MARCH 2016 NEWSLETTER

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Market Review

2016 started with a sharp worldwide market correction that saw the TSX fall 11.4% from the Dec. 31 close to the Jan 20 bottom. The S&P 500 also fell 11.4%. During the last few weeks of January panicky media stories were surfacing predicting dividend cuts at Canadian banks and the obsolescence of oil. The U.S. market bottomed on February 11, the same day that Jamie Dimon, the CEO of JP Morgan purchased 500,000 shares of JP Morgan between $53.13 and $53.30. With the shares currently trading at $59.22, his profit is currently $2.96 million US.

	Dec 31/15 Close	Quarterly Low	% Decline	Mar 31/16 Close	% Recovery
S&P 500	2,043	1,810	-11.4%	2,060	13.8%
S&P/TSX Composite	13,010	11,531	-11.4%	13,494	17.0%

	Mar 31/15 Close	Dec 31/15 Close	Mar 31/16 Close	90-Day % Change	1-Year % Change
S&P 500	2,068	2,043	2,060	0.83%	-0.39%
S&P/TSX Composite	14,902	13,010	13,494	3.72%	-9.45%

Source: Thomson One

We were fortunate to add some preferred shares and bank positions at attractive prices during the correction, but lost some ground on our U.S. positions as the U.S. dollar fell compared to the Canadian dollar.

We have had very strong outperformance during the last 12 months, partly due to our underweight in energy and materials, and also due to not owning Valeant Pharmaceuticals, which dropped from $256.67 one year ago to $34.05. Last summer Valeant had a larger market capitalization than the Royal Bank, and its fall from grace has had a significant effect on the TSX during the last year.

World Markets	YTD
S&P/TSX Composite	3.72%
S&P 500	0.83%
iShares MSCI China ETF	-4.57%
S&P/TSX Preferred Index	-5.62%
DJ Stoxx 50	-12.2%
MSCI Emerging Markets	5.37%
MSCI Japan	-15.1%

As of March 31, 2016 Source: Raymond James Ltd.

Canadian T-Bills and Bonds Yields

	Sept. 30, 2015	Dec. 31, 2015	Mar. 31, 2016
90 day	0.42%	0.51%	0.45%
180 day	0.44%	0.51%	0.49%
1 year	0.49%	0.51%	0.53%
2 year	0.515%	0.479%	0.538%
5 year	0.795%	0.733%	0.675%
10 year	1.428%	1.399%	1.225%
30 year	2.196%	2.150%	2.004%

Source: Thomson One

International 10-Year Bond Yields

	Sept. 30, 2015	Dec. 31, 2015	Mar. 31, 2016
Japan	0.35%	0.26%	-0.04%
U.S.	2.03%	2.27%	1.77%
Germany	0.59%	0.63%	0.15%
Canada	1.43%	1.40%	1.23%
U.K.	1.76%	1.96%	1.41%
France	0.98%	0.98%	0.48%
Spain	1.88%	1.76%	1.43%
Italy	1.72%	1.59%	1.22%
Portugal	2.38%	2.49%	2.92%
India	7.54%	7.76%	7.46%

Source: Bloomberg.com

Searching for Income

One of the most disappointing asset classes during the last two years has been reset preferred shares. These were introduced to the market in early 2009 when banks issued them with very attractive terms. However, with very high investor demand for income the terms got progressively worse and issues from 2010 onward experienced sharp losses.

Firstly, the 'reset' feature was often 1.5% to 2% over the 5-year Canada bond rate, with rates expected to rise by the reset date. With 5-year Canada bonds now yielding 0.675%, the dividends are now lower than the original rate. Secondly, in light of the dividend decreases and the sharp corrections of these preferred shares, investors now expect a yield closer to an equity return rather than a bond return. We feel that this represents a buying opportunity.

Example

XYZ* preferred share was issued in the spring of 2014 with a $1.10 dividend, yielding 4.4% on the original $25.00 price. They reset on March 31, 2020 at the 5 year Canada bond rate at the time plus 2.55%

Due to the falling interest rates and the negative sentiment in the sector these shares now trade at $18.35. The credit rating is BBB by Standard & Poor, the same as the Bank of Nova Scotia and higher than BCE.

Today's Price: $18.35 (yield to 31 March 2020 5.99%)

After 31 March 2020 the reset yield would be as follows:

5-Year Canada bond rate	**0%**	Reset rate	**2.55%**	Yield on $18.35	**3.47%**
	0.675% (today's rate)	Reset rate	**3.23%**	Yield on $18.35	**4.40%**
	2%	Reset rate	**4.55%**	Yield on $18.35	**6.20%**

Clearly these investments will perform better if rates rise. We will continue to add reset preferred shares as opportunities present themselves.

*As these shares have low daily trading volume, I have kept the name confidential so that we do not have to compete with non-clients reading this newsletter online when we buy these.

