

The O'Neill Wealth Management Group



Wealth Management
Dominion Securities

Q1 Executive Summary

The O'Neill Wealth Management Group
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We believe in helping clients build a better future. It is our purpose to be clear about each client's unique vision for their future, so together we can be confident it is achievable.

Confidence is built by being disciplined, employing a proven process systematically and consistently over time. This includes proper planning, evaluating current circumstances, and having a framework to make adjustments as personal conditions and priorities change. We set targets for how much to spend, save, and grow (return) over appropriate time frames. Suitable parameters and boundaries, in a personal Investment Policy are designed to successfully meet future goals, while managing risk along the way. A set of guiding principles for investment decisions takes into account the evolving *macro-view* for the economy, as well as developments at the sector and company level, so the Investment Strategy remains focused on real fundamentals, emerging risks and quality metrics. This discipline avoids complacency during good times, and panic during more challenging periods.

The New Year started on a positive note with strong performance from 2017 providing momentum for equity markets. The Global macro outlook was positive, the economic backdrop quite good on the heels of U.S. fiscal stimulus and a successful U.S. Tax Reform bill. Measured at US\$1.5 Trillion over the next decade, RBC Global Asset Management (RBC GAM) equates this to a possible +0.4% to GDP in 2018, and +0.3% in 2019. This is meaningful for corporate profit growth, which has been a positive contributor to investor confidence.

A correction that many would argue was overdue, arrived in February without a particular catalyst. Seemingly the market was responding with concern over higher inflation and interest rates, even though these were not new developments. As the quarter progressed into March, volatility in both directions continued. The S&P/TSX, Dow Jones, and S&P500 all ended the quarter in negative territory, ending a nine-quarter winning streak for the S&P500.

Despite the relative strength of the global economy, the most prominent risks to the continued expansion are themes we have been talking about for some time, namely the aging business cycle, and protectionism. It is important to distinguish "late-stage" from the "end of the cycle". The expansion is still underway, however we must be realistic and recognize that it will not continue indefinitely. The "late-stage" indicators include tighter financial conditions in the form of higher interest rates, rock-bottom unemployment rates providing less slack in the economy, and economic surprises that are becoming less reliably positive. Investor confidence is a key factor for supporting valuations. The recent pain inflicted in the US TECH sector for example has affected trust and confidence. Fundamentals remain solid and cash balances are rich, however as opposed to previous downturns, tech has not been viewed the 'safe haven' this time. With some of the positives fading, the impact of a breach of trust will be an overhang for a while.

The risk of protectionism is not new, but has definitely become more prominent this year. Now that the tax cuts are delivered, the White House has turned its attention to trade issues. U.S. tariffs are not just a risk, but an economic drag. NAFTA negotiations are ongoing, and China is in the crosshairs over intellectual property practices. The situation is fluid, though all is not lost, and with some luck, we could see the global economy largely unaltered. However, there remains an entirely conceivable scenario that includes a broader trade war which has the potential to offset the positives expected from U.S. tax reform. While he admits there is little precision to this analysis, Chief Economist for RBC GAM, Eric Lascelle assigns a 20% recession risk for the U.S. in 2018, and a larger 35% in 2019 as the cycle extends. Therefore we are more likely to grow than not this year, but the risks are building and cumulative.

Meanwhile the Canadian economy is facing its own challenges. After impressive economic growth in 2017, RBC Economics has lowered their estimates significantly to 1.75% in 2018 and 1.50% in 2019. Stability in oil prices has helped, however transport issues have limited the upside for Canadian companies. While OPEC appears committed to cuts, the U.S. is the new swing producer, responding to higher prices by rapidly increasing production. RBC GAM believes \$60-\$65 oil may be sustainable in the short-term, but in the medium to long-term, sees US\$50 as more realistic. Canada's growth challenges are due to two key themes; competitiveness and housing. Competitiveness is deteriorating due to falling U.S. tax rates, rising minimum wages, environmental regulations, and tariffs restricting exports. NAFTA is a material risk, with a "bad" outcome potentially subtracting up to 0.8% from Canadian GDP according to RBC GAM. Housing is facing a possibly more intense slowdown. The risk is elevated given the rapid rise in household debt and poor affordability. Regulators are finally serious about the issue, and as a result home sales have already come down. At a minimum it seems unlikely that housing will be able to continue to drive growth in the next 10 years as it has in the previous decade.

The increase in volatility this quarter is a reminder that we should not be complacent when markets are seemingly stable. This was a recurring theme during our reviews in 2017. Against a relatively constructive backdrop we maintained target weights for equities, but did so by frequently rebalancing back to the defined asset allocation percentages, in the form of profit taking on stocks. We have actively dialed back risk in our portfolios over the past several quarters in the following ways; rebalancing (described above); geographic and sector rotation in response to a dichotomy in valuations and/or concern about exposure to key risks, taking advantage of higher interest rates by moving to government-backed and other higher credit quality issuers and de-emphasizing corporate bonds. We have maintained flexibility with our "swing" positions which provide liquidity and offer a quick source of cash for purchase/rebalancing decisions. As risks were building we actively got more defensive, and prepared for opportunities ahead.

We expect more challenges in the coming weeks and months, as we gain clarity on key risks. As such, we believe it is prudent to expect lower rates of return on average and higher volatility in the near term. At the same time, you may expect every investment decision, financial planning discussion, and portfolio review meeting to consistently revolve around the common purpose of building confidence that your future is bright.

Wishing you a bright and beautiful spring!
Sincerely,

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Jennifer Shone
Investment Advisor

Dave Cajka
Wealth Advisor



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