



The Harbour Group of RBC Dominion Securities

Investment Strategy Update

September 2016 Conference Call



RBC Wealth Management
Dominion Securities



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OF RBC DOMINION SECURITIES

Executive Summary

- The ultra-low interest rates ushered in by the Brexit vote led stocks to new highs, but an increase in rates has brought on renewed volatility.
- Near record low yields combined with benign credit conditions have been a key force in pushing stock prices higher – the risk from here is a disorderly sell off in the bond market.
- This is particularly true on a sector basis, as “bond like” stocks have led in 2016 but have softened recently.
- We see potential risks headed into the fall as the U.S. election draws near and the Federal Reserve contemplates raising interest rates again.
- We do not expect either to derail the bull market, but don’t be surprised to see a correction.
- We believe we are in a firmly entrenched bull and that corrections are opportunities to buy, not sell.



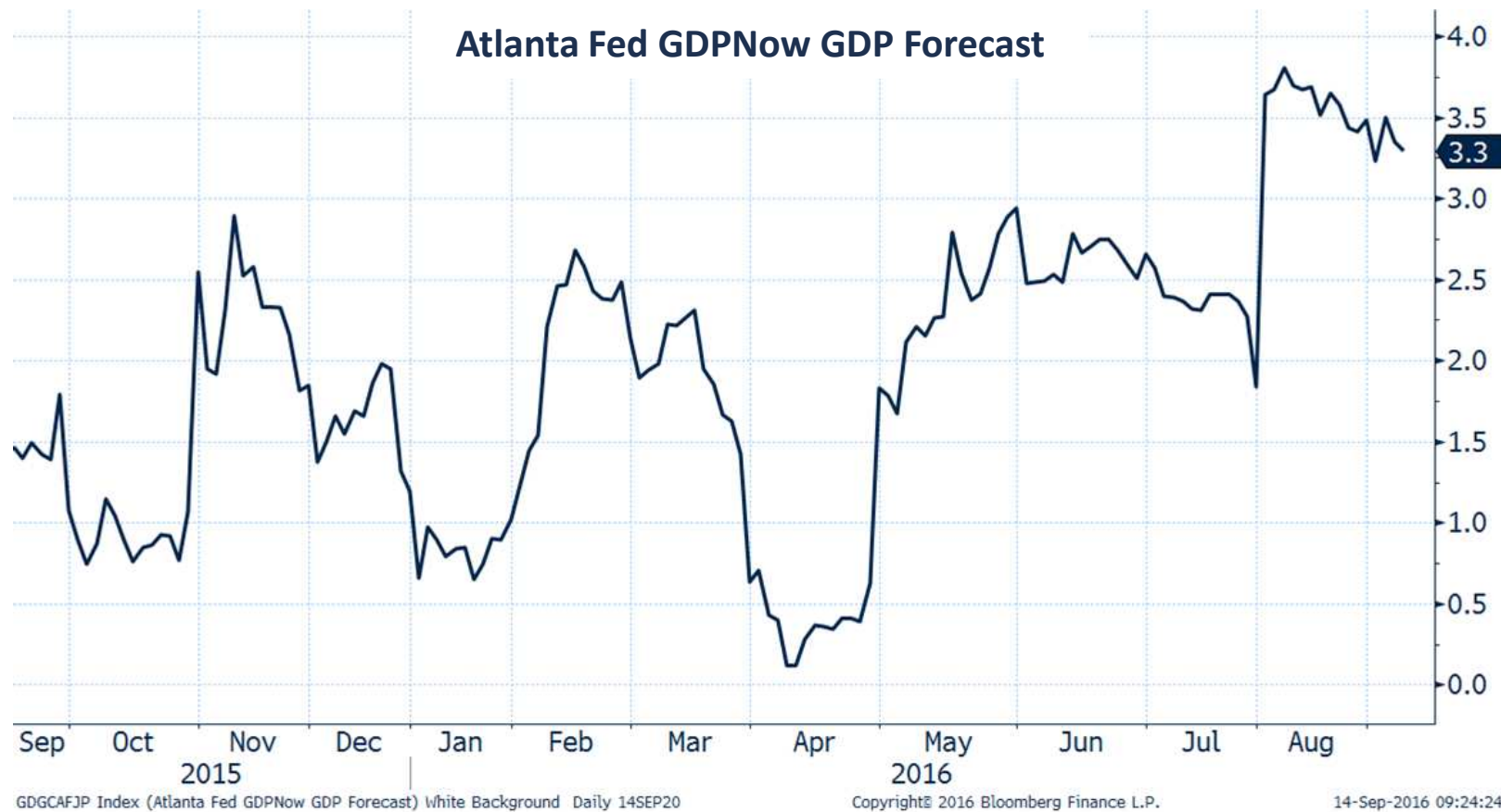
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Economic Data Suggests Continued Expansion

