THE RAE LIPSKIE PARTNERSHIP™ | PRIVATE WEALTH MANAGEMENT

June 2016 **Overview**

Random Gleanings…

Will The Donald Trump Clinton? You will have noticed that an everlasting election campaign is progressing(?) in the U.S. Never before have two probable candidates measured so high on the dislike scale as voters fret about Mr. (Outside) Trump's loose-cannon approach and Mrs. (Inside) Clinton's trustworthiness. Our Prime Minister has taken note and is sharpening his elbows for the inevitable conflicts, whoever wins.

Panama Progress. Unlike the above, we have seen little news about the near completion of a $5 billion expansion of the Panama Canal. A third set of locks and deeper channels will double capacity and allow wider-beamed ships (180' vs. 109'), including most liquefied natural gas tankers, to take this shorter route to Asia, knocking 35% off the transportation cost. U.S. ports plan to spend $150 billion over the next four years to handle the bigger boats. Wow.

Only in Government. In May, the Ontario Energy Board increased the price of already-expensive hydro because "Ontarians consumed less electricity than expected over recent months". Bad Ontarians! When abundant supply meets declining demand, shouldn't prices go down?

Only in Government II. And we quote: "(Waterloo) Regional staff expect to spend about $2.2 million to launch garbage ***cuts***", with plans to hire nine permanent and temporary staff to handle the reduction in service. Huh?

Phantom Car Theft. Your car is sitting in the garage, but it has been stolen. How so? A bad guy has hacked into the car's computer thingamajig and disabled the vehicle. The car's there but it won't pick the kids up. After some time to stew, possibly including some bad words, you get a message demanding ransom, often in non-traceable bitcoin. This is ransomware, it is growing rapidly and the possibilities for mass theft are mind boggling.

Hit the Road, Jack. Speaking of cars – the ones not disabled – people are driving them. After a driving lull in the recession, the U.S. Department of Transportation reports new records of miles driven month after month, including March, up 13 <u>billion</u> over last year (+5%), and a 12-month total of 3.2 <u>trillion</u> miles. Thanks to more jobs, higher consumer income and lower gas prices, this big and growing demand factor is a strong support for crude-oil prices.

And the Old Shall be New Again. Remember Polaroid Instant cameras with the grainy pictures? They're baaack. Notwithstanding the quality and convenience of digital photography these days, it turns out these old-school cameras with the expensive film are the Next Big Thing and young buyers are lapping them up. Apparently they are fun to use and they put out these cool things called prints.

Warm Enough for You? The strongest El Nino in 20 years is winding down after a year of generating extra heat for the globe and, recently, ideal conditions for the tragic Fort McMurray fire. Such large-scale warming systems in the past have generally been followed by El Nino's ugly sister, La Nina, so time will tell if we see the results of her cooling pressure next winter. Not too much pressure, please.

Teach your Children Well. A recent book, *Passing on the Right*, laments the dearth of conservative professors, noting, for example, that self-described Marxist professors make up 18% of humanities and social sciences faculties in the U.S., double the conservative level. As comrade Lenin said, "Give me four years to teach the children and the seed I have sown will never be uprooted". Hmmm.

On the Other (Invisible) Hand. 2016 marks the 240th anniversary of Adam Smith's seminal book, *An Inquiry into the Nature and Causes of the Wealth of Nations*, the continuing linchpin of the free, competitive, market-based economies that most developed (and successful) countries enjoy today. Thank you, Adam.

THE LEARNING CORNER

What (or Who) is TINA?

Don't worry, this section won't go into the musical attributes of *Rolling on the River*. We are here today to discuss the TINA acronym: **T**here **I**s **N**o **A**lternative. Some skeptics suggest it actually stands for Tina is no Acronym, but apparently it goes back to Margaret Thatcher's conviction (she had a few) that there is no alternative to free markets for modern societies to succeed. Recently it has been a useful description for investors and institutions forced to buy negative-rate debt (see Charting our Times), but our primary focus on the term relates to equity investment in a world of historically low interest rates.

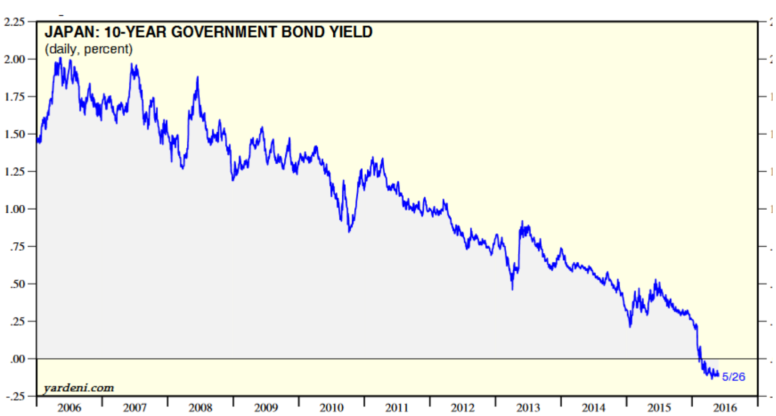
For many equity investors, the theory behind the acronym is simple: interest rates are so low they do not present a viable alternative to investing in the stock market. This is a bold assertion and is obviously subject to caveats depending on investor needs for security versus risk. It is true, though, that today's ultra-low interest rates can't meet fixed-income needs the way they once did and, while preferred-share dividends can help in this effort, they come with higher risk. Compared with low and flat interest rates, dividend yields are higher (the TSX index yield is 3.0%), and growing (the Big Five banks, for example, averaged 6% yearly dividend growth in the past 5 years). We understand the importance of investment balance and diversification but, in accordance with TINA, we maintain our preference for stocks in client portfolios.

