

Investment Focus

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Time: The Investor's Great Ally

It has been said that *"Time is the exponent that does the heavy lifting. The common denominator of almost all fortunes isn't returns; it's endurance and longevity."* As we look ahead to a new year, don't overlook the impact of compounding and time on investing success.

In investing, compounded returns can have a profound impact on portfolio values, but the potential outcomes are often overlooked. When given the choice between \$50,000 per year for 30 years or a penny that doubles in value each year for 30 years, many would choose the first option. This is because it is easy for us to think linearly — \$50,000 times 30 years would yield \$1.5 million. However, the effects of compounding aren't as intuitive: a doubling penny would result in a whopping \$10.7 million over the same period of time.

From an investing perspective, the significant outcomes from compounded growth may often be difficult to achieve in practice. One of the challenges is that compounding only yields impressive results over longer periods of time. This is because initial gains appear small at the onset and moderate in the middle — substantial outcomes are only realized in the latter part of the journey. Consider the doubling penny. After a full decade, it would have grown to just \$10.24. Even after fifteen years, it would be worth only \$327.68. With the other option, you would have banked \$750,000 by this time. Yet, remarkably, after 27 years, the doubling penny would exceed the \$1 million mark; after 30 years, it would be worth \$10.7 million. Of course, we recognize that the doubling penny's annual rate of return of 100 percent is unrealistic in investing. This example is meant to highlight the profound impact that compounding can have over time — let's not forget this started with just a penny.

Adding to the challenge is that investor behaviour can disrupt the path toward achieving these outcomes. During heightened uncertainty, periods of downward market volatility can act to derail investment focus, prompting some investors to react. We all know the oft-counterproductive behaviours, such as trying to sell before a market downturn or, worse still, abandoning stocks during a downturn, which deprives the investor of the ability to eventually recover. These appear to be intuitive actions in the face of uncertainty; in many ways, the compounding journey often demands seemingly counter-intuitive behaviour.

However, it's worth a reminder: the world has always been uncertain. Today is no exception. Many are struggling with a higher cost of living and elevated interest rates. Global economies are highly indebted, economic conditions are softening and we're likely to see lagging effects of the rate hikes, among other concerns. Yet, adverse macroeconomic events have always been part of the investing journey: recessions, financial crises, inflation, stagflation — even wars — history has included all of these terrible things. While they can derail the markets for temporary periods, it is investor reactions to these events that can derail compounding.

As advisors, we remain focused on managing portfolios to navigate the challenges that come with the changing times. As investors, don't overlook the importance of a commitment to the longer term: Let time in the markets be one of your keys to success. As we begin another year, we would like to thank you for entrusting us with your wealth management. Wishing you and your loved ones health, happiness and prosperity for 2024.

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- Perspectives on Consumer Sentiment

Estate Planning: Your Digital Assets May Have More Value Than You Think

Even if you're not a significant technology user, your digital footprint may be larger than you think. This may be an important consideration in estate planning. A recent article in the popular press serves as a reminder: While many digital assets often have little monetary value, they may have substantial sentimental value. Overlooking the transfer of these assets may have sad consequences. One widow could not retrieve thousands of photos stored on her partner's cloud account. Another wasn't able to access her late husband's Facebook page.¹

Canada lacks consistent legislation giving the executor or attorney the automatic authority to deal with digital assets, with rules varying by province — if they exist at all. Saskatchewan was the first province to introduce legislation that grants executors/fiduciaries access to digital assets.² Yet, even if laws do allow for authority, the reality is that access can be difficult if no provisions have been made by the deceased. Often, customer support for online accounts is limited, creating challenges and undue stress during an already emotional time.

Many of us carefully construct a plan for investments, real estate and other physical belongings; yet, as more of our lives operate digitally, we may not be doing a good job of planning for our digital assets. As a starting point, here are a few tips to begin the process:

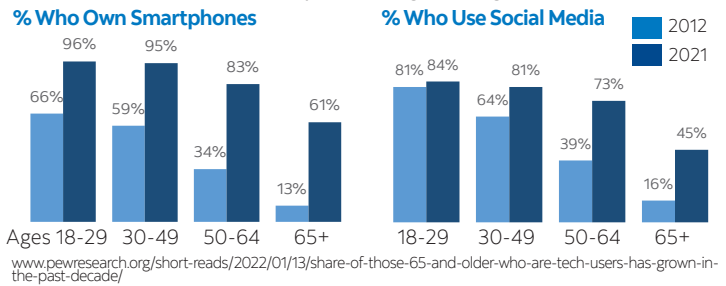
Take inventory — Just as we take stock of our physical assets for estate planning, doing this for digital assets is equally important. Keep a logbook of digital assets, including usernames and passwords. This should be stored securely and updated regularly.

