

High Level Investment Report

Trusted Advice & Peace of Mind

Issue #7/Summer 2016



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Team Update: Welcome Back Jocelyn!

I want to update everyone on my team situation, as **Jocelyn Leeds** returns from her maternity leave. She is back in the office August 2nd, and we are happy to have her back.

During the next month I will be transitioning from having a couple shared assistants on my team, to a dedicated full assistant with Jocelyn filling the role. Shelley Qually will also be dedicated to one other advisor in the branch, who she currently also supports. Jennifer will be here until end of September as part of her contract, and has been an awesome help to me and the branch this year. But as always, the branch is full of helpful staff, so all clients will be looked after no matter.

Brexit, Brexit! Read All About It!

By now all of you will likely have heard, read or even possibly discussed the UK "Brexit" with friends or family. The vote shocked many people around the world, and I think the political establishments of various countries might have been the most shocked of all. On June 24th, 2016 the United Kingdom voted to leave the European Union. The vote wasn't unanimous, in fact most of Scotland and the city of London voted to stay, but at the end of the tally there were enough votes to set the exit in motion.

I am not going to recap any more of the "Brexit" situation as this has been covered a lot in the media the last month. What I wanted to write about in this edition of the **High Level Investment Report** is the trickle down effects of the UK Brexit, how it impacts investors and savers, and how I feel it could impact your portfolio.

Let me start by saying that this is another geopolitical event that **reinforces my cautiously optimistic views on the market.** A year ago, in the Summer 2015 newsletter, I wrote about China and Greece's problems and why it was potentially good for your portfolio, something that maybe made no sense at all at the time. But since then, the defensive positioning of Gold, Gold shares and various tactical fund strategies have helped **keep my clients accounts very stable through various sharp market declines.** August & September 2015 and again in January & February 2016 were nasty months in the market, yet my clients' portfolios have stayed fairly consistent without large declines.

I will be the first to disclose to you however, that during the months when the markets rise substantially (typically after the large declines in the market), my average client isn't seeing those major gains. This is because I am positioning investments to create stable returns and defend as much as possible against the large, shocking drops that seem to be a regular event the past several years.

My personal views on the impact and effect of the Brexit vote are not negative for the United Kingdom. In fact I believe this will be a medium term surprise, as the UK benefits from being able to make independent decisions for their country and economy. Under the terms of the vote, they have a couple years until this "exit" could be complete and there is a chance that the vote could be denied and not implemented by the UK as well. However in today's world, to not go ahead with the public vote on a topic like this would result in major societal unrest in my opinion as the "average Joe" wants his democratic voice to be heard.

The potential risk of the "Brexit" vote is not for the UK in my opinion, but for other countries in the European Union that could decide to have their own referendum to leave the EU. Many of these countries have economies that pale in comparison to that of the UK. **If further "exit" referendums occur, it could eventually lead to a fracture in the European economic block, which causes uncertainty for markets around the world.** This has already been acknowledged by the European Union with promises for further stimulus and the UK even mentioning that they will be willing to provide stimulus if needed as they go through transition in the coming period (meaning more money printing and/or even lower rates to support markets and bonds specifically).

As I mentioned last year, **this is not always bad news.** For instance, the European Markets and Asian markets are down substantially in the past 12 months as they reflect the reality of their economic situation and **present opportunities for good returns from these levels in the years to come.** As of July 26th, 2016 the Dow Jones Euro Stoxx index was down 13.25% over the past 12 months. The Nikkei 225 in Japan was down 18.11%, and the China Shanghai Composite was down 19.69%.

