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TD Wealth

June 2024 Quarterly Update

It is mid-May as we share our thoughts with you on the last quarter and focus-in on some of the most common discussions we are having with our clients. Outside of the office, we are looking forward to a beautiful west coast summer which includes plenty of time spent on the water, BBQs and longer days. We look forward to hearing about your upcoming travel adventures, fishing trips, time spent with family and more!

In this issue we try to cut through the financial media noise and update you on where the markets and economy are at. We will also share our views on the U.S. election which is a very hot topic for Canadians and Americans alike. Additionally, we will share some wisdom from Warren Buffet – one of our favourite investors.

We will conclude with a brief overview of the 2024 Federal Budget proposal as it is impacting many of our clients. Although hard to conceptualize at times, we believe investment returns should be measured on an after-fee and after-tax basis which makes this discussion highly relevant.

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The BonnGasic Group | Wealth Management

Market Reflections

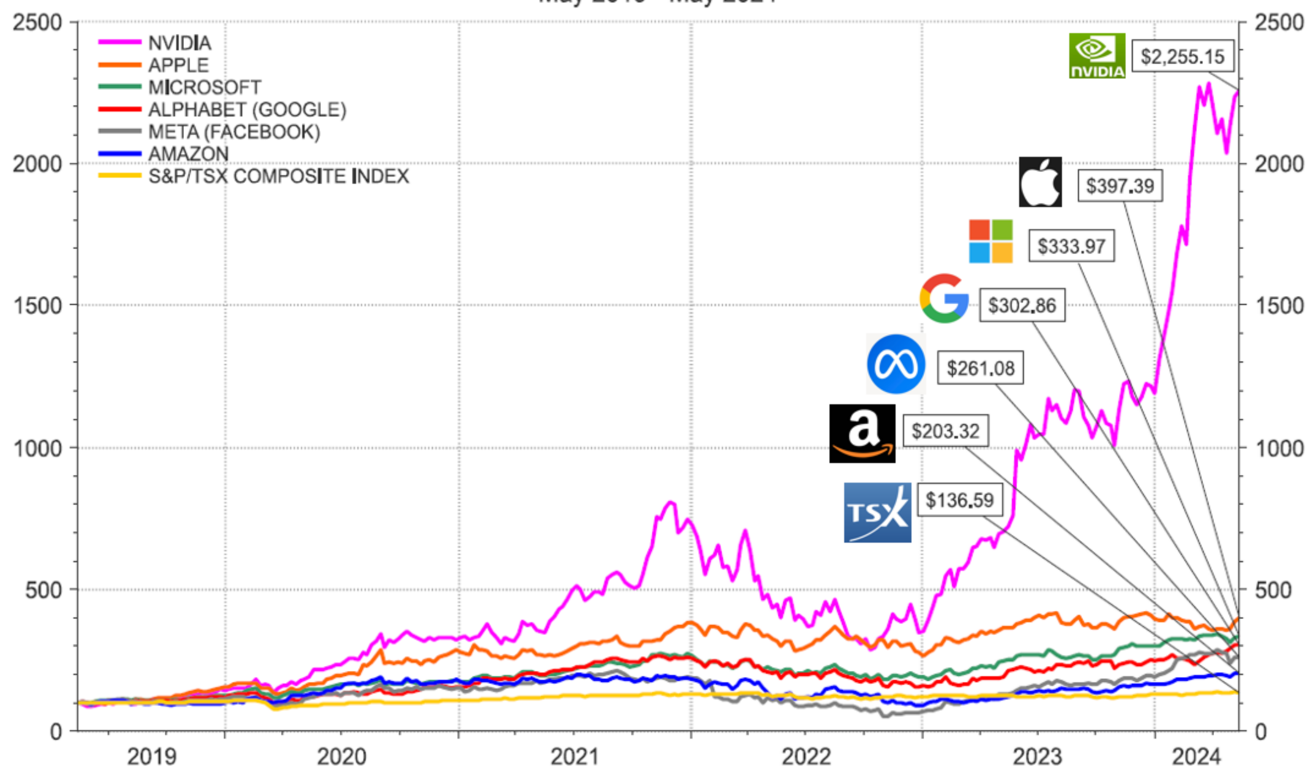
2024 year-to-date equity market performance has been fairly in-line with our expectations. Headline inflation in Canada and the US has decreased since November 2023 indicating that tighter monetary policy was working and suggesting that interest rates had likely reached their peak. Times like these can be very supportive for "risky" assets such as equities as investors begin to anticipate interest rate cuts ahead. What did perplex us was the amount of interest rate cuts that "the market" had been anticipating throughout 2024. The "market consensus" was for 4 or 5 interest rate cuts in 2024 in North America. To us this seemed too optimistic and unrealistic if the goal of central banks was to keep inflation in-check. All along we have believed that inflation rates and interest rates would stay "higher for longer".

