

INVESTMENT FOCUS

Personal Newsletter from Watermark Stone Wealth

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The return of cooler and shorter days reminds us that the end of year is fast approaching. There may be actions to take to support your 2020 tax position, including RESP contributions, tax-loss selling or charitable donations. Call if you require support.

Of the many challenges, Covid-19 has created an environment of rapid change. I continue to work hard to support you in these changing times. During this Thanksgiving season, I extend my thanks for your confidence in my services.

–Doug

The Unprecedented Speed of Change

If there's a common theme to characterize 2020, it is that change can happen at an unprecedented speed. While we experienced the fastest bear market in history in March, this was quickly followed by one of the strongest quarters for equity markets, despite what was happening on the ground. This was largely attributed to the remarkable speed and magnitude by global policymakers to provide stimulus.

The increasing speed of change continues to be driven by technology. Through the pandemic, it has helped to keep economies from completely shutting down. It has changed the way many live, from adapting daily activities of work and play to the confines of our homes.

Covid-19 has also accelerated a trend towards deglobalization, exposing the vulnerabilities of being over dependent on global supply chains. The U.S. has been increasingly vocal about protecting its national interests, reimposing tariffs on Canadian aluminum. In the summer, U.S. Secretary of State Mike Pompeo opened a new chapter in global tensions when he declared that free nations should be concerned with China's Communist Party: "distrust and verify."

Have we seen the worst from the spring economic shutdowns? There has been some optimism as short-term economic data has been "less bad" than expected. Canadian retail sales rebounded over the summer; unemployment figures released were better than anticipated.

However, we are confronted by continuing challenges. For many investors, today's concerns are likely different than those of early spring. The rebound of equity markets after the March lows created a disconnect between equity market performance and the broader economic state. We have yet to defeat the virus, though the race to finding a successful vaccine continues. What will drive economic recovery? How will we acclimate to high levels of national debt? With the prevailing uncertainty, gold has hit all-time highs. South of the border, massive stimulus efforts have pushed down the value of the U.S. dollar. Moreover, containment efforts have been slower than expected, hampered by social and civil unrest. With just weeks until the presidential election, all eyes will be on the U.S. as a change in leadership may be imminent.

During periods of extreme change, it is more important than ever to take advantage of professional advice in managing financial assets. Investing requires shifting gears on a continuous basis, particularly in assessing new situations. Changing market dynamics can mean additional risks, so careful review and monitoring of investments is vital. Balancing portfolio exposure to account for the many risk factors and potential economic outcomes can ensure that investing for the long term remains a profitable strategy. We continue to harness these inevitable changes so that your investments continue to work for you.

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Estate Planning: Looking Beyond the Will

The health-related consequences of Covid-19 have prompted many to contemplate the importance of estate planning. While creating and updating a will is an essential part of preparing for when we are no longer here, an area often overlooked is how things will be managed while we are alive but unable to provide direction.

Without properly documented instructions, there may be the potential for family disputes during stressful times. In some cases, a family may have to apply to the courts or have someone appointed as guardian to manage both personal care and property — a potentially lengthy and costly process. As such, the following should be considered in addition to your will:

Power of Attorney for Personal Care and Property — Do you have a plan in place to support you in the event you are unable to speak for yourself? One of the most important aspects of planning for incapacity is to identify substitute decision makers you trust to make financial and/or healthcare decisions on your behalf. They are often called an “attorney.”¹ Having this document in place generally allows the attorney(s) to make decisions if you cannot act for yourself. Generally, you are able to appoint a different attorney for Power of Attorney for Personal Care and Power of Attorney for Property.

Advanced Directive — What kind of care would you want to receive if you were unable to communicate? Our current crisis has led to the question of whether an individual would want to use a ventilator for life support. In provinces where applicable, this document provides specific medical or lifestyle decisions to clearly



indicate your wishes and provide guidance to your substitute decision maker.

Other Considerations

Beyond a will and Power of Attorney documents, there may be other documentation to consider. Beneficiary designations for registered plans² and beneficiaries of life insurance should be kept updated and revisited from time to time. The arrangement of assets, such as the use of joint ownership with rights of survivorship,³ may also be a consideration as, depending on the circumstances, it may help with the transfer of assets.

Estate planning goes well beyond a will. As estate planning is governed by provincial legislation, it is important to consult local legal and estate planning experts to ensure your will and Power of Attorney documents reflect your intentions.

Notes: 1. The name, terms and conditions of the Power of Attorney document vary by province (e.g. known as a mandatary in Quebec); 2. In Quebec, the designation may have to be done using a will; 3. Not applicable in Quebec.

Year-End Tax-Planning Checklist

It's only autumn, but this is a good time to be thinking about our financial affairs in preparation for the year end. December 31st is the deadline for many tax-related activities. As you consider the opportunities to best position yourself, here are some ideas:

✔ **Capital Gains/Losses:** Consider realizing capital losses to offset realized capital gains for 2020, or take advantage of the carry-back rules to recover taxes paid on taxable capital gains realized in three preceding taxation years. There may also be opportunities to transfer capital losses between spouses. In order to do this, please get in touch well before the end of the year.

