Money Never Sleeps

The Newsletter for the Informed Investor

Wealth Management
Dominion Securities

New Year 2017

Vito Finucci, B.Comm., CIM, FCSI
Vice-President & Director,
Investment Advisor
Associate Portfolio Manager
519-675-2011
vito.finucci@rbc.com

Jodie Fuller
Associate Advisor
519-675-2511
jodie.fuller@rbc.com

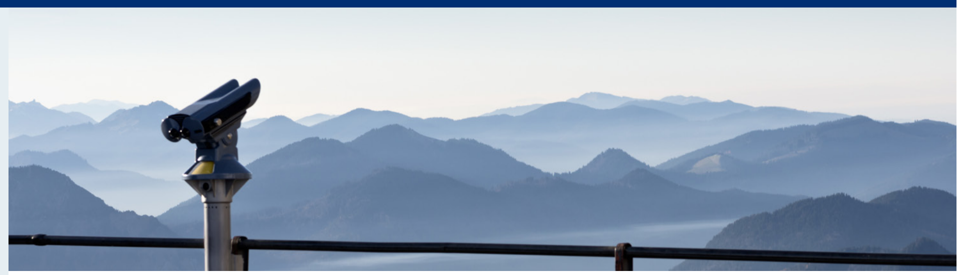
Sarah Smith, CIM, PFP
Associate Advisor
519-675-2505
sarah.e.smith@rbc.com

Jessica Basacco
Administrative Assistant
519-675-2021
jessica.bassaco@rbc.com

Gary Weatherup, CFP
Associate Advisor and
Financial Planner
519-675-2021
gary.weatherup@rbc.com

Fax: 519-675-2020
www.rbcds.com/vito.finucci

RBC Dominion Securities
148 Fullarton St., Suite 1900
London, Ontario N6A 5P3



The Donald, bulls and bears (oh my!)

Bull has a long way to go still, but may need a pause first

" 'Need' now means wanting someone else's money. 'Greed' now means wanting to keep your own, and 'Compassion' is when a politician arranges the transfer."

– American Journalist Joseph Sobra (1946-2010)

Over the holidays, you get bombarded with reviews of the past year and forecasts of 2017. I read them all, but don't put much faith in them. I have no idea what will transpire in 2017. Who predicted the Brexit vote, the Trump win, or the Cubs winning the World Series in 2016? Not many people.

In this world of growing populism, elections that throw the polls out the window, and geopolitical risk everywhere, most forecasts are just personal opinions and outright guesses.

So while the usual bull/bear debate rages on, if loyal readers will indulge me, I'd like to change the format of this issue a bit. Here's what I know:

Looking back

1. **The year 2016 was a U.S. presidential election year, and it played out as most have since 1950s.** We had a tough first quarter, down 10-12% by the end of February. We regained most of it (8-9%) in March/April, then we went sideways most of the summer. That was followed by a pullback in fall (we were down 5% in October), but ended with a decent fourth quarter where pretty well all returns for the year were made (bang on in the U.S.A.) So 2016 followed the template pretty closely.

2. **The market's start in the first two months of 2016 was the worst start to a year…ever!** (As measured by the S&P 500, down 10.5% for the month.)

3. **But the S&P 500 is now up eight years in a row:**

2009 +25.9%	2010 +4.8%
2011 +2.1%	2012 +15.9%
2013 +32.2%	2014 +13.5%
2015 +1.4%	2016 +11.9%

If 2017 is positive, it would tie the all-time record of consecutive calendar gains which occurred from 1991 to 1999.

4. Biggest winners in 2016? Everything all those forecasts from last January said not to buy: Brazil (+59%), Russia (+43%), Energy (+24%), Gold (was +30% until July) among others.

5. Biggest losers? What some forecasters last January insisted were buys: Healthcare (down over 4%), Biotech (down 16%), Solar stocks (down over 42%) as measured by ETF "TAN")

6. Don't listen to the "sirens" (i.e. the media). Those who listened to the Royal Bank of Scotland call to "Sell Everything" on January 12 missed out on a decent year. Other "gurus" like Bill Ackman, Jeff Gundlach and Bill Gross had some tough calls as well. After the Brexit vote, the majority of the calls we fielded were not to "buy" but to "sell" because the media made it sound like Armageddon. While markets had a tough 48 hours, Brexit proved to be a great opportunity to buy.

Consensus too was that a Trump win would "tank" the markets and a "Brexit-like" plunge would take place. Well, they were right on that one, for about four hours between 11:00 p.m. and 3:00 a.m. on election night when S&P futures were down about 5-6%, while most North Americans were sleeping. But by the time markets opened, the rally had begun and was followed by eight consecutive up weeks on the S&P 500.

7. Lower oil prices are good for the economy? Oil prices collapsed in January and February getting down to the high 20s and stock markets got hammered with it. It wasn't until oil prices settled and started to rally. The markets did the same thing in the fourth quarter – oil prices rallied and markets did as well simultaneously.

