CIBC World Markets Inc.
606 – 5811 Cooney Rd
Pacific Business Centre
Richmond BC V6X3M1

Tel: 604 270-6457
Fax: 604 273-7684
Toll Free: 1 800 341-9909

January 2017

In this newsletter:

- The year ahead outlook, opportunities and risks as ‘the Donald’ takes the helm
- Multiple currencies now allowed in RRSP/RRIF accounts
- Monthly statements in January will start showing performance; and a new annual report will show cost of money management
- What was learned from our client survey?
- CIBC Wood Gundy Miracle Day

The year ahead outlook, opportunities and risks as ‘the Donald’ takes the helm

When Trump descended down the elevator to make his announcement to run for the presidency, it was no surprise he quickly went off-script and proceeded to make statements that in a previous world would have disqualified him as fit to lead the most powerful nation on earth. Fast forward to today, and Trump will shortly begin ‘his great new adventure’ being addressed henceforth as ‘President Trump.’ This surprising outcome was (I thought) about as probable as my cat Puff maintaining dual-resident status at both my new home and the yard of my old home (three kilometers away). Each of these events definitely classify as ‘unexpected outcomes.’ No doubt 2017 will bring more surprises. In the meantime, how are clients doing return-wise and what may be in store for 2017?

Overall portfolio returns were reasonably good this past year. Canadian stocks did well; global equities and real estate investments trusts (REITs) did ‘so-so,’ while preferred shares had a strong year after causing us some grief in 2015. Bonds performed about as expected with the mix of corporate bonds and mortgage type investments we use generating a return in the area of 3 to 4%. We continue to protect against ‘interest rate risk’ (i.e. avoiding declining bond prices when interest rates increase), thus are not buying ‘long-term bonds.’

With respect to our outlook for 2017, low interest rates may continue to force more money out of the bond market into the stock market; and the U.S. economy looks reasonably strong – poised for a spike in ‘blood sugar’ as the new Trump

CIBC Wood Gundy

administration lowers corporate taxes and increases infrastructure spending. Last we checked, a combination of increased spending and lower taxes typically results in more government debt; but Trump seems to think he can fix that problem as well. In our view, the odds of Trump satisfying the high expectations he has created in his base of voters is unlikely, but we will certainly have an ‘interesting’ four years ahead.

On the risk side, valuations on equities are a bit ‘pricey’ and total government and consumer debt levels globally remain a concern. Also, a number of European elections will occur this year and while it looks likely the Euro community will stay together, it is also likely that markets will fixate from time to time on potential risk outcomes from these elections.

The threat from ISIS is dissipating somewhat but the Middle East continues to create geopolitical risk (as always it seems). The huge increase in oil and gas production in North America (through shale production and the oil sands) will mean that ‘economic threats’ from perpetual mid-east tension should decrease going forward. Trump’s likely approval of TransCanada’s Keystone pipeline is one of many new pipelines that will assist the U.S. towards less dependence on mid-east oil.

With respect to interest rates, the U.S. has finally begun its much delayed tightening phase with markets anticipating a further 0.75% rise in U.S. short-term rates in 2017. Central banks in Canada, Europe and Asia will likely avoid increasing rates until they see improved local economic conditions.

We think we are about a year away from increasing short-term interest rates in Canada. In the meantime, medium- and long-term interest rates (market, not central bank controlled) have seen a reasonable increase this past month. While we need to anticipate a further increase in interest rates, we think we are a long way away from any material increase in rates. Our average bond maturity is about four and half years out, which means clients earn a better rate than would be obtained by investing short-term, without taking too much in the way of ‘interest rate risk.’ We continue to emphasize quality in terms of issuers we use and are pleased to report that we have no material concerns with any of our many different corporate bonds held in client portfolios.

