	\$41.20

Source: J. Hirasawa Associates calculation.

This should also remind us of the value in investing funds for the future. With interest rates at near-zero levels, many savings accounts yield paltry returns. Add in the subtle effects of inflation and doing nothing with your money can have its own risks.

While the effects of the pandemic may have created short-term deflationary pressures, there are differing views on the longer-term path for inflation. With central banks pledging to keep interest rates low for the foreseeable future, there is the potential for rising inflation — traditional economics suggests that when rates are low and the economy grows, inflation generally increases. As well, in 2020 the Fed signaled a major shift in its approach to managing inflation, now allowing it to run above the previous two percent target. This significant change in policy stance was undertaken to try and stimulate growth and tackle unemployment as a result of the pandemic.

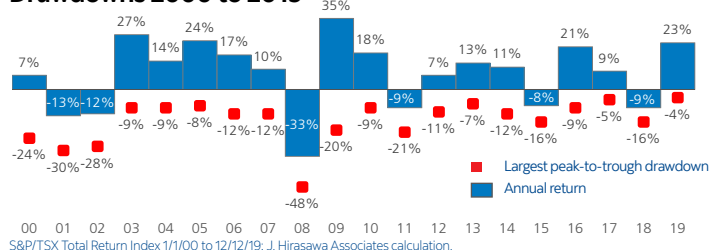
1. Bank of Canada monthly historical CSB rates and CPI. www.bankofcanada.ca

Reminders for the New Year: Building Wealth Takes Time

It may be easy to lose sight of the importance of time in building wealth. Today, the reasons are many: heightened market volatility, an increasing focus on immediacy and the influence of media in the digital age. Yet, in investing, having a longer time horizon takes advantage of compounding, which can have profound effects over time. This involves the difficult task of enduring inevitable and unpleasant short-term events like recessions and even an unexpected pandemic. The following may help to provide perspective:

Volatility is a Common Market Feature — The chart below shows the biggest peak-to-trough drawdowns each year for the S&P/TSX Composite Total Return Index and annual returns since 2000. In 12 of the last 20 years, there has been a double-digit, intra-year correction. Significant volatility is no stranger to the markets. Yet, in half of those years, the index finished in positive territory.

S&P/TSX Composite Total Return Index: Peak-to-Trough Drawdowns 2000 to 2019



Markets Are Cyclical: Nothing Lasts Forever — Equity and financial markets are cyclical. History shows that markets spend more time in positive than negative territory. Since 1956, there have been 13 bull and 13 bear markets. The average bull market has lasted 54 months, with an average gain of 131 percent, whereas the average bear market has lasted only 9 months, with an average loss of -27 percent.¹ Business cycles are also cyclical, typically lasting around

seven years. While Canada has had seven recessions over the past 50 years, they have lasted an average of only 11 months.³



Your Time Horizon May Be Longer Than You Think

The pandemic has put pressure on many incomes, which may require some to make adjustments to retirement options or timing. But don't overlook the opportunity to make up for lost time. Just as increasing longevity requires planning, it may also allow time for recovery. Consider that an investment with a five percent compounded annual return will double in approximately 14 years. As such, a 70-year-old may still have the potential for investments to double within their lifetime,² and possibly even twice if they become a centenarian.

The Impact of Time in Investing Can Be Significant — Time can be one of the investor's greatest allies. The chart below shows the impact of time in generating retirement savings: with a longer time horizon, an investor would require a significantly lower monthly investment to yield \$1,000,000.

Monthly Investment Amount Required to Reach \$1M Over

Years	At Average Annual Rate of Return of...		
	4%	5%	6%
20	\$2,726	\$2,433	\$2,164
30	\$1,441	\$1,202	\$996
40	\$846	\$655	\$502


*Assuming monthly compounding at annual rates of return shown. Effect of taxes, fees or inflation ignored. Source: J. Hirasawa Associates calculation.


Stay focused on your own investing time horizon and remember to keep time on your side.


1. S&P/TSX Composite 1/1/56 to 9/30/20; 2. Assumes average life expectancy of 83 years old; 3. "Business Cycles Since 1926. Commentary 366", C.D. Howe Institute.

In Short: Upcoming Changes That May Affect You


As always, change is imminent! In brief, here are some of the notable changes that have occurred in the last quarter or are upcoming:

 **Tax-Free Savings Account** — The **Tax-Free Savings Account (TFSA) dollar amount for 2021 is \$6,000**. This makes the total lifetime TFSA contribution room amount at \$75,500 (since 2009, for those eligible).