Practice digital housekeeping — Protect and secure your data, not just as part of an estate plan, such as regularly backing up important files, contacts, photographs and other information stored on your computer, smartphone or the cloud and encrypting sensitive data.

Consider a password manager — Often, keeping a list of accounts/passwords isn't enough, as we may forget to update it. A password manager may be helpful. These software programs maintain

Growth in Adoption of Smartphones & Social Media by Age

Here's how the adoption of key technologies has grown over a decade:



access information to digital accounts, including account numbers, passwords and other important data you might need to leave behind.

Create a legacy contact or plan — Did you know you can designate a legacy contact for Apple accounts or create a legacy plan for Google accounts? Some social media accounts also offer legacy options. For an iPhone or iPad, go to **"Settings"** and then tap your name. Under **"Password & Security"** you will see the **"Legacy Contact"** option. The system will generate an access key for your contact, which will need to be presented alongside a death certificate to access data. For Google, go to **"myaccount.google.com"** and tap **"Data & Privacy,"** then scroll down to **"More Options"** and look for the option **"Make a plan for your digital legacy."** You can decide when Google should consider your account inactive and what will be done with your data, which can be shared with someone you trust or deleted by the system.

Update your estate plan — Make sure your will and power of attorney documents (or other directives, the names vary by province) include language specific to digital assets, giving a representative authority to access, manage, dispose of and distribute them.

¹ "Life After Death: Secure Your Digital Legacy Before You Die," Julie Jargon. Wall Street Journal, April 25, 2023, A11; ² <https://dig.watch/updates/saskatchewan-ca-introduces-fiduciaries-access-digital-information-act>
As always, please consult an estate planning professional.

Canada Pension Plan (CPP) Reforms: For 2024, Expect to Pay More

The Canada Pension Plan has been in the spotlight as the Alberta government proposes creating its own retirement plan. For answers to questions about Alberta's potential divorce from the CPP, see: <https://www.cbc.ca/news/business/cpp-app-pension-questions-1.7011117>.

If you earn employment income, did you know you've been contributing more? In 2019, CPP reforms were put in place to address the decline in workplace pension plans and increase future benefits. In 2024, higher-income earners can expect to pay even more.

The reforms amended the CPP in two ways: i) increasing the income replacement to 33.33 percent from 25 percent of eligible earnings, and ii) increasing the upper limit for eligible earnings. The first phase (2019 to 2023) gradually increased the contribution rate by one percentage point on earnings between \$3,500 and the maximum pensionable earnings (MPE) limit. The second phase begins on January 1, 2024, and requires employees and employers to contribute an additional four percent on earnings between the MPE and a new ceiling. With a 2024 MPE of \$68,500, the new ceiling will be \$73,200 in 2024 and \$78,000 in 2025.¹

What is the potential impact?

Under the old rules, those retiring at age 65 in 2023 could receive a maximum annual CPP benefit of \$15,460.² Under the new rules, this would increase to \$23,490, or by over 50 percent. Consider also that this doesn't account for the 0.7 percent per month enhancement for those delaying benefits after age 65, which further increases the benefit. Studies continue to show that deferring to age 70 may be a financially wise choice should you live beyond average life expectancy.³

However, it will take time before the full impact is realized. Those retiring in the near term will see only modest enhancements since benefits are based on an average of the best 40 years of earnings. For details: <https://www.canada.ca/en/services/benefits/publicpensions/cpp/cpp-enhancement.html>

¹ For 2024, 107% of MPE; for 2025, 114% of MPE; ² For Q1 2023, \$1,306.57 under the old regime less \$18.24 enhanced benefit = \$1,288.33. www.advisor.ca/tax/tax-strategies/what-clients-should-know-about-the-cpp-reforms/; www.canada.ca/en/revenue-agency/news/2023/05/the-canada-pension-plan-enhancement-businesses-individuals-and-self-employed-what-it-means-for-you.html; ³ www.fpcanada.ca/docs/default-source/default-document-library/fpw/globe-article-delay-cpp.pdf



RRSPs & RRIFs: Be Aware of Taxable Withdrawals

As the cost of living has risen substantially over the past couple of years, some may consider accessing funds from the Registered Retirement Savings Plan (RRSP) or Registered Retirement Income Fund (RRIF). Yet, early withdrawals may be costly. Here are two reasons why:

Tax Implications — Consider that any withdrawal is subject to tax and must be reported as income on a tax return. For the RRSP and any RRIF amounts above the required minimum withdrawal, there is also an immediate withholding tax. If you are accessing funds to pay down short-term debt, you may end up paying more tax on the withdrawal than you'll save in interest costs.

