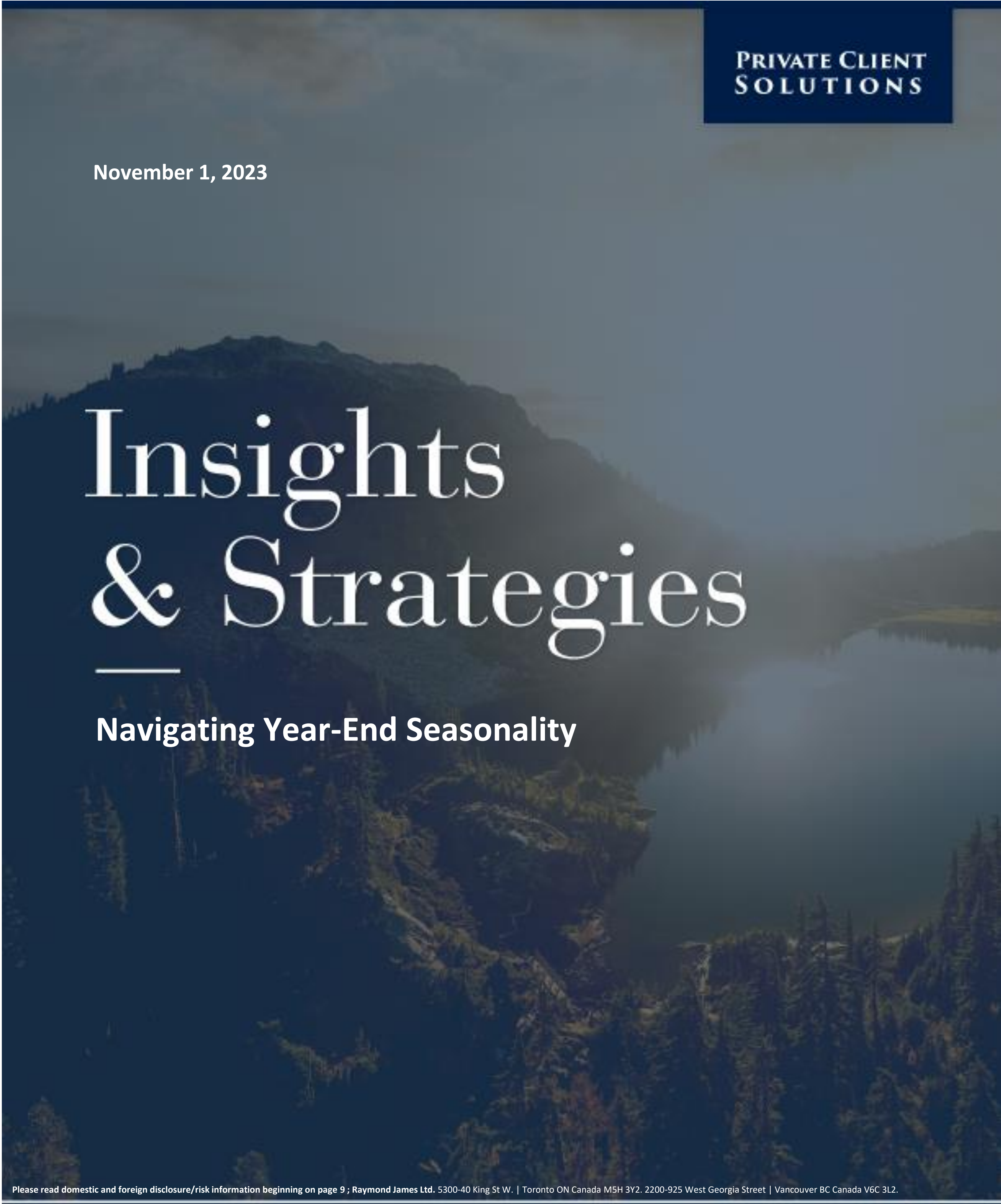


PRIVATE CLIENT SOLUTIONS

November 1, 2023

Insights & Strategies

Navigating Year-End Seasonality

RAYMOND JAMES®

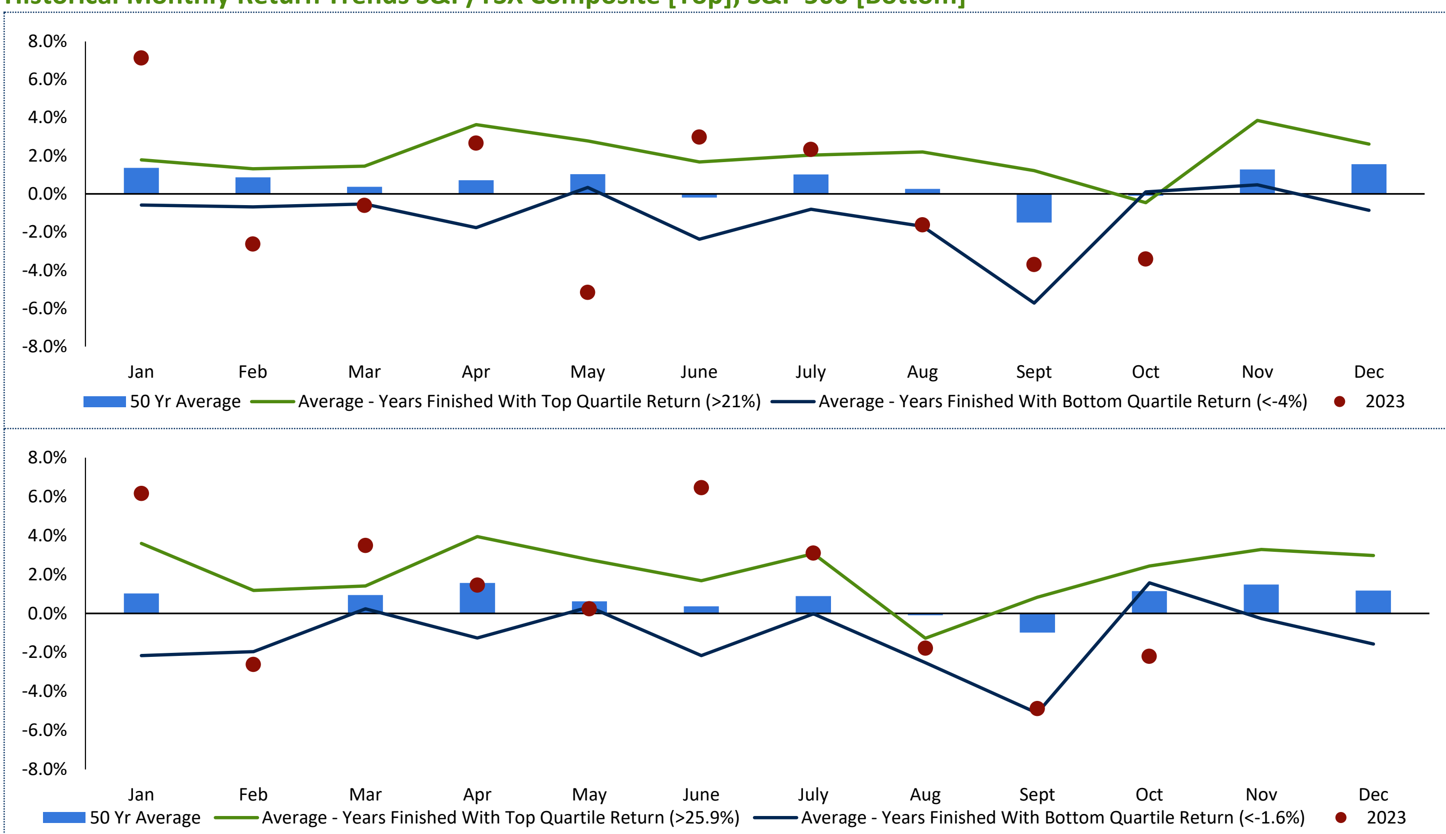
Inside This Issue:

Navigating Year-End Seasonality

Stock market seasonality refers to the patterns in price movements that occur predictably at certain times of the year. Towards the end of the calendar year, well-known trends, such as tax-loss-selling and the Santa Claus rally, always draw public attention. These trends can act as headwinds or tailwinds, or just add noise to an already uncertain market. Looking at historical data can give us clues about why these patterns occur and what they might mean in the current environment.

The graphs below illustrate the average monthly returns of the S&P/TSX Composite (TSX) and S&P 500 (SPX) over the last 50 years. The blue market return bars, reveal that on average, September is the most negative month in both Canada and the U.S. This seasonality is influenced, in part, by tax loss selling. Although tax loss selling can extend until December 27, money managers, depending on the fiscal year-end of their funds, tend to do these transactions starting as early as September and are finished by mid-December. Next is the "October effect", which suggests that stocks tend to decline during this month, as with the famous 1929 and 1987 market crashes. The 50-year historical data however indicates that this phenomenon is more psychological than factual. Under normal conditions, seasonality tends to improve from this point onward, transitioning from a headwind to a tailwind. Then, as the year draws to completion, historical data suggests above-average returns for both November and December.

Historical Monthly Return Trends S&P/TSX Composite [Top]; S&P 500 [Bottom]



Source: Bloomberg; Raymond James Ltd.; Data as of October 31, 2023.