We still like preferred shares which as mentioned previously had a much better year in 2016 due to an increase in the five-year Canada bond yield (which determines future yield) plus strong institutional and retail investor demand. Tax efficient preferred share yields in the 5% area are still too high in our opinion, so we continue to like this asset class in non-registered accounts. We also continue to like real estate investment trusts (REITs) with cash distributions of about 7% on the ones we are buying. For new buys, we emphasize REITs with above average distributions and ones that are priced below net asset value. Three of our current top picks (H&R, Dream Industrial and Artis) trade about 20% below the value of buildings they own.

Geographically, we cut back U.S. exposure a bit in 2016, and look to do more of same over the next year or two if we get a combination of lower Canadian dollar and markets versus U.S. dollar and markets.

In terms of exchange traded funds (ETFs, also known as indexes), we are almost finished discussing with each client a switch to Canadian-listed ETFs and have hitched most of our 'ETF wagon' to Vanguard Canada, due to their low cost approach, the fact that they do little in the way of 'security lending,' and because these Canadian-listed ETFs of foreign equity minimize the need for CRA's complicated Foreign Property (T1135) filing requirements.

So what can clients expect to earn return wise in 2017? Let's start with saying we are neither bearish nor overly bullish about the upcoming year. If stock markets are strong, it will be at least partly due to a lack of return in the bond market. Of more importance is what we can realistically expect to earn in the next five-year period.

To answer this question, let's start with looking at how much our average client has in 'fixed income,' namely bond and bond related investments and preferred shares. Our average client has about 42% of a typical portfolio invested in 'fixed income' investments. With this good level of fixed income, if we err, we will err on the conservative side. It is our objective to make about 3.5 to 4% on this fixed income part of the portfolio.

In order to make a 7% overall return, that means that the remaining stock and REIT portion of the portfolio (58% on average) needs to earn about 10%. We may make that or better in 2017, as anything of course can happen in a given year in the stock market, but of course, there is always the possibility of a losing year in stocks.

Historically, over past 100 years, the stock market has earned about 5% above inflation so with inflation averaging at about 1.5%; we can assume an expected

CIBC Wood Gundy

long-term return on stocks of about 6.5% per year. As you can see, the only way to target a 7% return would be if we place 100% of your portfolio in the stock and REIT market. That would be far too risky for our average client (who is 66 years old).

If we calculate the historical risk/return on a portfolio invested 100% in a well-diversified stock portfolio, the expected return in one given year is 6.5% +/- 17%, thus a range of -10.5% to +23.5% in 2 out of 3 years - on average.[1] Therefore, in one out of every three years, returns have been either lower than -10.5% or higher than 23.5%....and once in about every 20 years, the stock market has experienced a peak to bottom decline in excess of 45%. As you can see, stocks can and will fluctuate price-wise greatly.

Our message here with respect to future investment returns is twofold:

1. Today's low interest rate world means that we need to take a bit of risk to even generate 3.5 to 4% on the fixed income part of a portfolio; and low interest rates will challenge us on the return front over the years ahead.

2. The only way to expect a 7% per year overall long-term rate of return going forward is to take a lot more risk than we have in the past (at a time when stocks are not exactly cheap) by going 100% into equities/REITs.

Unless a client is on the young side and is prepared to take on a more risk, we feel our balanced approach (that we maintain right now) is most appropriate from a risk/return standpoint.

One of the responsibilities we have as your advisor is to set realistic and achievable return objectives. Thus, when we do financial plans for clients these days, we estimate about 5.5% long-term future rate of return. In the past, we have generally been able to exceed this return for typically constructed portfolios that have been with us for a number of years, but going forward, low interest rates will make it challenging to generate the kind of return we have generated in the past. This is not to say we won’t try our best to achieve a good rate of return but we will keep risk and generating investment income very much in mind with your portfolio management.

[1] Using average annual volatility of a combination of U.S. and Canadian large capitalization stocks from 1950 to 2015, per Moningstar Andex Chart 2015.