Stuff to make you say "Hmmm …"

1. President Obama remains the only President in all of U.S. history to never have a single year when the economy grew at least 3%, even with having two terms in the White House (as measured by U.S. GDP):

2009 -2.8%	2010 -2.5%
2011 +1.6%	2012 +2.2%
2013 +1.5%	2014 +2.4%
2015 +2.4%	2016 +2.2%

(Source: www.bea.gov/national/gdp)

Trump's proposal to cut corporate taxes from 35% to 15%, his pledge to cut waste and corruption, and reduce regulations, might be just enough to give him a 4-5% GDP? The dark days of "tax and spend" policies are giving way to an era of fiscal stimulus and pro-growth legislation not seen in 30 years.

2. The bearish perspective:

- Valuations by historical measures, are getting expensive. Doesn't mean high valuations can't go higher, but then it pulls future returns lower.
- Retail investors at 30% of total assets in the markets are near historically high levels (contrarian indicator).

Annual S&P 500 Gains/Losses Without Dividends Since 1950
Mid-Cycle Years Highlighted

Source: LPL Research, FactSet 11/30/16

All indexes are unmanaged and cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. All performance referenced is historical and is no guarantee of future results.

*Indicates first year of each four-year presidential cycle. Mid-cycle years (highlighted) are defined as more than a year away from the start or end of a recession.

Year	Winning President	Party	Return from Election Day Till Inauguration Day
1952	Eisenhower	Republican	6.3%
1956	Eisenhower	Republican	-6.7%
1960	Kennedy	Democrat	8.8%
1964	Johnson	Democrat	1.7%
1968	Nixon	Republican	-1.4%
1972	Nixon	Republican	4.2%
1976	Carter	Democrat	-0.1%
1980	Reagan	Republican	2.0%
1984	Reagan	Republican	2.8%
1988	Bush	Republican	4.2%
1992	Clinton	Democrat	3.2%
1996	Clinton	Democrat	8.8%
2000	Bush	Republican	-6.2%
2004	Bush	Republican	4.0%
2008	Obama	Democrat	-19.9%
2012	Obama	Democrat	4.0%
		Average	1.0%
		Median	3.0%
		% Higher	68.8%

Source: LPL Research, FactSet 11/04/16

Year	President	Senate	House	S&P 500 Performance Feb - Aug	Sep - Oct	Nov - Jan	Whole Year
1960	Democrat	Democrat	Democrat	2.4%	-6.3%	15.7%	-3.0%
1964	Democrat	Democrat	Democrat	6.2%	3.7%	3.2%	13.0%
1968	Republican	Democrat	Democrat	7.2%	4.6%	-0.4%	7.7%
1972	Republican	Democrat	Democrat	6.9%	0.4%	4.0%	15.6%
1976	Democrat	Democrat	Democrat	2.0%	0.0%	-0.8%	19.1%
1980	Republican	Republican	Democrat	7.2%	4.2%	1.6%	25.8%
1984	Republican	Republican	Democrat	2.0%	-0.4%	8.2%	1.4%
1988	Republican	Democrat	Democrat	1.7%	6.7%	6.6%	12.4%
1992	Democrat	Democrat	Democrat	1.3%	1.1%	4.8%	4.5%
1994 (mid-term)	*Democrat*	*Republican*	*Republican*	*-1.3%*	*-0.7%*	*-0.4%*	*-1.5%*
1996	Democrat	Republican	Republican	2.5%	8.2%	11.5%	20.3%
2000	Republican	Democrat	Republican	8.8%	-5.8%	-4.4%	-10.1%
2004	Republican	Republican	Republican	-2.4%	2.4%	4.5%	9.0%
2008	Democrat	Democrat	Democrat	-6.9%	-24.5%	-14.7%	-38.5%
2012	Democrat	Democrat	Republican	7.2%	0.4%	6.1%	13.4%
Election years ex 2008 (avg)				3.7%	1.3%	4.3%	9.1%
All years ex 2008 (avg)				3.3%	0.8%	4.6%	8.8%

Election years in recessions are shaded
Election years with power shift from Democrat to Republican are boxed
1994 midterm election with congress power shift from Democrat to Repulican is marked in Italic

Source: S&P/Haver Analytics, Deutsche Bank

- Interest rates are rising (Wall Street Axiom = Don't fight the Fed).
- Trump takes over in an aging economic cycle, with the U.S. $20 trillion in debt, a $700 billion deficit, unemployment at 4.60%, tightening of monetary policy, and 80% of households fully leveraged with little free cash flow.

3. **Trump is a gemini.** Geminis are excellent communicators, known for their fast, clever and curious minds, and are expressive and quick witted. Geminis have two different sides of personality and you never will be sure with whom you will face. Geminis can be sociable, communicate and ready for fun, while on the other hand, it can be very serious, thoughtful, restless and even indecisive. (Source: Astrology.com).

Sorry folks, had to put that out there since no one else has!