- Indicators from employment to manufacturing to inflation indicate recession risk is low.
- This has been corroborated by positive comments from management teams on recent earnings calls.



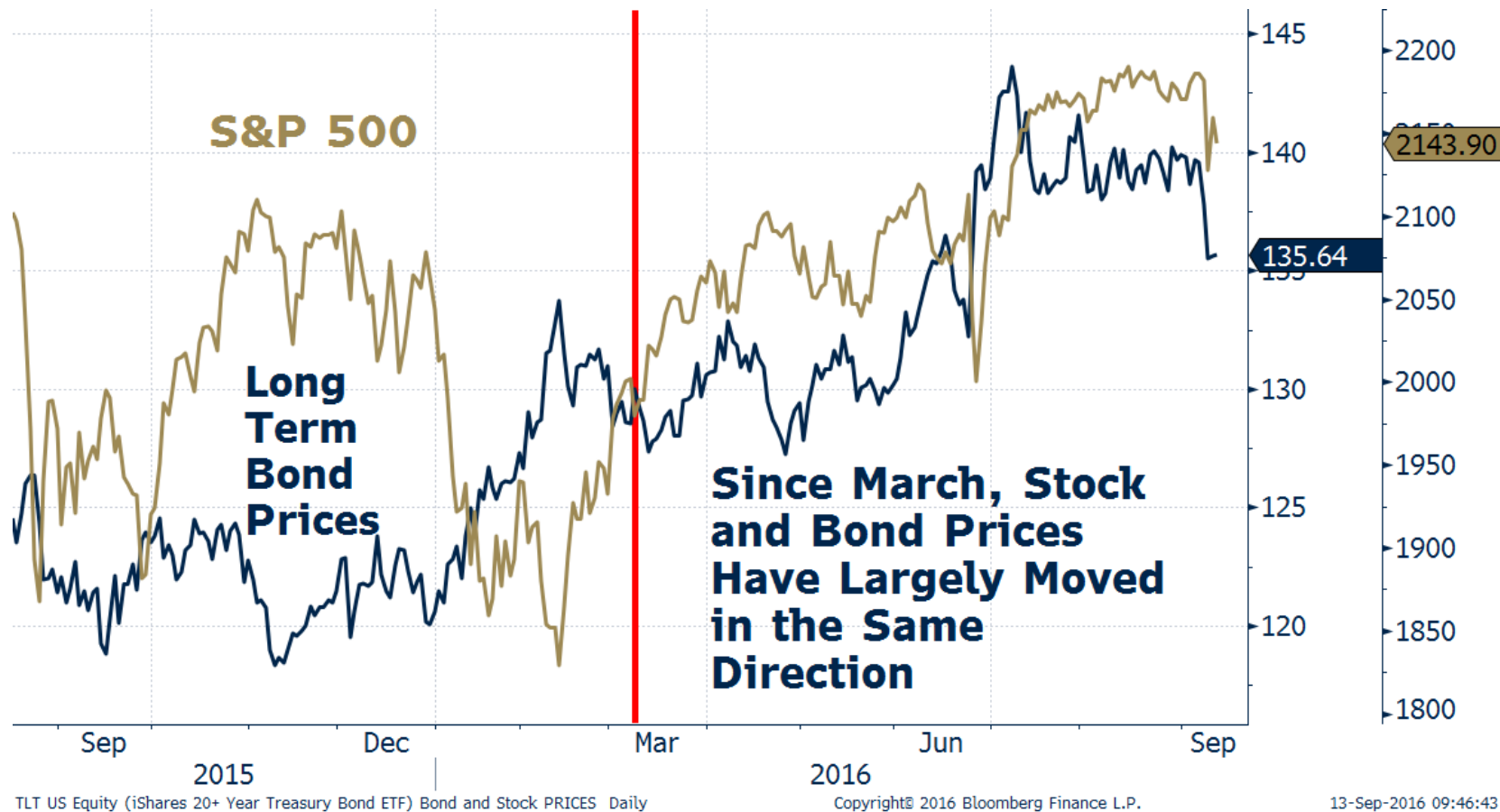
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Bond and Stock Prices Moving Together

