

Guagliano-Hedgcock Wealth Management Newsletter



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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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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

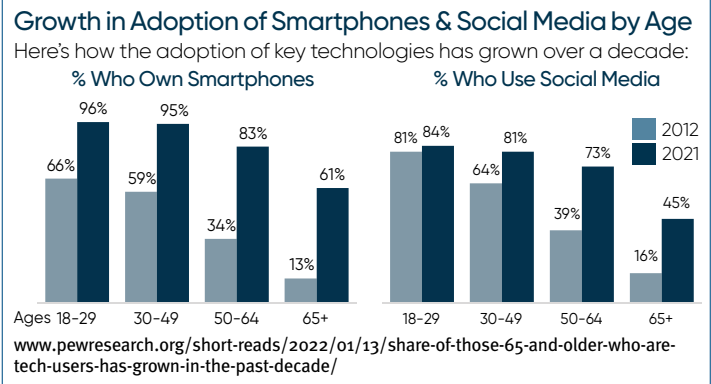
Canada lacks consistent legislation giving the executor or attorney the automatic authority to deal with digital assets, with rules varying by province – if they exist at all. Saskatchewan was the first province to introduce legislation that grants executors/fiduciaries access to digital assets.² Yet, 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 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.

CPP/QPP Reforms: For 2024, Expect to Pay More

If you earn employment income, you may have noticed more of your paycheque going towards CPP/QPP contributions. For higher-income earners, starting in 2024, expect to pay even more.

Back in 2019, CPP/QPP reforms were put in place to address the decline in workplace pension plans, amending the CPP/QPP 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/QPP 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 on the CPP changes, see: <https://www.canada.ca/en/services/benefits/publicpensions/cpp/cpp-enhancement.html> or for QPP: https://www.rq.gov.qc.ca/en/programmes/regime_rentes/Pages/regime-supplementaire.aspx

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 = \$1,288.83. 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 forego 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,³ 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.

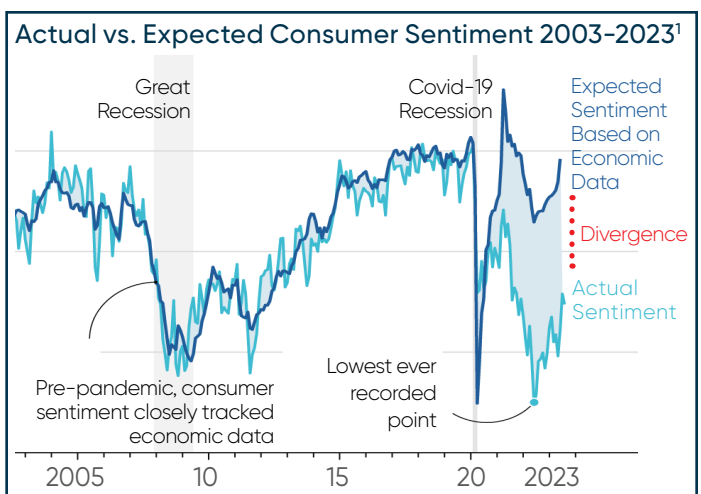
Base withdrawals on a younger spouse's age – If you have a younger spouse, use their age to result in a lower minimum withdrawal rate. This can only be done when first setting up the RRIF, so plan ahead.

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/July 2022 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.

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

Estate Planning: Did You Know Survivor Benefits May Be Lacklustre?

As we step into a new year, it is a time when many of us resolve to update our estate plans. As part of that planning, a key objective is often to help secure the financial well-being of loved ones, including mitigating potential income loss to protect a surviving spouse after the other's passing. Yet, a notable challenge often arises from a widespread misunderstanding surrounding survivor benefits.

While pensions from a deceased's workplace may continue, a survivor's pension benefit is often at a reduced rate. Many people don't realize that government benefits may be lacklustre, thereby leaving a shortfall in income or cash flow for the survivor. This may pose challenges because essential expenditures like property taxes and other bills often persist at their usual levels.

Consider the situation in which both spouses collect maximum CPP and OAS benefits – this could potentially provide over \$48,000 in annual retirement income for a couple, based on monthly CPP of \$1,306.57 (2023) and OAS of \$707.68 (Q4 2023) for a retiree at age 65. If one spouse were to pass away, consider that the deceased spouse's annual benefits, or around \$24,000, would be entirely lost.

This is because you cannot receive a survivor's pension while also receiving a full retirement pension: The most that can be paid to a survivor who is eligible for CPP benefits and the CPP survivor's pension is the maximum retirement CPP benefit. With OAS benefits, there is no survivor benefit. The CPP provides a "death benefit," limited to a one-time payment of \$2,500, available if the deceased has been a qualifying CPP contributor.

