

# MacDougall Wealth Management Group Newsletter



Summer 2021

## In this edition

Afraid You'll Outlive Your Funds?  
The Four Percent Rule Revisited.....1

In Short: The 2021 Federal  
Budget – How It May  
Affect You .....2

Some Summer Fun!.....3

Family Farm Transition –  
The Big Picture .....3

Talking to Adult Children:  
The Hot Housing Market.....4

## Afraid You'll Outlive Your Funds? The Four Percent Rule Revisited

How much can I spend in retirement so that I don't outlast my money? This is one of the more common questions we hear as we help clients to plan ahead.

This question also spawned the birth of the "four percent rule," which has become a commonly used guideline within financial planning circles. It is a simple way to think about retirement withdrawals. Adding all of your investments, you can withdraw four percent of the total during the first year of retirement. In subsequent years, you adjust this amount for inflation. This provides a good proxy for not outliving your money, assuming a 30-year retirement.

### The Origins of the Four Percent Rule

The "rule" has been around since 1994 when rocket-scientist-turned-financial-advisor Bill Bengen took on the task of determining a safe withdrawal rate to protect investors from running short of funds in retirement. Bengen's model assumed that there would be no severe market downturns and the investor would rely upon a predictable, steady stream of income. Here are some of his original findings:<sup>1</sup>

- › The "absolutely safe" withdrawal rate based on historical market returns was three percent. A portfolio would never be fully drawn down in less than 50 years.
- › A four percent withdrawal rate was considered safe as it never resulted in a portfolio being exhausted in less than 33 years.
- › The "worst-case" for a 4.25 percent withdrawal rate was a portfolio that lasted 28 years.
- › While the model was based on a 50/50 stock/bond portfolio, Bengen suggested allocating a greater proportion to equities, between 50 and 75 percent.

Of course, like most generalizations, Bengen's rule of thumb might not fit every investor's situation. After all, retirement spending isn't necessarily constant from year to year. Some retirees have greater expenditures earlier in retirement as they opt to enjoy their healthy years travelling the world or enjoying other costly pursuits; others may be confronted with high healthcare or caregiving expenditures as they age.

The rule was also based on a suggested portfolio composition and historical returns that were relevant in 1994. Things looked different back then. Treasury yields hovered around 8 percent; today, they are closer to 2 percent. Historical inflation at that time

was around 5.7 percent for the previous 25 years; today, the 25-year rate averages around 2.2 percent (see chart).

### Chart: A Lot Has Changed Since 1994...

	1994	2021
10-Year Govt. of Canada Marketable Bonds Rate (A)	8.63%	1.90%
25-Year Historical Rate of Inflation (B)	5.7%	2.2%
5-Year Avg. Residential Mortgage Rate (C)	7.89%	3.26%
Cost of 1L Whole Milk (D)	1.36	1.51
Cost of Eggs (doz. lg.) (E)	1.49	3.77
Price of Gas (reg. unleaded)/L (F)	0.52	1.25

Source: A: Bank of Canada; [www150.statcan.gc.ca/n1/pub/11-210-x/2010000/t098-eng.htm](http://www150.statcan.gc.ca/n1/pub/11-210-x/2010000/t098-eng.htm) (v122487) • B: [awealthofcommonsense.com/2020/10/what-if-the-4-rule-for-retirement-withdrawals-is-now-the-5-rule/](http://awealthofcommonsense.com/2020/10/what-if-the-4-rule-for-retirement-withdrawals-is-now-the-5-rule/) • C: Bank of Canada; [www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=3410014501](http://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=3410014501) • D: [fraserinstitute.org/sites/default/files/PerfectFoodinaPerfectMess.pdf](http://fraserinstitute.org/sites/default/files/PerfectFoodinaPerfectMess.pdf) • E: [archive.macleans.ca/article/1994/1/24/the-cost-of-feeding-canada](http://archive.macleans.ca/article/1994/1/24/the-cost-of-feeding-canada); D, E, F: [www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1810000201](http://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1810000201) • F: [www150.statcan.gc.ca/n1/pub/57-601-x/2010004/t182-eng.htm](http://www150.statcan.gc.ca/n1/pub/57-601-x/2010004/t182-eng.htm)

### The Rule, Revisited for 2021

Given that much has changed in 27 years, you may wonder if the rule has also changed. According to Bengen, yes – and his conclusion may be surprising. He recently suggested that he would actually recommend a higher withdrawal rate: "5.25 or even 5.5 percent, which is going to enrage people even more because it's higher...but that's what history has demonstrated."<sup>2</sup>

### Planning Ahead

If your wealth plan is in need of an update or if you would like to discuss your retirement income plan in greater depth, please don't hesitate to call.

