Market Update

April 2024

Important Topic: Market Timing masquerading as Thoughtful, Prudent, Gut Feel, Group Think or Plain To See

"The market is obviously expensive" "I am going to wait till there is less risk" "Things are going to get worse" "Everyone knows ...." And "Obviously markets can't keep going up" "This market correction has only started."

I have heard all the above quotes more times than I can count. In each case one is justifying one's desire and attempt to time the market (either selling or buying) while honestly believing that one is not.

In the moment it does not feel like market timing, but rather a proper course of action, easily justified. But in truth, as one does not know the future and cannot know it, one is, at best, playing the odds, and at worst, believing they have the rare ability to anticipate the future.

Here's an example: in early 2017, people were saying the US market (S&P 500) was overvalued. So, let's say you waited until March 23, 2020, the day of the bottom, and you bought. You still would have bought at prices 7% higher than in early 2017.

As human beings it is very difficult to set aside one's emotions. Even in supposedly objective analysis, one's bias, emotion, and thoughts often creep in undetected. We are all guilty of this at times.

But knowing we are human, we can anticipate such justifications, acknowledge it, account for it, compensate for it and involve others to help offset these tendencies and keep us on track.

For most years, the highest market values are in December as markets tend to move upward (something to think about).

For all other years one cannot tell which dates represent highs that should be avoided or lows that should be embraced. One simply cannot know.

Lastly, given that even if one invests at the year's highest market point, one is very likely to outperform money market or even GICs after 20 years, why try.

If one's funds are to be invested for the long term, one should probably invest as soon as one can. Waiting is almost always fear, masquerading as prudency.

Market Update:

April 2024 - The Governments New Capital Gains Tax

The Federal Liberal government has let us know their intention to change the way Capital Gains are taxed. Specifically, the Government is changing the amount of the gain that is taxed, known as the "inclusion rate".

Importantly, **individuals** will still be taxed at the lower 50% inclusion on the first **$250,000** of capital gains each year.

Most individuals therefore will not be affected, except in years when one realizes a large capital gain on the sale of a large investment such as a cottage, investment property, options or a business.

Unfortunately, **this advantage does not apply to Corporations or Trusts.** All corporations and trusts will be facing the higher capital gains rates on all of their gains.

A trust has the ability to payout its gains to the beneficiaries where the first $250,000 would face the lower inclusion rate.

Corporations – all corporations, including public listed companies – will be affected by this change.

Presently, the inclusion rate is 50%, meaning that if one has a Capital Gain of $186,916, 50% or $93,458 is taxed as income. This gain is then taxed at 53.5%.

If one is in the highest tax bracket, a gain of $186,916 has a tax calculation = $186,916 * 50% inclusion * 53.5% tax rate = $50,000

The proposal is to increase the inclusion rate to 66%, meaning that if one has a Capital Gain of $186,916, then 66% or $123,364 is taxed as income.

Then if one is in the highest tax bracket, a gain of $186,916 has a tax calculation = $186,916 * 66% inclusion * 53.5% tax rate = $66,000.

The tax is 32% higher – the final tax rate on the gain is now 35.3% instead of 26.7%.

Presently, the government intends to allow taxation at the lower inclusion rate until June 24.

As a result, many are wondering if they should do something before June 24?

Should they sell and realize capital gains before June 24 and then reinvest. This would lock in the lower tax rate but at the expense of having to pay the capital gains tax sooner.

Do I sell before June 24?

Consider the math:

Say you have an investment that cost $250,000 and is now worth $500,000. If you sell it and pay the 26.7% tax (50% inclusion) on the $250,000 gain = $66,875, you will be left with $433,125.

You then reinvest the $433,125. Let's compare that to the growth of the untouched original $500k.

Approximate Breakeven:

After 6 years assuming a return of 6% the $433,125 is worth $614,400 and the $500,000 is worth $709,260. Both now face 66% inclusion on the gain (but the former has the reset cost basis (much lower gain)).

The Reset Asset: Value $614,400. Tax on gain of $181,271 (614,400 - 433,125) * 35.3% tax rate = $64,007, leaving you with $550,389

The Original: Value $709,260. Tax on gain of $459,260 (709,260 – 250,000) * 35.3% tax rate = $162,165, leaving you with $547,095

Therefore, if you plan on holding the investment for 6+ years and do so on the expectation that you earn 6% per year (why else would you be investing?), then it is best to wait.

However, if you plan on selling soon, or you own an investment that is not doing well and not expected to do well, then selling now may make sense.

Another variable that affects the analysis: the amount of current unrealized gain

If the unrealized gain is 50% or greater than it is worth waiting. Paying the larger amount of tax sooner hurts.

If the unrealized gain is less than 50%, it is more worthwhile selling, but the savings are smaller.

Also, to be considered, importantly, is that selling a property or business before June 24 may be difficult. Given the possibility of more sellers appearing suddenly during this time period, and the buyers well aware of the looming deadline, it is possible that the price you receive is lower that what might be expected (or considered "fair").

Additionally, selling may have a series of costs including legal, commissions (selling and rebuying), land transfer tax, borrowing penalties and costs, etc.

Lastly, it is always possible that a future government lowers the inclusion rate back down to 50% making all of this activity pointless.

Conclusion: Each case should be looked at independently (and we are here to discuss) but as a rule of thumb I believe that a fair/strong investment (expect a return of over 6%) that is being held for the long term (at least 5 years) should be held.

What do I do going forward?

Personally – We would target a maximum of $250,000 of capital gains in any given year, if possible.

Corporately – There is nothing you can do except to try and delay capital gains as much as possible. Look for low turnover funds, corporate class structures, and long-term investments (as we do).

April was a negative month, but following 5 out of the ordinary positive months, one should still be feeling good.

Earnings are still growing, employment is strong and the economy is so strong governments are delaying interest rate cuts.

We are positive and optimistic about the short, medium, and long term, and, more importantly, our ability to meet our client's objectives. At the end of the day that last point is all that truly matters.

Sincerely,

- Meir & Adam

Index	Month	Year to date
Bonds FTSE Canada Universe Bond Index - CAD	-2.2%	-3.4%
Canadian Equity - S&P/TSX 60 Index - CAD	-2.2%	3.9%
US Equity – S&P 500 - USD	-4.2%	5.7%
International – MSCI EAFE Index - USD	-3.2%	2.5%
Emerging Markets - MSCI Emerging Markets Index - CAD	1.4%	5.9%
Real Estate - Dow Jones® Global Real Estate Index - USD	-6.6%	-7.9%
S&P/TSX Preferred Share Index - CAD	0.9%	10.1%

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BC25-018