Portfolio Management Commentary

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In stark contrast to the end of 2018, the first quarter of this year has shown some signs of life and encouragement. The lows on December 24, 2018 brought us within a percentage point of a bear market, but the buying cavalry came to the rescue and quickly started the reversion. So where does that leave us and the investment climate for this year? Well, I think the following three themes will play out for the remainder of 2019:

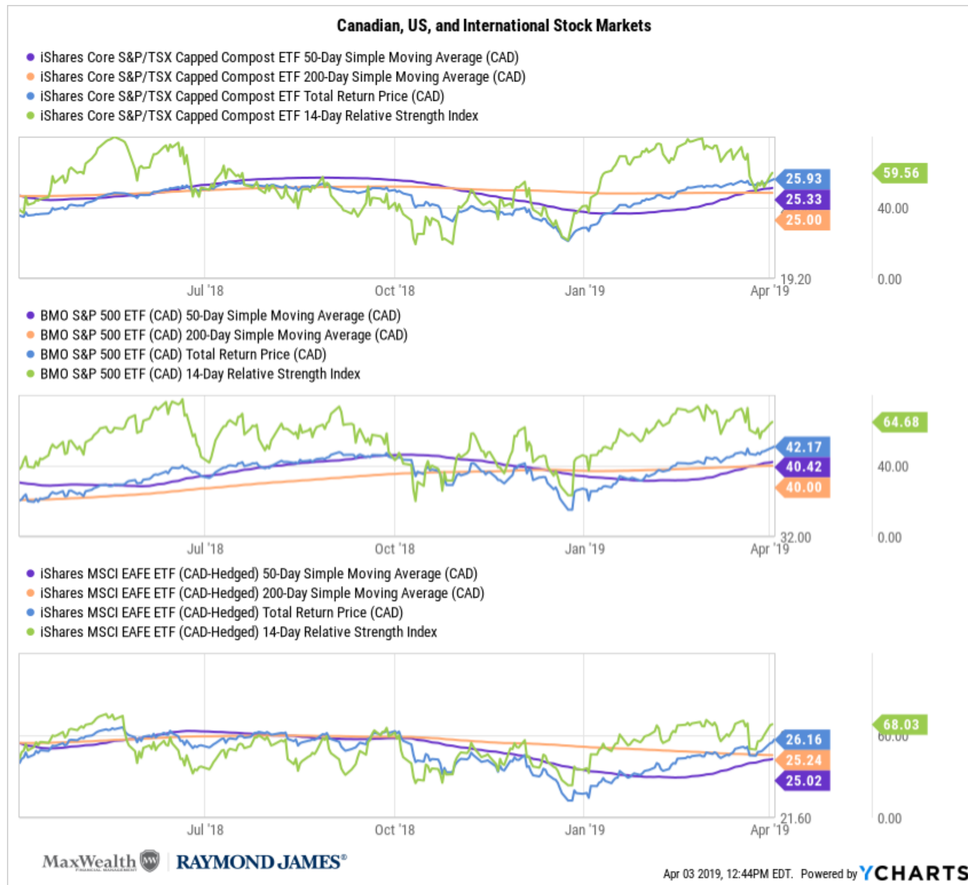
- **Don't Fight the Fed!** The US Federal Reserve has been very vocal about the pace and magnitude of future interest rate increases. This is generally seen as stimulative for the economy and the stock market. I think the Bank of Canada has a similar philosophy. Stephen Poloz, our governor, will have a tough time raising rates when personal debt loads in Canada are at record levels.

- **Stay Disciplined!** There is no need to chase assets, returns, or hot stocks. Invest in a diversified basket of assets and keep a little extra cash on the sidelines when the risk-to-reward equation is negatively skewed. Have a neutral view versus one overly optimistic or punishingly pessimistic. The truth is always between these polarities.

- **Give it Time!** Impatience is the kryptonite of investing, so remember it takes time for investments to reach their full potential. You didn't give up on your children the minute he/she started to walk. Consider this fact when you review the positions you hold as they are not all outperformers.

