Weekly Trends

PRIVATE CLIENT SOLUTIONS

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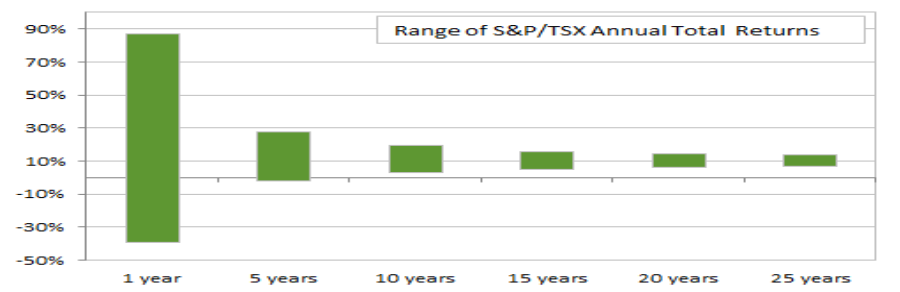
It's All About The Long Term

- During these challenging times we can often lose focus of the long term, and instead get caught up in the short-term gyrations of the equity markets. While this is understandable given the emotional and financial impact of market declines, focusing on the short term can often lead to poor decision making and costly mistakes to our long-term financial plans. By focusing on the long term it helps us to "see the forest for the trees" and avoid making investment mistakes that can have a deleterious impact to our financial plans. This week we examine the benefits of long-term equity investing.
- Looking at the S&P/TSX Composite Index (S&P/TSX), we calculated total returns (including dividends) for 1, 5, 10, 15, 20, and 25 year holding periods, using rolling monthly returns since 1956. For 1 year holding periods we found that the worst return was -39.2%. However, as we extend the holding period to 10 years and beyond we found that there has never been a negative total return on the S&P/TSX, with the worst 10 year return being 2.8% annualized. As the time horizon increases, annual total returns converge around the 9% to 10% range.
- Another way to look at returns is to know what $1 invested years ago would be worth today. If one invested $100,000 in the S&P/TSX in 1988 they would have $427,479 today assuming no dividends, or $857,154 including compounded dividends. Including dividends this equates to an 8.6% geometric return.
- Market corrections are never easy, but our analysis shows that investors that stay the course, taking a long-term perspective, are rewarded with solid equity returns, which go a long way in helping investors fulfill their financial goals.

Chart of the Week

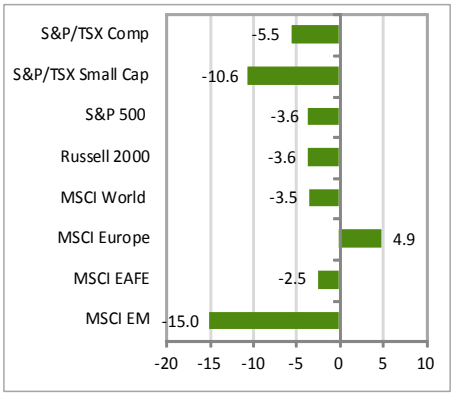
S&P/TSX Average Annual Total Returns Are Roughly 10%



S&P/TSX Returns	1 year	5 years	10 years	15 years	20 years	25 years
Best	86.9%	27.8%	19.5%	15.6%	14.1%	13.8%
Worst	-39.2%	-1.9%	2.8%	4.7%	6.2%	7.0%
Average	10.6%	9.6%	9.7%	9.8%	10.1%	10.2%

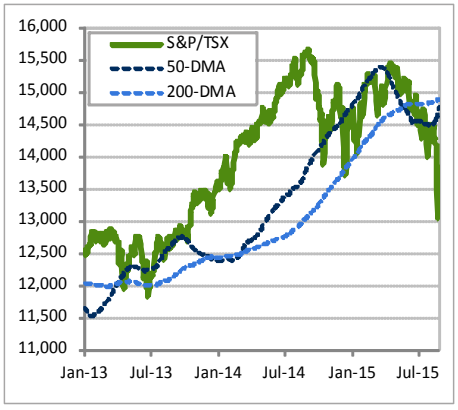
Source: Bloomberg, Raymond James Ltd.