- Continued ultra-low interest rates have led investors to re-rate stock prices higher.
- Given this relationship, keeping an eye on interest rates is as important as ever.



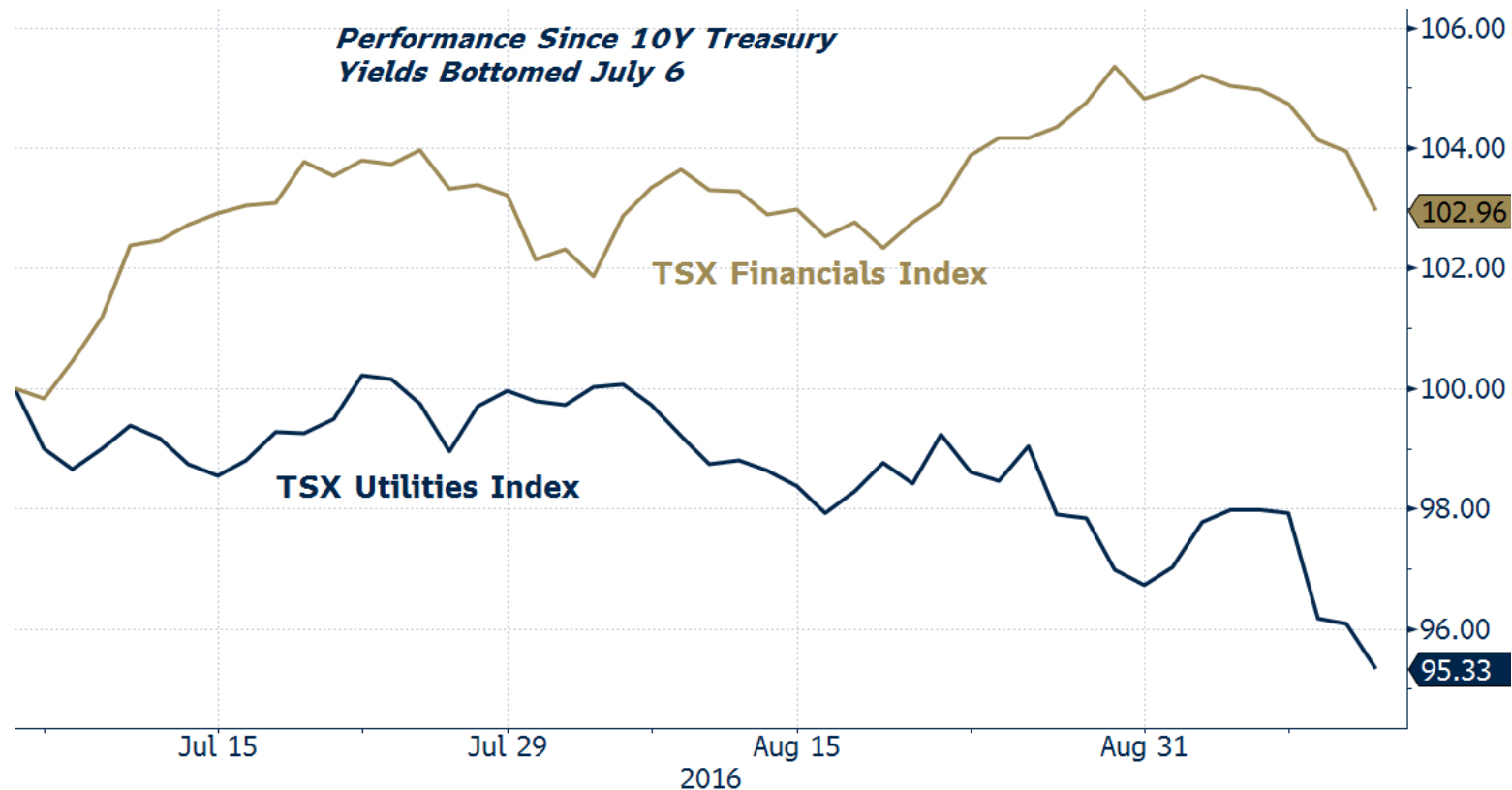
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“Low Rate Trade” Starting to Unwind?

