

Wealth Management & Capital Markets Perspective



Wealth Management
Dominion Securities

For the clients of Grimes Handscomb Asset Management of RBC Dominion Securities | Winter 2025

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Debunking debt disaster

By Atul Bhatia, CFA

Myths may be important to folklore, but they're not helpful in finance. We look at the facts behind some of the common myths surrounding the U.S. national debt.

The U.S. government has an incomprehensible amount of debt. The number is so large—\$35 trillion and counting—that we think it has lost any meaning. We find it incredible that Treasury debt to other U.S. government agencies—if broken out as a standalone—would itself be the third-most indebted nation on Earth, after the U.S. and Japan. Interest on the debt will soon be a trillion-dollar expense, larger than U.S. government spending on veteran benefits, education, and transportation combined.

The magnitude of these numbers has created a cottage industry of doom forecasting, with plenty of hyperbole but little analysis. We think it's helpful to take a look at some of the more pernicious and persistent debt myths.

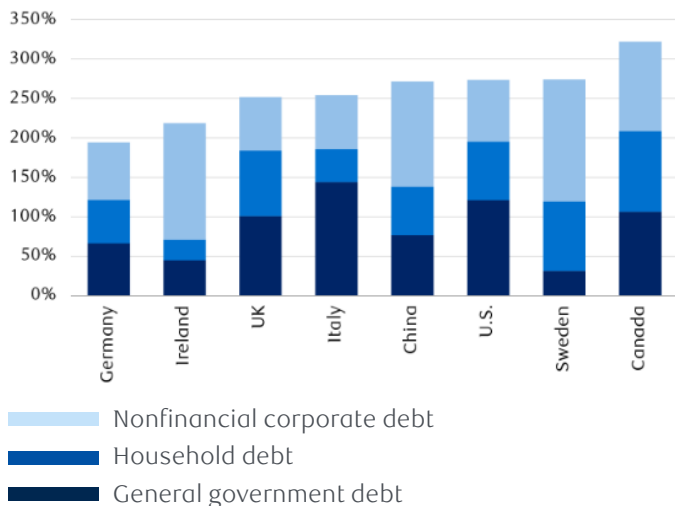
Myth #1: The U.S. economy is dangerously overleveraged

The biggest source of confusion that we see on the U.S. debt is that the number tells us something important. It doesn't—at least not by itself. That's because the government is only a small part of the U.S. economy. What matters for macroeconomic purposes is how much all stakeholders, public and private, have borrowed. And when we layer in household and corporate borrowing, it's apparent that the U.S. debt picture is relatively benign. Canadians, for instance, have leveraged more of their future production than Americans have, and U.S. borrowing is on par with Sweden and the UK.

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Not so very different after all: A broader measure of indebtedness shows the U.S. is fairly typical

Debt as percentage of GDP



Source – International Monetary Fund; percentage of 2022 GDP including bonds, loans, and debt securities

Worrying about government debt is analogous to someone claiming to be debt free because they paid off last month's credit card bill. That's a tough argument if the person still has a mortgage, car loan, or student debt.

Whether at the household or the national level, we're unlikely to reach the right conclusion if we only look at one slice of the pie.

Myth #2: Investors need to prepare for an upcoming U.S. default

Defaults generally occur when borrowers lack the resources to fulfill their promises. That's not likely to happen for the U.S. government, since the Treasury has only promised to give investors a set number of dollars at specified future dates. By happy coincidence, the U.S. government can manufacture dollars at the push of a button. In those circumstances, it would be an active choice for the U.S. to fail to meet its obligations. And given the lifespan of political careers after a sovereign default, we think it's a choice U.S. leadership is not going to make.

The legitimate concern around excess borrowing is not default but inflation. The dollars will be paid as promised, but investors won't be able to buy as much with the proceeds. This is a genuine risk. But it's a much different concern than default. Sovereign defaults are economic catastrophes for most strata of society and tend to precede years of slow growth. Inflation is a serious problem, but it's easier to deal with and usually orders of magnitude less severe than defaults.

Myth #3: Blame the politicians, they're the ones in control

The prevailing narrative is that profligacy created our debts. Whether its crazy spending programs or unfunded tax cuts, debt is just a result of poor political leadership.

To be fair, there's an element of truth to that view. Raising taxes is a political no-go, and there are certain programs that must be funded. Unfortunately, the uncuttable program costs exceed the un-raiseable tax proceeds. That's a structural political issue, and it's likely here to stay for the foreseeable future.

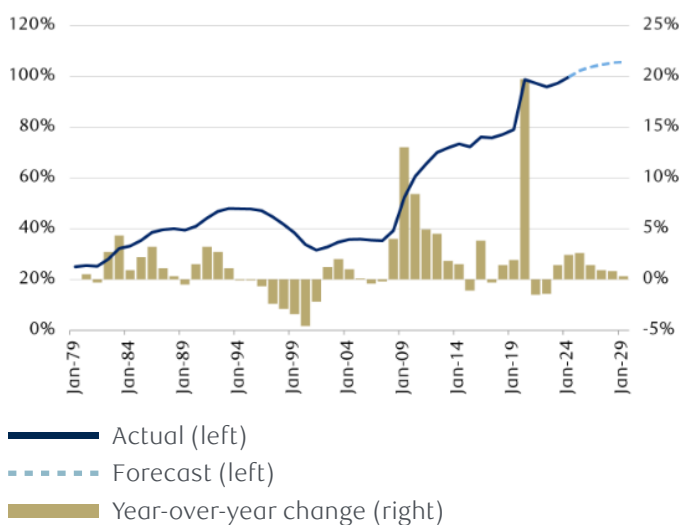
But the reality is the big run-up in government borrowing hasn't been a result of political will. The biggest increases are from the global financial crisis and the pandemic. Without those two events, the U.S. debt-to-GDP ratio would likely be around 40 points lower. It's difficult to argue, in our view, that politicians really had a choice when COVID struck or when the banking system veered toward collapse.