1,2. <https://awealthofcommonsense.com/2020/10/what-if-the-4-rule-for-retirement-withdrawals-is-now-the-5-rule/>

MacDougall  
Wealth Management Group  
4719 48<sup>th</sup> Avenue, Suite 200  
Red Deer AB T4N 3T1  
Tel: 403-348-2600  
Toll Free: 1-866-348-2633  
Fax: 403-348-0203

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## In Short: The 2021 Federal Budget – How It May Affect You

In April, the federal government released its first federal budget in two years. Perhaps most notably, the federal government expects to continue its significant spending – over \$101 billion for the next three years – to support strong economic recovery in the fight against Covid-19. It extended various emergency benefits, resulting in a record deficit and significantly higher projected debt for the foreseeable future.

Some would argue that the excessive spending has Canada wading into “Modern Monetary Theory” (MMT) waters. MMT suggests that federal government spending shouldn’t be constrained by its revenues, which are largely created through taxation. It suggests that countries that issue their own fiat currency should determine what their requirements are and spend accordingly, not worrying about running larger deficits as long as inflation is under control. Given the pledged spending, it may seem as though Canada is embracing this new way of economic thinking. And we’re not the only ones. Many governments have followed suit, with an estimated US\$12 trillion spent globally in just the first 8 months of the pandemic.<sup>1</sup>

While the future economic consequences are yet to be seen, the injection of significant liquidity into the economy appears to be having inflationary effects. We see increasing commodity prices (lumber prices have more than tripled this year!) and steepening grocery bills, as just some examples. Beyond the spending spree, the budget had no changes to personal or corporate income tax rates. Here is how you may be impacted:\*

**For Seniors: Extending Benefits.** Seniors who are 75 years or older as of June, 2022 will receive a one-time Old Age Security (OAS) payment of \$500 by this August. For this same group, monthly OAS payments will be increased by 10 percent beginning in July, 2022. If you aren’t in need of these funds, consider investing them. If you haven’t maxed out contributions, a tax-free savings account is an ideal way to potentially grow funds on a tax-free basis.

**For Investors: Green Investing.** The budget pledges \$8.8 billion over five years to support a greener future, including the issuing of \$5 billion of green bonds to finance green projects. The budget suggests that the presence of government-backed bonds may support more mature investors who are “looking for a green portfolio but also need to manage their investment risk.”<sup>2</sup> With the rise in support for green investing, if you are interested in incorporating environmental factors into your portfolio, please call the office.

**For High-Net-Worth Spenders: A Luxury Tax.** If you’re considering the purchase of a luxury vehicle in the near future, you may

want to do so by Dec. 31, 2021. As of January 1, 2022, sales of cars and personal aircraft with a retail price of over \$100,000, as well as boats priced over \$250,000, will incur a new tax. It will be calculated at the lesser of 20 percent of the value above those thresholds, or 10 percent of the full value of the vehicle.

**For Business Owners: Accounting for Capital Assets.** If you operate a Canadian-controlled private corporation, the business will now be able to purchase up to \$1.5 million of certain capital assets and fully expense these in the year they become available for use. This includes eligible assets purchased on or after April 19, 2021 and before 2024. There may be tax benefits achieved by immediately expensing certain assets so please consult a tax professional as it relates to your situation.

For greater detail on the initiatives proposed, see the Government of Canada website: [budget.gc.ca/2021/home-accueil-en.html](https://budget.gc.ca/2021/home-accueil-en.html)

1. [theglobeandmail.com/business/article-whatever-we-may-think-of-modern-monetary-theory-its-day-in-the-sun-has](https://theglobeandmail.com/business/article-whatever-we-may-think-of-modern-monetary-theory-its-day-in-the-sun-has) • 2. Budget 2021: A Recovery Plan for Jobs, Growth and Resilience, Government of Canada, page 166.

\* At the time of writing, the budget proposals had not been passed into law.

