ODLUM BROWN REPORT

07 2022

ODLUM BROWN
Investing for Generations®

INSIDE THIS ISSUE

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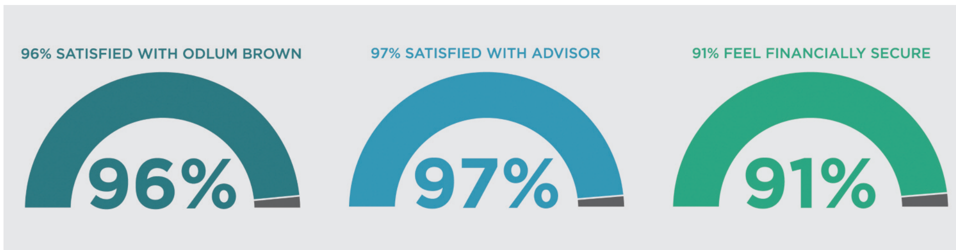
A Message from Our President and CEO: We Are Listening

I'm sure you've heard me say it before, and I'll say it again: at Odlum Brown, building portfolios is our business, but building relationships is our strength. Nothing is more important to us than providing our clients with the best possible experience, and ensuring our relationships with them are strong and lasting.

As we all know, a lot has happened over the past few years – in fact, that may be an understatement! As we all emerge from the pandemic and as Odlum Brown approaches our 100th anniversary as a firm, we felt this was the perfect time to gather input from our clients in a thorough and deliberate way.

In April, we launched the Odlum Brown Client Insights program to do just that. In partnership with an independent consultant, we surveyed a sample of over 12,000 clients to hear what was on their minds, learn about their experiences with our firm and their advisor, and discover what more we could do to meet their needs.

We are very proud of the results we received.



Indeed, many of the themes within the results confirm that what we are doing is working.

Common words our clients used to describe us were *reliable, trustworthy, friendly, knowledgeable* and *professional* – all things we aspire to be. We were also not surprised to learn that, when it came to why newer clients chose to work with Odlum Brown, the personal connection with the advisor and the strength of our firm's brand and reputation rose to the top.

We learned that the most important impact we have on clients and their families is that they now have a clear and meaningful vision for life in retirement. This is wonderful to hear, as guiding clients through significant life transitions is a critical piece of what we do. At the same time, financial success means different things to different people, and we help clients define and achieve a broad range of individual objectives. Survey results indicated that one of the dimensions with the highest importance rating was having an advisor who fully understands the client's financial goals, and we were pleased to also meet or exceed expectations in this area.

Most gratifyingly, we learned that a significant proportion of our clients provided referrals over the last few years – which, as we all know, has been a trying time. We always knew that our business was built on relationships, but for our clients to look to us as a trusted resource when it mattered most truly means the world to us.

These results give us much to celebrate and reinforce the value we offer, yet just as important are the opportunities for improvement. We are committed to not only hearing from our clients, but taking action on what they tell us.

We learned that there is strong value for clients in the current communications and meeting opportunities we offer, and those will continue. At the same time, client needs are evolving with respect to how the client experience is delivered. Virtual is here to stay, and based on these results we will explore ways to offer the most effective, flexible solutions going forward.

We also gained some useful insights into demographic differences in the way clients want to connect and receive information, as well as the impacts that are most important to them. For a firm that prides ourselves on *investing for generations,* we are excited to delve further into this data.

Continued on next page

 Continued from page 1

Harmony Arts Festival
July 29 – August 7, 2022
West Vancouver, BC

We are pleased to return as the Presenting Sponsor of the Harmony Arts Festival, a celebration of the arts in our community. The Festival is one of the North Shore's most popular community events, taking place in a spectacular setting along West Vancouver's waterfront.

With something for everyone, the Festival schedule includes visual art exhibits, dining experiences and free outdoor live performances. Most events are free to the public.

Visit harmonyarts.ca for more information.

Odlum Brown VanOpen
August 13 – 21, 2022
West Vancouver, BC

Odlum Brown is proud to be the Title Partner of the Odlum Brown VanOpen, the largest and most celebrated men's and women's professional tennis tournament in Western Canada and the Pacific Northwest.