Investments in the International markets are not well represented in many Canadians portfolios in general, as most of "our" money gets invested in Canada and in the USA. The North American stock markets have held up much better than overseas markets in the last 12 months, yet I believe they should be reflecting more realistic values

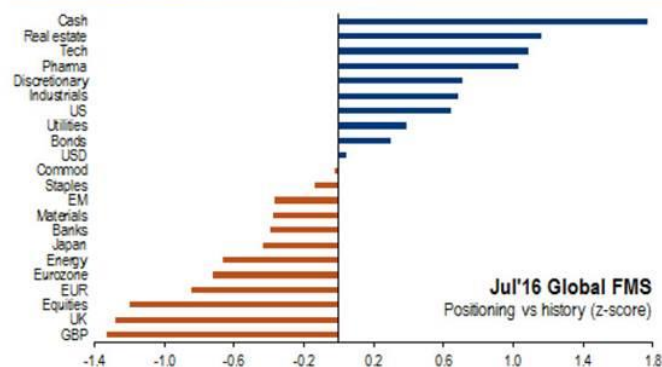
of the current economic situation. **By this I mean the U.S. markets are susceptible to declines that last longer than the short lived drops of the past 12 months.**

Where is the Opportunity?

Because of this belief I have positioned portfolios with global funds over the past year that can shift money to those markets at any time and move away from the North American markets if they start to fade. Moving to 100 percent cash isn't out of the question and actually occurred in one fund I use back in mid-January. As well, I have begun moving clients into **International Funds to get exposure to UK, China and other parts of Europe** and will continue to do this in the coming 6 months to 12 months, as it's a good time to invest when people are uncomfortable.

To illustrate the lopsided sentiment of investor sentiment, I have the chart below. Basically what it illustrates is the positioning in different markets, sectors, and currencies in July as compared to history. The Red List are parts of the market that are under-invested compared to history and the Blue List are those that are over-invested.

Exhibit 6: The Longs & Shorts, relative to Global FMS history*



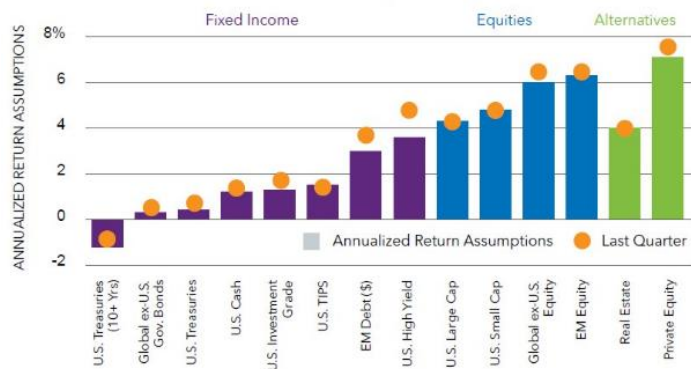
Source: BofA Merrill Lynch Global Fund Manager Survey

A contrarian would say that these trends always reverse, so there are opportunities in the Great Brittan Pound, UK & Eurozone Equities, Energy, Materials, Japan and Emerging Markets. The flip side is to focus on the crowded sectors being Real Estate, Tech, Pharma, Discretionary, Utilities and the U.S. These are areas of the market they have potential risk of underperforming as investor allocations rebalance towards averages.

The next page has a chart from BlackRock, which shows their 5-Year Asset Class Return Assumptions, as of July 2016.

CHART OF THE WEEK

BlackRock's Five-Year Asset Class Return Assumptions, July 2016



As one can see here too, the expected return on U.S. Large and U.S. Small cap companies is somewhere between 4-5% annualized, whereas Global ex-U.S. Equity expectations are 6%, and Emerging Market Equity is slightly above 6%.

Another benefit to the portfolios because of the geopolitical risks is **the strength in the Gold price and also the value of the gold shares**. A majority of my clients who fit the investment objectives to hold these investments should have noticed the **excellent performance of their gold investments in recent statements**.

The **price of gold was up \$100 per ounce the night of the Brexit vote**, and has moved up a lot since then. However, even before the UK vote, Gold had started the next "up leg" in [what I believe is a multi-decade Bull market for gold and silver and I have had this discussion with all my clients for years.](#)

I want to thank clients who have been with me for the past several years, who have trusted in this part of our investment strategy and many who also had the confidence to take my advice to add to their gold positions when they were in a losing position. It was a tough time for that part of the market, and not a fun time, but looking back at it now it can be seen that the decisions to hold tight, and even add to the sector was the right thing to do and investors are now being rewarded rapidly in 2016.

