Newsletter

Winter 2023

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Look Forward, Not Back

One of the weaknesses of human nature is our tendency to focus on what is most recent in our memories. Our minds are naturally influenced by things that have just happened, and this can impact the way we make decisions. In investing, this can be amplified. The market pendulum can sometimes swing from one extreme to the other, with prices often overshooting underlying "fair values" in both directions during the course of a cycle. As renowned investor Benjamin Graham once said, "*In the short run, the market is a voting machine. But in the long run, it is a weighing machine.*"

The year that has passed was no exception. Financial markets were largely challenged by the aggressive actions of central banks as they raised rates to combat high inflation. As a result, there was a significant reversal from the excessive exuberance that characterized 2021. While it's never easy to see asset prices under pressure, it has led to a more healthy outlook for how risk assets are viewed and, perhaps, more thoughtful consideration of how capital is deployed.

Yet, many of the same issues we faced in 2022 persist, including geopolitical tensions, lingering inflation, higher interest rates and continuing central bank tightening policies intended to slow economies. While these are important issues not to be trivialized, we shouldn't allow them to obstruct our view as we look forward.

This is because the investing journey can be a long one – depending on our objectives, sometimes as long as our lifetimes. For most investors, investing involves building wealth for down the road, and not tomorrow. We can often forget that short-term performance may have little impact on longer-term results.

Veteran investors recognize that market downturns are a normal part of the cycle and allow for them, often using them to build investment positions for the future. Despite the volatility of 2022, it is instructive that Warren Buffett continued on his buying spree, adding a record amount of purchases to his portfolio throughout the year.[1] He knows that interruptions will occur from time to time, and uses these periods to seek opportunity, strong in his conviction that better days lie ahead.

Likewise, we can all benefit from continuing to position ourselves for the years to come. Indeed, the opportunity to build significant wealth remains within reach for both young and old investors alike. We often use the "Rule of 72" as a simple way to estimate how many years it will take funds to double at various rates of return — and it's worth a reminder. By dividing 72 by an average rate of return of 5 percent, it shows that funds can double in around 14 years (72÷5=14.4). So, even if you've achieved the respected age of 70, chances are you can still live to see your funds double – and, twice still if you become a centenarian![2]

As we begin another year, don't lose sight of the importance of planning for the future. After a challenging year, I would like to express my gratitude for your continued confidence in my services. May 2023 bring brighter days and better markets. Continue to look forward, not back.

1. https://markets.businessinsider.com/news/stocks/warren-buffett-berkshire-hathaway-60-billion-record-stock-purchases-portfolio-2022-8; 2. Assuming average life expectancy in Canada of age 84 (females) and 80 (males); https://data.worldbank.org/

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RRSP Checkup: How Well Are You Managing Your RRSP?

It is once again Registered Retirement Savings Plan (RRSP) season. How well do you manage your RRSP? Here are some questions to ask:

Do you consider the timing of RRSP deductions? With any RRSP contribution, you're entitled to a tax deduction for the amount contributed so long as it is within the contribution limit. Keep in mind that you don't have to claim the tax deduction in the year the RRSP contribution is made. You can carry it forward if you expect income to be higher in future years such that you may be put in a higher tax bracket, potentially generating greater tax savings for a future year.

When do you make contributions? By making contributions at the beginning of the tax year or throughout the year, instead of waiting until March 1 for a deduction from the previous year, you may benefit from the longer time for tax-deferred growth. Due to the power of compounding, over time this can make a noticeable difference.

When was the last time you updated beneficiary designations? It may be beneficial to review account beneficiaries (in provinces where applicable), especially in light of major life changes. For example, in the event of separation or divorce, be aware that named beneficiaries may not be revoked, depending on provincial laws. Therefore, the designation of an ex-spouse may still be in effect.

Have you considered a spousal RRSP? For couples in which one spouse will earn a high level of income in retirement, while the other will have little retirement income, a spousal RRSP may potentially be a valuable income-splitting tool. If you are working past age 71 and have a younger spouse, you can no longer hold your own RRSP after the year you turn 71, but you can still make a contribution to a spousal RRSP as long as your spouse is age 71 or less at year end and you have RRSP contribution room. This may be a good way to get a deduction and shift income to a spouse.

