

Trump tax cuts fuel immediate returns

Share prices of companies in VPI Canadian Equity Pool are on the rise

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By Geoff Kirbyson

DONALD Trump will sign a new U.S. tax bill into law in the coming days, but even before it receives the presidential stamp of approval, it has already had an impact on Canadians' portfolios with U.S. holdings.

In a nutshell, the overhaul of the U.S. tax system will reduce the corporate tax rate south of the 49th parallel from 35 per cent to 21 per cent, give other business owners a new 20 per cent reduction on business income and add \$1.5 trillion to the national debt over the next decade. (All figures are in U.S. dollars.)

Companies across the board will feel the impact but the higher an industry's current tax rate, the higher the upcoming savings will be. Companies with a large percentage of their operations in the U.S., which have traditionally had a higher tax rate, will

also see significant savings.

It has been easy to see investors' anticipation as they've been voting with their wallets in the month leading up to this week's votes in the Senate and House of Representatives. Shares in railway Union Pacific and financial services provider Wells Fargo have gone up from \$120 to \$135 and from \$52 to \$60, respectively, in the past couple of weeks.

"The market has been getting excited about this," said David Atkins, portfolio manager of the VPI Canadian Equity Pool, in which shares of both companies are held. "The stock prices of those businesses have been moving higher in anticipation of a tax rate of 21 per cent."

Union Pacific's effective tax rate last year was 37.9 per cent while Wells Fargo paid 29 per cent tax.

"Any lowering of the corporate tax rate for those two businesses drops right down to the bottom line to their

earnings. They'll have more earnings to reinvest in themselves or pay out in higher dividends," Atkins said.

Other beneficiaries could include Canadian companies with a significant footprint south of the border, such as TD Bank and auto parts manufacturer, Magna International, he said.

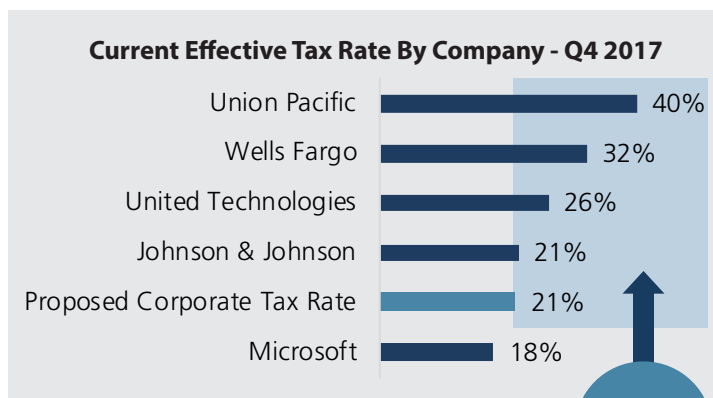
The shares of other U.S. firms with lower corporate tax rates, such as Johnson & Johnson, which paid an 18.6 per cent tax rate last year and is also in the VPI Canadian Equity Pool, have had very little price movement in re-cent weeks.

In a research paper published earlier this month, Sal Guatieri, Toronto-based senior economist at BMO, said the tax cuts will give the U.S. economy a "moderate lift."

"This is a big step forward in passing the largest overhaul of the tax system in three decades," he said.

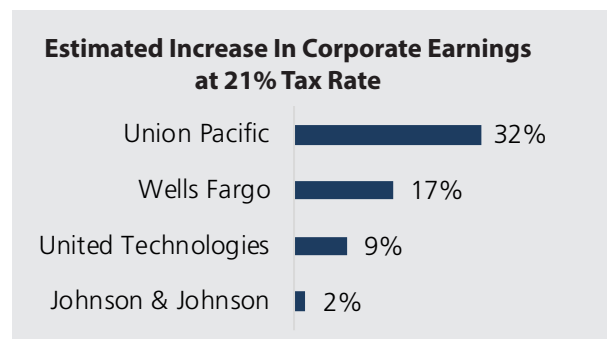
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How the U.S. holdings in the VPI Canadian Equity Pool are affected by new U.S. tax rates



Effective tax rate based on last quarter's financial statements.

Source: S&P Capital IQ, Value Partners Investments Inc.



Earnings growth based on actual reported earnings LTM versus pre-tax earnings LTM with the proposed 21% corporate tax rate. Share price change represents price change from November 15, 2017 to December 11, 2017.

Source: S&P Capital IQ, Value Partners Investments Inc.

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