For survivors not receiving maximum CPP benefits, perhaps due to time out of the workforce, lower CPP contributions or other reasons, they may be entitled to a survivor's benefit. Survivors are eligible for 60 percent of the deceased spouse's CPP pension (if over age 65; under this age, survivor benefits are 37.5 percent of the deceased's pension, plus a flat rate, if that spouse is not receiving other CPP benefits). When combining multiple benefits, the total amount of combined CPP benefits paid is adjusted based on the survivor's age and other benefits received. You will

need to apply for survivor benefits, keeping in mind that back payments will be made for up to 12 months, so delaying may result in lost benefits.

Since CPP and OAS can make up a significant portion of a couple's retirement income or cash flow when both are living, thinking ahead about the potential loss of these benefits – or any income stream – is an important consideration. When reviewing wealth plans, having an income buffer in the event of the loss of one spouse or planning to pivot and use other sources for retirement income may be considerations. For information on CPP survivor benefits, see: www.canada.ca/en/services/benefits/publicpensions/cpp/cpp-survivor-pension.html

Estate Planning for Spouses: Tools to Consider

Addressing income loss is just one consideration when estate planning to protect a spouse. Others may include asset protection, planning for the tax efficiency of assets, minimizing probate or other estate tax, control over asset distribution and others. In brief, here are some tools that may be valuable:

- › **Trusts** – May help to protect and manage assets for the benefit of spouses who need support, or other heirs.
- › **Joint Ownership** – May help to bypass probate, provide tax efficiency and simplify the transfer of assets.
- › **Spousal Rollover** – Can allow for the tax-deferred transfer of assets between spouses upon the death of one spouse, preserving more of the estate's value for the surviving spouse.
- › **Insurance** – May provide support for long-term care, financial security, estate preservation, estate equalization or liquidity to cover immediate expenses or other estate expenses, such as taxes. Insurance can also provide creditor protection or help to facilitate the transfer of a business.



During Uncertain Markets: How Dollar-Cost Averaging Can Help

Renowned investor John Templeton is remembered for advocating the 'principle of maximum pessimism': *"People are always asking me where is the outlook good, but that's the wrong question. The right question is: Where is the outlook the most miserable?"*

In investing, while the concept of buying securities at low prices and selling them at high prices may seem obvious, it may be a lot more difficult for investors to do in practice. Bottoms tend to occur when sentiment is at its lowest, and the natural inclination may be to sell, not buy. As Templeton reminds us, these are precisely the times that can turn out to be some of the most opportune.

For many of us, it's not easy to commit new funds to an investment during uncertain times. This is where a dollar-cost averaging (DCA) program may be a useful technique. A DCA program mandates regular, modest investments, rather than one major lump-sum commitment. Thus, investors need not focus on thinking about market movements to prompt buying decisions. DCA can also align nicely with personal cash flow, as contributions are made at regular intervals, such as monthly or quarterly. This promotes the discipline of saving on a steady basis. Not only can it remove the emotion from investing decisions and match cash flow, but for longer-term investors DCA can also help to build future returns – even when prices may be falling over extended periods.

How can a DCA program help during down markets? A real-life example (chart) shows the potential impact over a prolonged bear market. It may be hard to remember, but the last sustained S&P/TSX Composite bear market occurred after the dot.com bust of 2000 and lasted 25 months, ending in September 2002.¹ The chart uses actual returns of the S&P/TSX Composite Index to depict a DCA program where, each quarter, \$1,000 was invested. Despite poor market performance, the DCA program resulted in a modest gain of \$1,130 (\$17,130 less the \$16,000 invested) and, more importantly, the ownership of significantly more units, which benefitted the portfolio as time went

on. Given a constant investment amount, consider that you can purchase more units when prices are lower and fewer units when prices are higher. By contrast, had the lump sum investment of \$16,000 been deployed at the beginning of the period, it would have returned a small loss, with an overall value of \$15,633 and just 1,902 units owned compared to the 2,084 units under the DCA program.

Profiting Through a Bear Market: DCA Using S&P/TSX Index During 2000 to 2003

Quarter	Index/1000	Units	Units Owned	Total Value
12-99	8,4138	118.85	118.85	\$1,000
03-00	9,4624	105.68	224.53	\$2,125
06-00	10,1995	98.04	322.58	\$3,289
09-00	10,3779	96.36	418.94	\$4,348
12-00	8,9337	111.94	530.87	\$4,743
03-01	7,6080	131.44	662.31	\$5,039
06-01	7,7364	129.26	791.57	\$6,124
09-01	6,8386	146.23	937.80	\$6,413
12-01	7,6884	130.07	1067.87	\$8,210
03-02	7,8515	127.36	1195.23	\$9,384
06-02	7,1456	13995	1335.18	\$9,541
09-02	6,1804	161.80	1496.98	\$9,252
12-02	6,6145	151.18	1648.16	\$10,902
03-03	6,3433	157.65	1805.81	\$11,455
06-03	6,9831	143.20	1949.01	\$13,610
09-03	7,4211	134.75	2083.76	\$15,464
12-03	8,2209	–	2083.76	\$17,130

Source: S&P/TSX Composite Index closing figures, 12-31-99 to 12-31-03. Past performance is never indicative of future performance.

