Wealth Matters – Winter 2017

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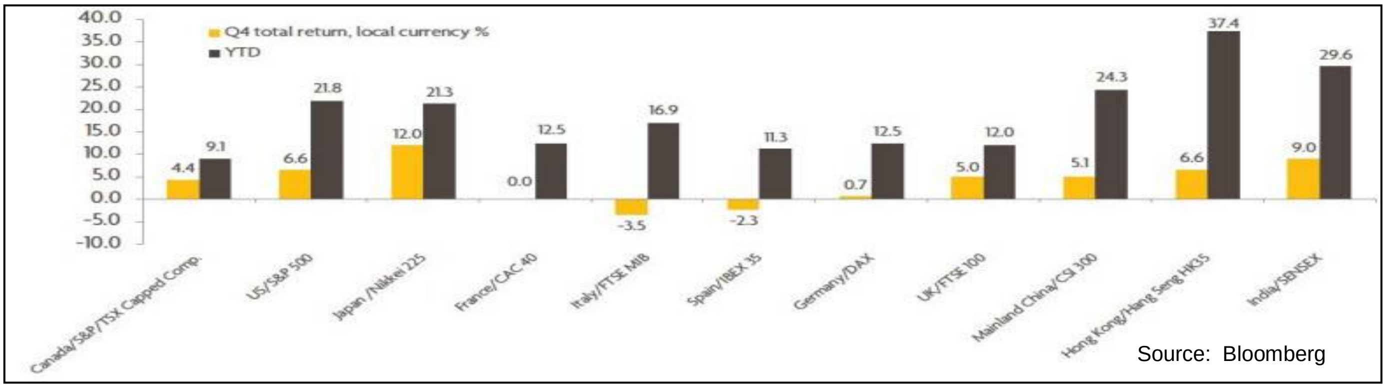
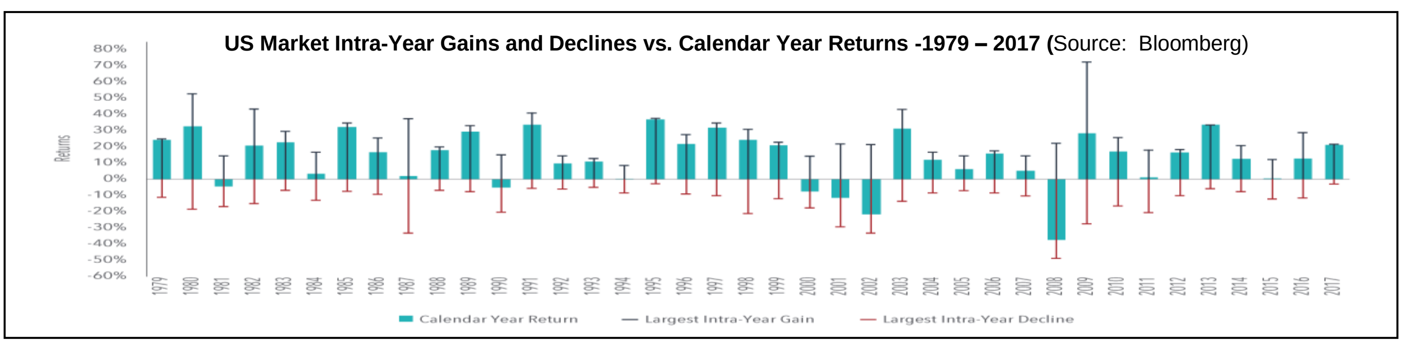
Investment Market Commentary

2017 was a good year for stocks almost everywhere in the world and most global equity markets continued their upward trajectory in the last quarter of 2017. Robust global economic growth, strong corporate earnings, accommodative financial conditions by central banks, and benign inflation combined with the expectation of US tax reform, fueled broad gains across both developed and emerging markets. This strong economic backdrop overrode any geopolitical concerns or global indebtedness that dominated news headlines throughout 2017.



The year opened with enthusiasm over the pro-business agenda of the new Trump administration but uncertainty around trade and immigration policies persisted. Failed attempts at travel bans and health care reform along with a war of words with North Korea preoccupied the media. Eventually, the Republican-led house passed the highly anticipated tax reform legislation just before the Christmas holiday.