Non-Portfolio Benefits

Lastly, the **non-portfolio benefits** of these geopolitical risks **are the resulting lower interest rates** that seem likely to **remain for longer than expected just** one year ago. This opportunity may last for a long time, but could easily go away next month.

You may hear about **negative interest rates** in the media on bonds around the world. If so, and even if not, **what needs to be understood is that there are over \$11.7 Trillion in Sovereign Government Bonds (and growing) around the world that provide a negative return** (as per an interview with BlackRock Fixed Income CIO, Rick Reider, on CNBC June 29th).

I will mention this again. **There are currently likely more than \$12 Trillion of bonds that if you bought today you will guarantee yourself to lose money for the term of the bond!** Much of this is because European, Japanese and other countries overseas are **printing money to purchase bonds** to keep their value up and **keep interest rates low** (when a bond goes up in price, interest rates fall. Therefore printing trillions of various currencies by governments to buy bonds pushes their prices up and rates fall, to the point that there has become no expected return on the bond). For **Investment portfolios it doesn't provide returns we have seen in the past, however, the non-investment opportunities are what's most important for my clients to pay attention to.**

If **you have debt on your house or a second property or a line of credit**, you may soon see rates decline because our bond markets in Canada and the U.S.A are starting to replicate the European and Japanese markets. **When rates on bonds fall, so do the fixed rates on mortgages.** If they aren't falling, you at least are now **likely to have a longer period of lower rates than would have been expected last fall** when the U.S.A discussed raising rates 4 times in 2016 (so far they haven't done it once).

I also believe the odds of the U.S. having to introduce stimulus again (money printing) within the next 12 months is high, based on my views of the U.S. economic conditions. This would be in the form of more bond purchases (**keeping rates low**) and the Canadian Bond market is likely to react similarly as it normally does.

We are already seeing the yield on Canadian Government Bonds fall in July, therefore **I want to mention that you should be trying to pay off debt at any opportunity possible because when rates are low, a lot of your payment goes straight to principle.**

Important considerations:

I recommend that if your Fixed Rate mortgage doesn't come up for renewal for another couple years, but fixed mortgage rates in the next while on new 5 year fixed terms are quite a bit lower than your current rate, you should find out what it would cost to "blend and extend" your mortgage. What this means is you can bust your mortgage but rather than payout the penalty, the bank just gives you a rate that isn't quite as good as a brand new mortgage, but it's better than you have now.

For instance, if you have 2.5 years until your mortgage renews and your current rate is 3.30%, but you see new 5 year fixed rates advertised at 2.50%, you could ask your mortgage professional if you can break out of your mortgage early to extend for a new 5 year term at a rate somewhere between 2.50% and your current 3.30%. Because there will be a penalty, your new rate might be offered at 2.70% to 3%, which isn't as good as 2.5% but you are much better than 3.30% and extending your low rate for an extra 2.5 years is a good thing! **The reason to do this is because you don't know how long rates will stay low and when they do begin to rise, they are likely to rise rapidly** because of the efforts to keep rates lower for as long as possible. In other words, the interest rates are being kept low by Government strategies because of high levels of global debt, and at some point their efforts will be less effective and we will see rates rise rapidly in my view. I just don't know when it could happen.

Many clients don't have mortgage debt, and so this strategy doesn't pertain to you. However if this is the case, **I still encourage you to pass this newsletter along to your adult children or other family and friends who may be in a debt position, to get them thinking about debt reduction and accelerated debt repayment while it doesn't cost a lot to pay back.**

I can't personally do mortgages, but rate direction is market driven so I can provide my views. If anyone needs info on the strategy above I can always connect you to one of our **Specialized Lenders** to discuss the options and impact of making changes like these to their debt structure.

To close out this edition of the High Level Investment Report, I want to wish everyone a wonderful summer.

Enjoy time with family, and try not to think about investments, as that's my job for the summer for you!

Take care,

Ryan Cockburn