Have you planned for your RRSP's eventual maturing? There may be benefit in gradually drawing down RRSP funds as you approach retirement. This may be useful if an individual is

currently in a lower tax bracket than they expect in future years. Others may seek to limit future sources of taxable income in order to minimize the possible clawback of income-tested government benefits such as Old Age Security. One strategy may be to use RRSP withdrawals to fund Tax-Free Savings Account (TFSA) contributions (subject to available room). As the TFSA grows, there may be greater flexibility to receive tax-free income that can augment or replace Registered Retirement Income Fund (RRIF) withdrawals later. At death, TFSA funds can pass tax-free to heirs, unlike residual RRSP/RRIF funds that are subject to tax, potentially at high marginal tax rates.

Do you allow your RRSP to grow uninterrupted? Consider the implications of making taxable withdrawals from the RRSP to pay down short-term debt. You may be paying more tax on the RRSP withdrawal than you'll save in interest costs. In addition, once you make a withdrawal, you won't be able to get back valuable RRSP contribution room. There may be better options, such as a TFSA in which contribution room resets itself in the following calendar year.

Always seek assistance from tax professionals regarding your situation.

RRSP Contribution Deadline: March 1, 2023 for the 2022 tax year, limited to 18 percent of the previous year's earned income, to a maximum of $29,210 (for the 2022 tax year).

A Brighter Side to Inflation: The Largest Index Adjustment in Years

There may be some good news that comes with the significant inflation we've been enduring. The adjustments made to certain government income tax and benefit amounts — such as the basic personal amount (the federal non-refundable tax credit on an income tax return), the annual dollar limit for the TFSA and the GST/HST tax credit — will be the highest seen in many years. This is because the government adjusts these amounts based on inflation using consumer price index data. With inflation reaching 40-year highs in recent times, the indexation increase is the largest since the 1980s.

Indexation Increase Per Year, 2019 to Current

2019	2020	2021	2022	2023
2.2%	1.9%	1.0%	2.4%	**6.3%**

Many of these adjustments take effect on January 1, such as the increase to the TFSA dollar limit. However, other adjustments will take place on July 1, such as income-tested benefits like the GST/HST tax credit and the child disability benefit, as this coincides with the beginning of the program year for these benefits. It will also increase our income tax brackets.

Why is this important? The adjustment helps compensate for the higher cost of living we are experiencing. For instance, if the tax bracket thresholds are not indexed to inflation, an increase in income would mean higher taxes paid and a loss of purchasing power. This occurred when Alberta de-indexed its tax brackets in 2019, effectively forcing Albertans to pay $646 million more in taxes from 2020 to 2022.[1] Alberta will resume indexing for the 2022 tax year.

For more information on the indexation adjustment, please see: https://www.canada.ca/en/revenue-agency/services/tax/individuals/frequently-asked-questions-individuals/adjustment-personal-income-tax-benefit-amounts.html

1. www.cbc.ca/news/canada/calgary/alberta-taxes-indexation-inflation-1.6510978

2023 TFSA Dollar Limit: As a result of adjustments for inflation, the 2023 TFSA annual dollar limit will increase to $6,500, bringing the eligible lifetime amount to $88,000. The annual dollar limit hasn't increased since 2019.

Don't overlook the opportunity for tax-free growth!

Investing Resolutions for 2023

A recent article in the *Washington Post* offered a different perspective to the view that kids these days are getting too much screen time. In fact, there's another demographic struggling to put down their devices: baby boomers. As one man put it: "*My 75-year-old dad's phone may as well be an implant; he lives with it like a teenager*!"[1] Of course, this has implications for our investing ways. With easy access at our fingertips, we may all be guilty of checking investment accounts too frequently.