- Interest rates are still extremely low, but it appears that for the “low rates” trade to deliver continued outperformance, interest rates have to hit lower and lower levels.
- 10-year bond yields have only risen modestly since the post-Brexit lows, but the TSX Financials have outperformed Utilities by over 7% since then.



STUTIL Index (S&P/TSX Composite Utilities Sector Index GICS Level 1) Fins and UT

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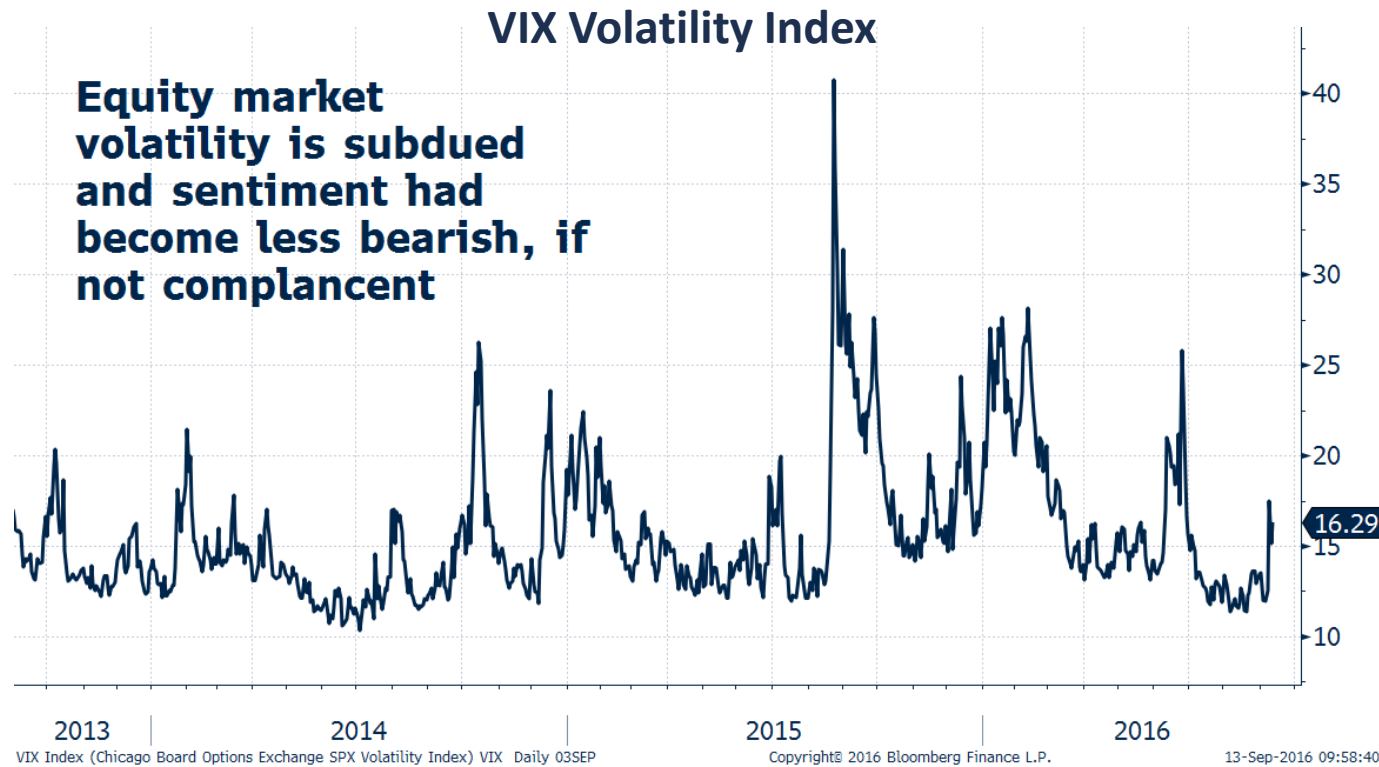
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Volatility is Low, Which is Unlikely to Last

