Angas Shick Group
PRIVATE WEALTH COUNSEL

Investment Commentary Q1 2018

Summary

It has been a tough quarter for investors. The positive returns from 2017 have been erased from the markets, and volatility has returned, causing investor sentiment to go from euphoric to fearful. As at March 31, 2018, the S&P 500 was down -1.2% YTD while the S&P/TSX was down -5.2% YTD.

All the major developed markets experienced negative performance except for the MSCI Emerging Markets Index which eked out a slightly positive performance of just less than 1%. All Canadian sectors had negative performance except for information technology and real estate. All US sectors also experienced negative performance except information technology and consumer discretionary.

The sharp market drops in Canada and the US were caused by inflation fears, tight conditions, protectionism and peaking global macro trends. Fundamentally, the global growth story remains supportive: PMI momentum (purchase management index, a leading indicator for growth) has started to slow, but activity is still trending at robust levels.

The economies in both Canada and the US continue to grow.

Model performance

Our Canadian Dividend Equity Model Portfolio slightly underperformed the S&P/TSX Composite Total Return Index with a return of -5.4% for the first quarter. The Canadian yield stocks have declined more than the general market due to interest rate hikes and inflation fears. We decreased exposure to this sector and took profits in Emera and Fortis which proved to be timely.

Dream Global REIT and InterRent REIT increased 11.4% and 5.4%, respectively, in March on the back of declining interest rates; the 5-year Canadian government bond decreased by ~7 bps during the month to 1.97%, making Dream Global and InterRent's respective 5.8% and 2.7% dividend yields relatively more attractive. Suncor Energy also enjoyed a solid 5.3% increase in March after tracking the price of rising crude oil, which increased by 5.4% during the month. ShawCor declined 7.4% during the month on the back of weaker-than-expected Q1/18 guidance. We exited our Shawcor position.

The Balanced Growth portfolio which consists of 5% cash, 20% fixed income, 40% Canadian equity and 35% foreign equity was down -1.7% for the 3 months ending March 31, 2018, and up 3.5% for the 12 months ending March 31, 2018, which beat the benchmark in both time periods. The portfolio continues to benefit from our exposure to the global markets which have not declined as much as the Canadian market. The allocation to cash and fixed income has also helped to shelter the portfolio from experiencing the full effects of negative global markets.

Trades

We were very active in the quarter as the markets presented some opportunities. We trimmed Emera and Fortis to reduce our exposure to utility stocks. We trimmed WSP Global to realize some of the profits. We used the proceeds to buy Restaurant Brands due to valuation and expected earnings growth. We sold CN Rail, CNQ and Shawcor to buy Vermillion Energy, Brookfield Asset Management and TFI International, as we expect these securities to benefit from the current market conditions. We sold half of Pure Industrial as we wanted to initiate a position in InterRent Reit (the balance will soon be redeemed for cash from a recent buy-out). We sold Open Text and invested the proceeds in Sierra Wireless. All these moves benefited the portfolio except for the Sierra trade which was a bit early; however, we believe there is good long term potential in this stock.

Dividend Increases

During the last quarter, dividend payout increases were announced by, BCE, Brookfield Asset Management, Enbridge, Exchange Income Corp, Restaurant Brands Intl, Royal Bank, Suncor, TFI Intl, Telus and TD Bank.

What's next?

Escalating U.S. and China trade rhetoric has hijacked markets in the last few weeks, making it nearly impossible for investors to stay focused in light of extreme volatility. We believe the most likely scenario for trade is that the U.S. and China are setting the foundation for negotiations, which should bode well for earnings. The supply/demand picture for commodities remains favourable and our exposure to energy should be beneficial. The S&P 500 and the Nasdaq have had a few successful rebounds from their respective 200-day support lines which technically indicate a market rebound. Equities are the most oversold since late 2015, and if the trade situation doesn't escalate further, we believe a lot of bad news is already priced in to most stock valuations.

This latest bout of political theatre with Trump hitting China with tariffs and the Chinese retaliating with tariffs of their own has led to uncertainty. The situation may not be as bad as it seems, and could be just another example of Trump's negotiating techniques. One thing for certain is we can expect more moderate returns from the financial markets in this late stage of the growth cycle and much higher volatility, something that investors may not be used to.

As always we will be monitoring the political and economic climate to look for opportunities to re-balance the portfolio in terms of asset mix and asset allocation. We are slightly overweight cash and will be able to take advantage of these opportunities and offset some of the volatility at the same time. We will not be adding to our Canadian content until we see clearer evidence that the NAFTA agreement will go ahead and the main drivers of the Canadian economy, mostly the energy and commodity sectors, show signs of renewed investor confidence.

On the economic front, we remain focused on inflation, interest rates, and the leading and trailing economic indicators which all continue to support moderate global growth with no recessionary pressures in sight. Although market expectations have been tempered somewhat, we are still predicating another positive return for the portfolio this year.

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