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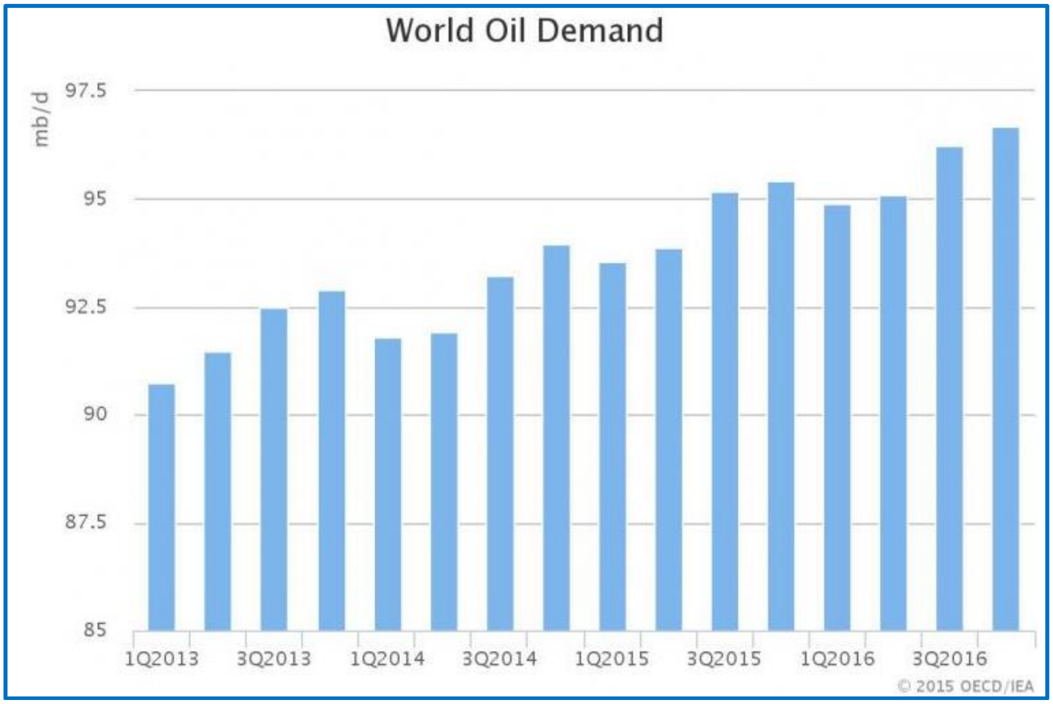
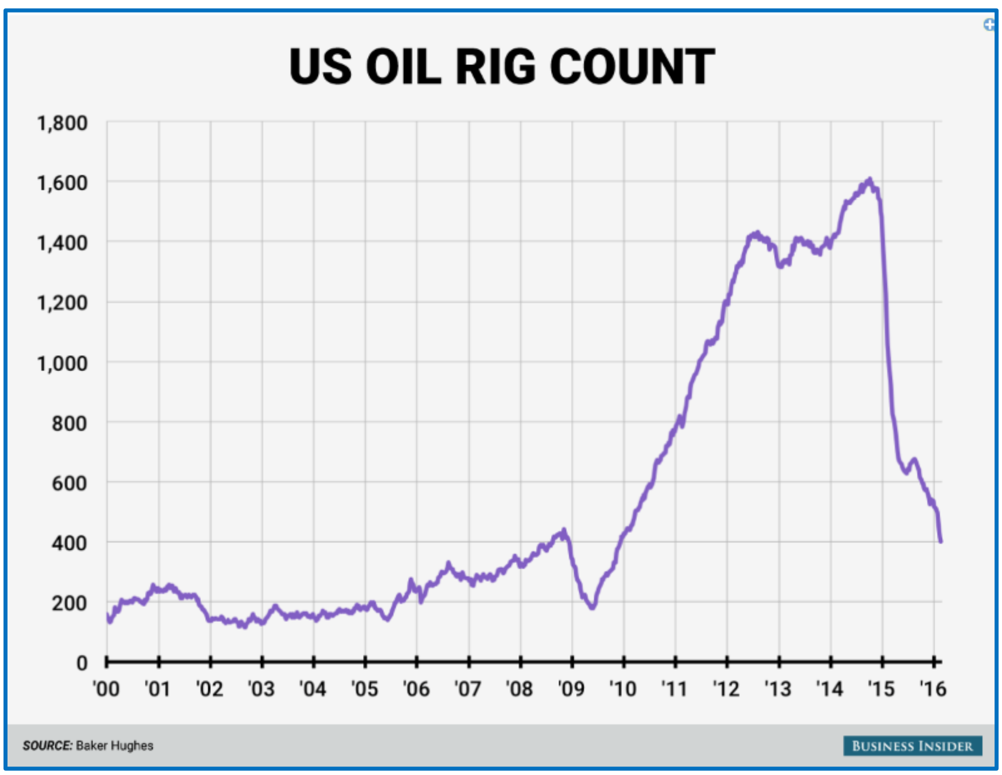
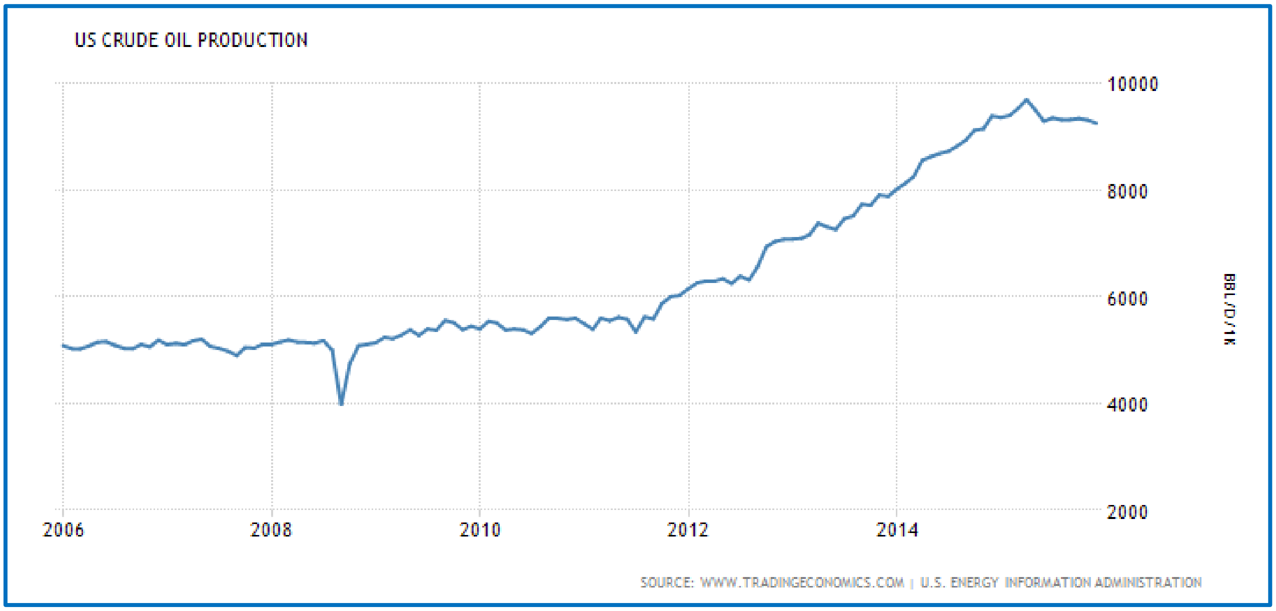
Oil