## Some Summer Fun!



**Iain**  
Not done yet, but so close!  
250 Puch Allstate  
(SGS conversion) 1996.

**Dianne**  
Kayak trips  
with the  
entire gang.



**Kit**  
Digging  
for fossils  
with the  
family.



**Samantha**  
River walk's  
with Billi girl.



**Shay**  
There is a new driver in town...  
Shay teaching her niece to drive!



# Family Farm Transition – The Big Picture

**"It was the best of times, it was the worst of times" ...**

– *A Tale of Two Cities, Charles Dickens*

Whether that opening sentence from *The Tale of Two Cities* describes 2020 to you, all of us have faced an unprecedented year of challenges whether financially, emotionally, within our families or in a way unique only to ourselves. A Global Pandemic will do that to you. Countries, governments, communities, our friends, and families have all struggled with something unheard of in most of our lifetimes. Our day to day lives have been severely impacted in most areas and will continue to be for the foreseeable future.

With that being the situation going into 2021, that essential business, the Canadian Family Farm, can still receive the necessary attention it deserves especially if transition or succession are top of mind for you and your family. In "the best of times" – pre pandemic – according to Statistics Canada, only 8 percent of all farm families had

a written succession plan. Additionally, the study highlights, more farmers are over 70 than under 35. Family farm transition therefore should be front and center within farm families today but clearly it is not.

The reasons for this varies and "the worst of times" – the pandemic – certainly hasn't helped farming families proceed with planning their succession. Emotions, family issues, perceived complexities, financial and tax issues combined with the present social environment can create a sense of ... "It can wait". Hopefully this article can assist farm families into looking at the "Big Picture" and not getting caught in the details which can derail the succession process before it even gets started.

Big picture family farm succession includes communication, following a formal process, staying focused on

the ultimate goal, and revisiting and updating your plan regularly.

## 1. Communicate with Family the Process

This means more than idle conversations over coffee or the fender of the tractor. Open conversations with

all members of the family are critical and essential. It probably will be emotional and not everyone may agree.

If you create a safe place for family discussions and understand that these conversations are integral to ensure the deep thoughts, aspirations, and perhaps past family squabbles, are laid bare for all to consider will help ensure the success of YOUR family plan. By the way it won't all be negative. Past assumptions, personal perceptions, and conflicts will hopefully be revealed, discussed and potentially resolved.

When these issues are discussed in a family meeting special consideration must be given to YOUR plans overall process, then communicated, agreed to and followed by the

participants. These family meetings are essential for the parents to communicate that a formal succession process will be embarked on by the family to ensure all members of the family are considered and to identify what the best course of action is for everyone in the family. The formal process will assist the family to focus on the ultimate goal of the family and the family farm succession plan, and not on minor details.

## 2. Focus on the Ultimate Goals

We have heard so often... "the devil is in the detail". Those words have never been truer than when it comes to farm families and the succession of the family farm. The tax planning is complicated by inconsistent farm incomes, high expenses, significant asset holdings, and low liquidity which makes the reality of creating

a realizable family farm succession plan especially problematic. And you haven't touched the fair vs equal issue yet! But don't lose hope.

If you follow a formal process focusing on the ultimate goal, you will have a greater chance of success. Fundamentally you have to give up the notion in your succession plan that you can divide up the family farm on equal lines perhaps using some formula or equation. Fair will NOT be equal. Remember to focus on the end goal which is to create a transition solution unique to your family farm situation and a succession plan the family supports and understands. Family harmony is essential as you still want your family to sit around the table

at Christmas and other holidays. There are no easy answers and it is hard work. If you get through the formal process once it will be easier to revisit and adjust the plan as circumstances change.

## 3. Revisit. Revisit. Revisit.

Once you have been through the formal process you will have to revisit your succession plan on a regular basis. Your plan is NOT a one size fits all until the end of time. It is not done once and put in a binder to gather dust.

It is in the most real terms... "a living, breathing document". As you have probably realized this succession process is not only integral to your family legacy but also to your family harmony. As we have experienced in 2020 unknowns can come at us any time. If you hold to the process of revisiting your plan regularly with all family members, the plan will continue to have that regular breath of life to ensure it is relevant, realizable, and most

of all continues to be supported by the family. Things do change including family priorities, new life goals,

and health issues. These changes can fundamentally change key elements once integral to your succession plan. Such changes may affect your progress but will not derail it.



## Talking to Adult Children: The Hot Housing Market

For those of us who can remember, the average cost of a Canadian home was around \$164,000 when we started the millennium.<sup>1</sup> In just over 20 years, this has risen to around \$716,000 – and, what you get for that price can vary depending upon your location.<sup>2</sup>

What is driving these increases? Lack of supply in some markets has helped push prices higher. As prices continue to increase, many buyers have entered the markets feeling a sense of urgency and fear of missing out. Low borrowing costs have also prompted some to take on mortgages beyond their means. With prices at all-time highs, there has also been increasing speculation.