The 106 month bull market is now the second longest on record and the S&P 500 racked up an amazing 62 new all-time highs in 2017. In the fourth quarter, the S&P 500 gained 6.6% in US dollar terms (7.2% CAD), with gains fueled by continuously better than expected profits, as well as the announced US tax cuts. Although energy had been a drag for most of 2017, the sector rebounded in the fourth quarter on the back of a strong increase in oil prices. Remarkably, US equities delivered positive returns in every single month of 2017, the first time this has happened since 1958. On average, US equities experience an intra-year drawdown of about 14%. In 2017, the maximum drawdown for the index was less than 3%. For the year, the S&P 500 returned almost 22%, but only 13.5% in Canadian dollar terms due to the strong recovery of our currency.



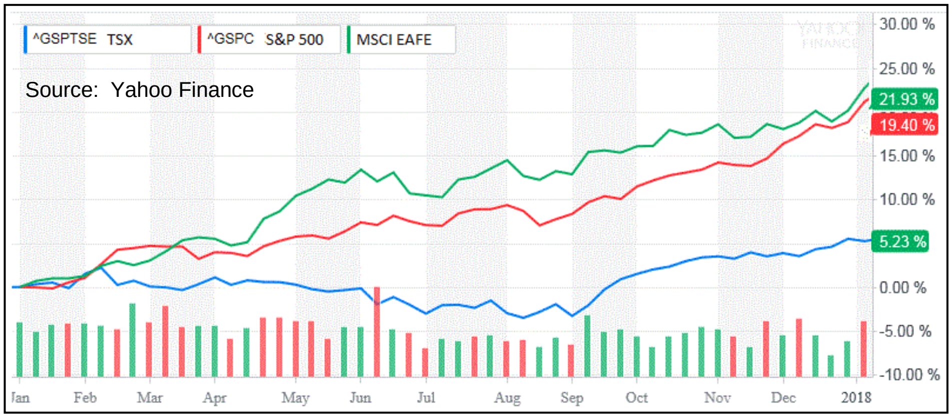
In Canada, the surprisingly robust economic recovery failed to translate into an equally impressive year for the S&P/TSX compared to other major markets. In the first half of 2017 the annualized pace of real GDP growth was about 4% which is well above Canada's sustainable growth rate at full capacity. With declining economic slack and growing concerns of inflationary pressure, the Bank of Canada hiked interest rates twice catching markets by surprise and leading to a rapid surge in the loonie by over 10% from May to the peak in September. Real GDP slowed in the second half leading markets to scale back expectations of more rate hikes. Market gains were limited as the heavyweight energy sector fell 7% on the year despite a 12% rise in oil prices, a symptom of the lack of pipelines to deliver oil to the market. The S&P/TSX underperformed other major markets earning a 4.5% return over the fourth quarter and a decent 9.1% for the year.

Overseas stock markets produced strong gains driven by a healthy rebound in economic growth. European economies were among the brightest spot with the Eurozone GDP expanding at the fastest pace in a decade. China's GDP growth rate posted its first uptick since 2010 leading emerging market equities to an extraordinary gain in Canadian dollars.