The big story of the TSX over the last two years has been the price of oil with West Texas crude falling from $106.93 in June of 2014 to a low of $27.24 on February 10, 2016. The price fell in spite of rising demand, and was caused by increased supply. Saudi Arabia has been producing close to maximum capacity and U.S. shale production increased sharply between 2009 and 2014.



Currently the market dynamics seem to be pointing to a rosier future for oil producers. The U.S. oil rig count has dropped from 1,600 rigs to 400, and U.S. production has already started to fall. With rising demand and falling supply we expect that world inventories will start to decline, perhaps this summer with the driving season.





The recent upturn in the price of oil has already moved the Canadian dollar from $0.6850 in mid-January 2016 to $0.7699 on March 31, 2016. A rising price of oil will also be supportive of the Canadian economy and markets in general.

Quote for an Election Year

> "I try to invest in businesses that are so wonderful that an idiot can run them because sooner or later, one will."
>
> - Warren Buffett

This quote may apply to politics in the Western world. Currently most of the U.S. presidential candidates are promoting higher tariffs, more regulations, or higher taxes, none of which are good for the economy or the stock market. While elections may seem like a circus, and the candidates don't always seem to represent society's brightest and best minds, the world's free enterprise democracies seem to thrive in spite of the political leadership. For this reason we should look at political rhetoric and turmoil during the U.S. election season as potential opportunity rather than reasons to build an underground bunker and invest in canned food.

Outlook for 2016

At this time it is hard to expect a 'bull' market to start from here. Due to the cheap valuations compared with bonds and other alternatives we do not expect a major 'bear' market either. With the market potentially in a trading range we will continue to add the highest quality equities on pullbacks and watch our asset allocations to potentially trim weaker securities on rallies.

Client Appreciation Event / Open House

Mark your calendars for Thursday, June 23! We are again hosting our annual client appreciation at the Westwood Tennis Club in Nanaimo from 4:00pm to 7:00pm. Dave Hart will again be playing guitar music. Look out for your mailed invitation at the beginning of May.

With the addition of Mark and Meaghan as Associate Advisors, we now have the ability to take care of more relationships. If you have friends who have expressed an interest in finding a new advisor, we would be delighted to hear from you. Just call our office at 250-729-2830 and we'll take it from there. Thanks!

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