RAYMOND JAMES | DOUGLAS DUNCAN wealth management

JUNE 2017 NEWSLETTER

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Market Review

A sell-off this quarter has led to the Canadian market producing a negative return for 2017. Resource companies have been the biggest contributor to the decline, but banks and REITs have also had modest pullbacks over the past few months. US markets continue to trade close to all-time highs which were reached ***after*** former FBI boss James Comey testified under oath against President Trump.

	June 30/16 Close	March 31/17 Close	June 30/17 Close	90-Day % Change	1-Year % Change
S&P 500	2,098	2,363	2,423	2.5%	15.5%
S&P/TSX Composite	14,064	15,548	15,182	-2.4%	7.9%

Source: Thomson One

World Markets	YTD
S&P/TSX Composite	**-0.69%**
S&P 500	**8.22%**
iShares MSCI China ETF	**25.1%**
iShares S&P/TSX Preferred Index ETF	**6.20%**
DJ Stoxx 50	**4.60%**
iShares MSCI Emerging Markets EFT	**18.2%**
iShares MSCI Japan EFT	**9.80%**

As of June 30, 2017 Source: Thomson One

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Canadian T-Bills and Bonds Yields

	Dec. 31, 2016	Mar. 31, 2017	June 30, 2017
90 day	**0.47%**	**0.53%**	**0.72%**
180 day	**0.57%**	**0.55%**	**0.83%**
1 year	**0.64%**	**0.64%**	**0.97%**
2 year	**0.747%**	**0.744%**	**1.094%**
5 year	**1.116%**	**1.111%**	**1.378%**
10 year	**1.721%**	**1.621%**	**1.750%**
30 year	**2.313%**	**2.301%**	**2.129%**

Source: Thomson One

International 10-Year Bond Yields

	Dec. 31, 2016	Mar. 31, 2017	June 30, 2017
Japan	**0.04%**	**0.06%**	**0.07%**
U.S.	**2.44%**	**2.39%**	**2.30%**
Germany	**0.20%**	**0.32%**	**0.46%**
Canada	**1.72%**	**1.62%**	**1.75%**
U.K.	**1.23%**	**1.14%**	**1.25%**
France	**0.68%**	**0.96%**	**0.81%**
Spain	**1.38%**	**1.64%**	**1.51%**
Italy	**1.81%**	**2.30%**	**2.14%**
Portugal	**3.73%**	**3.93%**	**3.00%**
India	**6.51%**	**6.67%**	**6.51%**

Source: Bloomberg.com

Loonie Soaring like a Hawk

With the Bank of Canada talking up the currency recently, 82% of watchers believe we will get an increase to interest rates at the next meeting on July 12th. This has caused the loonie to appreciate 6% since the May 4th low, and has been moving shorter term bond prices lower (and interest rates higher). Market watchers should note that short term rates have been rising, but long term (30 year) rates have been falling. This is a sign that we should be cautious and not be too aggressive with our investment choices.

Home Capital Turbulence

Subprime lending in Canada is now over $1.6 trillion, 12.5% of the Canadian mortgage market. Many of the borrowers are self-employed individuals, which prevents them from qualifying for traditional mortgages at the best rates offered by the major banks.

Home Capital Group (HCG) has been one of the largest lenders in this market for years and has had a steady history of profits and low defaults, but became the target of short sellers when bad news of irregularities with some loan applications were released.

During this quarter investors lost confidence in the company and began withdrawing deposits. Home Capital has historically relied on short term deposits for 70% of its funding and investors depleted these accounts from $2 billion to $100 million in a few short weeks. This prompted the company to get a "gun to the head" line of credit which started with a $100 million non-recourse payment and a 10% interest rate. *When you add the non-recourse payment to the 10% interest rate, the initial $1 billion drawdown was actually at a 20% cost.*

Today it looks like confidence has been partially restored to Home Capital as Warren Buffett's Berkshire Hathaway has emerged as the largest shareholder and also extended a $2 billion line of credit at a slightly lower 9% interest rate. It will be interesting to see if Berkshire keeps their investment in Home Capital, as the share purchases had a number of restrictions such as limited voting rights, and a four month lockup on any stock sales. Warren accumulated his position in Home Capital at an average cost of $10/share and is up 70% on the stock purchases while collecting a 9% interest rate on the line of credit.

Home Capital Group is an example of how quickly a loss of confidence can affect a financial institution and why we're happy that none of our clients had an investment in Home Capital shares. We continue to hold a number of the major banks as core positions in client portfolios.

Below is Home Capital Group's one year chart:

Source: bigcharts.com

Amazon Juggernaut

When Amazon started selling books online in 1995, the majority of people did their shopping at the local mall. Shoppers only had the options of what was available in the store and there was limited opportunity to compare prices with competitors. As the internet and online shopping have become available to more people, Amazon has expanded into electronics, home appliances, clothing, and toys, taking market share from traditional retailers. Online shoppers enjoy Amazon's lower prices and plentiful product options. Today shoppers spend $370 billion USD online annually, and Amazon earned $43.74 billion USD in revenues in 2016.

