

Clarke Wealth Management's Quarterly Newsletter



Wealth Management
Dominion Securities

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Clarke Wealth Management
RBC Dominion Securities Inc.

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Loonie Tunes

On the backdrop of the recent interest rate hike the Canadian dollar has regained lost territory, but current household debt and commodity prices may limit further upside. Weighing the factors that could further propel the loonie, we conclude that there is a stronger set of arguments to support that expansion may be difficult to achieve.

The recent sharp move higher in the Canadian dollar reflects a fairly optimistic view of the economy and expectations of meaningful interest rate hikes from the Bank of Canada (BoC). We believe the unwinding of a significant short position in the Canadian dollar has contributed to the magnitude of the move.

BoC policy shift spurred a surge in the loonie

The Canadian dollar currently sits at a nearly 2-year high at US\$0.80, following a 9% rally since early May. In a matter of six months, the central bank has shifted from having a rate cut 'on the table' in January, to implementing a 25 basis point (bps) rate hike in July. This shift in policy prompted a radical adjustment in market expectations and the Canadian dollar has been the best performing currency amongst its G10 peers since May.

The market is pricing a second 25 bps rate hike coming from the BoC in October, and the overnight rate reaching approximately 1.5% by mid-2019. We believe the BoC will need to not only raise rates, but also convince the market we are getting more rate hikes than are currently priced in for there to be a continuation of the recent moves higher in short-term yields which have translated into a stronger Canadian dollar.

Short veering may have played a role in the sharpness of the Canadian dollar's rally

The loonie's recent strength comes after a large net short position had been built in the currency, which left it vulnerable to a positive surprise. This generally runs counter to how the majority of market participants are positioned. With the Canadian dollar position now more neutral, we think demand for the loonie driven by short covering may be less of a driver going forward.

What could drive the loonie even higher?

The simple answer is a follow-through from the rebound in commodity prices. Stabilization in the commodity complex last year helped bolster confidence in the currency. Within the commodity complex, crude oil prices tend to have the largest impact on the Canadian dollar and have been the most important driver in recent years net to interest rate differentials. Oil is firmly in the middle of its recent US\$40-\$55 per barrel trading range, but a supply disruption or a geopolitical development could push oil toward the upper end of this range and extend the recent phase of Canadian dollar strength.

What could limit further upside or weigh on the loonie?

Elevated household debt could constrain the BoC's ability to meaningfully increase



interest rates and embark upon a traditional tightening cycle. A closer look at the evolution of Canadian household debt over the last 10 years points to a heightened amount of borrower sensitivity to interest rates. An approximate 300 bps decline in the effective interest rate over the last decade means that Canadian households are outlaying less in annual interest payments in 2017 than they were in 2007, despite carrying nearly twice as much household debt 10 years later.

Markets are pricing in more hikes in Canada than the U.S. over the next 12 and 24 months. This stands in stark contrast with RBC Capital Markets' most recent forecast which calls for three rate hikes from the BoC over the next 18 months, but five hikes from the Fed over the same time period. If the RBC Capital Markets view plays out, that would likely result in a weaker Canadian dollar.

Despite the recent string of softer economic data compared to improved readings in Canada we believe the U.S. economy is better equipped to handle higher short-term interest rates than the Canadian economy as its labour market boasts lower unemployment and higher wage growth, which filters through to a higher inflation profile for the broader economy. RBC Capital Markets is forecasting 2.8% GDP growth in the U.S. in 2018 versus 2% in Canada in 2018.

Concurrent with the BoC rate hike in early July, the banking sector regulator (Office of the Superintendent of Financial Institutions) released a draft proposal for mortgage underwriting guidelines that contained a

number of provisions that could cool mortgage originations. While this is only a proposed policy at the moment and much uncertainty exists, RBC Capital Markets recently noted that the adoption of some or all of the measures included in the draft guidelines could reduce the availability of mortgage credit. We believe this variety of tightening could reduce the need for the BoC to increase interest rates going forward.

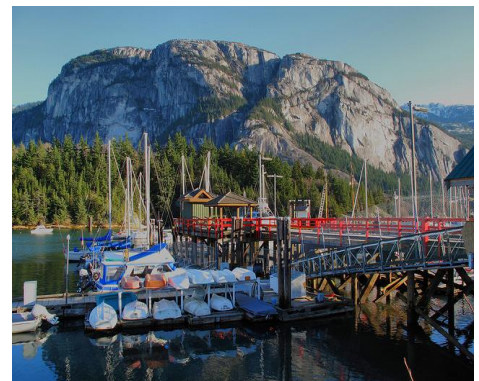
Closing thoughts: longer-term weakness likely

We are forecasting a weaker Canadian dollar over the medium term. Strength in commodities or continued gridlock in Washington are two of the more meaningful drivers that could help propel the loonie higher in the near term. But from a longer-term perspective we think the Canadian dollar already reflects an optimistic view of the direction of the economy and expectations of meaningful interest rate hikes from the BoC. We think the burden of expectations could eventually weigh on the currency.

