Fall 2021

Financial Focus

NATIONAL BANK FINANCIAL
WEALTH MANAGEMENT

Take financial stock to make change happen

Whether brought on by the pandemic, a financial milestone or just a new life stage, many of us are looking at major changes like early retirement, moving to a new province, changing careers or starting a business. If you've done the hard work of deciding which changes are right for you, how do you go about understanding the financial changes that are required? Here are three things you can do now to understand the numbers behind any change:

1. Determine where you stand today. Your current financial status is the foundation on which you'll build your next lifestage decisions. Creating a net worth statement is a great place to start. A personal net worth statement is a snapshot of an individual's financial health. It is a summary of what is owned (assets) minus what is owed to others (liabilities). Another example: If you are considering early retirement, request a pension statement from the Government of Canada or Retraite Québec to receive an estimate of your likely benefits.

2. Get a realistic view of the financial costs of your new life. The next step is to attach some hard figures to your thoughts and dreams. Start with some research. Whether you're looking for house prices in another province, tuition fees for a degree or training program, or costs of running a small business, a little online digging will locate the information you're seeking. Put that new-found knowledge to work by creating a blueprint such as a moving budget, a business plan, or a regular savings program, if you need to build some capital to support your aspirations and ambitions.

3. Seek professional financial advice for all scenarios. There is seldom just one way to reach a goal, and professional advisors can help you explore the options. Professional accountants, for instance, can run multiple financial scenarios evaluating alternative approaches. Experts such as business advisors can also help with knowledge you may not already have, such as funding sources, grants and tax breaks. And, don't forget to speak to us about investment and savings strategies to help you reach your goals.

Next steps: Your investment plan should always reflect your goals – so if they have changed, let's talk soon. We can help you align your assets to your aspirations.

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Autumn has arrived – the traditional season of giving thanks. We hope you continue to have many things for which to be grateful but, most importantly, your own good health and that of your loved ones. Hopefully, this year we will all be able to gather with others and share good times in person. We, too, have much to be thankful for, including your continued faith in our work to help you prosper, now and in the future. As society begins to function in a more familiar way, we would be happy to reconnect on the practical aspects of your financial life: your investment portfolio, your goals, and any financial opportunities that need to be tended to before year's end.

NASH
Family Wealth Management

Looking for more after-tax retirement income? Consider these strategies

Once you've retired, your financial focus will become making the most of your retirement savings – and that means paying as little tax as possible. Fortunately, there are things you can do to structure your income flow in a way that maximizes your after-tax income. Consider the following:

Look at the order in which you withdraw income. The traditional rule of thumb is to withdraw first from accounts that are not tax-deferred (your non-registered investment accounts, for instance). The idea is to put off withdrawals from Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs) where all proceeds are taxed as income, attracting the highest rate of tax regardless of how they were earned. It also allows those investments to continue to grow tax-deferred. The truth is that this rule is simplistic and overly focussed on current tax savings. Your strategy really depends on how much you have and where those assets are held. It may be that income should be drawn from a mix of sources to achieve the best tax-efficiency both in current and future years. The right order for you will also depend on a number of factors, including whether maximizing government benefits such as the Canada Pension Plan (CPP) and Old Age Security (OAS) is vital, if you want or need to keep your portfolio growing in retirement, and if you have non-investment income from a rental property or part-time employment. Estate planning goals may also impact your withdrawal order strategy.

Use your TFSA wisely. Tax-Free Savings Accounts (TFSAs) can play a useful role after you've retired because of their main benefit: money earned inside the account is not taxable – even when you withdraw it (unlike RRSPs and RRIFs). If you have retirement assets in a non-registered account, they may be better off in a TFSA (up to the contribution limit), thereby earning income tax-free. Remember that TFSA contribution limits are cumulative and provide room of up to $75,500 as of 2021, if you've been eligible to contribute since 2009. TFSAs also provide a great place to "park" money in retirement. This could include money that you have been required to withdraw from your RRIF but for which you don't have an immediate use, as well as money put aside as an emergency fund for unexpected expenses. By sheltering these funds and their profits from tax, you'll ensure you get the benefit of all your savings.