- August 2016 saw the smallest range between the monthly high and low for the S&P 500 (1.29%) since 1965.
- That statistic alone doesn't guarantee future volatility, but upcoming events including what is sure to be a truly nasty U.S. election and likely another rate hike from the Federal Reserve suggest to us that we shouldn't get too used to the recent calm.

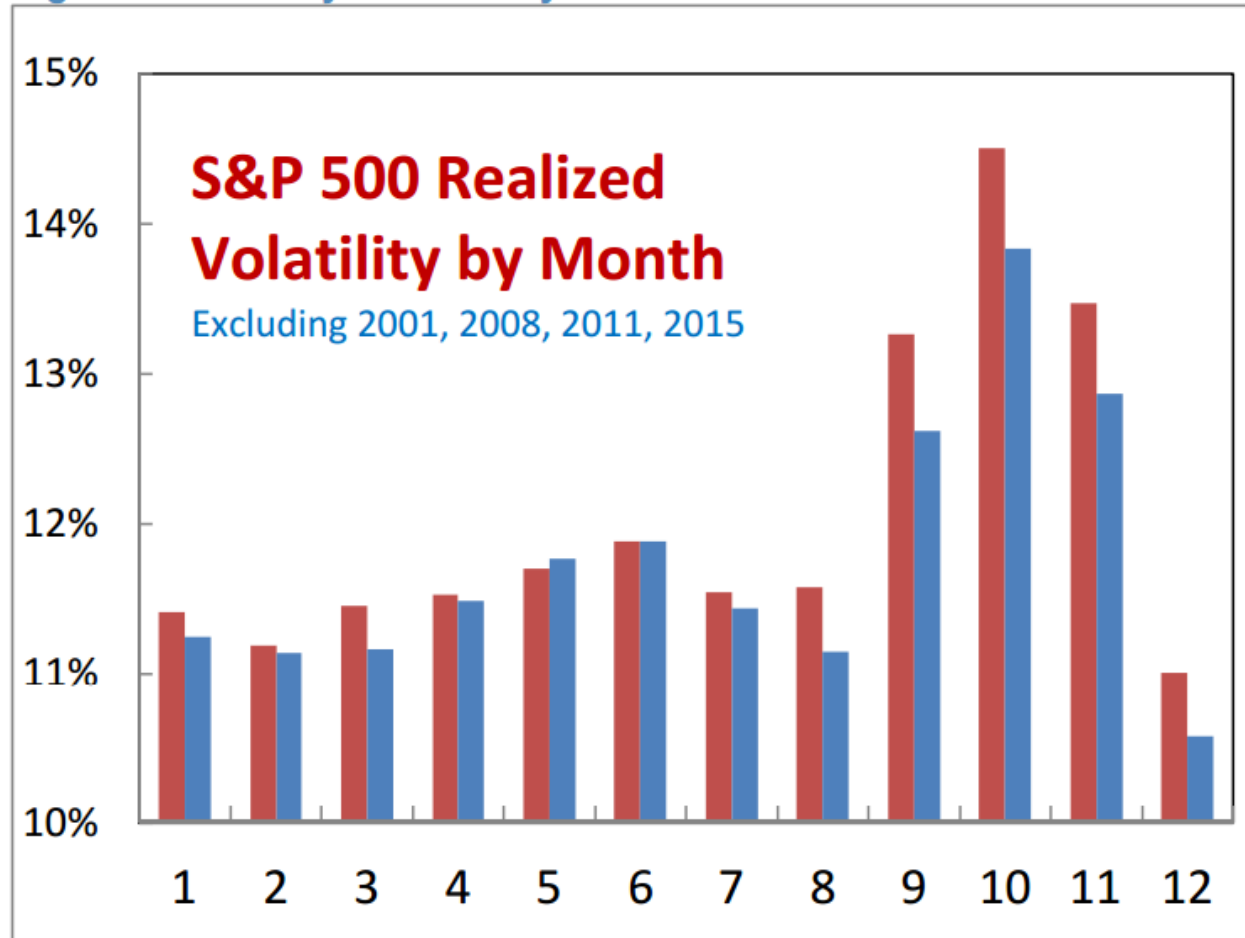


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The Autumn Months are Prone to a Rise in Volatility...