CIBC Wood Gundy

Multiple currencies now allowed in RRSP/RRIF accounts

Our firm sent out a letter announcing this new service about a month back and many clients had questions. Going forward, clients with U.S. stock investments inside Registered Retirement Savings Plans (RRSP), Registered Retirement Income Funds (RRIF) and Tax-Free Savings Accounts (TFSA) will see cash dividends (or sale of their positions) show up in separate U.S. 'sub account.' This will mean U.S. transactions/dividends will stay in U.S. dollars, just as is the case today in non-registered accounts. Thus, we now have the option to either reinvest U.S. dollars directly into U.S. investments, or convert same into Canadian dollars. This does not affect many clients as most of our U.S. exposure is in non-registered accounts.

By the way, you can also hold Japanese yen, Australian dollars, Euros, UK Pounds, New Zealand dollars and Swiss francs inside these same registered accounts (as we can today in non-registered accounts). Not often, but occasionally, we have a client who would like to do this.

Monthly statements in January will start showing performance; and a new annual report will show cost of money management

Better ongoing performance calculations and a clearer picture of money management cost begins in 2017. On your January statement, you will see a rate of return calculation (for each account separately). You will also start receiving an annual report that shows how much you have paid CIBC Wood Gundy on that account in the past year. This is part of new disclosure rules involving most of Canada's investment industry (unfortunately, the separately regulated insurance industry has decided not to disclose this information).

Better disclosure is good news for consumers as many Canadian investors do not have a good handle on what their investment management company earns. We hope that our Pope Team clients will not be surprised. We have done our best to inform clients over the years about how much and how you pay our firm. We have done this in various ways; in meetings and phone calls, showing what we earn on our model portfolio that we provide at meetings, and via a report we prepared as part of our Pope Team newsletter sent to clients (see pages 3-7 of the newsletter from April 2014 on www.thepopeteam.ca). Clients in our 'Index and Stock Strategy' also receive a letter each year summarizing cost. Some

CIBC Wood Gundy

though may certainly have questions regarding this new report. Please do not hesitate to call in.

What you pay has a direct effect of course on what you earn. We try to keep portfolio cost down to a reasonable level and to make as much of this cost (as possible) ‘tax deductible.’

Fees that have been hard for clients to quantify in the past will now show up on this annual report; for example trailer fees (how much our firm earns from mutual funds companies), and commissions on stock and bond trades. The report will also show compensation received by CIBC Wood Gundy (not paid by clients) from companies we use for GICs and ‘new issue’ preferred shares, convertible bonds, or common stocks.

Our practice continues to be at below industry average cost levels and we are committed to maintaining that.

What does not show up on this new report is any cost you incur that is not paid to CIBC Wood Gundy. In our practice, we keep that cost down to a low amount (by buying most investments directly) and are committed to continuing to bring this cost down. We hope that at some point all outside management costs will be disclosed as too much money in Canada is, in our opinion, invested in mutual funds with high management fees.

Our new ‘discretionary’ portfolio management service we announced a little while back will allow us to further minimize outside management cost and will also help make clients’ costs more ‘tax deductible.’ It will also make cost easier to understand as all trading commissions, mutual fund trailer fees and annual RRSP/RIFF fees will be eliminated. We are ‘pilot’ testing this method with some existing clients as well as all new clients (this year) and are introducing it to clients in meetings, with the objective of a full roll out in about six months’ time. All existing clients will have the option of maintaining things ‘as is’ or moving to this new method.

What was learned from our client survey?

Every two years, a random sample of about 50% of our team’s clients are mailed a survey from an outside firm on CIBC Wood Gundy’s behalf. It is a very long survey so we really appreciate that a number of clients spent the time to fill it out.

CIBC Wood Gundy

We go through the results thoroughly and always learn things that we can work on. Overall client satisfaction rates remain high so thanks for the nice feedback. Based on the client survey, we are going to work on:

1) Doing more financial plans and financial plan updates. With the addition of Susan to our team, we have more than doubled the number of financial plans/updates this past year, and we will try and accelerate that in 2017. We initiate this in client meetings and sometimes over the phone. In the meantime, please call Susan or any team member if you wish to either do the plan, or update one. It's a very worthwhile exercise.