Split pension income if eligible. Splitting income is a strategy that allows couples to reduce taxes by transferring pension income (for tax purposes) from the higher-income earner to the lower-income earner. The transferring spouse or common-law partner can give up to 50% of their eligible pension income to the receiving spouse or common-law partner. If you are 65 years of age or older, eligible sources for pension income-splitting include an RRIF, a registered pension plan, and an annuity purchased with funds from an RRSP. If you are under age 65, eligible income is mainly limited to registered pension plan benefits and certain payments resulting from the death of a former spouse or common- law partner. You can begin pension income-splitting at age 55 if you retire at that age and have eligible pension income. Note that residents of Quebec under 65 cannot split pension income for provincial income taxes.

Use T-series mutual funds. For mutual fund investors, T-series MFs may provide a more tax-efficient way to generate income from your investments. T-series funds are designed to provide a predictable and sustainable cash flow, often at a set percentage, which helps with cash-flow planning. Depending on the fund's earnings (usually interest income, dividends and capital gains), the fund may also distribute a portion of the investor's original investment, known as Return of Capital (ROC). ROC is usually not taxable, resulting in a more tax-efficient payout for you. If you are not currently in T-series funds, it may be possible to transition to the T-series version from the series of the fund you currently hold without triggering a tax liability. A Word of Caution: When you receive an ROC distribution, you will lower the Adjusted Cost Base (ACB) of your holdings, which could have tax implications later. Careful planning and monitoring are required.

Next steps: Everyone's situation is unique and there is no "off-the-shelf" solution. While obtaining tax-efficient cash flow is an important goal, so is maintaining the right asset allocation for your portfolio's long-term health and managing risk according to your own tolerance level. Professional tax and investment advice are needed to achieve the right balance for you.

With the economy accelerating, where do money managers find investing opportunities?

As the major Western economies throw off the shackles of the pandemic, economic growth is accelerating, with Gross Domestic Product (GDP) predictions having been upgraded several times already this year for many countries. Will this rising tide lift all boats? Or, will certain styles of investing offer the potential for better returns this year?

Ideal conditions

As our *3rd Quarter Market Outlook*[1] noted, economic growth seems set to expand considerably thanks to several positive trends: vaccinations are well under way; reopening is proceeding across North America; pent-up demand is strong; and household savings are high. But it is these very circumstances that may allow some companies and sectors to outperform versus others. Inevitably, there will be winners and relative losers as the economy shifts from lockdown mode to more typical conditions.

Which sectors?

Even a casual observer or news watcher will have noticed the winners and losers at a sector level last year. As sections of the economy ground to a halt, airlines, hotels and restaurants, brick-and-mortar retailers, and oil and gas companies suffered as demand dried up – and some failed to survive at all. Meanwhile, technology companies, online retailers, and pharmaceutical firms did well as their business models allowed them not only to keep doing business, but also for many to experience a surge in demand from stuck-at-home consumers.

For portfolio managers, the question will be: When will those depressed sectors come back to life – and which sectors and companies will provide profitability that will drive share price growth? Conversely, will those sectors that did well last year continue to do so, or are they likely to experience a pullback? While many economists and commentators are predicting a "Roaring Twenties"-style comeback with a splurge of consumer spending, there are still risks ahead, including a potential resurgence of inflation and ongoing uncertainty as the pandemic continues to cause travel restrictions and the potential for further lockdowns.

Value or growth?

Many portfolio managers are characterized as having an investment style, often using a "value" or "growth" filter to assess potential stocks. Depending on the approach, the opportunities in the post-lockdown economy may look very different.

Value-focussed managers seek out quality firms whose market prices do not accurately reflect their intrinsic value. They pay close attention to a company's financial information such as its debt levels, price/earnings (p/e) ratio, price/book value ratio, and dividend yields to determine whether its stock is overpriced, underpriced, or fairly valued. Value stocks tend to do well at the beginning of an economic cycle, which may be where we are now, and value managers will be looking for those relative underperformers ready to excel.

