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RICHARDSON Wealth

Market Ethos

The latest market insights from Richardson Wealth

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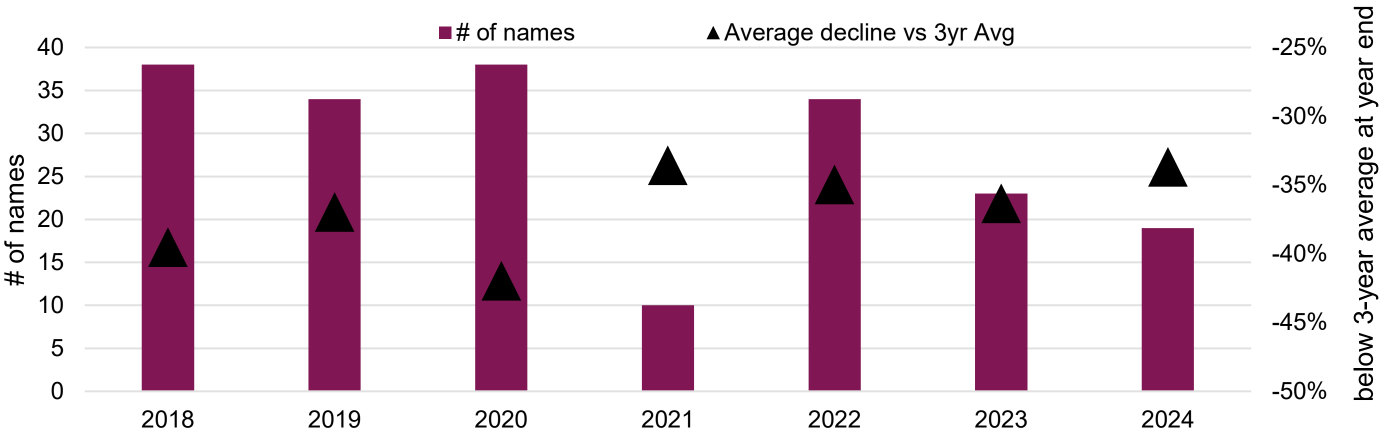
Tax loss selling: Not a lot on the naughty list

Summary: Tax loss selling at this time of year can often lead to weakness in beaten down names that rebound in January as investors re-purchase after waiting the required time. However, this year may be the opposite given how few tax loss candidates are available and the strong gains markets enjoyed over the past couple years. More investors may be waiting to realize those great gains in the new year, pushing out the tax bill another year.

It's that time of year, when people think a little bit more about nice gifts for their loved ones … and tax loss selling. Tax loss selling is common for those who own individual stock positions. Find names that have declined on the year relative to your cost base, or are sitting with an unrealized capital loss, and sell them. Realize the loss to offset gains elsewhere or put it in the bank for future gains. The company sold can perhaps be repurchased after waiting the appropriate amount of time.

So why is this a bizarre year? Well, markets have really enjoyed a strong couple of years which has made tax loss-selling candidates few and far between. We conducted this analysis over the past seven years and looked at how many members of the TSX were down over -20% near year-end compared to their average price over the previous three years (names are included below). Down a lot from your three-year average would certainly make for a good tax loss-selling candidate. Today there are only 19 names that are down over -20% (purple bars in chart), and the decline is not as severe as most other years (black triangle). That is the lowest showing since 2021. This year is really starting to look more and more like 2021.