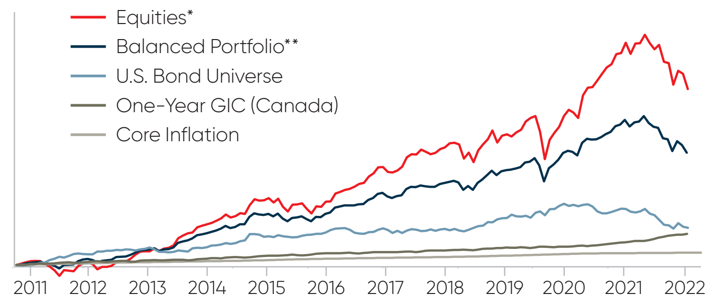
In this regard, and as we begin a new year, here are three resolutions that can help to make better investors:

Pay less attention to investment accounts. It's worth a reminder: Emotions can impact our investing decisions. When we are threatened by the possibility of losses, our brains take control to avoid these losses and we may not make the best investing decisions. In 2022, excessive pessimism dominated the markets. As one market pundit noted, perception swung from "flawless to hopeless," and, for many, the urge to react may have felt overwhelming. One important variable for investing success is how long you are able to stay invested. As such, consider checking accounts less frequently.

Look beyond annual returns. As we saw in 2022, markets will go down, just as they go up, and returns can vary quite significantly from year to year. While we commonly discuss "average" returns, it's worth repeating that annual returns often do not fall close to this average. Consider the wide dispersion of S&P/TSX Composite Index annual returns since 1981 in the chart. In 19 of 41 years, returns were less than the average of 6.7 percent. Almost one-third of the time, they were negative. Yet, average returns compounded over time can lead to superior results. Consider that an investment of $55,000 would yield about $209,000 in 25 years at a compounded annual average rate of return of 5.5 percent; yet, in 55 years, it would yield over $1 million.

Remember that equities continue to be one of the best wealth generators of asset classes. Given the market volatility in 2022 and with yields on low-risk, fixed income alternatives at levels not seen in over a decade, products like guaranteed investment certificates may look appealing. While this may be a good opportunity for cash on the sidelines, equities continue to be one of the best asset classes in which to generate wealth and beat inflation over time.

Cumulative Returns by Investment Strategy, 2011 to Nov. 2022

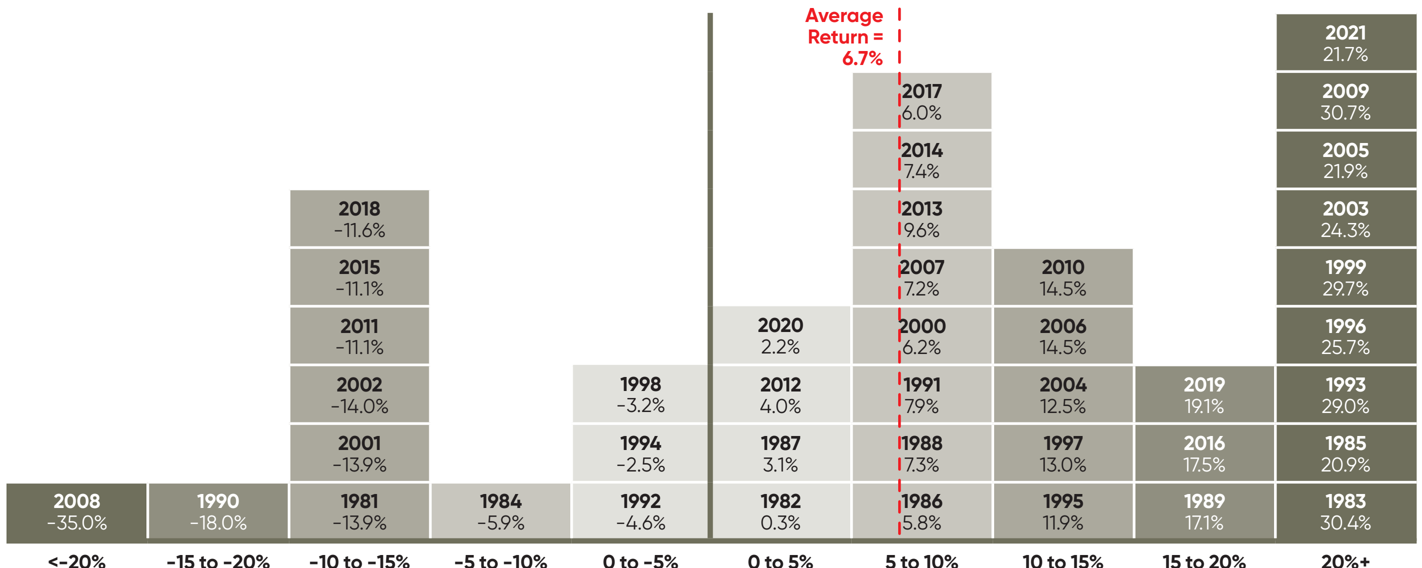


*35% S&P 500, 35% S&P/TSX, 20% MSCI EAFE, 10% MSCI EM;
**60% Equities, 40% Fixed Income

A well-constructed portfolio has been put in place to meet your goals over the longer term. Have confidence that your plan continues to work for you.