The situation is especially discouraging for the younger generation who may feel as though home ownership is quickly becoming out of reach. In a recent interview, Robert Kelly, former Chair of the Canadian Mortgage & Housing Corporation (CMHC), suggested that we have a problem and better education is needed.<sup>3</sup> He is an advocate for stiffening the current mortgage rules and suggests that the federal government needs to provide support to increase the housing supply across many markets.

For the younger generation still hoping to enter the housing market, Kelly suggests keeping these four considerations in mind:

**Consider that a house is not a guaranteed investment.** While we may have become used to a hot housing market, it hasn't always been this way. Kelly points to U.S. housing data over 100 years, which shows an average increase in value of around one percent per year. Buyers also need to consider that there are many hidden costs associated with home ownership and, unlike other investments, it often involves a significant up-front cost.

**Focus on needs vs. wants.** Focusing on what is needed may help buyers to make more prudent decisions. While a 4,000 square foot home may be the aspiration, a smaller footprint is likely to sufficiently meet an individual's living needs while being more financially achievable.

**Factor in the risk of rising interest rates.** Consider the impact of a reset in interest rates one or two years down the road. Many mortgage holders may not factor in the likely scenario in which interest rates increase by one percent. Would you still have discretionary income to go on vacation or eat out at restaurants?

**Think about absolute debt – and lower it.** When holding a mortgage, it is important to consider not just the monthly payments, but also the total amount of debt. The average Canadian household debt-to-income ratio is extremely high

at around 175 percent<sup>4</sup> – the highest of the G7 advanced economies. This puts many individuals at risk of default, such as in the event of a job loss. Kelly suggests that a responsible debt level is around 90 percent, where many G7 countries currently sit.

### How About Your Personal Situation?

We have been approached by clients who have asked for perspectives on selling their home. While the gains may be enticing with prices at all-time highs, keep in mind that if you were to sell your home you would still need a place to go – which will likely incur a financial and perhaps even a lifestyle cost. Care should be taken when evaluating the options. Another option may be to sell a home and then rent, potentially leading to higher discretionary funds to support retirement or to gift to children during your lifetime. Renting may also be more pragmatic for many younger folks, in instances where taking on higher debt loads does not make sense.

1. [theglobeandmail.com/real-estate/the-market/canadian-home-value-has-doubled-since-2000-report/article4249097](http://theglobeandmail.com/real-estate/the-market/canadian-home-value-has-doubled-since-2000-report/article4249097) • 2. [cbc.ca/news/canada/photos/canada-real-estate-prices-scroller-1.6004260](http://cbc.ca/news/canada/photos/canada-real-estate-prices-scroller-1.6004260) • 3. [bnnbloomberg.ca/real-estate/video/canada-has-a-problem-former-cmhc-chair-robert-kelly-on-the-nation-s-hot-housing-markets-2160679](http://bnnbloomberg.ca/real-estate/video/canada-has-a-problem-former-cmhc-chair-robert-kelly-on-the-nation-s-hot-housing-markets-2160679) • 4. [ctvnews.ca/business/canadian-households-added-record-mortgage-debt-in-q4-statcan-1.5344672](http://ctvnews.ca/business/canadian-households-added-record-mortgage-debt-in-q4-statcan-1.5344672); [data.oecd.org/hha/household-debt.htm](http://data.oecd.org/hha/household-debt.htm)

Iain MacDougall, B.Sc., Ag., Econ., CIM®  
Investment Advisor, Portfolio Manager,  
Sr. Vice-President  
iain.macdougall@nbc.ca

Samantha Jones, B.Mgt.Fin., MBA  
Associate Investment Advisor  
samantha.jones@nbc.ca

Kit Richmond, B.Sc.  
Associate Investment Advisor  
christopher.richmond@nbc.ca

David L. Zimmel,  
CPA CA, CPA (Ill. USA), CMC, FEA  
Senior Tax and Estate Advisor

Dianne Hughes  
Branch Administrator,  
Investment Associate  
dianne.hughes@nbc.ca

Shaylene Strangways  
Investment Associate  
shaylene.strangways@nbc.ca

Cori Timmons, BA, CFP, CLU, ChFC  
Estate and Insurance Advisor



**MACDOUGALL**  
Wealth Management Group

**MacDougall Wealth Management Group**  
4719 48<sup>th</sup> Avenue, Suite 200, Red Deer AB T4N 3T1  
Tel: 403-348-2600 | Toll Free: 1-866-348-2633 | Fax: 403-348-0203

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