Conference Call

Sell In May and Go Away did not this year: Here's Why!

Q3 2016

Welcome to our third quarter 2016 conference call. We host these quarterly calls to provide you some general market information and outlook for the economy and markets, as well as the activity in your portfolios. You can find all our previous calls plus a wealth of information about our services on our website at **www.advice-first.ca**.

"The information in this conference call is derived in part by Counsel Portfolio Services and IPC Private Wealth - both divisions are affiliated entities of IPC Securities Corporation ."

For the third quarter of 2016 almost all markets moved higher, except for Denmark. Even Brazil who has been struggling witnessed a strong recovery and moved higher with the rise in commodity process. We had increase political risk with elections looming as well as increased uncertainty regarding the global economy and the potential US Federal Bank interest rate increases.

The world remains in an environment mostly defined by:

- Slower economic growth
- Low Inflation
- Again Populations (especially amongst developed countries)
- Higher Income Inequality
- Elevated Debt loads
- And a shortage of safe assets that pay a yield

Yet the market performed well over the quarter and here is why "Sell in May and Go Away" did not work this year:

- We experienced improving credit markets which was a problem during the crisis of 2008
- Better than expected economic data was reported in the 3rd quarter
- Interest rates remained low as the US Federal Bank did not raise rates
- And Brexit concerns began to ease

We expect to remain in a slow growth, low inflation environment and will most likely remain for some time. Central bank activity in global investment markets continues as we saw:

- The Bank of England buying up Corporate Bonds to support UK businesses in a post Brexit environment
- The Bank of Japan continues to buy ETFs on the Nikkei to support stock prices in Japan
- The European Central Bank continues to sovereign debt to support the Eurozone.

We are still a stimulus flooded world and the central banks continue to have a large amount of influence in the markets.

On the Canadian side, we are coming through the tailwinds of low oil. Oil is now trading in the $43 range after hitting lows near the $30 range. The worst might be behind us as the price slowly recovers and OPEC announced potential production cuts this November, but oil remains a political commodity and the recovery could be bumpy or take longer than many hoped.

On the US side, GDP growth slowed a bit the third quarter but the US is still considered a market of safety. Technology stocks did very well in the third quarter – up +12% as a group. However, political and geo-political risk remains elevated going into the election.

For International Markets, Global Corporate earnings are slowly recovering. Global trade is no longer decelerating. Brexit negotiations won't begin until next year. Japan continues to look for ways to stimulate their economy with tight labour markets. China's economy has recently managed to stabilize growth around 6% GDP.

So where has the volatility come from in 2016?

In 2016 we have witnessed three sell offs in the market. The first was coming into the year in January. We witnessed a 10% sell off on the S&P500 which bottomed around the middle of February. This was going to be the next 2008 as some had feared. The year started out rough but it began to recover, and had fully recovered by the second half of March. What caused the downturn? Looking back we can point to reports and speculation that the US Federal Reserve Bank was going to increase rates as many as 5 times in 2016. But so far this year (at the recording of this call) there have been 0 rate increases. The market reacted on the potential of 5 increases but no rate increases materialized.

We had a second downturn in June with the results of the Brexit vote in early June. But the market once again recovered very quickly and fully recovered by the end of June.

In the 3rd quarter we saw a smaller downturn with the US Federal Reserve Bank announcing potential rate increases and outlook. We have seen fairly flat markets in the 3rd quarter as markets prepare for the US election and US Fed Bank outlook. So what did the Fed Bank say in Q3? They expect a recession sometime, maybe in 2019. As such they could raise rates so that the US 10 year treasury notes yield around 1% prior to a recession, but all in all they expect rates to remain low until 2029.

Some of the other developments we are watching include:

- Negative Interest Rate Policy around the world. Japan is the biggest nation using Negative Interest Rate Policy. We will have to wait and see how this policy strategy affects economies and markets.
  - The goal of NIRP is to stimulate consumption, stimulate bank lending, reduce debt service burdens and weakens the currency relative to other currencies.
  - But the potential unintended Consequences could include reduced pension plan performance as pension plans rely on a healthy portion of bonds in their portfolio, reduced bank profit margins, and it keeps weak companies alive longer with cheap debt.