As of mid-May, the market's tone has changed, and the "higher for longer" narrative has become the dominant one. Inflation in the US is stickier than expected and many believe that getting inflation down to 2% will take more time than previously thought. US Headline Inflation is currently 3.4%. *Translation?* US interest rate cut expectations are down to just one or two 25 bps cuts, potentially in the fall or winter. The US economy is simply doing too well to justify cutting rates (as measured by growth, labour, productivity, etc.). Canada's economy is a bit worse – growth is low, the labour market is weakening, and productivity is negative. Canadians are also very interest-rate sensitive with higher personal debt-levels and risk much higher mortgage payments as rollovers occur in 2024 and 2025. Headline inflation in Canada is 2.9% and the Bank of Canada has suggested that there could be a cut as early as June or July 2024, with a few more to follow.

As of January 1st – May 15th, 2024, in Canadian dollar terms, equity markets have delivered very strong returns globally due to the fact the markets priced in significant rate cuts this year. The US continues to lead the world (from mega-tech exposure), with the S&P 500 and NASDAQ up 10%, followed by Asian and European markets, and then the laggard being the Canadian S&P/TSX up 6.13%. As many investors have unhedged investment portfolios, when the Canadian dollar is weak and the US dollar is strong, any exposure in US markets on an unhedged basis will contribute to your total investment return. This phenomenon continues to play out as the USD remains at high-levels due to their interest rate policy divergence relative to other developed countries.

For a visual reference, see the chart on Page 3 which illustrates the impact of the "Magnificent Six" mega-tech companies against the S&P/TSX over the past 5-Years. Moving forward, if rates remain at a higher level, market return expectations will need to recalibrate, or strong earnings growth will need to drive the market higher (not simply P/E or valuation expansion). Put simply, a lot of things need to continue to go right for equity market returns to stay this elevated for the remainder of the year.

While it may be easy to experience "FOMO" or the "Fear of Missing Out" when we look at the Magnificent Six (or Seven) technology companies tied to artificial intelligence, Warren Buffet, CEO of Berkshire Hathaway, has mixed feelings and shared his wisdom during his May Annual General Meeting. He quoted, *"It (AI) has enormous potential for good and enormous potential for harm". "When you think about the potential for scamming people… scamming has always been part of the American scene. If I was interested in investing in scamming – it's gonna be the growth industry of all time".* Interestingly, he drew comparisons to nuclear weapons. *"We let the genie out of the bottle when we developed nuclear weapons, and that genie has been doing some terrible things. I don't know of any way to get that genie back in the bottle. And AI is somewhat similar. It's part of the way out of the bottle".*


Growth of $100 by Magnificent 6 vs. S&P/TSX Composite Index
May 2019 - May 2024
NVIDIA
APPLE
MICROSOFT
ALPHABET (GOOGLE)
META (FACEBOOK)
AMAZON
S&P/TSX COMPOSITE INDEX
$2,255.15
$397.39
$333.97
$302.86
$261.08
$203.32
$136.59
0
500
1000
1500
2000
2500
2019
2020
2021
2022
2023
2024
Source: LSEG Datastream

Early Thoughts on the US Election

As you might expect, one of the most frequent conversation topics we've been having with clients has been surrounding the upcoming US election. This is a dramatic affair, and one that we should monitor as its outcome does impact all of us as Canadian investors, both directly and indirectly.

Clearly, US elections have a direct impact on our investments in American companies, which in most cases form significant portions of our portfolios. However, US policy decisions also directly and indirectly impact Canadian and global companies that we invest in. US monetary and fiscal policies have global sway, and can drive global expectations of inflation, interest rates, foreign-currency exchange rates, international relationships (or lack thereof), and an untold number of other significant economic factors.