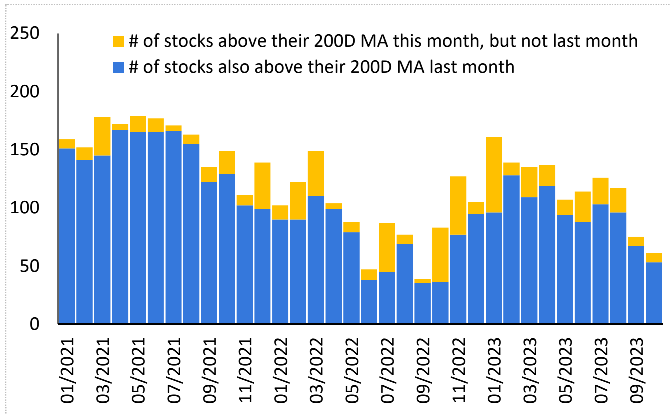
The year-end effect known as the "Santa Claus rally" typically occurs around Christmas and sometimes extends into the first few trading days of the new year. During this period, there is often a surge in stock prices and trading volumes. This surge has been attributed to numerous factors, including tax considerations, fund manager window dressing, positive investor sentiment, holiday optimism, and anticipation of the new year. This time of the year also coincides with when professional money managers are more likely to be on vacation and retail traders, generally being a more optimistic bunch, have more influence on prices.

Implications for Today's Market

The seasonality patterns mentioned above are based on average market conditions, over a long period of time. To provide more insightful analysis for the current environment, those graphs also display the average returns in each month for years that ended with top quartile returns and those that ended with bottom quartile returns. Additionally, we included the monthly returns of 2023 as red dots on the graphs. For both the TSX and SPX, in the first half of this year, the monthly returns were quite erratic, reflecting high market volatility. However, since July, the 2023 monthly returns have more closely aligned with the average trend of years ending in the bottom quartile. This alignment is evident in the three consecutive months of weakening returns and the magnitude of the recent dip. As of the year-to-date returns, both the TSX (+0.1%) and SPX (+10.7%) are still above the bottom quartile cut-offs, especially for the SPX.

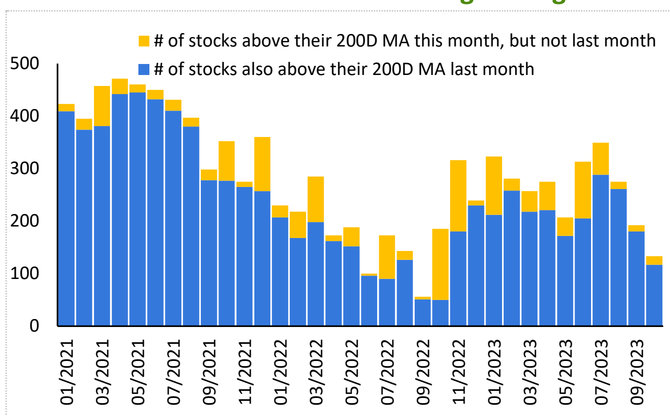
Two aspects of the market that we are watching to see how 2023 will end are corporate earnings and market breadth/strength. For the TSX, year-over-year next-twelve-month earnings per share (YoY NTM EPS) growth is still negative, which means that combining the EPS of all the companies in the index provides a lower forecast of profits than last year at this time. We anticipate ongoing pressure on earnings due to the global economic slowdown and remain cautious about negative surprises and guidance adjustments during the current earnings season. Additionally, market breadth is currently considered weak, as we have more stocks declining than advancing. The number of stocks trading above their 200-day moving average (200D MA), has significantly declined in September and remained weak in October. Concerns about earnings and the fading momentum may indicate lacklustre performance for the remainder of the year and less positive year-end effects. For the SPX, despite its YoY NTM EPS growth turning positive earlier this year, the recent increase seems counterintuitive given rising interest rates and slowing nominal GDP environment. We anticipate that earning expectations might decrease later this year and into 2024, if our expectations of a recession in the U.S. come to pass. The concentrated leadership of the "Magnificent 7" has been widely discussed this year. Similar to the TSX, the market breadth of the SPX is also weak; the number of stocks trading above their 200D MA has significantly declined since August and is still bottoming in October. Despite the SPX generating approximately 11 per cent year-to-date, 10-year U.S. Treasuries touching 5 per cent and growing concerns over a slowing economy might mute potential year-end benefits.

Number of Stocks Above 200D Moving Average - TSX



Source: Bloomberg; Data as of October 30, 2023.

Number of Stocks Above 200D Moving Average - SPX



Source: Bloomberg; Data as of October 30, 2023.