We continue to watch oil especially any developments in Saudi Arabia and OPEC. Their inventories are falling and they may have to borrow money. They need a higher oil price as their current production policy is hurting their income needs.

We continue to watch Global GDP Growth and is remains on trend. Global growth is expected to grow at 3.4% and this is in line with longer term trends. If the US is growing at 2% then the rest of the world needs to pick up the rest. India is growing at 7.5%, China at 6%, South Korea at 2.75% and Mexico is growing at 2.75%

We are seeing higher levels of share buybacks from companies which are reducing the supply of shares on the market. As such this gives a lift to stock prices if demand is greater than supply. With interest rates so low, companies can issue a bond at 1.5% and use the proceeds to buy back their stock which pays a 3% dividend. That saves the company money, improves their performance which helps to increase the stock price.

So even though many said this would be the year to sell in May and go away, it did not happen. There are too many factors that are supportive of the market. There simply was not enough fear to continue to drive markets down.

Having said that two of our investment specialists have taken a bit more cautious stance in the third quarter in our Canadian and North America Dividend mandate as well as the Global Small Cap mandate.

Starting with Lincluden Investment Management, the investment specialist for the Canadian and North American Dividend mandates, remains somewhat cautious on the current state of the Canadian economy. The Canadian dollar continues to remain depressed relative to the U.S. dollar due to low oil prices, as well as divergent monetary policies between the Bank of Canada and the U.S. Federal Reserve. Valuations of most high quality names outside of resource sector remains elevated offering limited opportunity. The portfolio is structured to take advantage of mispricing opportunities in higher quality names, while benefitting from the steady flow of above-average dividends from these holdings. The portfolio is expected to benefit from a repricing of its undervalued holdings as well as an above market dividend yield, while protecting capital due to the focus on quality and value.

Wasatch Advisors, the investment specialist for the Global Small Cap mandate, has taken a more cautious approach in its allocations. Following Brexit, Wasatch reduced its U.K. and European exposure as a way to mitigate risk in the face of uncertainty. In addition, they shifted the mandate to have overweight exposures to markets that appear to have strong consumer growth and that look relatively attractive, in Wasatch Advisors' view, in a potentially deflationary environment.

As the team that oversees all aspects of your financial plan, we continue to monitor your portfolio in light of market volatility and where we are in the economic cycle. We will continue to monitor central bank policy to stimulate economies globally. We believe you will see much more infrastructure spending in Canada and the US in the months and years ahead. Also, in 2016 and 2017 we will see some important elections – notably – France, Iran, and Germany (now that the US election is behind us).

We Now Know the Outcome of the Unpredictable Election

This election feels a lot like Brexit, but it really is not the same. The UK has 2 years before Brexit to materialize – The US election results with a Trump win is a much shorter term to see potential changes. There will be a transition period though.

Initially, stock markets will react to the unexpected election results and may see an initial sell off followed by a rally, once some of the uncertainty dissipates.

With a Trump win the most likely themes that will play out at this time are:

- Lower Taxes
- Repatriation
- Pro-Business policies
- Pro-Fossil Fuel policies
- Obamacare will be put under a microscope with potential changes
- This result could benefit banks and small cap stocks

Here's what to keep in mind:

- The US government is still a system of checks and balances. Trump can't just make sweeping changes such as ripping up NAFTA and building walls.
- Political rhetoric that usually changes from campaigning to reigning. The rhetoric is not reality
- Changes take time. There will be a transition period. Trump has his own transition to manage.
- Corporate America will continue on this morning. The economy is not shutting down.
- Don't Panic – Selling into this market is very difficult and dangerous because you also have to time the re-entry. In today's market, rallies can happen very quickly with high frequency trading models and the use of ETF's.
- Keep your long term goals front and centre.
- Stay diversified.
- Don't chase returns such as gold (which is considered a safe haven in these times)
- Let the Investment Specialists buy into the weakness.

If you have any questions or comments or would like to review your portfolio, please connect with us through our website at www.advice-first.ca or give us a call at 519-578-9504.

Warm Regards to all of you. We will speak to you again in the New Year to recap the last quarter of 2016. Bye for now!

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