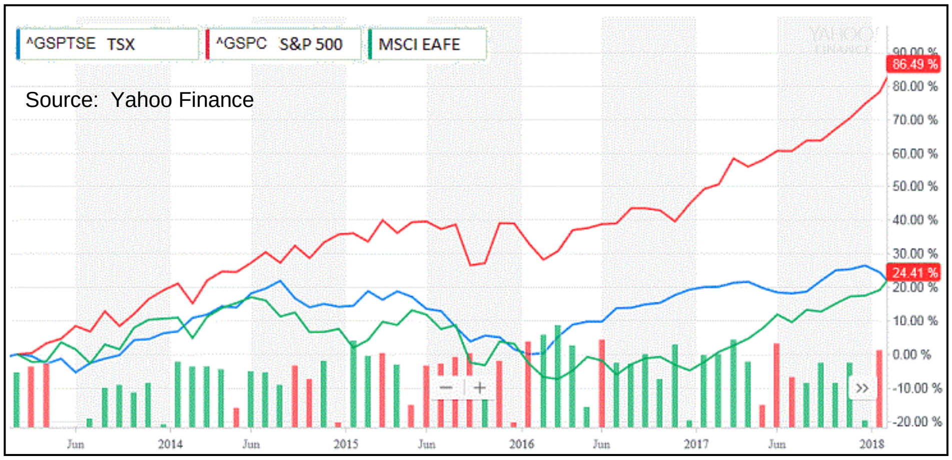
The Canadian bond market experienced bouts of volatility during the final quarter of the year, but ended the quarter in positive territory, with longer-term bonds outperforming their short-term counterparts. The first two months of the quarter saw bonds react favorably to slower third-quarter economic growth, as well as the dovish tone in the Bank of Canada's October and December decisions to keep the overnight target rate unchanged at 1%. While the Bank of Canada noted that both the Canadian and global economies were evolving as projected and that inflation continued to edge higher, they indicated that the global outlook remains subject to considerable uncertainty, notably with respect to geopolitical developments and trade policies (specifically NAFTA renegotiations). During the month of December, however, the robust economic data, including strong November inflation numbers, pushed short rates back above early-October levels, while longer rates moved up only marginally. The net decline in long-term interest rates combined with the longer duration of these bonds resulted in long-term bonds performing particularly well over the quarter, with the long-term bond index returning 5.2% compared to 0.3% for the short-term bond index. Overall, the Canadian bond market (FTSE TMX Canada Universe Bond Index) returned 2.0% in the fourth quarter and 2.5% for the calendar year. While the path taken by U.S. interest rates during the quarter was quite different to that in Canada, net interest rate movements in the U.S. over the quarter were not that dissimilar to those in Canada, although U.S. shorter-term rates rose much more than in Canada and long-term rates moved slightly higher.

The currently favorable global economic environment and accommodative financial conditions continue to provide support to corporate earnings and global equity markets. As such, we continue to favor equities over cash and bonds, but remain mindful of the risks inherent in the equity market, and the need to maintain some fixed income for defense. In terms of equity allocation, we continue to maintain a globally diversified approach, but with reduced exposure to markets that are fully valued. We expect central banks to carry on with gradually withdrawing stimulus and for interest rates to move higher. As such, we continue to position the fixed income portion of our clients' portfolios in funds with higher-quality, shorter-duration bonds in order to preserve capital. Should we witness a correction in the markets this year, our active managers have the ability to act defensively and select which investments to be in, when compared to passive management.

Benchmark Returns



2017 calendar year performance. Price returns in local currency. Canadian equities (S&PTSX) in Red, USA (S&P 500) in blue, International (MSCI EAFE) in green. Canadian equities were down most of the year until the third quarter.



For perspective, the same curves are shown for a 5-year period beginning January 2013. The commodity decline of 2015 can be seen holding back Canadian and international benchmarks, while US equity prices largely shrugged off these issues.

Total Returns CAD$ to December 29, 2017											
Canadian Dollar ($US/$CAD)	*2.73%*	*-0.52%*	*7.02%*	*5.04%*	*-2.58%*	*-4.04%*	*-4.53%*	*-2.36%*	*1.55%*	*0.65%*	*0.05%*
Name	1M	3M	12M	2Y	3Y	4Y	5Y	10Y	15Y	20Y	25Y
Canada											
91d T-Bills	0.04%	0.23%	0.56%	0.53%	0.57%	0.65%	0.72%	1.01%			
FTSE TMX Short Term Bond	-0.46%	0.28%	0.08%	0.54%	1.23%	1.68%	1.70%	3.16%			
FTSE TMX Universe Bond	-0.41%	2.02%	2.52%	2.09%	2.56%	4.09%	3.01%	4.67%			
FTSE TMX High Yield Bond	0.60%	2.39%	9.94%	13.38%	7.34%	6.12%	5.97%	7.20%			
Canadian Equity											
S&P/TSX Composite	1.20%	4.45%	9.10%	14.93%	6.59%	7.57%	8.63%	4.65%	9.02%	7.03%	9.04%
S&P/TSX SmallCap	2.59%	4.69%	2.75%	19.29%	7.24%	4.76%	5.32%	2.39%	5.58%		
TSX Sectors											
Cdn. Energy	1.71%	2.06%	10.61%	11.72%	-1.80%	-5.65%	-2.13%	-2.98%	5.57%		
Cdn. Materials	3.73%	5.00%	7.67%	23.30%	6.28%	3.99%	-3.68%	-1.85%	5.92%	4.98%	
Cdn. Consumer Staples	0.07%	5.12%	7.68%	8.37%	9.38%	18.03%	19.12%	13.65%	10.82%	12.85%	
Cdn. Health Care	24.40%	46.65%	39.60%	11.01%	-0.46%	4.46%	11.42%	12.68%	6.06%	3.98%	
Global Gold	0.83%	-0.24%	1.35%	23.69%	11.19%	6.69%	-7.39%	-3.58%	0.69%		
U.S.A.											
S&P 500 (LargeCap)	-1.58%	7.21%	13.84%	11.19%	14.36%	16.70%	21.29%	11.12%	8.25%	6.50%	9.63%
Russell 2000	-3.05%	3.88%	7.12%	12.28%	12.86%	13.25%	19.54%	11.34%	9.47%	7.19%	9.49%
International											
MSCI Europe	-1.18%	2.80%	17.95%	7.09%	10.14%	8.28%	13.10%	4.42%	6.98%	5.20%	8.46%
MSCI Japan	-1.96%	9.09%	16.23%	7.62%	14.94%	12.38%	16.77%	5.89%	5.53%	3.34%	3.13%
MSCI EAFE (Net)	-1.10%	4.78%	16.83%	6.99%	10.65%	8.87%	13.02%	4.40%	6.46%	4.56%	6.39%
MSCI EM (Emerging Markets)	0.89%	8.07%	28.71%	18.05%	12.39%	11.04%	9.70%	4.49%	10.96%	7.39%	7.93%