In conclusion, although historical return patterns can offer some insights, the current heightened economic and market uncertainties stemming from macro factors like inflation and rate hikes make it extremely challenging to predict short-term market movements. Attempting to time the market has rarely been a reliable strategy. Therefore, as we approach year-end, the most prudent approach for long-term investors is to ensure that their investment strategy is suited to their objectives and risk tolerance, while tactically taking advantage of tax-planning techniques and opportunities to rebalance their portfolios in consultation with their trusted advisor.

Neil Linsdell, CFA, Head of Investment Strategy
Eve Zhou, Multi-Asset Analyst

Navigating Tax Loss Selling Season

It's that time of year when our attention turns towards tax planning, and having to decide on how we deal with stocks that have weighed on our portfolio returns so far this year. That's right, its tax-loss selling season! Compared to 2022, markets have recovered in many areas since last year's declines, however, the contribution to this year's recovery has been concentrated in the information technology and energy sectors, whereas financials, communication services, and utilities have all weighed on Canadian markets. Concerns around inflation and higher interest rates have contributed to this year's carnage. As the 2023 year-end approaches, we give an overview of tax loss selling, highlight its impacts on markets, provide an example of this strategy, and screen for possible tax loss selling candidates to help clients harvest tax savings from underperforming securities.

Understanding Tax Loss Selling

Tax loss selling, or tax harvesting, is a strategy used by investors to lessen their tax liabilities by offsetting capital gains with capital losses. This involves selling off securities in non-registered accounts that are trading at a loss (i.e., below their original cost) to offset a capital gains tax liability. Should capital gains not be available this year, then the realized capital losses can either be carried back three years to offset gains realized in those years, or carried forward to reduce capital gains in upcoming years. However, this isn't about investors ditching their investment strategy, but about finding a tax-efficient way to stick to their game plan. As such, the proceeds from the sold security can be reinvested in a similar security to maintain one's asset allocation and expected return profile.

Market Impacts

Tax loss selling can have significant impacts on markets, particularly towards the end of the calendar year, possibly leading to increased selling pressure and market volatility. For instance, companies that have seen their stock prices decline throughout the year may experience more selling pressure as investors engage in tax loss selling, potentially leading to further declines. As investors adjust their portfolios for tax optimization purposes, investors may also see increased market volatility as a result.

An Example

Take the following scenario involving an investor with two stocks held in their non-registered account. The investor purchased $10,000 worth of Stock A earlier this year that is now worth $6,000. Should the investor sell Stock A, they would realize a capital loss of $4,000. On the flip side, they've sold Stock B and have realized a gain of $4,000. Without tax loss selling, the $4,000 gain from Stock B would be taxable at the capital gains tax rate. However, if the investor were to sell Stock A and realize the $4,000 loss, then that would offset their $4,000 gain, effectively reducing the capital gain on which they would have been taxed. The investor can then use the $6,000 in proceeds from the sale of Stock A to purchase a different security. It's important to note that the investor cannot simply repurchase Stock A immediately after selling it. Given the tax rules around superficial losses, an investor must wait 30 days before repurchasing the same security where they are claiming a loss. However, the investor might choose to replace Stock A with a different stock or ETF that serves a similar purpose in their portfolio.

Keep in Mind

- *December 27*: If you intend to crystalize a loss for the 2023 tax year, Canadian taxpayers must sell the shares on or before December 27 for settlement on December 29 for both Canadian and US markets.
- *Settlement date*: Sale of securities must settle before the last business day of the calendar year if investors want to use their loss to offset capital gains that year. The settlement date is two business days after the trade for the majority of equities, bonds, mutual funds and ETFs; and one business day for call or put options.
- *Superficial loss rule*: An investor or an affiliate (i.e., spouse, common law partner, corporation controlled by the investor or partner, etc.) must wait 30 days before repurchasing the same security where they are claiming a loss.

Tax Loss Screen

To identify potential tax loss selling candidates, we screen for S&P/TSX Composite index-listed companies that have fallen more than 20% YTD as at October 30. The following table includes this year's basket, which contains 41 names, more than half of which are from the materials and real estate sectors, with the remaining allocations spread across nine other sectors, including utilities, consumer discretionary, industrials, and financials. If history holds, the tax-loss selling basket may see further weakness during selling season (November to mid-December) and subsequently recover into year-end once the selling pressure subsides (mid-December to mid-January). Investors looking to play the bounce may wish to begin accumulating. For those looking to crystalize losses for tax-loss purposes, while maintaining broader sector exposure after selling their position, our Investment Products team has identified an ETF for consideration. By selling the equity and buying similar exposure through an ETF, an investor can harvest their tax loss while staying invested.