As we enter the 2nd quarter, I suggest some caution with our expectations. While there has been some progress on the US-China trade dispute, the deeper issues of intellectual property rights, unauthorized surveillance, and possible corporate espionage will take time to work through. This should cause more volatility in the near term. I see this as an opportunity to acquire assets at better valuations. Composite economic data suggests a slowing of the global economy. This should be carefully watched. I know the "R" word is being bandied about by the news these days, but slowing doesn't necessary mean contraction. Caution is warranted, but not pessimism. Once again, the opportunity exists for us to profit from a misunderstanding of the facts. We will look for quality assets at reasonable prices.

On a positive note, the visual picture of the markets looks very encouraging. All the major world indices are now above their 50- and 200-day moving averages and their short-term momentum (14-day RSI) has confirmed this move higher. I suspect we may see a pause here as investor's approach the all-time highs of last September and become more tentative in committing more capital. Interestingly enough Canada is the first to overcome the previous highs. From a longer-term perspective this is a positive development and supportive of Jeff Saut's, Raymond James' chief market strategist, thesis that the secular bull market still has years to run. Canada's market is basically in three main categories: financials, energy/materials, and industrials. If these sectors are showing improvements then that speaks well for future global growth and offers a nice counterpoint to the data discussed above.



Your Portfolio

We made some positional changes to most of the portfolios back in mid-January. We sold out of COW (iShares Global Agriculture ETF) and booked a small profit. Clearly this was done too early as the position rallied another 8%, but hindsight is a luxury only after the fact. For the Balanced Income & Growth Portfolio, we exchanged our holding in ZDY (BMO US Dividend ETF) for ZLU (BMO Low Volatility US Equity ETF). This was done to counteract the anticipated increase in volatility for the coming year. So far, the performance is roughly equal, but I believe we will be rewarded for this tactical shift later in the year. The Disciplined Growth Portfolio sold the XCG (iShares Can Growth ETF) and the (iShares S&P US Mid-Cap ETF) because of low trading volumes and replaced them with XIU (iShares S&P/TSX 60) and ZLU (BMO Low Vol US Equity). VEE (Vanguard FTSE Emerging Market All Cap ETF) was also added to the Disciplined Growth Portfolio with a 5% weighting. This gives us some exposure to the future areas of economic growth at compelling valuations. As mentioned in a separate email, we closed out the “gold rush” trade and booked a healthy profit for the Disciplined Growth Portfolio. The other area of the greatest change was a repositioning of our fixed income holdings. This was largely focused in the Income Builder Portfolio and Balanced Income & Growth Portfolio. For starters we sold our Canadian corporate bond holdings (HAB) and reallocated the capital to ZAG (BMO Aggregate Bond Index ETF) to upgrade the quality of the fixed income holdings. The average credit score goes from BBB to AA. We also trimmed our holdings in ZEF (BMO Emerging Markets Bond) and HPR (Horizons Active Preferred Share ETF) to increase credit quality and we used the proceeds to add to ZAG. ZAG has a longer maturity time horizon and I wanted to increase this as I believed that Canada was not going to raise interest rates. As of this date this has been the correct call, and given the most recent stance from the Bank of Canada, I do not see the path to higher rates at this time. For the Income Builder Portfolio we added a new position called PIMCO Monthly Income. PIMCO are the world’s largest active bond manager and they have extensive experience is generating quality returns for clients. We added this position for the yield and exposure to the US.

Final Thoughts

The start of 2019 has been positive for investors and reflected nicely in your quarterly returns. Almost overnight the mood has shifted from one of extreme negativity to one of hope and prosperity. My suggestion is to temper your emotions and recognize that one quarter means very little in the overall scheme of things. Markets have a way of regressing to the mean and I am sure that 2019 will be no different.

A final point is worth mentioning before I close my comments for this quarter. Be skeptical of comments made on or about the yield curve. While its inversion has been shown as an effective predictor of recessions there tends to be a lot of debate on which yield curve to use. Is it the 2-year and 10-years, the 3-month and 30-year, etc.? Also, the timing of the recession call is quite a bit after the inversion, at the steepening, and capital markets tend to do quite well for the next 12-16 months. Once again be careful with comments made out of context and without the support of further economic/market deterioration.

If any of the points mentioned peak further interest in you please reach out to me for a more in-depth discussion.

Many Happy Returns,

Patrick

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