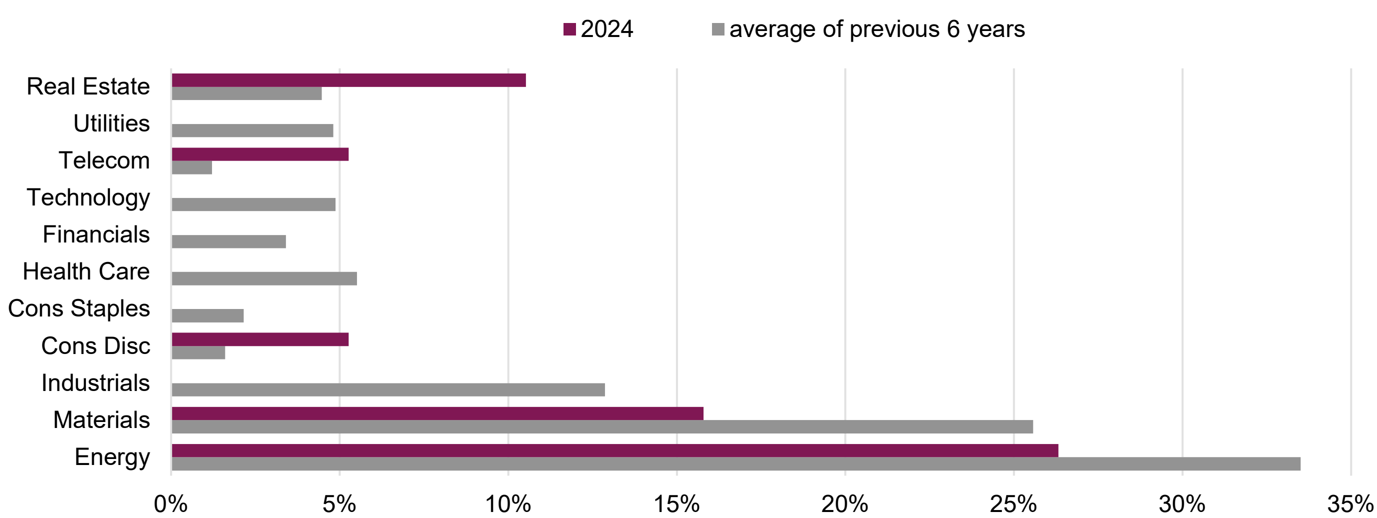
This tax loss season has fewer names and they are not down as much as most other years



Source: Bloomberg, Purpose Investments, Universe TSX Composite

That isn't the only reason this year appears a bit strange. The average size or market capitalization of tax loss candidates tends to be on the smaller size. Over the previous six years, the company size averaged about $3.4 billion. This year, it is a much larger sample with the average size $6.7 billion. BCE and Nutrien are skewing the average much higher than normal. The sector breakdown is very different as well. Tax loss selling candidates tend to be most prevalent in the resource space, energy and materials. This year, fewer names from on the resource side and more from Telecom, Consumer Discretionary and Real Estate.

Sector breakdown of tax loss candidates from Real Estate, Telecom and Consumer Disc vs Resource sectors