Larbi Moumni, CFA
VP, Head of Portfolio Advisory

Tax Loss Securities and ETF Options Name	Ticker	YTD % Price Change
Communication Services		
ETF Option: BMO Global Communications ETF (COMM-CA)		
Cogeco Communications	CCA-CA	-28.1%
Consumer Discretionary		
ETF Option: BMO Global Consumer Discretionary ETF (DISC-CA)		
Pet Valu Holdings	PET-CA	-34.3%
Canada Goose Holdings	GOOS-CA	-35.7%
Park Lawn	PLC-CA	-36.6%
Aritzia	ATZ-CA	-53.9%
Consumer Staples		
ETF Option: iShares S&P/TSX Capped Consumer Staples Index ETF (XST-CA)		
Jamieson Wellness	JWEL-CA	-35.4%
Energy		
ETF Option: iShares S&P/TSX Capped Energy ETF (XEG-CA)		
Precision Drilling	PD-CA	-22.5%
Financials		
ETF Option: iShares S&P/TSX Capped Financials Index ETF (XFN-CA)		
Laurentian Bank of Canada	LB-CA	-20.2%
Trisura Group	TSU-CA	-32.9%
Nuvei	NVEI-CA	-45.5%
Health Care		
ETF Option: iShares Global Healthcare ETF (XHC-CA)		
Tilray Brands	TLRY-CA	-34.6%
Industrials		
ETF Option: BMO S&P/TSX Equal Weight Industrials Index ETF (ZIN-CA)		
Brookfield Business Partners	BBU.UT-CA	-20.4%
Cargojet	CJT-CA	-29.8%
Ballard Power Systems	BLDP-CA	-31.9%
Information Technology		
ETF Option: iShares S&P/TSX Capped Info Tech ETF (XIT-CA)		
Dye & Durham	DND-CA	-48.8%
Materials		
ETF Option: iShares S&P/TSX Capped Materials ETF (XMA-CA)		
Nutrien	NTR-CA	-21.6%
Orla Mining	OLA-CA	-21.9%
Fortuna Silver Mines	FVI-CA	-22.0%
Osisko Mining	OSK-CA	-23.1%
Filo	FIL-CA	-23.6%
First Quantum Minerals	FM-CA	-29.3%
Endeavour Silver	EDR-CA	-29.5%
MAG Silver	MAG-CA	-31.9%
Transcontinental	TCL.A-CA	-32.4%
Canfor	CFP-CA	-33.0%
First Majestic Silver	FR-CA	-33.2%
K92 Mining	KNT-CA	-33.4%
Novagold Resources Inc	NG-CA	-38.1%
Real Estate		
ETF Option: iShares S&P/TSX Capped REIT Index ETF (XRE-CA)		
SmartCentres REIT	SRU.UT-CA	-20.3%
RioCan REIT	REI.UT-CA	-20.7%
First Capital REIT	FCR.UT-CA	-24.2%
Crombie REIT	CRR.UT-CA	-24.6%
StorageVault Canada	SVI-CA	-27.1%
H&R REIT	HR.UT-CA	-28.2%
Allied Properties REIT	AP.UT-CA	-36.0%
NorthWest Healthcare Properties REIT	NWH.UT-CA	-57.6%
Utilities		
ETF Option: iShares S&P/TSX Capped Utilities Index ETF (XUT-CA)		
Capital Power	CPX-CA	-22.2%
Brookfield Infrastructure Partners	BIP.UT-CA	-26.8%
Boralex	BLX-CA	-34.6%
Innergex Renewable Energy	INE-CA	-45.9%
Northland Power	NPI-CA	-46.1%

Source: FactSet; Raymond James Ltd.; Data as of October 30, 2023.

Tax Loss Harvesting with ETFs

Exchange-traded funds are well known for their transparency, low cost, and diversification characteristics; however, they can also be useful vehicles to consider for tax-loss harvesting strategies during this time of the year. While an investor may choose to sell an individual stock and replace it with another stock for tax-loss harvesting purposes, utilizing an ETF instead can offer unique diversification benefits.

Selling Stocks at a Loss and Using ETFs for Tax-Loss Harvesting

As the ETF marketplace continues to grow, the list of available ETF offerings across various sectors and sub-sectors continues to grow as well. This is advantageous from a tax-loss harvesting perspective as it allows investors the ability to replace the exposure of the stock that has been sold within their portfolio with an ETF that can provide more broad-based equity exposure to that sector or industry. Oftentimes investors will look to replace securities they have sold with ETFs that offer a high positive correlation with that security in order to maintain a similar exposure for that portion of the portfolio. With this approach, broad-based passive sector ETFs allow investors to maintain broad-based sector exposure for the security that was sold for tax-loss purposes without triggering the superficial loss rules. As an example, one may consider selling **BMO.TO** at a loss and replace it with the **BMO Equal Weight Canadian Banks ETF (ZEB.TO)**.