✔ **Income Splitting:** There are various ways to split income. For example, you may pay reasonable salaries to spouses for services provided to your self-employed business or private company. You may elect to split eligible pension income with a spouse on your tax return. With interest rates at low levels, income splitting with a spouse may also be achieved by way of a prescribed rate loan. A tax advisor can provide the best options available to you.

✔ **RRSP Contributions:** Why wait until the last moment if you are planning to make Registered Retirement Savings Plan (RRSP) contributions for the 2020 year? Remember, you can contribute until 60 days after the calendar year to impact 2020 taxes.

✔ **RESP Contributions:** If you have a Registered Education Savings Plan (RESP), consider making a contribution before year end. While this won't impact your 2020 taxes, you may benefit from the Canada Education Savings Grant for 2020.

✔ **Charitable Donations:** Make eligible charitable donations before December 31st to benefit your 2020 taxes. Remember that gifting publicly-traded securities with accrued capital gains to a registered charity not only entitles you to a tax receipt for its fair market value, but also eliminates the associated capital gains tax.

✔ **RRSP Conversion:** If you turned 71 this year, make sure to collapse your RRSP. Consider making a final RRSP contribution, as this must be done by year end, not the usual March 1, 2021 deadline.

✔ **Pension Income Tax Credit:** If you're at least 65 years of age and don't have eligible pension income, consider purchasing an annuity or opening a small Registered Retirement Income Fund before year end to claim the federal pension income tax credit. Eligible pension income may also be split with a spouse on a tax return.

Many of these actions require planning, so don't wait until it's too late. For further assistance, please contact us and, as always, seek advice from a tax professional.

How Does Quantitative Easing Affect the Markets?

Given the upward momentum in equity markets after the March lows, many investors have been asking how quantitative easing (QE) has played a role. Here are some answers to your QE questions:

What is QE? In order to support economies, policymakers can engage in fiscal or monetary policy. Fiscal policy refers to government spending and tax policies. Monetary policy is used by central banks to control the supply of money. Traditionally, this has involved changing the key interest rate — i.e., lowering rates reduces the cost of capital and entices businesses and consumers to borrow more, increasing the money supply. However, as interest rates have approached near-zero levels, more unconventional approaches like QE have been required. With QE, the central bank purchases financial assets from financial institutions and issues credit to their reserves, thereby increasing the money supply.

During the 2008/09 financial crisis, the U.S. Federal Reserve began its first foray into QE, purchasing over \$4 trillion of government bonds until 2014. Today, it has expanded QE to include mortgage-backed, corporate and municipal bonds. The Bank of Canada began its first-ever move into QE this past April.

How does QE affect equity markets? There are various reasons why QE is said to be supporting the equity markets. When central banks purchase government and other bonds, yields are pushed down, reducing the return on these safer assets. As such, investors look further along the risk curve, such as to equity markets, in search of greater returns. QE and other stimulus actions have also increased liquidity and the money supply, which may have flowed into equity markets. These actions also provide confidence that central banks will continue to support economies through difficult times. Some market analysts contend that this leads to artificially-inflated asset prices.

What does it mean for your portfolio? In some ways, the actions taken by central banks have changed certain historical assumptions about the financial markets. This may be why there are so many opinions of what



is yet to come. Is inflation imminent? Some argue that stimulus actions have put excess funds into economies, which is inflationary. If the world moves towards deglobalization and supply chains exit China, higher production costs will lead to higher prices. Many central banks also want moderate inflation. Inflation worries may explain the increasing interest in gold and cryptocurrencies.

Yet, when QE ended in 2014, many economists expected to see a substantial rise in inflation. This never occurred and the stock market advanced in the years that followed. It remains unclear exactly what happens to equity markets upon the departure from low-interest rates and easy money from central bank policy. Eventually, economies will need to acclimate to significant debt levels, the consequences of which are yet to be seen.

However, one reason for investors to maintain confidence is that well-constructed portfolios use asset allocation and diversification, not just across different asset classes, but also risk factors, to help mitigate risk. This involves balancing portfolio exposure to account for the ongoing uncertainty and the potential economic outcomes in the near term. Another reason? Being invested. Participation is key to generating returns for the longer term. History has shown that even the worst periods of retrenchment have been followed by times of economic growth. This time is likely no different.

The Continuing Case for Diversification

Uncertainty has always played a common role in the financial markets, but due to Covid-19 the path forward may feel particularly uncertain. In these times, diversification remains an important element of portfolio construction. The chart (right) shows the performance of select asset classes/geographies over the past decade (in C\$). Here are some observations, which provide the case for diversification:

- No single asset class consistently performs at the top over time. A diversified portfolio can give access to the best performing asset classes every year.
- As we have seen with Covid-19, industries, sectors and even entire asset classes can fall out of favour, and sometimes with little warning. Diversification can help to protect from the downturns that may affect asset classes at different times.
- There is often a large gap in performance between the best and worst performing asset class. Diversification helps to smooth out performance returns within a portfolio.

