THE KELLAND BULLETIN

Left to Right: Tyler, Talea, Domenic, Nicole, Sarah, Cassie, Alex, Emily, Rob, Aggie, Natalie, Sara, Adam, Angelo, Britt, Luke

MARKET RETURNS

Year to date, in the first 1/3 of 2024, the TSX is up 4.35%, the Dow Jones Industrial Average (the DOW) is up 1.46% and the tech heavy NASDAQ Index, in the U.S., is up 2.93%. GICs year to date are up 1.67% based on a 5.00% annualized return. Our daily interest savings account continues to pay 4.75 – 4.90% on an annual basis. From an investors perspective it is nice to see the fixed income side of the ledger offering better returns versus the 2010-2022.

DIVERGING ECONOMIES

Economic data from March and published in April shows diverging economies between the U.S. and Canada. Canada's unemployment rate grew to 6.1% while inflation declined to 2.80%. GDP and productivity levels in Canada are also weaker than the U.S..

In the U.S. unemployment sits at 3.80% and inflation remains above 3.0%. Inflation in the U.S. remains higher than their central bank desires. Interest rate declines in the U.S. have been delayed and will likely be fewer in number and shallower in nature due to a stronger economy and higher inflation. Inflation peaked in both countries in 2022.

Canada based on its economic data is poised to reduce interest rates and may do so as early as June. The risks to decreasing interest rates before the U.S., is potential weakness to our currency. The benefits are stimulating our economy, as inflation appears to be tamed and economic growth is not as strong as is desired.

MARKET VALUATIONS

As we have been saying, the U.S. market by almost all metrics is fully valued by historical standards. That said, the pendulum of both emotions and valuation can remain elevated in the too positive or too negative camp (direction) for extended periods of time (months, and quarters). In the end, valuation always rights (the pendulum) itself. We much like the U.S. market, but are cautious on valuation, as the price you pay for a business matters.

CANADIAN BANKS – UNDERVALUED, COUPLED WITH EXCELLENT LONG TERM PERFORMANCE

Canadian banks are trading at attractive valuations relative to the broader Canadian market. Bank of Montreal's analysts suggests they are at a 28% discount to the broader market, and remain 14% below all-time highs.

The big 6 Canadian banks have historically delivered strong performance over the "long term", as investors have rewarded their soundness and conservative practices. Going back to December 31, 1987 the TSX bank index has not only outperformed the broader TSX Index, but also, and more impressively the MSCI World Index (in CAD$). Since December 31, 1987 (35 years) the TSX bank index has averaged 11.57% per annum. Over the same time period the TSX Index has averaged 7.79% annually, and the MSCI World Index 8.14% per annum.

We are strong advocates of the Canadian banks as core holdings. As well, just for holding the big 6 banks you will earn an annual dividend yield (which typically increases yearly) of between 3.80% - 6.57% depending upon the bank.

CAPITAL GAINS NEW INCLUSION RATE - PROPOSED CHANGES

In Canada, a taxpayer is required to include 1/2 of their capital gains in computing their income for tax purposes. The 1/2 capital gains inclusion is applied to both Canadian individual taxpayers and Canadian Corporations.

The 2024 Federal Budget proposes the changes noted below to the capital gains inclusion rate on or after June 25, 2024. The illustrations provided are intended to highlight the potential impact and are not to be construed as tax advice. We encourage clients to reach out to their tax accountants for more information. As always, feel free to reach out to our team for more information.

Individuals – The capital gains rate increases from 1/2 to 2/3 on capital gains realized in the year where capital gains exceed a $250,000 threshold. The example *assumes client(s) are at top marginal rate – 53.53%.*

Individual - Sole Non-Registered

Cpital Gain	Current Rules	Proposed Rules	Additional Taxes Owing	New Blended Rate	Additional % Tax Rate Increase
$ 250,000	$ 66,913	$ 66,913	$ -	26.77%	0.00%
$ 500,000	$ 133,825	$ 156,129	$ 22,304	31.23%	4.46%
$1,000,000	$ 267,650	$ 334,563	$ 66,913	33.46%	6.69%

Individual - Joint Non-Registered

Cpital Gain	Current Rules	Proposed Rules	Additional Taxes Owing	New Blended Rate	Additional % Tax Rate Increase
$ 250,000	$ 66,913	$ 66,913	$ -	26.77%	0.00%
$ 500,000	$ 133,825	$ 133,825	$ -	26.77%	0.00%
$1,000,000	$ 267,650	$ 312,258	$ 44,608	31.23%	4.46%

Corporations and Trust – The capital gains inclusion rate increases from 1/2 to 2/3 for all capital gains (there is no $250,000 threshold applied).