Investors may also wish to leverage an entirely different ETF that provides some other exposure or perhaps a simple money market ETF to hold during the waiting period if they are unsure about the underlying exposure of the sold stock in the current environment.

Selling ETFs at a Loss and Using other ETFs for Tax Loss Harvesting

There are times where the security targeted for tax loss harvesting is an *ETF* rather than an individual stock. In these situations, there are a few common scenarios where an investor may benefit from using another ETF for tax-loss harvesting. Below are a few common scenarios where an ETF tax loss harvesting strategy may be leveraged and, under CRA guidelines, should not be considered a “superficial loss”.

Replace an Unhedged Index ETF with its Equivalent Hedged Version (and vice versa)

Investors may wish to move from a hedged ETF to its unhedged option (or vice versa) for tax-loss harvesting purposes. Switching into a hedged (or unhedged ETF) may be considered materially different and may not trigger CRA’s superficial loss rule. Keep in mind, while you will maintain the underlying security exposure, the currency difference could potentially have a meaningful impact on performance.

Replace a Market Cap-Weighted Index ETF with a Similar Equal-Weighted Index ETF (and vice versa)

While two ETFs that track the exact same index will likely be considered identical property, investors may wish to screen for ETFs that track different indexes to avoid CRA categorizing the sale as a superficial loss. A common example would be to sell an ETF at a loss that tracks a market capitalization-weighted index and buy a similar equal-weighted index (or vice versa). By doing so, investors can maintain their desired exposure with a similar alternative while also harvesting capital losses. Below are two ETF pairs that track the Canadian utilities and REIT sectors that an investor may wish to consider for tax loss purposes. The various correlation measures further highlight the strong positive relationship between these two ETF pairs.

Performance	YTD
iShares S&P/TSX Capped REIT Index ETF (XRE.TO)	-9.76%
BMO Equal Weight REITs Index ETF (ZRE.TO)	-10.76%
iShares S&P/TSX Capped Utilities Index ETF (XUT.TO)	-11.59%
BMO Equal Weight Utilities Index ETF (ZUT.TO)	-15.77%

Correlation Matrix	1 Year	3 Year	5 Year	10 Year
XRE.TO/ZRE.TO	0.99	0.99	0.99	0.99
XUT.TO/ZUT.TO	0.95	0.95	0.94	0.93

Source: Capintel, performance as of 19/10/2023, correlation matrix as of 30/09/2023

Replace a Broad Universe Bond Index ETF with a Similar Broad Universe Discount Bond Index ETF

Some investors may use a broad aggregate bond index ETF for their exposure to the Canadian fixed income market. One of the most widely held ETFs in Canada is the **BMO Aggregate Bond Index ETF (ZAG.TO)**. By leveraging a similar discount bond ETF, such as the **BMO Discount Bond Index ETF (ZDB.TO)**, investors can replace **ZAG.TO** at a loss with an ETF that provides similar exposure as it pertains to duration, yield, and credit quality while also avoiding CRA’s superficial loss rule (given both ETFs follow two different indexes). In addition, the approach found in **ZDB.TO** also takes advantage of any current after-tax benefits found in discount bonds.

Performance	YTD
BMO Aggregate Bond Index ETF (ZAG.TO)	-2.08%
BMO Discount Bond Index ETF (ZDB.TO)	-2.22%

Correlation Matrix	1 Year	3 Year	5 Year	N/A
ZAG.TO/ZDB.TO	1.00	1.00	1.00	0.99

Source: Capintel, performance as of 19/10/2023, correlation matrix as of 30/09/2023

Investors should consult a tax specialist before enacting any of these strategies. This report simply serves as a reminder of common ETF tax loss harvesting scenarios.