After a two-year hiatus, the tournament returns this year bigger and better than ever. Now a combined ATP Challenger Tour 125 and WTA 125 event, this year's event at Hollyburn Country Club is sure to draw top talent from around the world.

For more information, visit vanopen.com.

The meaningful feedback gathered from the Odlum Brown Client Insights program will lay the foundation for our firm's strategic initiatives over the next several years, as we strive to meet our clients' needs.

If you are a client who received and participated in the survey – my sincerest thanks. Your input is so valuable, and as a token of appreciation we have made a special donation to the BC Children's Hospital Foundation on behalf of everyone who responded.

If you didn't get the chance to participate – we still want to hear from you. Your Odlum Brown Investment Advisor or Portfolio Manager is always a phone call or email away, and would love to learn more about your experience as a client.

At Odlum Brown, clients come first – always. For nearly 100 years, that commitment has not wavered, and as we envision the future of our great firm, we know it never will. Thank you for partnering with us on your journey to achieve your financial goals.

DEBRA DOUCETTE
President and Chief Executive Officer

The Sugar Crash Will Pass

Stocks have dropped meaningfully due to the rise in interest rates and the possibility of an economic recession. For the year through to mid-June, the Canadian and U.S. equity benchmarks declined 6.5% and 17.8%, respectively. Similarly, the Odlum Brown Model Portfolio fell by 8.4%.

COMPOUND ANNUAL RETURNS* (Including reinvested dividends, as of June 15, 2022)

	YTD	1 YEAR	3 YEAR	5 YEAR	10 YEAR	20 YEAR	INCEPTION**
Odlum Brown Model Portfolio[1]	-8.4%	2.3%	10.2%	8.6%	13.0%	11.2%	14.0%
S&P/TSX Total Return Index	-6.5%	-0.4%	9.6%	8.5%	8.7%	8.0%	8.5%
S&P 500 Total Return Index ($CDN)	-17.8%	-3.7%	10.1%	10.7%	15.8%	8.0%	9.8%

* Except for YTD period. ** December 15, 1994.

While it's natural to consider exiting the market when headlines are scary and stocks are dropping, acting on that instinct is why the average investor tends to underperform. Humans are emotionally wired to buy high and sell low. Successful investors appreciate those tendencies and resist the urge to act on them.

Our excellent long-term record was not achieved by market timing. Rather, it was accomplished by accepting market volatility and remaining invested though good times and bad. We are thoughtful about the quality of the businesses we own and the price we pay for them. That discipline means we typically don't keep pace with market averages in roaring bull markets, but we make up for it when times get tough. Over the last 28 years, we have underperformed the S&P/TSX Total Return Index by an average of 0.4 percentage points during up months and outperformed by an average of 1.7 percentage points in months when the market fell. By losing less in tough times, we have more money to grow and compound during good times.

The latest downdraft in stock prices was triggered by the U.S. Federal Reserve's surprise 75-basis-point increase in administered interest rates on June 15. The hefty increase is warranted by the continued intensification of inflationary pressures; the U.S. Consumer Price Index (CPI) hit 8.6% year over year in May. For context, Canada's May CPI was 7.7%, year over year.

The media has amplified the significance of the big rise by highlighting that the last time interest rates rose by this much was 28 years ago, in November 1994. The following month, Mexico experienced a currency crisis, and Orange County, California filed for bankruptcy protection. The sudden change in interest rates no doubt influenced those events, and it's quite possible that the recent rapid escalation in borrowing costs will cause another financial incident or two.

While that sounds threatening, consider that stocks are typically closer to their lows when bad things are happening, which can create opportunities for investors. Indeed, that was the case in 1994. We established the OB Model Portfolio on December 15, 1994, and the timing proved to be outstanding.

Over the following five years, the portfolio compounded at an annual rate of nearly 21%. The world has greater challenges today, and equity valuations are not as attractive as they were back then, so it's unrealistic to expect super-sized performance over the next five years, but respectable high single-digit returns are quite likely.