Equity Market YTD Returns (%)



Canadian Sector	TSX Weight	Recommendation
Consumer Discretionary	6.9	Overweight
Consumer Staples	4.3	Market weight
Energy	19.2	Market weight
Financials	35.8	Market weight
Health Care	6.1	Market weight
Industrials	8.0	Overweight
Information Technology	2.8	Overweight
Materials	9.6	Underweight
Telecom	5.2	Market weight
Utilities	2.2	Underweight

Technical Considerations	Level	Reading
S&P/TSX Composite	13,827.5	
50-DMA	14,352.7	Downtrend
200-DMA	14,751.0	Downtrend
RSI (14-day)	43.5	Neutral



Source: Bloomberg, Raymond James Ltd.

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It's All About The Long Term

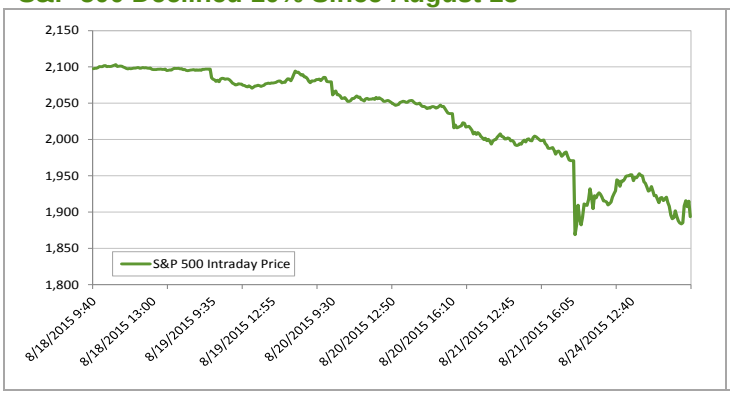
During these challenging times we can often lose focus of the long term, and instead get caught up in the short-term gyrations of the equity markets. While this is understandable given the emotional and financial impact of market declines, focusing on the short term can often lead to poor decision making and costly mistakes to our long-term financial plans. But, it's the long-term disciplined plans that will help investors realize their financial dreams, not the daily swings in the markets that few people can consistently profit from. Now, this is not to say that during challenging times, tweaks should not be made to portfolios and that we should stick our heads in the sand. As market conditions change, so should our positioning. But, by focusing on the long term it helps us to "see the forest for the trees" and avoid making investment mistakes that can have a deleterious impact to our financial plans. With that said, this week we examine the benefits of long-term equity investing, and why we must not lose focus of this.

First, let's address what led to the recent market weakness, and try to put the declines into perspective. We believe there are four key factors at play:

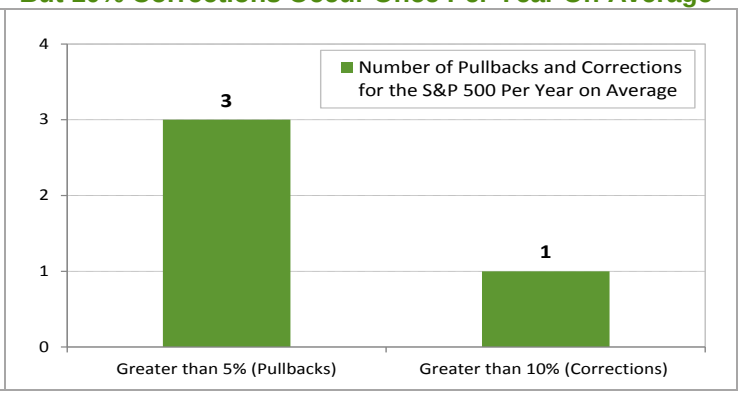
- **China:** As a result of the continued slowdown in the Chinese economy, policymakers decided to devalue the Yuan in effort to spur exports. This was followed by the China Flash PMI which showed that manufacturing declined to a four year low. With China being the second largest economy, concerns over the slowdown manifested in declines across the global equity markets.
- **Prospect of Fed tightening:** With the gradual improvement in the US economy the Fed has been signalling its intent to raise interest rates in the coming months. This expectation of rate hikes has weighed on investor sentiment and has contributed to the recent declines.
- **No 10% correction since mid-2011:** The S&P 500 has gone on one of its longest streaks without a 10% correction and therefore was overdue.
- **Weak seasonality:** Finally, as we've highlighted a number of times in recent months, June to September is the worst period of the calendar year for equities.

We believe the confluence of these factors led to the steep declines in the global equity markets. The S&P 500, for example, declined over 200 points (-10%) in just one week. While this is very unsettling, we believe the weakness should be viewed in the context of what's "normal". Based on our analysis, we have found that the S&P 500 endures three 5% pullbacks and one 10% correction every year, on average. So, we believe the recent weakness, while difficult, is "normal".