Don't Overlook the Opportunity for Tax-Advantaged Growth

RRSP Deadline: February 29, 2024, for the 2023 tax year, limited to 18 percent of the previous year's earned income to a maximum of \$30,780.

2024 TFSA Dollar Limit: \$7,000, for a total eligible lifetime TFSA contribution amount of \$95,000.

For RRSP holders, early withdrawals may have additional tax implications. If your current income is higher today than in the future, you may be paying higher taxes today. You will also forgo the opportunity for continued tax-deferred compounding, perhaps the most beneficial

aspect of the RRSP: A 35-year-old who withdraws \$18,000 from the RRSP would have \$100,000 less in retirement savings by age 65 at an annual return of 6 percent. Notably, once you make a withdrawal, you won't be able to get back the valuable contribution room.

Asset Values — Market volatility in 2023 put many asset values under pressure. Keeping funds within these plans can be beneficial to allow asset prices to recover.

RRSP Withdrawals: Alternatives to Consider

For those saving for retirement, if funds are needed, consider accessing other accounts, such as the TFSA, where contribution room resets itself at the start of each year. Consider also that the RRSP may allow

for tax-free withdrawals and recontribution for qualified home purchases or educational purposes via the Home Buyers' Plan or Lifelong Learning Plan. For more information, contact the office.



RRIF Withdrawals: Ways to Minimize the Impact

For those in retirement, allowing funds to remain in the RRIF may be challenging since minimum withdrawals are required each year. However, here are some ways to minimize the impact:

Withdraw at the end of the year — This may allow greater time for asset values to recover. Making withdrawals at the end of each year also allows for a longer period for potential growth within the plan.

Make an "in-kind" withdrawal — If you aren't in need of funds, with an "in-kind" withdrawal for the required amount you will continue to own the security. While the fair market value at the time of withdrawal will be considered income on a tax return, if transferred to a TFSA (subject to available room), any future gains will not be subject to tax.

Split RRIF income with a spouse — RRIF income qualifies as eligible pension income for pension income splitting. If you have a lower-income spouse and you're 65 or older, you can split up to 50 percent of your RRIF income to reduce your combined tax bill.

If you are turning age 71 in 2024, here are additional options...

Make the first withdrawal next year — You aren't required to make a withdrawal in the year that the RRIF is opened. You can wait until the end of 2025, the year in which you turn 72, to make the first withdrawal.

Base withdrawals on a younger spouse's age — If you have a younger spouse, use their age to result in a lower minimum withdrawal rate. This can only be done when first setting up the RRIF, so plan ahead.

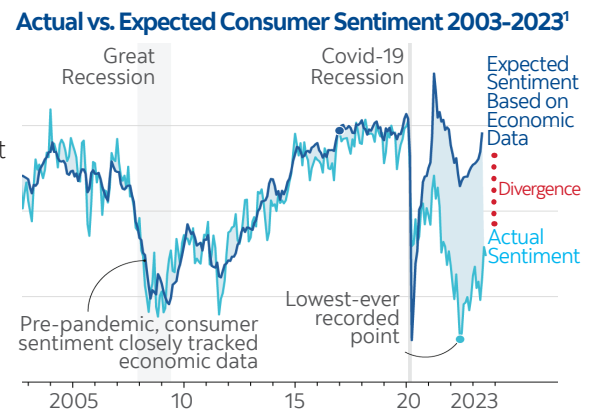
Looking Back, Looking Forward: Keeping Perspective

According to *The Economist*, consumer sentiment is at some of the lowest levels in decades. Yet, this collective feeling does not accurately reflect the actual economic data. Since the pandemic, there's been a growing divergence between sentiment and economic performance.¹

This may not come as a surprise. After all, we've been confronted with new challenges, many of which have come about quickly, such as inflation and higher interest rates. However, a closer look at the economic data may provide some perspective: We've also achieved a tremendous amount of progress in this economic cycle. The latest data shows that Canadian household net worth increased for the third consecutive quarter, by 3.4 percent to reach \$15,704 billion in Q1 2023.² In Q2, U.S. households held the highest levels of net worth ever recorded.³ Canadians and Americans have never been wealthier.