Growth managers seek out companies whose earnings they think will grow faster than those within their industry or the overall market. They look for firms that have high earnings growth rates, a high return on equity, high profit margins, and low dividend yields. As the economy accelerates, growth managers will continue to see opportunities in companies that are riding a wave of growth and can expect continued high levels of profitability as consumers and businesses begin spending with gusto.

Next steps: For the individual investor, considering the different approaches used by professional managers offers a way for a client to better understand equity markets and investment performance better. But the most important approach is to adhere to the foundations of a diversified portfolio matched with your individual risk profile and investment goals. A portfolio review is a great way to reconnect with your personal investment plan.

1 National Bank. *3rd Quarter Market Outlook*. June 25, 2021. https://www.nbc.ca/personal/advice/savings-investment/market-outlook-3rd-quarter.html

Canada: Land of the unicorn?

What's a unicorn and why have there been so many sighted in Canada this past year? This phenomenon – when a privately-held, start-up company is valued at over $1 billion – has happened with unusual frequency in Canada in 2021. While it's certainly good news for many of the unicorns' founders and early investors, what does it mean for you?

In the first half of 2021 alone, ten Canadian high-tech companies achieved unicorn status as the technology sector in Canada has boomed, attracting the interest of venture capital firms from here and beyond. These unicorn companies span a wide variety of technology – from improving everyday use of the internet to leading-edge AI.

It's important to note that venture capital firms have an appetite for risk that few individual Canadian investors share. Because these young companies are privately held (at least for now), most of us can't buy into them. But the frenzy of unicorn announcements and the performance of the technology sector overall could have you thinking about how to join in.

Keep in mind that for every Shopify (now Canada's largest company by market capitalization, at time of writing), hundreds of start-ups fail to achieve their potential and many fail outright. And, as the status of Shopify shows, technology is now a mainstream economic sector: these cutting-edge, innovative companies are present throughout the market, from global giants paying dividends to speculative start-ups.

Next steps: If all the coverage of these kinds of investment opportunities has caught your eye, let's discuss your portfolio goals to put this trend in perspective.

Reviewing beneficiary designations is no small matter for your estate plan

Reviewing and updating the beneficiary designations on financial accounts and insurance policies can seem like a minor administrative matter. However, a recent court case in Nova Scotia shows how major, and potentially devastating, an issue it can be. Earlier this year, the CBC reported that a widow with a young daughter was left without access to her deceased husband's Registered Retirement Savings Plan (RRSP) proceeds despite his having created an up-to-date will – including a clause to revoke outdated designations. The husband had long ago designated his mother as the beneficiary and made no updates to the account after his marriage. Whatever the details of this case, the lesson for all is clear: a regular review and updating of beneficiary designations is sound estate planning practice.

What is it? Registered financial plans, including RRSPs, Registered Retirement Income Funds (RRIFs) and Tax-Free Savings Accounts (TFSAs), as well as life insurance policies and many pensions, allow you to name a person to whom the proceeds of the account or policy will accrue should you die. Note that residents of Quebec do not have the ability to name a beneficiary within the registered financial plan documentation and must use their will to achieve their estate planning goals for these accounts.

What are the benefits? Naming a beneficiary means that the proceeds remain outside your estate and therefore are not controlled by the executor or the estate trustee, are not governed by the will, do not require probate, and no estate administration taxes are payable. The proceeds are paid directly – and often, quickly – to the beneficiary. It is common and sound planning to name your spouse if you have one, as it can expedite payments to them at a time when the funds may be needed. Note that if you do not want to name a person or prefer these assets to be considered as part of your estate, you can name the estate itself as the beneficiary.

Time for an update? As with the case of the family in Nova Scotia, many of us made beneficiary designations when opening our accounts years ago and have forgotten about them. If you cannot recall the beneficiary of each of your accounts and policies, that's a sign that a review is long overdue. As with other aspects of your will and estate plan, any life change should trigger a review – including marriage, separation or divorce, or the death of anyone named as a beneficiary in your plans or will. And as estate matters are covered by provincial law, if you move to another province, you should understand how things work there and review your entire estate plan accordingly.

Next steps: If you think it may be time to review your beneficiary designations on your financial accounts, don't hesitate to get in touch. Also, be sure to reach out to your professional insurance advisors and pension administrators, if appropriate.

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