S&P 500 Declined 10% Since August 18



But 10% Corrections Occur Once Per Year On Average



Source: Bloomberg, Raymond James Ltd.

What Can We Expect Over The Long-term?

Stepping back from the day to day trading, we believe it's crucial that investors take a longer term approach. We believe this for two key reasons. First, as we've already intimated, it is very difficult to consistently try to time market peaks and bottoms. Let's review the last two major pullbacks/corrections as examples of this. In October 2014, the S&P 500 was trading in a strong uptrend, the US economy grew at a robust 4.3% in Q3/14, and S&P 500 corporate profits were healthy, growing 7.7% Y/Y in Q3/14. Despite this, the S&P 500 came under significant selling pressure, declining 9% in October. In this recent correction, the S&P 500, while trading in a range for most of H1/15, was still trading above its 200-day MA, with US economic data generally getting better. Then, like today, a global growth scare and concerns over a Fed rate hike unleashed a torrent of selling, pushing the equity markets aggressively lower. From our perspective, little has actually changed over the last two weeks, yet investors collectively became worried and decided to sell stocks. It is very hard to know when this will unfold. The second, and more important reason why we believe investors should focus on the long-term is that long term historical equity returns are impressive, and more than sufficient to help investors meet their financial goals.

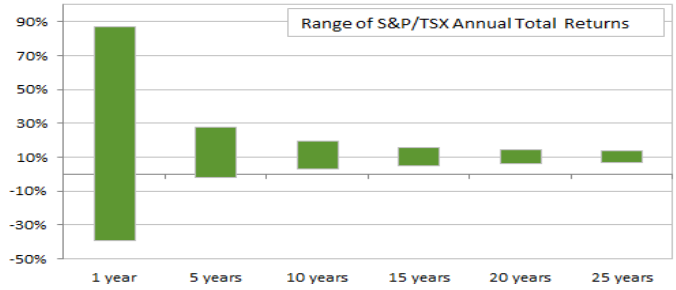
Looking at the S&P/TSX, we calculated total returns (including dividends) for 1, 5, 10, 15, 20, and 25 year holding periods, using rolling monthly returns since 1956. From the accompanying table we note that the average annual total returns over all of the holding periods is between 9.6% and 10.6%. For 1 year holding periods we found that the worst return was -39.2%. However, as we extend the holding period to 10 years and beyond we found that there has never been a negative total return on the S&P/TSX, with the worst 10 year return being 2.8% annualized. As the time horizon increases, annual total returns converge around the 9% to 10% range.

Another way to look at returns is to know what $1 invested years ago would be worth today. If one invested $100,000 in the S&P/TSX in 1988 they would have today $427,479 assuming no dividends, or $857,154 including compounded dividends. Including dividends this equates to an 8.6% geometric return.

Finally, we looked at the worst case scenario, assuming that an investor bought the S&P 500 at each market top since 1950 and calculated how long before the investor was back to even. We found, on average, the investor was even within 3.6 years.

In summary, market corrections are never easy, but our analysis shows that investors that stay the course, taking a long-term perspective, are rewarded with solid equity returns, which go a long way in helping investors fulfill their financial goals.

S&P/TSX Total Returns Over Different Holding Periods



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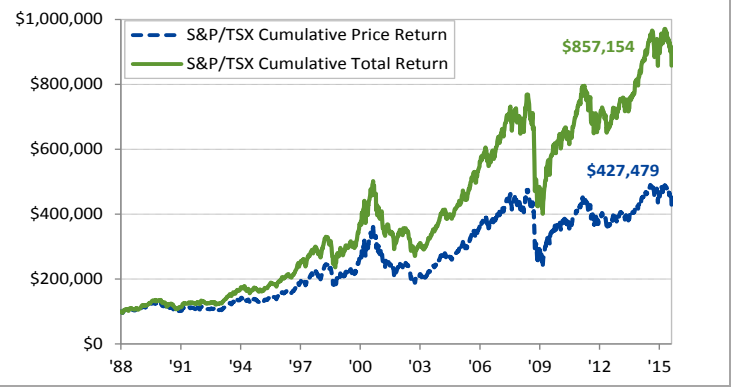
Value Of $100,000 Invested In The S&P/TSX Since 1988



Source: Bloomberg, Raymond James Ltd.

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