Figure 2: Volatility seasonality



Source: J.P. Morgan QDS.



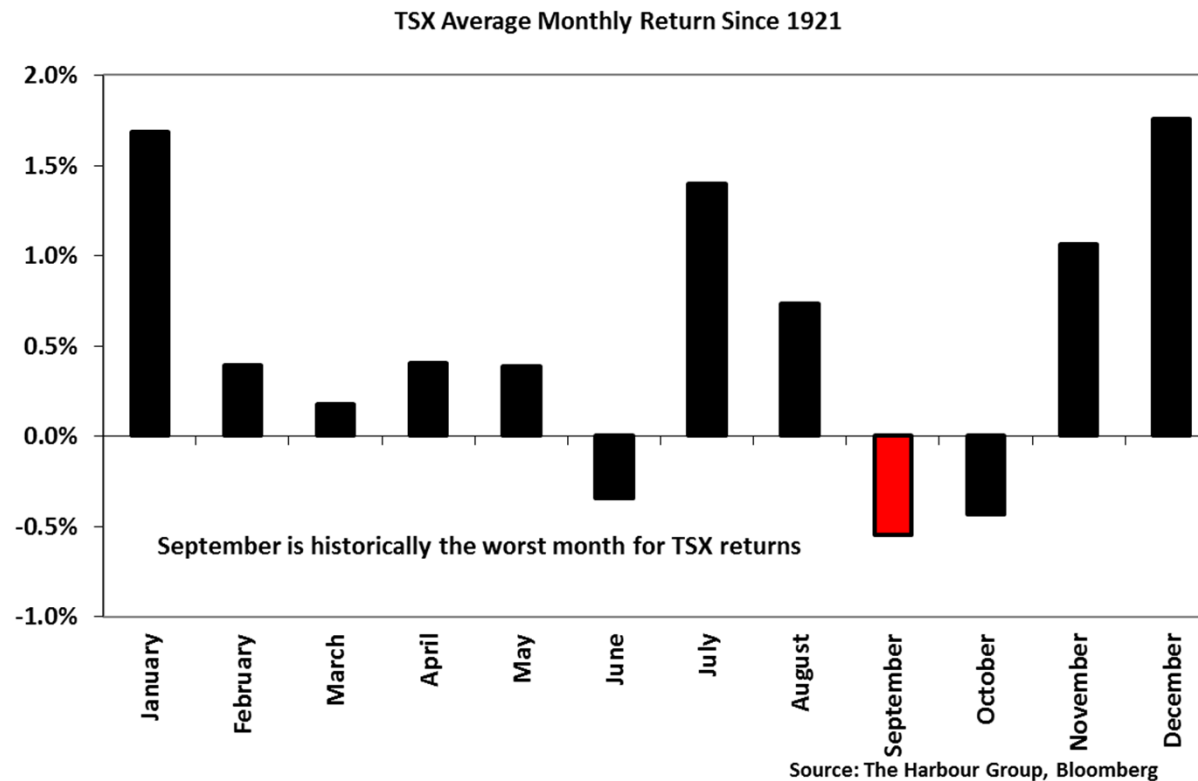
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...And Risk of a Correction is Ever Present

- We often see volatility over the summer and fall months, with September historically worst.
- That said, we have found these to be unreliable short term trading signals, as in any given year the odds aren't much better than a coin toss. In fact, the TSX in September has been up as often as it has been down since 1921.