1. https://www.washingtonpost.com/technology/2022/11/12/boomers-screentime/

S&P/TSX Composite Index Annual Returns, 1981 to 2021



For 2023: Expect Continued Volatility; Maintain Perspective

For those who pay regular attention to the markets, if they've felt more volatile over recent times, you're not mistaken. Periods of greater volatility tend to coincide with market drawdowns, and 2022 was no exception. There were 102 days in which the S&P 500 Index had a move of one percent or more, significantly higher than in previous years (chart, below).*

Incidence of Large Daily Moves: S&P 500

Year	Intrayear Drawdown	+/-1% Move	+/-2% Move	+/-3% Move
2022*	-25.4%	102	38	10
2021	-5.2%	55	7	0
2020	-33.9%	110	44	24
2019	-6.8%	38	7	1
2018	-19.8%	47	20	6
2017	-2.8%	8	0	0

*To Oct. 21/22. https://awealthofcommonsense.com/2022/10/animal-spirits-bear-market-math/

Periods of downward volatility tend to be difficult, even for the best of us. Modern behavioural scientists suggest that we feel the pain of loss about twice as much as the pleasure of a similar-sized gain. Even medical doctors agree that "*market volatility is bad for your health*," causing undue stress, generating feelings of worry and sometimes leading to poor decision making.[1]

An Earnings Recession? Maintain Perspective

As we move into 2023, we expect periods of volatility to continue. With persistent inflation, the central banks are expected to continue raising rates to bring down inflation. Rate hikes are intended to slow the economy, which has prompted new concerns over a potential earnings recession.

While slowing the economy will put downward pressure on corporate earnings, there are reasons to keep perspective. Over the longer term, the stock market is driven by fundamentals such as corporate earnings. While the biggest bear markets often coincide with the largest declines in earnings,[2] history has shown that changes in fundamental drivers, like earnings, may not necessarily lead to the same outcome. For instance, in the 1980s, earnings didn't grow that much, yet the markets would post significant gains (chart, below). Indeed, there are many paths that the economy and markets can take. What if economies slow and inflation can be reeled in, yet labour markets remain relatively strong? What if earnings don't fall much during the economic slowdown?

Are There Ways to Help Manage the Volatility?

While it would be ideal to be able to hedge against the risks of slower earnings, inflation, rising rates or a recession, doing so would likely lead to a portfolio that offers a limited chance of upside. No one can consistently anticipate the timing of these changes, so, as advisors, we act as risk managers using strategies to help manage through difficult times. This includes having a plan in place based on individual risk tolerance and goals, using a disciplined approach that emphasizes quality, diversification and asset allocation and making prudent changes where necessary. For investors, having the patience to see through these periods is important. The same doctors suggest focusing less on our portfolios and instead getting exercise, eating healthy and engaging in activities like sports or meditation to worry less about volatility; perhaps good resolutions as we start a new year. After all, "*attitude and perspective go a long way in both your health and investing*."

Earnings Growth & S&P 500 Total Returns

Decade	Earnings Growth	S&P 500 Total Returns
1930s	-42.2%	-0.5%
1940s	157.8%	140.4%
1950s	46.1%	486.6%
1960s	70.5%	112.2%
1970s	157.1%	76.8%
1980s	53.9%	403.7%
1990s	110.6%	432.8%
2000s	5.8%	-9.1%
2010s	173.6%	256.7%

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

*When annualized. Data at 10/21/22.

1. https://www.cnbc.com/2015/09/09/market-volatility-is-bad-for-your-health-commentary.html; 2. https://awealthofcommonsense.com/2020/04/the-relationship-between-earnings-and-bear-markets/

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