KING DON VS. GODZILLARY

CHARTING OUR TIMES

Investors know all too well that bond yields are extremely low today. In Canada, federal government bonds pay just 0.75% for 5 years and only rise to a still miserly 1.30% for a 10-year period. 1.3% doesn't seem like much of a return when you are looking at investing your money for 10 years. In fact, the domestic interest-rate landscape is very discouraging, but look at the chart below. It shows the yield on the equivalent 10-year bond in Japan, and that yield is actually negative today. This means that a buyer of this bond is willing to pay a price that guarantees a negative return for the 10-year holding period. And Japan is only joining other countries in Europe where investors are faced with negative rates on bank deposits and shorter term bonds. Apparently negative rates now apply to about $7 trillion of government debt around the world.

If this makes you scratch your head and say huh?, welcome to the club. Negative interest rates are the extreme result of aggressive central-bank policies to boost economic activity, but why would anyone be willing to pay the bank or government to hold money for them? It is hard enough to stomach buying the low rates in Canada, but at least they are positive. Negative-rate buyers include investors who have to own such holdings according to regulation or policy; people who think they can still make money on them from currency or even more negative rates; those who have no more room under the mattress; and investors who demand or require the guaranteed return, even if negative. Interesting times, indeed.



Source: Haver Analytics.

IN THE OFFICE

Hello, Goodbye

We have some great news followed by some bittersweet news.

On May 4, 2016, we acquired FI Capital Ltd., a subsidiary of FaithLife Financial in Waterloo. With this transaction, The RaeLipskie Partnership now manages approximately $1 billion in client assets. FI Capital has had a strong history of serving their clients and providing strong investment returns. We look forward to continuing that relationship with FI Capital's clients. We also say hello and welcome to Duncan Smart, CFA, joining us from FI Capital. We now have 23 employees in our Waterloo and Burlington offices.

Unfortunately, at the end of July, we will be saying goodbye and best wishes to a long-term member of our staff. Pat Haylock has decided she would like to retire and spend more time with her husband, and visit her two daughters who have moved to Calgary and Seattle. Pat has been a valued member of our team for over 16 years and we'll miss her – her expertise in her work, her laugh, and her famous bean dip. Leslie Stallard, who currently works in our back office, will be training with Pat and taking over for her. If you are Pat's client, we are sure you will enjoy working with Leslie.

We are:

Ken Rae, CFA

Brian Lipskie, CFA

Ted Brough, CFA

Jo-Ann Carlisle, CIM

Taylor Echlin, F.C.S.I.

Jim Harper, FCPA, FCA

David Martin, CIM

Andréa Miljkovic, CFA

David Paleczny

Derek Rae, CIM

Duncan Smart, CFA

Rick Vandermey, CFA

Thomas Pick, M.B.A.

The RaeLipskie Partnership provides discretionary "fee-only" portfolio management for high net worth individuals, endowments and charities.

The RaeLipskie Partnership

20 Erb Street West, Suite 201
Waterloo, Ontario N2L 1T2
T 519 578 6849
F 519 578 7269
Toll Free 888 578 7542

1100 Burloak Drive, Suite 300
Burlington, Ontario L7L 6B2
T 905 336 8962
F 519 578 7269
Toll Free 888 578 7542

THE BIG PICTURE

Mixed Signals

In the first half of 2016, the Canadian economy has been providing rather divergent signals as to the underlying strength and possible future direction of our economy. The first quarter of the year saw Canada bucking the global trend towards softer GDP trends, with an anticipated first quarter 2016 GDP growth rate of approximately 3% (annualized). The strength in that period appears to have been both externally (trade) and internally (consumption) driven. That result would be one of our better quarterly performances in some time and substantially stronger than the lackluster performance of late 2015. The impact of a weak C$, continued strength in employment and a buoyant housing market seem to be among the contributors to the gains. A mild winter may also have helped by pulling forward some spending plans into the earlier part of the year.

More recently however, the trend has been weaker, and not just because of the impact of the wildfires in Alberta. Capital spending in the energy sector has been sharply lower through 2015 and into 2016, but more recently "capex" in the manufacturing sector has turned down as well. Continued strength in employment and consumer spending, at the same time that business investment to support future growth weakens, creates a "chicken and egg" dilemma – which one leads and which one lags? Our export performance faces a similar conundrum, with our weak currency (at least until recently) providing a competitive advantage especially with our largest trading partner, the US. Our weak loonie of course is in large part a reflection of a strong US dollar, and that strength seems to be catching up with the US as it experiences sluggish growth of late. While currency can act as part of the global economy's self-balancing mechanism, it's a mechanism that takes some time to re-calibrate itself. We are seeing a positive response to the weak loonie in tourism activity. Our improved competitive position from the weak dollar should be beneficial to investment plans, but those plans take some time to implement, especially when the change in the currency has been as dramatic as we have witnessed. At the same time, corporate profits have been in a funk. The combined effect of energy sector profit declines and significantly reduced investment plans in that sector have resulted in a downturn in corporate profits in both Canada and the US.

However, the combination of oil prices soon rolling past the two year anniversary of their peak level (June 2014 at approximately $106/bbl) and the recent rally in commodity prices, along with other factors, may be contributing to a bottoming in corporate profits, which could provide a positive boost to our economy, and allow Canada to maintain economic momentum. An improved profit outlook would also provide underpinning to the equity markets.

QUOTE of the DAY

The nine most terrifying words in the English language are: "I'm from the government and I'm here to help."

- Ronald Reagan