The pandemic has caused tremendous dislocations in the world economy, and the war in Ukraine is adding to those disturbances. The unprecedented government and central bank stimulus saved the world from a depression, but also exaggerated a lot of trends, both good and bad. The economic and stock market recoveries were outstanding, but they have been accompanied by terrible and unwanted inflation. Investors don't know whether they are coming or going due to all the economic crosscurrents, extreme volatility, and intense debate and uncertainty in the media regarding where the world is headed.

Stepping back from the confusion and considering the evolution of events during the pandemic, one can appreciate how investors have been whipsawed by their emotions. Fears in the early days of lockdowns made investors overly pessimistic. Likewise, exuberance during the reopening recovery was overdone. We believe the fear of persistent inflation and higher interest rates will prove unwarranted as well.

When the world shut down, everyone expected economic chaos: soaring unemployment, collapsing incomes, falling home prices, rising loan defaults and bankruptcies. Instead, we saw rapid economic and stock market recoveries thanks to unprecedented fiscal and monetary stimulus: incomes rose, consumer spending accelerated, house prices soared, default rates stayed low and businesses survived. It all makes sense with hindsight. But the authorities overstimulated the economy and induced an economic sugar rush. It wasn't sustainable because it fueled inflation. That, too, makes sense with hindsight.

The world is now experiencing an economic sugar crash, as the authorities withdraw stimulus to correct their excesses and get inflation under control. Stocks are leading indicators, and their current funk is clearly telegraphing slower economic growth and weaker corporate profits. A recession is possible and likely probable.

Inflation is a lagging indicator, and it will fall as the economy slows. Inventories are rising rapidly on the goods side of the economy, where the early and greatest inflationary pressures exist. Bloated inventories mean that price discounts will likely follow. Service sector inflation has heated up, too, as economies have opened up, but we think inflationary pressures there will be fleeting. With inflation-adjusted incomes falling, savings rates declining below pre-pandemic levels, credit card balances soaring and the cost of debt rising, consumers can't sustain spending at current levels.

Sugar rushes and subsequent crashes don't last. Odds are good that inflation will abate and the economy will stabilize. Investors were too exuberant during the recovery, and they will probably be too pessimistic as the economy slows. It's obvious, looking back, that many stocks were bid too high during the good times, and it's quite likely that many of today's stock prices will look like bargains in three to five years.

We are confident that the quality businesses we own will survive and ultimately thrive.

MURRAY LEITH, CFA
Executive Vice President and Director, Investment Research
@murrayleith

[1] The Odlum Brown Model Portfolio is an all-equity portfolio that was established by the Odlum Brown Equity Research Department on December 15, 1994, with a hypothetical investment of $250,000. It showcases how we believe individual security recommendations may be used within the context of a client portfolio. The Model also provides a basis with which to measure the quality of our advice and the effectiveness of our disciplined investment strategy. Trades are made using the closing price on the day a change is announced. Performance figures do not include any allowance for fees. Past performance is not indicative of future performance.

Planning to Keep a Family Vacation Home After You're Gone

After you've built special family memories in a vacation home, it's easy to take for granted that it will continue being enjoyed by your family even after you're gone. Without advance planning, however, those cottage dreams may not survive your passing. Here are a few considerations to help when planning what will happen to your family vacation home after you're gone.

Talking with your family

Before you begin planning, it's worth having an honest conversation with your family to discover if they share your dreams to keep the property in the family. Perhaps they don't anticipate enjoying it as much if you're no longer around, or they may be concerned with other priorities such as paying down debt, growing a business or funding children's education. They may even worry about family squabbles over how time is allocated or costs are shared, once you're no longer at the centre of such decisions.

How will taxes be paid?

It is important to consider when or if taxes will be due, and, if so, how those would be paid. Real estate is subject to capital gains taxes upon death unless a principal residence exemption (PRE)[1] or a tax-deferred rollover (e.g., to your spouse), is available and claimed. The current capital gain inclusion rate is 50% of the gain, which is the taxable portion. Note that transferring a property to joint names with someone other than your spouse is usually considered a disposition at fair market value (FMV), which can accelerate the timing of capital gains before your death.