10 Amazing Vancouver Hikes

Dog Mountain

A 30 minute drive from downtown Vancouver, this hike will take only about 2 hours to complete, but offers a beautiful scenic view of Vancouver's harbor.



Stawamus Chief

High above the town of Squamish the Chief is a popular hiking destination offering views of Howe Sound and mountains in Garibaldi Provincial Park. The Chief is one of North America's largest granite monoliths and is fairly difficult to complete consisting of three peaks.

Time to completion varies: the first peak is 4km and takes roughly 2 to 3 hours. The second peak, is the largest of the three summits, and takes most 4 to 5 hours. The third peak is 7km and should be given 5 to 7 hours.

St. Mark's Summit

Nearby Cypress Mountain, you must hike 11 km through the Howe Sound Crest Trail to reach the summit which boasts surreal views of the mouth of Howe Sound. Give yourself 5 hours to complete this scenic trail.

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If you're up for a challenge and would like to do a little camping, you can hike all 32 km of the Howe Crest Sound Trail in 1 to 2 days. There are other mountains along the trail with great views.

Mount Cheam

Mount Cheam is the highest peak in the Fraser Valley, and also claims some of the most spectacular views. One of the benefits of this hike is it's not that difficult with a logging road taking you to the base of the trail, from there it's about a 1 hour hike. On a clear day you can see Agassiz, Chilliwack and Fraser Valley.

Garibaldi Lake

This hike may seem endless at times, but the effort is definitely worth it once you see the turquoise coloured water of Garibaldi Lake. There is a beautiful campground along the shoreline if you'd like to stick around and watch the moonlight glitter on the water.

Mount Baker Recreation Area

Not in Vancouver, nor in Canada for that matter, this hiking destination offers a slew of other summer activities including horseback riding, camping and mountain climbing.

In the winter Mount Baker Ski Resort has some of the best powder to be found and is current reigning world champion for the most snow in one year.

Crown Mountain

In order to access the Crown Mount trail you will have to take the Grouse Mountain skyride. Just past the Grizzly Bear refuge the 5 hour round trek begins. This is not an easy

hike, but on a clear day the Capilano Watershed, the Lions Gate Bridge and Vancouver City are all visible from its peak.

The Binkert Lions

The Lions Gate Bridge is named after these two peak that are visible from Vancouver. This hike will take you 8 hours along the Binkert Trail, but you can also hike to the Lions from the Howe Sound Crest Trail that begins in Cypress Provincial Park.

This is likely the most difficult hike on the list, and you can only reach the higher peak (West Lion) as the East Lion is protected in the Vancouver watershed. Rock climbing equipment may be needed to summit the West peak.

Mount Seymour

A 5 hour hike from the Ski Resort parking lot along the edge of Mount Seymour's ski run will take you to the summit. There are amazing views of the Lower Mainland and Vancouver on the way.

Sendero Diez Vistas

Named after its ten views, this 4 to 6 hour hike offers views of the Indian Arm and Bunsen Lake in Belcarra Regional Park. On your way down you may want to take a quick drive to the nearby notoriously warm Sasamat Lake and go for a dip.



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Sean Sullivan has earned the Chartered Investment Manager designation

After receiving certification in Advanced Investment Strategies last year, Sean completed the Portfolio Management Techniques course in May of this year as well as the 2 years of work experience required to earn the designation. Completion of the CIM meets the regulatory requirement to be able to provide discretionary portfolio management and demonstrates proficiency and adherence to professional standards that enables one to become registered as a Portfolio Manager, Advising Representative or an Associate Advising Representative.

Some benefits of completing the CIM include:

- Proficiency to provide money management services to high-net-worth and institutional clients
- Comprehension of the application of portfolio management in the context of Canadian markets and regulatory requirements
- Ability to identify clients' objectives and constraints
- Competency to develop appropriate investment policies and strategies, taking into consideration market and economic conditions
- In depth understanding of analysis of investment products that represent both traditional and alternative asset classes
- Proficiency in the implementation of policies and strategies through portfolio construction
- Understanding of the techniques used to measure and evaluate portfolio performance

At Clarke Wealth Management we are dedicated to enhancing our knowledge base so as to be better able to service our clients.



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