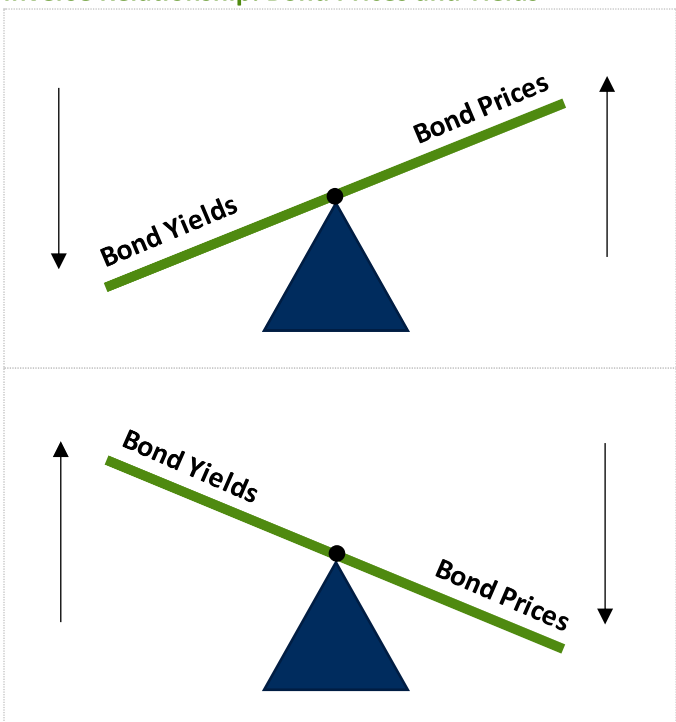
__Luke Kahnert, MBA, CIM__
__Mutual Fund and ETF Specialist__

Prices, Yields and Your Personal Portfolio

When the news reports that equity markets are higher, it's pretty clear they are referring to higher stock prices. However, if the same thing is said about fixed income, you may need to clarify if the news source is referring to prices or yields. In the world of bonds, either can advance. Recently, the US 10-year treasury made headlines by rising above 5 per cent for the first time in 16 years, which may sound great on the surface (and is if you wish to initiate a new position or add to a current one) but it translates to a lower bond price, which would be a negative for existing holders if they wish to sell. Here, we discuss the inverse relationship that prices and yields hold and how tax considerations may alter investment decisions in a fixed income sleeve.

Traditional bonds have fixed coupon payments, so when interest rates rise, the value of those fixed payments are reduced and the market value of the bond will decrease, all else held equal. This describes the inverse relationship that bond prices and bond yields hold. Over the past couple of years, we have witnessed a drastic increase in the overnight rate set by the Bank of Canada (BoC), causing yields on bonds to increase as well. Holding true to this inverse relationship, it is natural that bond prices have fallen. But why must this happen?

Inverse Relationship: Bond Prices and Yields



Source: Raymond James Ltd.

New bonds are being issued by corporations and government entities all the time. When they are brought to market, they are issued with a coupon that, when combined with the face value of par (100), provides the purchaser with a yield that matches today's environment. For example, a five-year high quality corporate bond may come with a coupon (and yield) of 5.35 per cent today. Bonds that were issued in a different yield environment, such as that from just a few years prior, carry much lower coupons that reflect that time. So, if an investor can purchase a new issue security with a 5.35 per cent yield, how can a bond that carried a 1.90 per cent coupon stay attractive to investors? The answer is with a lower price, as the return to maturity is a combination of both the coupon payments and the difference between purchase price and maturity value. In a rising rate environment, outstanding bonds will see their prices fall to make their yields competitive to similar investment alternatives.

Before transacting on this strategy, consider:

- Account Type: many bondholders look to purchase fixed income within tax-sheltered accounts, given that interest is taxed more heavily than capital gains or dividends. If bond positions are held in your RRSP or TFSA or other tax-sheltered account, this strategy would not benefit you.
- Overall Investment Strategy: buy-and-hold investors who plan to maintain a position until maturity may wish to consider if the switch trade would be beneficial to them. Although bond prices may fluctuate month by month on client statements, bonds that successfully reach maturity pay back their principal at that time (the bond returns to par).

Tax considerations are a meaningful factor when calculating personal fixed income returns. Fixed income investors who utilize bonds in their taxable accounts should consider the after-tax yields of their holdings, factoring in the different tax treatments of bond components (principal price change vs interest payments). Doing so could result in a desire to change the fixed income products you are holding, the account type you are holding them in (e.g. inside or outside registered plans), or strategy implementation to maximize after-tax yield. We suggest consulting a tax professional, as they would be best equipped to assist with your unique situation. The general effect, however, is that capital gains are taxed more favourably than income, so targeting coupon-paying bonds that are trading at a discount may be a preferred strategy versus those that have higher coupons (and are trading closer to par).