We don't have a crystal ball and we certainly don't care to make predictions of the ultimate outcome. What we do try and consider are the relative impacts of both candidates' platforms on key sectors of the economy. Below is a very simple table that summarizes some of the highlights that we are watching:

Under Biden		Under Trump	
Outperform	**Underperform**	**Outperform**	**Underperform**
• Clean energy as energy transition continues • Semiconductors and Materials due to productivity enhancement technologies and industrial sector investment	• Healthcare due to a focus on reducing drug provider costs • Financials from regulatory oversight in consumer fee protections and corporate transactions • Traditional energy producers	• Small cap stocks due to domestic economic focus • Financials from reduced regulations • Traditional energy producers • Healthcare from pricing power and repeal of Affordable Care Act	• Clean energy following rollback in climate action policies • Retail stocks due to import tariffs and higher input costs • Communication Services due to pushback against legacy media

Bipartisan

- Both candidates are expected to have a "tough on China" economic policy

A lot can and will happen between now and election day on November 5th. Our views are sure to evolve as time goes on, but broadly speaking, one takeaway is that regardless of how this election evolves, under both candidates' platforms there are going to be sectors of the economy that are expected to outperform and underperform. We continue to believe that long-term diversified exposure to US equities remains a core pillar of a well positioned portfolio.

Canada's 2024 Federal Budget

Discussing changes to Canada's federal budget tends to be a rather dry subject, at least in a good year. Unfortunately, this year the budget included some big changes that do have the potential of negatively impacting many of our clients.

The most notable change in the 2024 budget is the proposed increase in the capital gains tax inclusion rate to 66.67%, from 50%, taking effect on June 25, 2024. More precisely this increased inclusion rate impacts individuals who realize more than $250,000 in capital gains annually and affects all capital gains realized within corporations and trusts.

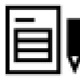
On first blush, many Canadians would most likely jump to the conclusion that this change does not impact them. However, there are many common scenarios that could subject them to this higher tax rate:

- The sale of a family cottage or secondary investment property is very likely to push you into the 66.67% capital gains tax inclusion rate.
- Following the death of a loved one, the Estate could easily crystalize a capital gain above the $250,000 threshold amount when you factor in the value of the non-registered investment accounts and secondary real estate properties, ultimately resulting in a higher tax bill and a lower inheritance.
- Incorporated professionals, like most family doctors, will be subject to the full impact of the higher tax rate (no $250,000 exception to be provided for corporations), putting an even further strain on recruiting new doctors to Canada.

This is not the first time in Canadian history that we have seen changes to the capital gains tax inclusion rates. In 1988 the inclusion rate was increased to 66.67% from 50%, and then in 1990 it was increased further still to 75%. By 2001, the inclusion rate had come full circle back down to 50% and remained at this level until now.

It is still early days and the proposed changes have not yet been ratified into law. The government has not even released the draft legislation for review yet. There are many factors that you need to consider when assessing how these changes impact you personally. We certainly do not encourage clients to prematurely rush and realize gains before June 25th simply to lock in lower tax rates as the benefits of long-term tax deferred growth are still material. However, it would be prudent to have a discussion with your accountant or tax advisor to identify what steps you may want to take.

We've said it before and will repeat ourselves here – we are big believers that all our clients should work with a professional accountant or tax advisor. If you don't currently work with one, we would be happy to make a few recommendations. If you are interested in learning more about these changes, we would be happy to send you additional resources.



We Want to Hear from You

We want our dialogue with you to go beyond our formal portfolio reviews. We continually strive to enhance our services to serve you better. To do that, we would greatly appreciate your feedback.

- Are there specific topics or information you would like covered in our future newsletters?
- Is there interest in in-person workshops around estate planning, inter-generational wealth transfer, philanthropic gifting or ethical investing?
- Do you need help understanding your investment account statements?
- Are there any other areas of our service you'd like to discuss?

Your feedback is a valuable gift to us. Occasionally, you may receive an e-mail survey from TD Wealth which is *anonymous.* We believe you deserve exceptional service, and your honest input is crucial in helping us achieve that goal. If you find anything on the survey that falls short of a 10/10, we encourage you to reach out to us directly. Your insights are our compass for continuous improvement.

Reaching the Team

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