4. **If history is a guide…**

- The Fed is tightening, not easing, and in the past six decades, 10 of 13 such cycles ended badly for the economy.
- This is an important one! Every Republican President since Eisenhower oversaw a recession in the first half of their term, regardless of who had control of the House and Senate.

Looking ahead

Since 1950, the first year of the President's term returned only 6%, the worst out of the four years. Year three is historically the best with a +16% gain on average, so a big difference.

Interestingly enough, if you start in 1997 (the first year of Bill Clinton's second term) the first year of the presidential cycle has been +14% on average and has been the best of the four years, topping the 9.7% gains in year three.

What happens from election day to inauguration day?

We've had an 11-12% rally on the S&P 500 since election day. Similarities are being drawn to Trump's victory to that of Ronald Reagan's. The latter has a 9% market increase from election day to inauguration day, only to be followed by a recession and a 20% market decline at one point in his first year as President; but finished with a +33% gain in 1980.

Summary

As we head into 2017, trying to predict the markets is often quite pointless. We end 2016 with a market that is short-term "overbought" with perhaps too much optimism near term but with a longer-term secular bull market in place.

Investors who were resigned to more years of stagnant growth were caught off guard with the regime shift with Trump. All of a sudden there is a pro-growth and "reinflation" trade happening and the market has "recalibrated" itself accordingly. Now it will come down to: will the reality match the hype?

The "melt-up" we've had could go on for a bit longer, but then the earnings will have to match up to sustain valuations. Comparisons to the early 1980s and Ronald Reagan are common, but this is 2016, not 1980.

Debt levels are much higher, interest rates have been going down for 30 years, and we are at the end of a demographic baby boomer "boom," not the beginning. Trump also has headwinds against him in the forms of technology advancements and globalization, both of which have been job killers in the U.S.A.

The consensus trade remains a strong U.S. dollar, sell gold, benign inflation, and commodities which as measured by the CRB Index hit a 45-year low in 2016 (since 1973) are "verbotten." I would guess consensus will be wrong once again.

I believe we remain in a secular bull market that began in 2009, broke out in 2013 and again late 2016, and has years to go. Will we have pullbacks/corrections? Of course, but they allow investors to reload every time that bogeyman pops up now and then.

The President-elect himself stated on December 17 that he will do his best to "keep it going."

"I'm honoured by the bounce. They're all talking about the bounce, so right now everybody in this room has to like me at least a little bit, but we're going to try and have that bounce continue."

Everyone who has bet against him has been wrong so far.

Around the globe

Canada (Selective Buy)

- Stimulus package kicks in 2017, but suffering from structural and cyclical contraints, especially in energy and resource patch.
- Canadian economy remains highly dependent on oil.
- BOC not in a rush to tighten.

U.S.A. (Strong Buy)

- U.S. dollar strength carries on. Fed Reserve has shifted policy
- Foreign policy will be more "muscular" under Trump
- Consumer back in game, U.S. businesses more optimistic
- If markets can shift to earnings driven, huge upside potential
- Biggest wild card is the President elect and his policies

Europe (Hold)

- How Brexit will actually be implemented will weigh in 2017
- Populism on the rise – Germany, France and Netherlands have elections and Europe remains vulnerable to both populism and protectionism
- Risk of sovereign default (Italy?) rising

Asia (Avoid)

- Japan has had negative rates for over two years and "umpteen" stimulus packages with little effect
- China remains a question mark but downside risks in immediate future seems to have ebbed
- Territorial disputes continue (North Korea – who knows?)

Emerging Markets (Avoid)

- Strong U.S. dollar hurts on top of debt levels
- Russian reemergence with a "friendly" USA
- If commodities have bottomed, will help Brazil, Russia and other exporters
- If Trump's election creates rising protectionism, will hurt EMs.

Notes

- Hillary Clinton's campaign spent a whopping $1.2 Billion, a record amount, on her second failed bid for the White House, according to the New York Post, and twice as much as what Donald Trump spent ($600 million), reportedly $66 million of which was his personal money. (Source: New York Post)
- Windy City? The city of Chicago had 762 murders in the year 2016, a sharp rise from 492 in 2015. (Source: Wikipedia)
- Uber effect? New York City tax medallion prices hit a peak of just over $1 million in 2013-2014. Once Uber entered the picture, prices fell, and as of the end of 2016 are just above the $500,000 level. Disruptive technology? You bet. (Source: NYcitycab.com)

A special welcome to all new clients who have joined us

Thank you especially to clients who have mentioned our name to people they know. As a sign of gratitude, four times a year we'll randomly select a client who has introduced our services to a friend for special acknowledgement via a nice dinner at one of the finer restaurants in London.

Congrats, Donna B., our winner this quarter!

Please don't keep us a secret!

We are very happy and proud of the clients we serve in our practice and we are always open to serve more clients just like you. Should you be talking to someone who is unhappy with their current advisor, or would like a second opinion, we would be grateful if you passed on our numbers: 519-675-2011 or 1-800-265-5911. Thanks for keeping us in mind.

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