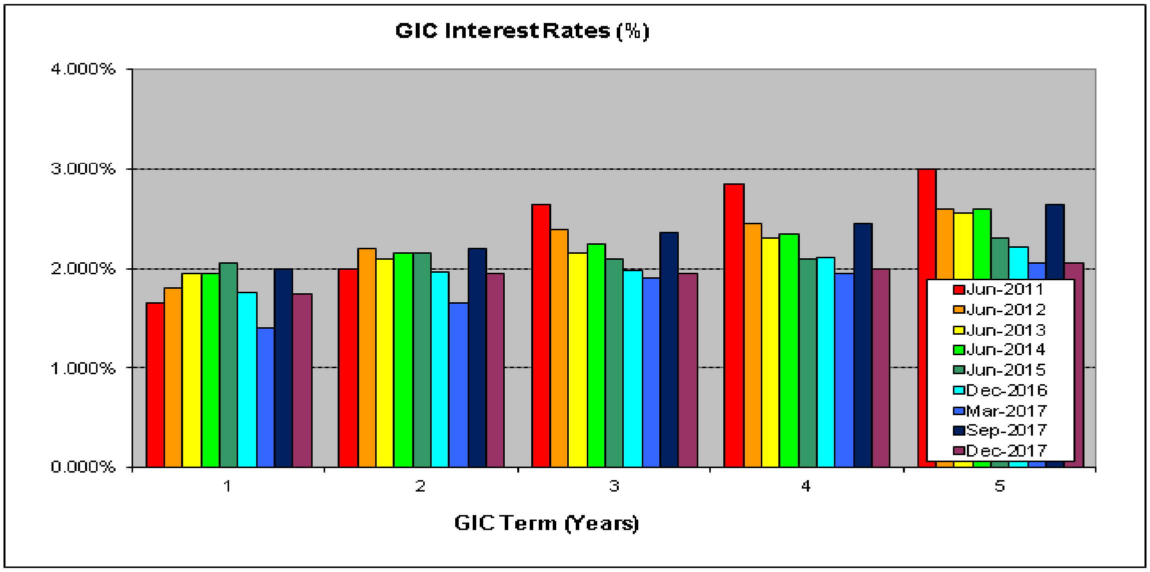
(Source: Guardian Capital Advisors)

Interest Rates

Bond Yield on US 10year government bonds rose to 2.41% by year-end as unemployment rates continued to fall and expectations of future inflation rose. Also the US Federal reserve began to slowly sell off its huge bond inventory at the end of the 3rd quarter, and the market expects further gradual hikes in the Fed's overnight rate.

Source: Cannex Financial Exchanges

Surprisingly, top GIC rates fell off slightly across the board from September to December. Digging into the data a little deeper, though, shows the spike in September rates was due more to a single institution offering rates well above the average, and on that basis the rate market is about where it was a year ago.



Feedback

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