



Portfolio Managers Commentary – Q2 2016

“There is virtually always an apocalypse du jour going on somewhere in the world. And on the rare occasions when there is not, journalism will simply invent one, and present it 24/7 as the incipient end of the world..” – Nick Murray

Why we buy what we buy

In the first quarter commentary, I talked about stocks and how the collective wisdom of the market values, or prices, companies. Continuing on with that theme, it’s important to understand why I may recommend a particular stock, bond, or any investment for one person, and why that same security may not be appropriate for another.

In some ways, it’s fair to ask, “Why is ABC, Inc. a good fit for Barry but not for Susan?” I’ve often compared a carefully crafted investment plan to a financial roadmap. When you embark on a vacation, a roadmap is the essential tool that keeps you on the road to your final destination. The same holds true for your financial destination, or what I like to refer to as your financial goals. What’s necessary to get one individual to his or her destination may not be appropriate for someone else. Everyone starts at a different place and has different needs.

Think of it another way. Let’s say two people are interested in becoming physically fit. One of them is training for his or her first marathon and another hopes to become an accomplished tennis player. The weekly regimen a physical trainer would prescribe might include some of the same exercises, say warm-ups and stretches, but the similarities may quickly end at that point.

The same holds true for retirees Bob and Sally, whose financial plan is primarily designed for income and the preservation of capital, as compared to Linda, who won’t be retiring for another 25 years. Unlike Bob and Sally, Linda may have a much larger concentration of stocks and more aggressive investments that simply aren’t the right fit for Bob and Sally.

Linda isn’t nearly as concerned about a steep sell-off and might even relish the opportunity to buy more shares in the event of a decline. However, Bob and Sally must take a much more cautious approach. Hence, what I might recommend for one person, I do not recommend for another.

Simply put, much like an exercise plan, recommendations vary based upon individual goals and tolerance for risk and volatility.

Eschewing the flavour of the month

By taking such an approach, we may choose to avoid stocks that are hot today, or tips you may have heard from acquaintances. To visualize it yet another way, each investment sits in your portfolio for a reason, much like a piece in a puzzle. And a piece that fits into one puzzle may not be right for another puzzle. Whatever your goals may be, the asset allocation we recommend is designed with your objectives in mind. Choosing investments outside the chosen strategy can lead you astray.

I'm proud to say that all of the portfolios we manage held up extremely well during the recent British Referendum, validating our disciplined approach to investment management.

Political tremors create economic waves

I don't want to spend too much time talking about the referendum but there are a few points I want to touch on. As you recall, on June 23rd, the UK voted in a nonbinding referendum to exit the 28-nation economic and political bloc called the European Union. Though "Brexit" was chosen by a narrow margin, the people had spoken.

Given that it's a nonbinding referendum, British lawmakers could ignore the results. While there has been some talk that a UK exit will never happen, at this juncture, it doesn't seem likely the referendum will be ignored. Nonetheless, a victory by the "Leave" camp wasn't supposed to happen. While the vote was expected to be close, pollsters, analysts, and even the bookies who took bets all projected "Remain" would squeak through with a win. In advance of the vote, stocks rallied in anticipation "Leave" would go down to defeat.

Whether good or bad, continuity usually benefits markets because it provides certainty. However, markets hate *heightened* uncertainty. More accurately, short-term traders dislike added uncertainty and are much quicker to hit the sell button than longer term investors, who are more tolerant of disappointments.



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Why might this event be viewed as heightened uncertainty? Well, we're in uncharted waters. No nation has ever asked to leave the EU. Could Brexit fuel other separatist movements and create additional economic uncertainty in Europe? Might we see the euro currency, which is shared by 19 nations, begin to unravel? How might this pressure an already fragile European banking system? And will the U.S. dollar begin to strengthen as global investors see the relative safety of the U.S. as a shelter from the stormy global environment?