This again highlights the point that the government is only a relatively small part of the economy. If we look back to the last U.S. budget surplus in the 1990s, there were movements to control spending and raise taxes, but a major driver of the surplus was the rise of the internet and the concurrent economic growth.

Debt reduction is less about annual fiscal budget tightening than about avoiding catastrophes and reaping the fruits of innovation.

U.S. debt rise is driven by crisis response

Federal debt held by the public (% of GDP)



Source – RBC Wealth Management, Bloomberg; 2024 and later represents Bloomberg consensus forecast

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Myth #4: Reducing debt will make everything better right away

The old adage to “be careful what you wish for since you just might get it” is particularly apt when it comes to investors and government debt reduction.

The rise in U.S. government debt has been accompanied by solid investment returns across most—if not all—asset classes. Debt-funded government spending played a real role in those results. At its core, debt is about moving demand through time; borrowing adds to today’s demand and repayment reduces today’s demand. If the U.S. were to shift to debt reduction, it’s very likely that economic growth—and by extension corporate earnings—would decline, at least in the short term. Investor optimism around lower debt could help offset some of the effects of slower growth, but there is little empirical support for that idea.

Reality check

Despite the scary and oft-repeated headlines around U.S. debt, we struggle to see what keeps the fear going. Equity markets are at or near all-time highs; borrowing costs across the economy are largely manageable; and economic growth is strong with inflation declining. This has largely been the case for the U.S. for most of the past four decades, a period marked by rising government debt.

Is every dollar of U.S. government spending efficient? Of course not. Could tax policy be made more rational and do a better job of fomenting growth? Absolutely. But it’s a far cry from saying the world is not ideal to saying that we are on the verge of an economic apocalypse. To us, that leap, like much of the discussion on the U.S. debt, is better suited to economic mythology than financial reality.

A year of giving back

This past year, Grimes Handscomb Asset Management gave back to our community in meaningful ways.

Following our participation in the RBC Race for the Kids, we recently volunteered at the Scott Mission, where we helped prepare over 300 meals and holiday gift packs for families in need.

We also rolled up our sleeves and donated blood at Canadian Blood Services to support those requiring urgent medical care.

To close the year, we organized a Christmas toy drive, collecting and donating toys to bring holiday joy to children in our community.

These experiences continue to remind us of the power of collective action and the importance of compassion in our work and lives. We are proud to contribute to a stronger, more caring community.



Administrative corner

Tips to streamline your tax reporting:

- Tax slips will be mailed beginning in early February 2025 until approximately the end of March. In addition to your tax slips, your tax package will include your fee summary, gain/loss report and foreign property summary.
- Please provide the tax package in its entirety to your accountant. If you would like your accountant to receive a duplicate copy of your tax package, please let us know.
- For a more efficient and environmentally friendly option, consider switching to eTax. With electronic delivery, you'll receive your tax package securely via WM Online, saving time and paper. To learn more about this option, please contact us directly.

RBC Dominion Securities – Tax reporting schedule	
RBC DS completes all tax reporting by	March 31, 2025
Important personal tax deadlines	
Personal income tax installments	March 17, 2025 June 16, 2025 September 15, 2025 December 15, 2025
Personal income tax return filing	April 30, 2025
Self-employed income tax return filing	June 16, 2025
Balance owing for taxes payable	April 30, 2025

TFSA and RRSP information

TFSA information	
Maximum annual contribution limits	\$5,000 each year 2009 - 2012 \$5,500 each year 2013 - 2014 \$10,000 for 2015 \$5,500 for 2016 - 2018 \$6,000 for 2019 - 2022 \$6,500 for 2023 \$7,000 for 2024 - 2025
Maximum contribution limit since inception	\$102,000 from 2009-2025, if born in 1991 or earlier and eligible resident of Canada during those years
RRSP information	
RRSP maximum annual deduction limit	18% of the prior year's earned income to a maximum of: \$31,560 for 2024 – deadline March 3, 2025 \$32,490 for 2025 – deadline March 2, 2026

Benchmarks

Equity market 12 month trailing return (for month ending December 31, 2024)	
S&P/TSX composite total return index	21.7%
S&P 500 total return (C\$)	35.7%
S&P 500 total return (U\$)	25.0%
DJIA total return (C\$)	24.8%
DJIA total return (U\$)	15.0%
Nasdaq composite price return (C\$)	39.7%
Nasdaq composite price return (U\$)	28.6%

RBC CM Canadian bond market indices 12-month trailing return (for month ending December 31, 2024)	
Short-term index	5.7%
Intermediate-term	4.6%
Three-month T-Bill (C\$)	5.0%
Three-month T-Bill (U\$)	5.5%



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