Recently Amazon announced its intention to purchase the high-end grocery store chain Whole Foods (WFM) for $13.7 billion. Amazon will acquire Whole Foods' 465 physical store locations. Amazon already delivers non-perishable food stuffs to its customers but has not been able to offer the same service for produce, meat and dairy products. By acquiring Whole Foods, Amazon now has the opportunity to utilize Whole Foods' existing retail centers to offer more products to its customers.

After the takeover was announced on June 16th, brick-and-mortar grocery retailers Walmart (WMT), Costco (COST), Target (TGT), and Loblaws (L) dropped 4.7%, 7.2%, 5.1% and 3.6% respectively. Many people expect Amazon to take market share from traditional grocery stores by lowering food prices and offering more products. Amazon has not yet announced whether it will introduce immediate changes to Whole Foods' day-today operations, and most people still shop at their local grocery store. In a recent Nielsen survey, only 4% of North American respondents said they regularly shop for groceries online. While it may take time before Amazon starts delivering tomatoes to your door, we can expect changes in the grocery business over the next few years.

The Disrupters

The internet has created an environment where online companies can disrupt established industries. Amazon disrupted the retail business. Netflix and YouTube have taken away viewers from cable networks. Two of our holdings Google and Facebook have displaced traditional newspapers as the favoured advertising medium.

Google has the ability to place advertising on a reader's browser based on other websites that they have visited, ensuring advertisers that the reader has an interest in their product or service.

Alphabet Inc. (Google) GOOGL-US

In our March 2017 newsletter, we recommended Alphabet Inc. Since March 31, 2017 Alphabet's stock has risen from $847.80 to $929.68, a 9.7% gain.

Below is Google's six month chart:

Source: bigcharts.com

With products like Google Maps, YouTube, Chrome, and Android, Alphabet has been a disrupter in many industries. Google search engine has replaced the need for the phone book, leaving the Yellow Pages (Y) Company as a shell of its former business.

Considering its rapidly increasing revenues and profits, Alphabet trades at a reasonable valuation. For investors looking for technology exposure and growth, Alphabet can be accumulated at current levels.

Facebook Inc. (FB-US)

Facebook is another company that has become an industry leader. Since March 31, 2017, Facebook has increased from $142.05 to $150.98, a 5.9% gain.

Below is Facebook's six month chart:

Source: bigcharts.com

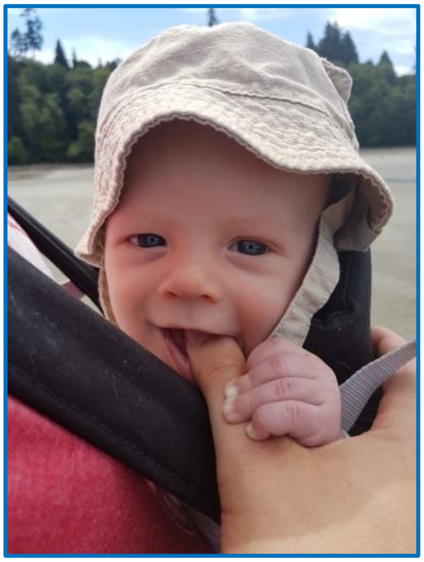
<u>Meaghan's 10 Year Anniversary on Facebook</u>

In 2007 Steve Jobs introduced the first iPhone, J.K. Rowling released the last book of the Harry Potter series, and sub-prime mortgage loans in the United States were beginning to unravel. It was the year I created my Facebook account.

Compared with today, Facebook offered few functions; nonetheless, its users were hooked. My friends and I constantly updated our profile pictures and wrote messages on each other's walls. That year Facebook reportedly had 50 million users and earned $153 million in revenue.

Today Facebook has 2 billion monthly users globally who message their contacts, live stream video, post photos, read real or fake news and connect with new friends. The average user spends 50 minutes per day on Facebook, Instagram and Messenger platforms, giving Facebook unlimited access to users' personal data. As users reveal their lifestyles through their Facebook activity, advertisers can focus their efforts towards their target market on Facebook's platforms. This strategy has worked well. Since its IPO in 2012 Facebook has grown its revenues each year, with $27.6 billion in 2016.

Like Google, Facebook has a reasonable valuation in keeping with its growth rates and can be accumulated for investors looking for growth.



Biggest Gain for Douglas Duncan Wealth Management

Graeson packed on the pounds this quarter weighing in at 14.5 lbs. He's now 14 weeks old and has grown 79%.

Strategy for the summer

At this time we have a neutral stance on the markets with few 'table pounding buys' available. For clients looking to invest further funds, we have been adding dividend paying shares, and Google and Facebook, mentioned above.

Have a great summer and please call if you have any questions.

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. Our team is licensed in BC, as well as other provinces in Canada. Just call our office at 250-729-2830 and we'll take it from there. Thanks!

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