While these are longer-term concerns, there were a couple of immediate casualties. British Prime Minister David Cameron, who was adamantly opposed to Brexit, quickly resigned and the British pound fell to its lowest level in over 30 years.

Looking ahead

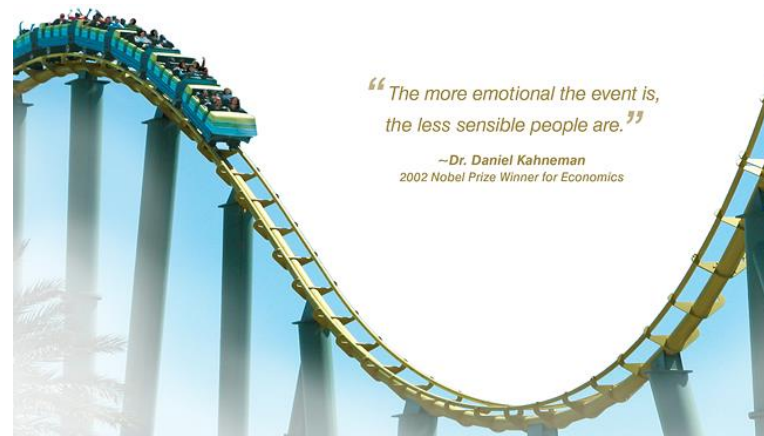
The irony of the outcome of the Brexit vote is that the London Financial Times Stock Index known as the FTSE 100 or Footsie for short; broke out to its highest level in 11 months! At the same time, the stock markets in Germany, France, Spain and Italy are still toiling near their lows. The market has cast its own vote on the outcome of the election and its looking pretty good for the U.K. and not so good for the rest of the Eurozone.

In fact, around the world we are seeing some very bullish chart patterns emerging in the major international markets, particularly in Asia and North America. Leading the way are U.S. stocks as the S&P 500 Index closed at a record high as of the writing of this commentary. U.S. bond yields are at record lows and corporate bond yields are at their lowest level since the 1950's. Capital has very few options remaining suggesting further inflows into large, good quality dividend paying companies.

The search for yield has helped boost the performance of the focused dividend strategy portfolios we manage. The year to date returns for our Growth, Balanced, and Conservative investment mandates has been very strong and the asset allocation is well positioned in anticipation of further gains for the remainder of the year.

What's an investor to do?

Control what you can control – the investment plan – and be very careful about making a rash decision based on an emotional selloff. Stocks took a beating in the wake of the Brexit vote but quickly recovered nearly all of their losses by the end of June. I understand that most investors don't fully understand the impact of what just happened in Europe in relation to their investments. Honestly, many analysts would concede there are many unknowns.



My goal, however, is to keep you focused on your financial goals and objectives. Emotionally based decisions rarely work out in your favor. Whether large or small, whether highly sophisticated or simply a novice, investors price stocks through their collective buy and sell decisions. When new information is disseminated in the marketplace, stocks may react either positively or negatively, depending on how the information is viewed.

By itself, the UK's economy won't send the U.S. economy into a recession. But Brexit creates a new level of uncertainty and risk. However imperfectly, investors attempt to discount the event, pricing in how it may affect the U.S. economy and corporate profits.



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Final thoughts

Democracies can sometimes be messy. What just happened in the UK and the gridlock in Washington are just a couple of examples. I believe Winston Churchill described it well when he said, “Democracy is the worst form of government, except for all the others.”

While we do not know where the waves of populism that are swelling in the U.S. and Europe may take us, they represent the will of free citizens. Democratic freedoms enable the ordinary to do the extraordinary; to innovate, create wealth and fuel new economic growth. True, free elections aren’t always neat and tidy, but history strongly suggests they are a vital ingredient for long-term economic success.

I hope you’ve found this commentary to be educational and helpful. Thank you very much for the trust and confidence you’ve placed in my team and my firm.

Sincerely,

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