In the U.S., Q3 GDP was recently reported at 4.9 percent, marking the highest economic growth since 2014, after adjusting for the pandemic.⁴ While recent Canadian GDP reports indicate stagnant output over the past two quarters, let's not forget that the central banks' objective in aggressively raising rates was to slow economic growth to curb inflation. Over the past two years, economic resilience

has surpassed expectations, partly due to low unemployment rates. In Canada, this fell to a historical low of 4.9 percent in June 2022⁵ and continues to remain at relatively low levels.



As we begin another year, keep perspective. Don't lose sight of the economic and wealth-building progress that can be achieved even during seemingly challenging times.

1. <https://www.economist.com/graphic-detail/2023/09/07/the-pandemic-has-broken-a-closely-followed-survey-of-sentiment>; 2. <https://www150.statcan.gc.ca/n1/daily-quotidien/230614/dq230614a-eng.htm>; 3. https://www.federalreserve.gov/releases/z1/dataviz/z1/balance_sheet/chart/#units:usd; 4. <https://www.investopedia.com/shoppers-boosted-u-s-economic-growth-to-fastest-in-years-8382874>; 5. Since 1979.

For 2024: Consider Insurance as Part of a Broader Investment Strategy

As a new year begins, many of us refocus our financial goals. This may be an opportune time to assess insurance needs to help protect loved ones. For high-net-worth (HNW) investors, consider the opportunity to use life insurance as part of a broader investment strategy.

With rising rates, there has been increased attention to low-risk, fixed-income investments like Guaranteed Investment Certificates (GICs). Yet, insurance may provide an alternative that can produce a more favourable financial result after factoring in the potential tax implications. Consider the potential tax implications for a GIC returning four percent held in a non-registered account: after tax, this would yield two percent for an investor with a marginal tax rate of 50 percent.

At a basic level, many permanent life insurance products have fixed premiums and a guaranteed payout at death. As such, it is possible to calculate a rate of return (IRR) on the premiums. Since proceeds upon death are paid tax free, the only variable is the age of death. Take, for example, a whole life policy for a non-smoking, healthy 50-year-old male who pays an annual premium of \$14,000 for a \$1 million policy:

Illustrative: IRR for \$1M Whole Life Policy with \$14,000 Annual Premiums

Age at Death	IRR	Equivalent Pre-Tax Fixed-Income Return*
75	7.35%	10.5%
80	5.13%	7.33%
85	3.67%	5.24%
90	2.64%	3.78%

*Based on a marginal tax rate of 30%.

Insurance: Complement a Portfolio's Fixed Income Component

Permanent life insurance may be a way to achieve fixed-income exposure. A participating whole life insurance policy (or "par policy") allows you to share in the potential surplus earnings of the insurer. Your premiums go into a broader "participating account" that is professionally managed by the insurance company, which is used to pay insurance claims, expenses, taxes and other costs. The majority of the assets in the account are typically longer-term debt instruments, such as public and private fixed-income investments, bonds and mortgages. The account may include real estate or equity holdings. This provides the policy owner with access to a low-cost, widely diversified portfolio that is often difficult to replicate for individual investors.

The Par Policy: Additional Benefits for HNW Investors

In addition to the traditional benefit of supporting loved ones in the untimely death of an income earner, there may be additional benefits. The participating investment account is tax-sheltered for the policy owner, compared to a fixed-income portfolio of investments that would be taxable. Based on the account's performance, annual "policy dividends" are often issued to policyholders. These can be used to purchase additional paid-up insurance that would increase the policy's death benefit coverage, which the beneficiary will receive tax free upon the death of the insured. This provides the policy with the potential to outperform the after-tax fixed-income component of a traditional balanced portfolio.

In the event of a premature death, the par policy would have a high probability of outperforming the fixed-income component of a traditional investment portfolio (i.e., the increasing IRR at a lower age depicted in the chart). The estate value may also be higher, as income and any growth would be earned on a tax-free basis inside the policy. Death benefits paid from the policy may not be subject to probate where the policy is owned outside of a corporation and certain specific beneficiaries have been named, such as a spouse or children (in provinces where applicable).

For business owners, there may be additional tax benefits through the use of the company's capital dividend account, further enhancing the value of the estate. Corporations with active business income may also be able to offset the tax that can result from the passive income rules.

Be aware that funds must be committed to this strategy, so sufficient assets must be available after premiums are paid to cover lifestyle and other needs annually. If premium payments stop, the policy could lapse; or, if the policy is surrendered, the policy owner would be entitled to a surrender value. If funds are required, the cash value may be withdrawn or borrowed against. Annual policy dividends are not guaranteed, though many of the large life insurance companies have paid these on a regular basis. Policy premium rates will vary by age and health; a medical is often required to determine premium payments.

If you are interested in learning more, please contact the office.

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