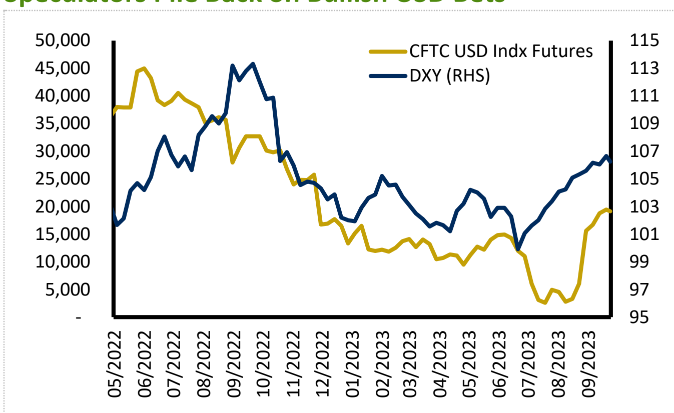
Charlotte Jakubowicz, CMT, CIM
Vice President, Fixed Income and Currencies

Don't Dump the "Buck" Just Yet

As the saying goes, "a rising tide lifts all boats." In this case, the recent rise in U.S. yields has undoubtedly precipitated the strength in the U.S. dollar. Coupled with the belief that the Fed will keep rates "higher for longer", the market's hottest catchphrase these days, expectations have been for the U.S. dollar to drift higher from here as we head into year end.

Higher U.S. yields, particularly on the long-end of the curve, which have been leading to tighter financial conditions, have likely been welcomed by the Fed as it does some of the heavy lifting by raising market borrowing costs. As the U.S. economy continues to show surprising resiliency, particularly on the labour front, the market is expecting the Fed to leave rates well above most of its major peers through next year. This has fueled bullish speculative bets on the U.S. dollar, according to latest data from the Commodity Futures Trading Commission, as relative interest rate spread differentials widen in the USD's favour.

Speculators Pile Back on Bullish USD Bets



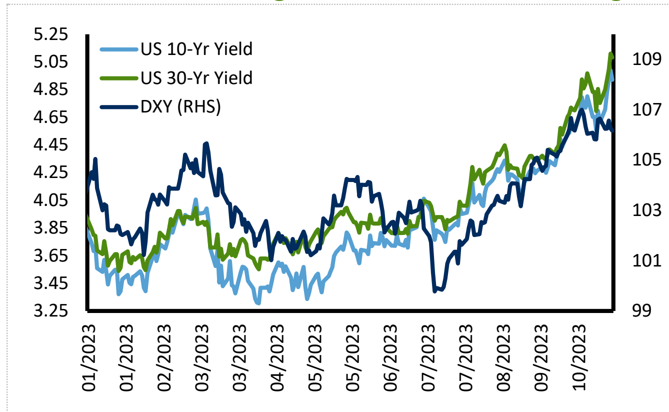
Source: FactSet; Raymond James, Ltd.; Data as of October 20, 2023

Term Premiums, Yields & USD Move in Lockstep

Many have attributed the recent surge in U.S. yields not to higher inflation expectations or even a higher terminal rate for the Fed, but instead the bond market's heightened term premium expectations. In essence, the market is now pricing in an extended period of elevated macro and geopolitical uncertainty, hence the demand for additional yield to compensate for the risks associated with holding longer-term bonds.

Until the time U.S. long-term yields stabilize to some degree or return to a more normalized trading range, we continue to maintain a near-term bullish outlook on the USD at this time. Looking out to next year, there will surely be a resurgence of the "dollar short" theme as attention shifts to the proximity of a potential Fed rate cut. However, given expectations that the Fed will keep rates elevated in light of the apparent strength of the U.S. economy, a scenario which contrasts that of its major peers where economic growth is feeling the weight of tighter monetary policy, the path to a possibly weaker USD will likely be a protracted one.

USD Rallies to 2023 Highs as Bond Yields March Higher



Source: FactSet; Raymond James, Ltd.; Data as of October 20, 2023

Things to Keep in Mind

Many have been waiting for U.S. dollar weakness to ensue once the Fed had a grip on inflation, economic growth was dialed back a few notches, and the market's focus shifted to timing when the Fed would begin to reverse course. Instead, the U.S. economy has shown a surprising willingness to buck the market's most pessimistic forecasts; pushing many Fed officials to keep up with the hawkish rhetoric. This has kept the U.S. dollar supported on many fronts and has led to the DXY U.S. Dollar Index to trade at its highest levels since November 2022, at the time of writing. In addition to the surge in bullish speculative bets on the U.S. dollar, the FX options market has also moved in lockstep with so called risk reversals moving higher, signifying increased demand for upside protection.

The most apparent risk to this bullish dollar narrative is naturally if the U.S. economy stumbles and begins to feel the weight of higher interest rates. There is also the very real possibility that market expectations for Fed rate cuts will be pushed out further.

At the time of writing, the futures market is pricing in nearly 60bps of easing for the Fed by the end of next year. Surprisingly, the market has not priced in a similar breadth of easing for the BoC, which currently stands at roughly 35bps. A possible realignment of BoC rate-cut expectations to align more to the profile of the Fed may provide an added impetus for further upside in USD/CAD over the near term.

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Head Trader, Currencies

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