Common planning strategies for a family vacation home

Before taking any action, it's important to consider planning strategies such as the ones below with your estate and tax planning professionals. For example:

Continued on next page

- **Leaving the property to family as a bequest in your will –** The primary benefits of this option are the deferral of taxation until your passing, the possibility of claiming the PRE for an extended period and maintaining control of the property up until that time. Furthermore, you could bequeath the property to a testamentary trust through your will, prolonging your control over the property posthumously while allowing for its use by your selected beneficiaries.

  The primary drawbacks of such a plan include the application of probate on the FMV of the property at the time of death (up to 1.4% in BC) and the tax liability assessed upon the estate for any capital gains taxes arising on the deemed disposition. If there is insufficient liquidity within the estate, the property itself may need to be disposed of to pay the resulting tax.

- **Transferring the property before passing –** This strategy may result in a number of benefits, including a potential reduction in capital gains tax as the future growth is taxable in another individual's hands, or the potential for the transferee to claim their own PRE. Transferring early may also allow for a disposition over time which may ultimately reduce tax – capital gains on a disposition of property can be recognized over a period of up to five years if the proceeds are received equally over the same period of time. This can prevent the capital gain from being taxed at a higher marginal rate. Lastly, probate fees would be avoided.

  Drawbacks to transferring early include the loss of control over the property, the potential for the property to compose a portion of marital assets in the event of a transferee's relationship breakdown and the application of property transfer tax assessed on the FMV, depending on the jurisdiction in which the property is located.[2]

  Careful consideration must also be given to the form of transfer – gifting versus selling. Where a property is gifted to a child or other non-arm's-length individual, the transferor is deemed to have received FMV proceeds and must pay capital gains tax thereon. The transferee is then deemed to have an adjusted cost basis in the property at that FMV, ensuring that any future capital gains tax will only be based on future growth in value. However, where the property is sold for anything other than FMV, the transferor is still deemed to have received FMV proceeds, while the transferee is deemed to have an adjusted cost basis equal to whatever amount they actually paid. This results in double taxation for the family as a whole.

- **Using a co-ownership agreement to outline expectations –** Creating a co-ownership agreement could help alleviate future disputes and promote family harmony. For example, the agreement could clarify who pays future upkeep and renovation costs, how rental income will be allocated, who can occupy the home for which periods, how future disputes will be managed and/or what restrictions might be placed to prevent selling or encumbering the property, such as stipulating that certain persons must consent to a sale or mortgage.

- **Using insurance as part of your strategy –** An insurance specialist can help determine whether life insurance is appropriate for your planning goals. For example, they can help determine if the liquidity in your estate will be sufficient to cover the estimated capital gains taxes and other obligations arising after your death and, if not, recommend a life insurance solution to enhance that liquidity. Or, if you plan to transfer property before death, they can suggest solutions to build additional wealth that could be used to cover later costs, such as maintenance or renovations, so that the property can remain in the family.

  Insurance may also be appropriate to help provide an 'equalization payment' if children or grandchildren will disproportionately share in the vacation property. In each of these scenarios, life insurance death benefits can be paid tax-free.

If you would like more information on the insurance options available through Odlum Brown Financial Services Limited, contact us through your Odlum Brown Investment Advisor or Portfolio Manager.

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Tax and Estate Planner
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[1] The PRE is an exemption on the capital gains tax arising on the disposition, deemed or otherwise, of real estate that has been 'ordinarily inhabited' in any given year of ownership by the owner or the owner's children or grandchildren. While 'ordinarily inhabited' is not defined by the Income Tax Act, the courts have allowed relatively short periods of time to qualify, so long as there is some regularity to it. Only one PRE can be claimed for any particular year.

[2] Property transfer taxes apply in varying rates in a number of provincial and territorial jurisdictions across Canada. In BC, the general property transfer tax rate is 1% of the FMV up to and including $200,000; 2% of the FMV greater than $200,000 and up to and including $2,000,000; and 3% of the FMV greater than $2,000,000.