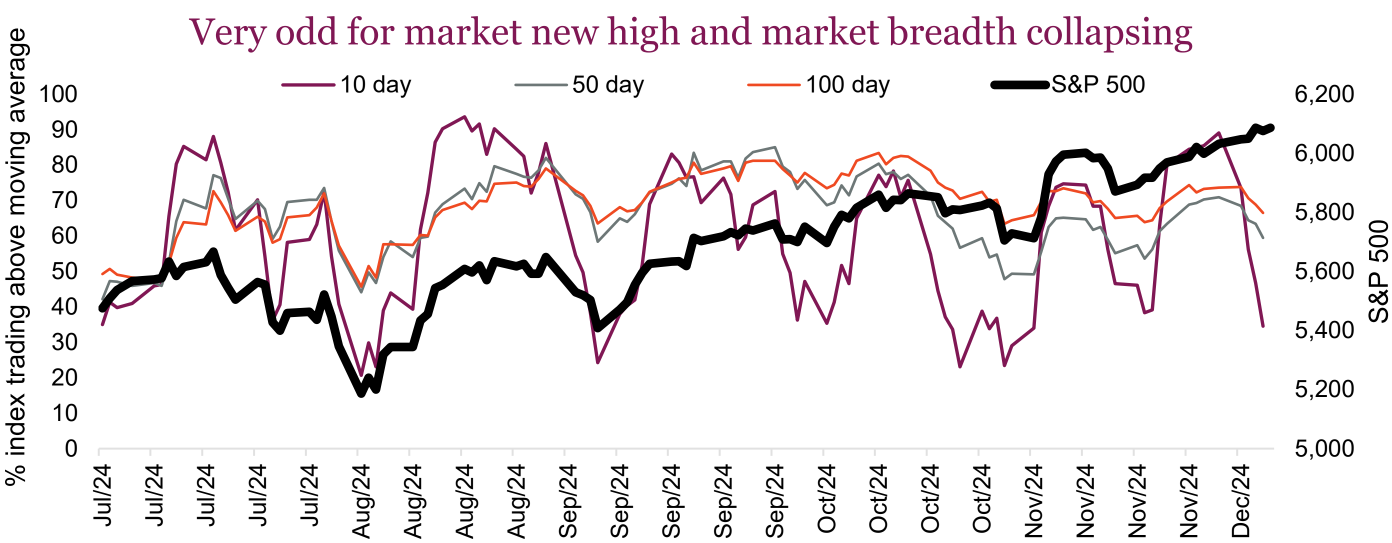


Source: Bloomberg, Purpose Investments, Universe TSX Composite

Tax loss selling does create some added selling pressure on tax loss selling candidate names as the calendar year nears its end. And subsequently, assuming investors re-purchase early in the new year, some buying pressure in January. This contributes to the January effect, that is usually more prevalent for small cap names (as they tend to get pushed around more by buying/selling pressure due to being less liquid).

However, this year may be a unique one. Given markets have largely gone up over the past couple years, tax loss selling just isn't as big a factor this year. In fact, there may be more folks waiting to sell in the new year to lock in some of those great gains over the past year – and by doing so, delay the tax bill until the 2025 taxation year (payable in 2026 for most). This year it may be more about the delay of realizing tax gains vs tax loss selling.

One thing we have learned over the years is that markets often move faster and sooner than one would normally expect. Maybe there are many people coming to the conclusion that January could see selling pressure as investors lock in some of the great gains over the past few years, and finding ways to do it sooner. Selling in tax free accounts, using options/derivatives to effectuate the strategy without triggering the capital gains. Hard to say, but we have started to see an odd development even for the mighty S&P 500. Breadth has been deteriorating rather quickly while the market makes new highs.



Source: Bloomberg, Purpose Investments

Only 34% of the S&P 500 constituents are trading above their 10-day moving average. Now 10 days is not very long but the 20-day is falling fast too and the longer time periods appear to be rolling over. Eroding market breadth with an index sitting at all-time highs is not encouraging. Maybe it is time to think about locking in some of those fantastic gains over the past few years and looking for a better entry point, especially if one develops in January.

Name	Sector	% below 3yr avg
TILRAY BRANDS INC	Health Care	-55%
SSR MINING INC	Materials	-51%
ALGONQUIN POWER & UTILITIES	Utilities	-41%
NORTHWEST HEALTHCARE PROPERT	Real Estate	-40%
BLACKBERRY LTD	Information Technology	-40%
INNERGEX RENEWABLE ENERGY	Utilities	-35%
SUPERIOR PLUS CORP	Utilities	-35%
PAREX RESOURCES INC	Energy	-34%
NORTHLAND POWER INC	Utilities	-34%
BCE INC	Communication Services	-33%
ALLIED PROPERTIES REAL ESTAT	Real Estate	-30%
BIRCHCLIFF ENERGY LTD	Energy	-30%
BRP INC/CA- SUB VOTING	Consumer Discretionary	-29%
VERMILION ENERGY INC	Energy	-28%
NUTRIEN LTD	Materials	-27%
STORAGEVAULT CANADA INC	Real Estate	-26%
BAYTEX ENERGY CORP	Energy	-25%
FIRST QUANTUM MINERALS LTD	Materials	-24%
VEREN INC	Energy	-22%

Source: Bloomberg, as of 6 Dec 2024

Source: Charts are sourced to Bloomberg L.P., Purpose Investments Inc., and Richardson Wealth unless otherwise noted.

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*This report is authored by Craig Basinger, Chief Market Strategist at Purpose Investments Inc. Effective September 1, 2021, Craig Basinger has transitioned to Purpose Investments Inc.