During times of uncertainty, DCA may be a useful strategy for some investors to take the emotions out of investing while continuing to put money to work. DCA is a good reminder that a thoughtful investing plan can result in positive progress toward achieving wealth-building goals, even during down-market times.

1. Of over one year. The last bear market during the pandemic lasted less than two months. The prior bear market of 2008/2009 during the Global Financial Crisis was only nine months long.



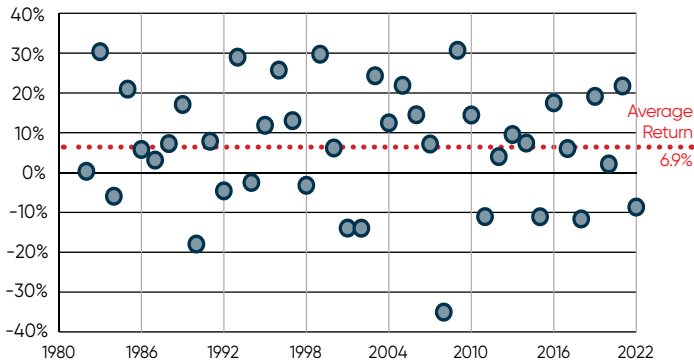
Reminders for the New Year: The Investing Road is a Long One

As we move into another year, what's your investment focus? Given the volatility of 2023, it can take discipline to stay focused on our objectives, but here are three perspectives:

1. Worth a reminder: Annual returns are almost never "average."

While we often talk of average returns for indices like the S&P/TSX Composite, annual returns often vary from the average. The visual shows the wide dispersion of annual returns of the S&P/TSX Composite Index since 1981: 83 percent of the time, annual returns did not fall within +/-2 percentage points of the long-term average return of 6.9 percent (red line). Almost 30 percent of the time, annual returns were negative. Investors should expect a wide range of outcomes each year.

S&P/TSX Composite Annual Returns, 1981 to 2022

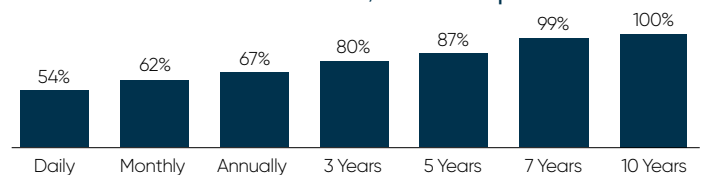


2. Investing often requires patience. Markets will experience both ups and downs, and recoveries can often take time. After the last bear market – the shortest in history at a mere 33 days during the pandemic – we may have been conditioned to believe that the markets should quickly rebound. However, a look back at S&P 500 bear markets over the past 50 years (chart) shows that it has taken an average of 30 months to recover to previous highs. Consider that a 50 percent loss requires a 100 percent gain to recover. Down-market times are a normal part of the investing process and may be opportune times to build portfolios for the future. Eventually, the pendulum swings back.

S&P 500 Bear Markets Over the Past 50 Years				
Peak	Trough	% Decline	Peak-to-Trough Months	Breakeven Months
1/11/73	10/3/74	-48.2%	21	46
11/28/80	8/12/82	-27.1%	20	23
8/25/87	12/4/87	-33.5%	3	17
3/24/00	10/9/02	-49.1%	31	48
10/9/07	3/9/09	-56.8%	17	37
2/19/20	3/23/20	-33.9%	1	6
1/3/22	10/12/22	-25.4%	9	?
Average		-39.1%	14.6	29.5

<https://awealthofcommonsense.com/2023/03/why-the-stock-market-makes-you-feel-bad-all-the-time/>

Chart: How Often is the S&P/TSX Composite Positive?



S&P/TSX Composite Index, no dividends reinvested. "Daily" returns, 1/1/80 to 5/1/23. For all others, rolling monthly returns, 1/1/70 to 5/1/23.

3. Navigating volatility: Extend your time horizon. The more you check your portfolio, the more volatile it will feel because of the greater likelihood of seeing negative performance. History has shown that by checking the markets daily, the chances of seeing a negative return are 46 percent. However, this reduces to 0 percent for 10-year rolling monthly returns. As the graph reminds us, taking a longer-term view smooths out the impact of shorter-term volatility. Extending an investing time horizon provides the opportunity to ride out market fluctuations and volatility and, by staying invested, investors are more likely to benefit from the market's overall upward trajectory.

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