 **Income-Splitting Opportunities** — The Canada Revenue Agency (CRA) prescribed interest rate for spousal loans remains at one percent: the lowest possible rate. Making a bona-fide loan to a spouse for investment purposes is one way to split income and lower taxes, by putting family investments in the hands of a lower-income spouse. In October, the CRA confirmed that refinancing an existing prescribed rate loan at a lower rate may be done with part of the proceeds from the original loan without triggering the attribution rules.¹

 **Working from Home** — The 2020 Fall Economic Statement announced that the home office expense deduction will be simplified. The CRA will allow employees working from home in 2020

due to Covid-19 with modest expenses to claim up to \$400, without the need to track detailed expenses and will not request employees to provide a signed employer form.²

 **Covid-19 Benefits** — New Federal government pandemic-related benefits began in the fall, including for those who become ill or miss work to care for a sick family member. A withholding tax of 10 percent will be deducted. U.S. citizens in Canada who received U.S. Covid-related government assistance will not have to include payments on Canadian tax returns. For detailed information, see: <https://canada.ca/en/services/benefits/ei/cerb-application/transition.html>

 **Legal Tender** — Bid farewell to \$1, \$2, \$25, \$500 and \$1,000 bills in circulation. As of January 1, 2021, they no longer have the official legal tender status as an approved payment of debt.

For more information on any of these changes, please call the office.

1. https://investmentexecutive.com/news/industry-news/cra-offers-flexibility-on-prescribed-rate-loans/?utm_source=newsletter&utm_medium=nl&utm_content=investmentexecutive&utm_campaign=INT-EN-All-afternoon; 2. <https://investmentexecutive.com/news/industry-news/feds-to-allow-up-to-400-for-home-office-expenses/>

Estate Planning & Your TFSA: Different Beneficiaries May Have Implications

With the lifetime contribution amount now totaling \$75,500 in 2021 (for those eligible since 2009), the Tax-Free Savings Account (TFSA) has become a significant investment vehicle. If it will play a substantial role in your estate plan, understanding the impact of naming different beneficiaries is important.

While any income or capital gains earned in the TFSA to the date of death are exempt from tax, keep in mind that the way that beneficiaries are named and structured may have differing financial implications. As such, it is important to carefully plan ahead.

If you haven't revisited your TFSA beneficiary designations since opening the account, perhaps now is a good time to review them. Here are some things to consider:

Deciding "Where" to Designate a Beneficiary — In all provinces except Quebec, you may designate a beneficiary of your TFSA by naming them in the plan documentation or in your Will.¹ If a beneficiary is designated within the TFSA plan documentation, the main benefit is that you'll be able to minimize probate taxes as the value of the TFSA will generally not pass within the estate.

If Naming a Spouse, Designate as a Successor Holder — If you intend for a spouse (or common-law partner) to be the plan's beneficiary, they should be designated as a "successor holder," which is a designation only available to spouses. This allows the spouse to automatically become the holder of the TFSA at your death, simply through a name change on the account. If the spouse already has their own TFSA, they will now have two accounts. If they wish to consolidate accounts, they can directly transfer part or all of the value from one account to the other. This transfer doesn't affect their own TFSA contribution room.² If the spouse is designated only as a beneficiary, as with any designated beneficiary, any increase in the value of the TFSA after the deceased's date of death will generally be subject to taxes.



Planning for a Minor as Beneficiary — Careful planning should be done when designating a minor as the TFSA beneficiary. Depending on the applicable provincial laws, proceeds will generally need to be paid to a parent on behalf of the minor child, a court-appointed guardian of property, or an appointed trustee (i.e., such as through a testamentary trust created under a Will for the benefit of the minor). In some cases, a parent may not automatically be considered the guardian of a child's property and as such may need to apply to the courts. In other cases, if no trustee is named, TFSA proceeds may be paid into the courts. Keep in mind that the involvement of the courts can be a time-consuming and costly process. As such, it is advised to consult with a legal advisor to plan for naming a minor beneficiary.

Designating a Charity — If you wish to make a gift to charity as part of your estate plan and are seeking opportunities to minimize the taxes paid by your estate, consider designating a charity as a beneficiary of a registered plan. With the TFSA, any value on the date of passing would not be considered as taxable income. However, the full value of the RRSP or RRIF would generally be considered to be taxable income in the year of passing (unless there is a successor or spouse beneficiary who can roll the amount to their own registered plan). A charitable donation tax credit can be used to reduce taxes payable in the year of death.

1. In Quebec, beneficiaries cannot be named within plan documentation; they must be named within the Will; 2. Unless there is an excess amount in the deceased's TFSA at the time of death.



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