2) Offering a 'service agreement' whereby you can see and confirm that various aspects of your financial life are being looked at (estate planning, tax planning, etc.) We are working on bringing this into to our meeting process.

3) Working with your children, if they are interested in our services, as well as working with your other professionals (your accountants/lawyers). We are pleased to do that anytime. Regarding accountants, we will continue to work with them on your behalf in terms of getting them required tax information/capital gain/loss information.

This is just a small sample of what we learned. Thanks again for all the great feedback.

CIBC Wood Gundy Miracle Day

Our team has again dedicated a percentage of fees/commissions towards funding the 'Scientist in Residence' program. This year, we are funding the program at Britannia Elementary in East Vancouver. This is where a University of British Columbia scientist spends the school year working with students and teachers, developing lesson plans and doing experiments and field studies with the children. It's a great program, and the kids really enjoy it. Also, our firm's 25 year or so hot breakfast program continues strong at five inner-city schools in Greater Vancouver and remains well-funded. Over 750 kids are fed a healthy hot breakfast each day. This year, CIBC as a whole raised $7 million dollars for kids. Miracle Day is just one of many charitable endeavours that CIBC and CIBC Wood Gundy pursue.

CIBC Wood Gundy

We are grateful for your continued support. And thanks to those who mentioned our practice to family and friends during the year.

All the best in 2017 and please call or click anytime.

Regards,
CIBC Wood Gundy

Neil Pope, MBA, CIM
Portfolio Manager
First Vice-President
604 207-8578
neil.pope@cibc.ca

Rick Aulik, CFP, CIM, FCSI
Investment Advisor
604 207-8585
rick.aulik@cibc.ca

Susan Christie, BA, CIM, CFP
Associate Investment Advisor
604 207-8570
susan.christie@cibc.ca

Melanie Burns
Client Associate
604 207-8583
melanie.burns@cibc.ca

Cheryl Sy, B.Sci.
Client Associate
604 207-8581
cheryl.sy@cibc.ca

Sophie Tu, B.Comm.
Client Associate
604 207-8576
sophie.tu@cibc.ca

CIBC Wood Gundy

Disclaimers

This information, including any opinion, is based on various sources believed to be reliable, but its accuracy cannot be guaranteed and is subject to change. CIBC and CIBC World Markets Inc., their affiliates, directors, officers and employees may buy, sell, or hold a position in securities of a company mentioned herein, its affiliates or subsidiaries, and may also perform financial advisory services, investment banking or other services for, or have lending or other credit relationships with the same. CIBC World Markets Inc. and its representatives will receive sales commissions and/or a spread between bid and ask prices if you purchase, sell or hold the securities referred to above.

CIBC Wood Gundy is a division of CIBC World Markets Inc., a subsidiary of CIBC and a Member of the Canadian Investor Protection Fund and Investment Industry Regulatory Organization of Canada.

Clients are advised to seek advice regarding their particular circumstances from their personal tax and legal advisors.

Securities

Artis Real Estate Investment Trust	2a,2c,2e,2g
Dream Industrial REIT	2g,7
H&R REIT	2g,3a,3c,7

Disclaimers

2a This company is a client for which a CIBC World Markets company has performed investment banking services in the past 12 months.

2c CIBC World Markets Inc. has managed or co-managed a public offering of securities for this company in the past 12 months.

2e CIBC World Markets Inc. has received compensation for investment banking services from this company in the past 12 months.

2g CIBC World Markets Inc. expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

3a This company is a client for which a CIBC World Markets company has performed non-investment banking, securities-related services in the past 12 months.

3c CIBC World Markets Inc. has received compensation for non-investment banking, securities-related services from this company in the past 12 months.

7 CIBC World Markets Corp., CIBC World Markets Inc., and their affiliates, in the aggregate, beneficially own 1% or more of a class of equity securities issued by this company.