	Current Rules	Proposed Rules	Current Rules	Proposed Rules	Current Rules	Proposed Rules
Canadian Corporation (Ontario)						
Capital Gain Triggered	$ 250,000	$ 250,000	$ 500,000	$ 500,000	$ 1,000,000	$ 1,000,000
Capital Gain Inclusion Rate	50.00%	66.67%	50.00%	66.67%	50.00%	66.67%
Total Taxable Capital Gain	$ 125,000	$ 166,675	$ 250,000	$ 333,350	$ 500,000	$ 666,700
Corporate Tax Rate Paid	50.17%	50.17%	50.17%	50.17%	50.17%	50.17%
Corporate Income Taxes Paid	$ 62,713	$ 83,621	$ 125,425	$ 167,242	$ 250,850	$ 334,483
NERDTOH collected - 30.67%	$ (38,338)	$ (51,119)	$ (76,675)	$ (102,238)	$ (153,350)	$ (204,477)
Corporate Income Tax Paid After Dividend Refund	$ 24,375	$ 32,502	$ 48,750	$ 66,003	$ 97,500	$ 130,007
Total Cash Available to Distribute	$ 225,625	$ 217,498	$ 451,250	$ 434,997	$ 902,500	$ 869,994
Personal Income Tax (Ontario) - All Cash Paid						
Tax-Free Capital Dividend	$ 125,000	$ 83,325	$ 250,000	$ 166,650	$ 500,000	$ 333,300
Dividend (Non-Eligible)	$ 100,625	$ 134,173	$ 201,250	$ 268,347	$ 402,500	$ 536,694
Marginal Tax Rate on Taxable Dividend	47.74%	47.74%	47.74%	47.74%	47.74%	47.74%
Personal Income Taxes Paid	$ 48,038	$ 64,054	$ 96,077	$ 128,109	$ 192,154	$ 256,217
Total Taxes Paid (Corporate + Personal)	$ 72,413	$ 96,556	$ 144,827	$ 190,112	$ 289,654	$ 386,224
Additional Taxes Owing		**$ 24,143**		**$ 45,285**		**$ 96,570**
Effective Rate	29%	39%	29%	38%	29%	39%

OTHER ITEMS TO CONSIDER

- These budget changes are proposed, not yet enacted.
- During my career I have seen the capital gains inclusion rate vary between 0-75%. A new government could change this rate.
- Capital gains grow tax free until sold (crystalized). If you have a longer term time horizon, allowing these assets to grow and compound tax free over time may be more advantageous.
- The vast majority of our clients will not be affected by these new rates.
- If you do have capital gains in a holding company or corporation, and do plan on taking capital gains this year, or in the next couple of years, it may be beneficial to do so before June 25th.
- Each instance is unique to the client's taxation situation, it is not one size fits all.
- Most investors are not selling their cottages or secondary residences to avoid this new rule by June 25th. The same principal should hold for investors with a longer term investment time frame.
- At ScotiaMcLeod, we "officially" cannot provide taxation advice. Please consult your accountant for how these rules effect your unique circumstance.
- As always, feel free to contact a member of our team. We are here to assist.

SINKING SHIPS AND SOARING STOCKS

Today, the wreck of a ship called the Vasa is housed in a museum in the heart of Stockholm – a reminder about ambition overtaking execution. In 1626, King Gustav II Adolf, driven by a vision of naval dominance, commissioned the construction of a warship that would be the envy of the Baltic Sea. Vasa set sail on its maiden voyage from Stockholm as the city's inhabitants lined the harbor, eager to witness their nation's triumph. Yet, their pride turned to horror as the Vasa sank mere minutes after embarking. We can see this historical episode as a parallel for the pitfalls of modern investing, where the allure of chasing returns, following fads, or investing in meme stocks can lead to a portfolio's downfall. The Vasa's story is a vivid reminder that ambition, unchecked by prudence and without a strong foundation or strategy, can lead to disaster. Key research sheds light on how over-trading, spurred by overconfidence, can significantly erode investment returns – by almost 7% a year. Investors who make spur-of-the-moment decisions based on the latest purported news or trends can destabilize their portfolios. Academic and industry evidence is clear: chasing returns, succumbing to investment fads, or getting swept up in the frenzy of meme stocks can be perilous. It serves as a vivid reminder that in seeking financial rewards, balance and stability are key. The appeal of quick profits, especially from trending stocks or speculative ventures, can lead to portfolio decisions that mirror the bad decisions which proved fatal for the Vasa. Investors can draw several key lessons from the Vasa's demise. Diversification: Diversification spreads risk and can prevent a portfolio from sinking under the weight of a single failed investment. The value of caution: investors should take note and resist making last-minute changes from well-thought out plans, especially during times of exceptional market exuberance, and particularly when it comes to more high-risk, speculative assets. Foundation before innovation: innovations in investing, such as new financial products or emerging sectors, should be approached with a solid understanding of their foundation and risks. Learning from mistakes: investors, too, should learn from their mistakes and the missteps of others, using these lessons to build more resilient strategies.

REALISTIC RETURNS

Numerous online financial content creators claim that stocks can be expected to return an average of 10 to 12 per cent a year. This belief is misguided, and can lead to some questionable advice. Before debunking it, it's important to understand the origin of the idea that stocks return 10 to 12 percent. For the 20 years ending December 2023, the S&P 500 returned 9.69 per cent. An important point is that you can't buy groceries with nominal returns; we need to look at real returns. Take the 15 years ending April, 1985, as an example for why this matters: The U.S. stock market returned a nominal annualized 10.85 per cent, but inflation ran at 7.05 per cent. The real return, which is what matters to investors, was tiny. (These were high inflation years). Global real stock returns from 1900 through 2023 were 5.16 per cent annualized. Following this process gives a real expected return of 4.62 per cent, or a nominal 7.24 per cent assuming 2.5 per cent expected inflation – a number clearly much lower than 10 per cent. I don't want to crush the dreams of people banking on 10 per cent returns to meet their goals, but counting on returns that match the best historical period for the best performing stock market is likely to lead to bad long term outcomes.

SUMMARY

From all of us at the Kelland Group, we would like to wish you a great month of May. As always we care, and we are all here to assist you in a professional manner.

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