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What if Trump Wins?

- This question has been coming up with increasing frequency.
- We think the kneejerk reaction to a Trump victory would be weakness in equity markets and the USD. The implication for bonds is uncertain, as it would be a tug of war between flight to safety and the higher inflation risk under a Trump regime.
- Longer term, we think the impact would be limited to higher inflation expectations, as the U.S. president has limited power without Congress on side.

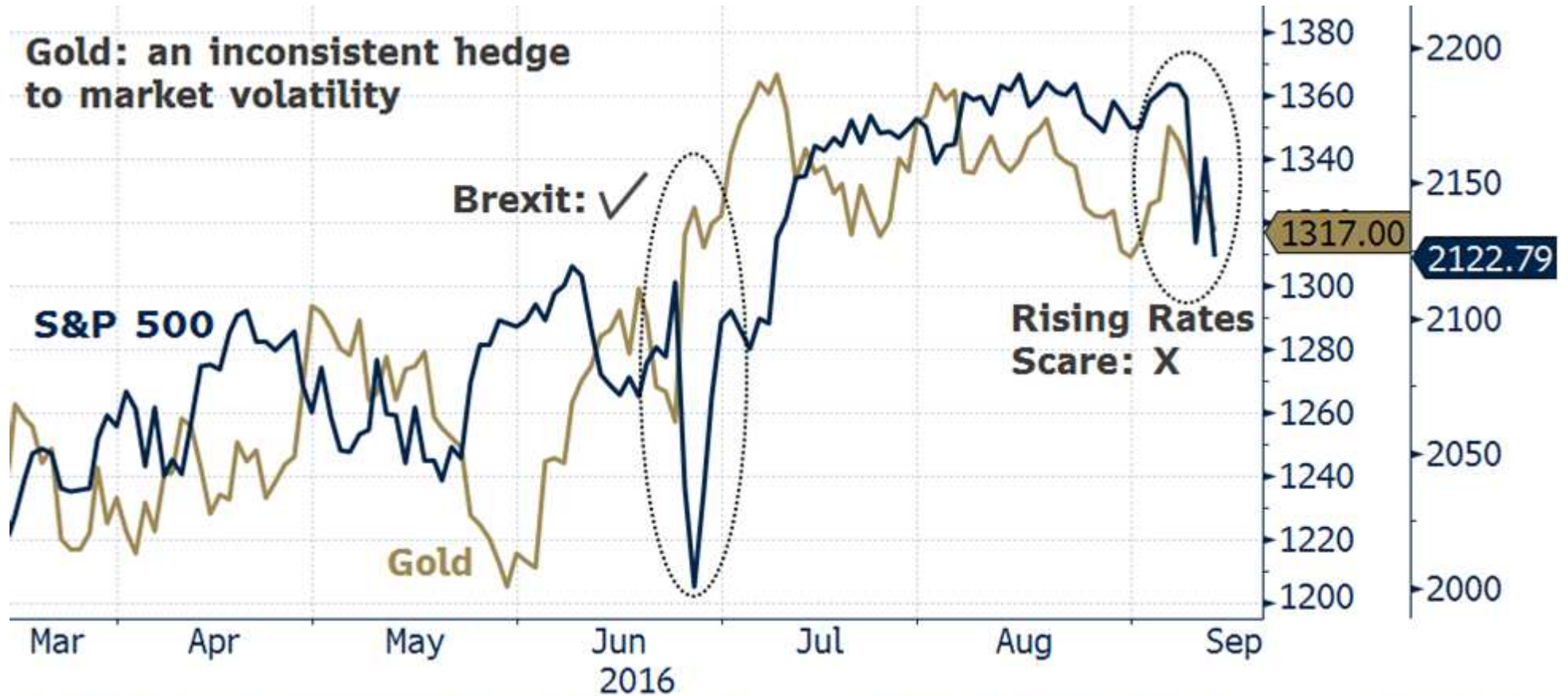


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Gold Has Not Protected Capital in September...