- Markets change, and so does your portfolio. This is why rebalancing on a periodic basis is important, to ensure your portfolio maintains its appropriate strategic asset allocation.

Annual Returns of Key Asset Classes, Best to Worst: 2010 to 2019

2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Canadian Equities 17.61%	U.S. Bonds 10.59%	EM Equities 15.61%	U.S. Equities 41.27%	U.S. Equities 23.93%	U.S. Equities 21.59%	Canadian Equities 21.08%	EM Equities 28.26%	U.S. Bonds 8.92%	U.S. Equities 24.84%
EM Equities 12.67%	Canadian Bonds 9.67%	Int'l Equities 14.72%	Int'l Equities 31.02%	U.S. Bonds 15.39%	U.S. Bonds 20.46%	U.S. Equities 8.09%	Int'l Equities 16.82%	Global Bonds 7.70%	Canadian Equities 22.88%
U.S. Equities 9.06%	Global Bonds 8.26%	U.S. Equities 13.43%	Canadian Equities 12.99%	Canadian Equities 10.55%	Int'l Equities 18.95%	EM Equities 7.34%	U.S. Equities 13.83%	U.S. Equities 4.23%	Int'l Equities 15.85%
Canadian Bonds 6.74%	U.S. Equities 4.64%	Canadian Equities 7.19%	U.S. Bonds 4.60%	Global Bonds 9.65%	Global Bonds 16.15%	Canadian Bonds 1.66%	Canadian Equities 9.10%	Canadian Bonds 1.41%	EM Equities 12.43%
Int'l Equities 2.13%	Canadian Equities -8.71%	Canadian Bonds 3.60%	Global Bonds 3.94%	Canadian Bonds 8.79%	Canadian Bonds 3.52%	U.S. Bonds -0.80%	Canadian Bonds 2.52%	Int'l Equities -6.03%	U.S. Bonds 3.37%
U.S. Bonds 1.24%	Int'l Equities -9.97%	Global Bonds 2.01%	EM Equities 3.93%	EM Equities 6.63%	EM Equities 2.04%	Global Bonds -1.45%	Global Bonds 0.34%	EM Equities -6.87%	Canadian Bonds 2.81%
Global Bonds 0.04%	EM Equities -16.40%	U.S. Bonds 2.01%	Canadian Bonds -1.19%	Int'l Equities 3.67%	Canadian Equities -8.32%	Int'l Equities -2.00%	U.S. Bonds -3.18%	Canadian Equities -8.89%	Global Bonds 1.44%

Past performance isn't indicative of future performance. Emerging Markets Equities: MSCI EM GR; Canadian Equities: S&P/TSX Composite TR; International Equities: MSCI EAFE; Canadian Bonds: FTSE TMX Canada Universe Bond Index; U.S. Equities: S&P 500 TR; Global Bonds: Barclays Global Aggregate Bond TR; U.S. Bonds: Barclays US Aggregate Bond TR. In Canadian dollars, unhedged.

The Role of the Executor: A Large One

Have you been named as an executor/estate representative/liquidator/estate trustee of someone's estate? If so, you have been entrusted with a very important role.

Most people are honoured to be named as executor, as it signifies respect and trust in their abilities. However, many people don't realize just how much responsibility is involved. As such, here are a few things to keep in mind:

It is time consuming. Settling an estate generally takes about 18 months on average, but some estates may take several years to settle depending on complexity. The scope of an executor's duties may be wide, including arranging the funeral, finding, itemizing or even managing the estate's assets, applying for probate (in provinces where applicable), calling financial institutions to notify them of the death, filing income tax returns, liquidating or distributing assets as directed by the will, and more. The role may also involve visits to various financial institutions, as well as meetings with accountants, lawyers and perhaps even creditors and beneficiaries.

There are legal implications. As an executor, you may be held personally liable for any losses caused or errors made as you settle the estate. As an example, if the estate's assets were distributed prior to the estate's taxes being paid, the executor could be held personally liable for the balance of taxes due.

You may be required to manage conflict. Even within the most harmonious of families, conflicts can emerge as an estate is settled. Often there are conflicts between executors and beneficiaries. Decisions will need to be made and the involved parties may not always agree, even if the executor acts without bias.



Your place of residence may have consequences. There may be complications to the estate if you, as executor, and the estate reside in different jurisdictions. For example, if you were appointed as the executor when living in Canada, but you decided to become a non-resident of Canada, the estate may also be considered a non-resident of Canada. This could potentially trigger negative tax consequences. Executors residing in a different province than the jurisdiction of the estate may also face challenges such as being required to post an estate administration bond. Even if you do live in the same province, but are located in a different city, you may be required to travel distances to meet with financial institutions or settle assets.

Seek Advice

If you have been appointed as an executor and want to learn more, or if you would like an introduction to an estate planning specialist to discuss your situation, please get in touch.

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