SPX Index (S&P 500 Index) White Background Daily 13MAR2016-13SEP2016

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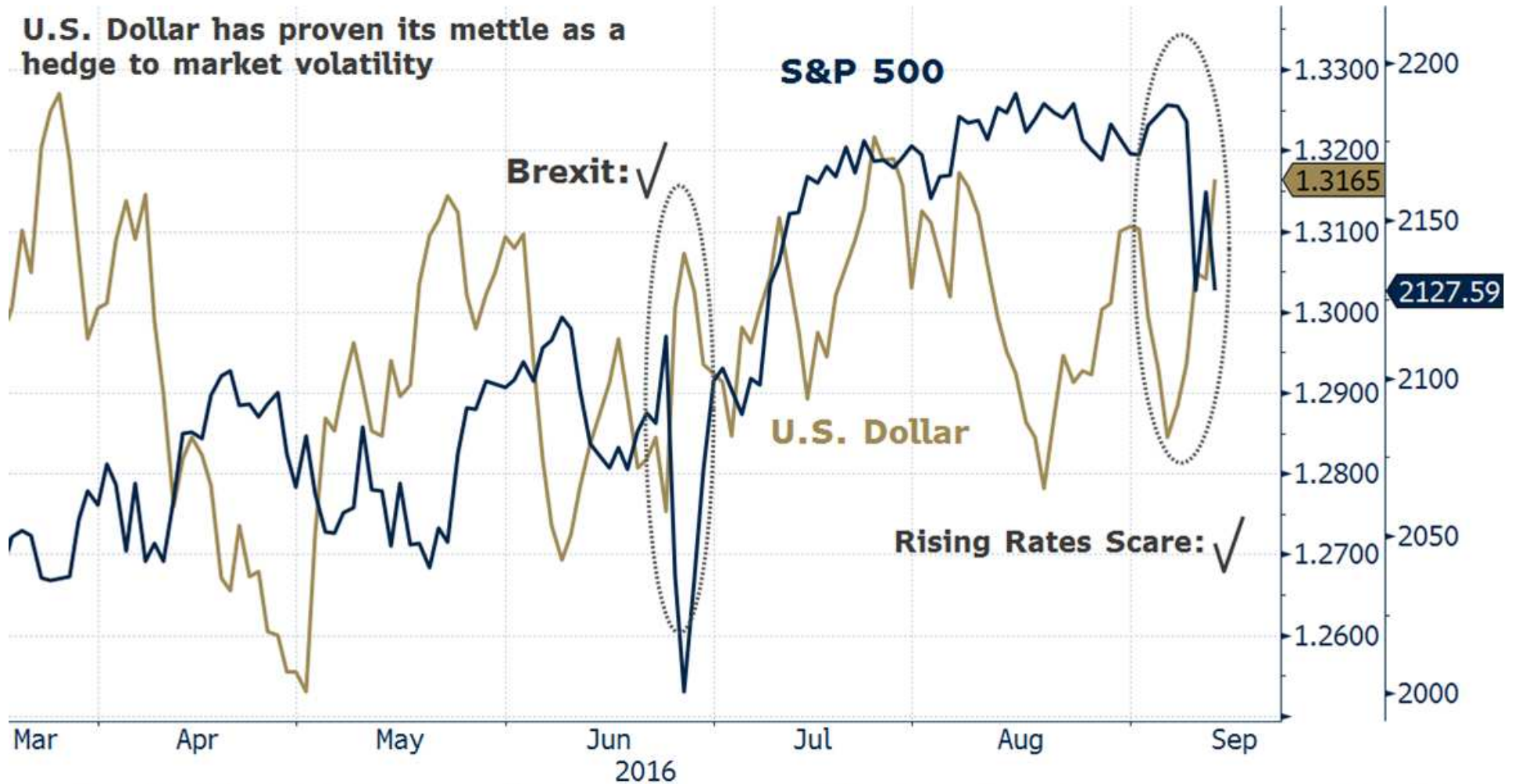


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... But the USD Has Proved Its Worth



SPX Index (S&P 500 Index) Gold and SPX Daily 13MAR2016-13SEP2016

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Bottom Line

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