First Quarter 2018

"One, Two, Three, Four, I Declare a Trade War"

President Trump Stirs the Pot with Tariffs on Solar Panels, Washing Machines, Steel and Aluminum Imports

The Team:

Brian Steele, CA, CPA, CFA®

Laura Prust, CIM®, CPCA

Jeannine Campbell

Kelly Edmonds

Matthew Bell, CFA®

Raymond James Ltd.

595 Parkside Drive Unit #1 • Waterloo, Ontario, Canada N2L 0C7 • T: 519.883.6040 • F: 519.883.6079 • Toll Free: 1.877.642.6408

Member of Canadian Investor Protection Fund

Quarterly Summary and Musings on Quarterly Happenings

Continuing a multi-year trend, the Canadian equity market (S&P/TSX composite index) underperformed the US and global equity markets in the first quarter, ending the quarter down 4.5% versus the US (S&P 500) and global (MSCI World) markets which were down -0.8% and 1.7% respectively. Canadian equity markets were negative throughout most of the quarter while US and international markets roared in January before erasing those gains and then some in February.

The consumer discretionary, financials, industrials, technology and real estate sectors led the S&P/TSX composite index while the consumer staples, energy, health care, materials, telecom and utilities sectors trailed.

US Tariffs

In January, the Trump administration slapped steep tariffs on imported washing machines and solar panels. Markets and foreign governments did not take notice of the tariffs due to the specific targets being almost exclusively Chinese made and marginal relative to the broad economy. In March, the Trump administration imposed tariffs on steel and aluminum imports. As steel and aluminum are used to make numerous products, these tariffs did not go unnoticed. Corporate figures in the US and abroad lambasted the tariffs as a tax on everything, hurting corporate profits and boosting prices/inflation. US politicians in Trump's own, generally anti-tax, party unsurprisingly decried the tariffs as a tax on the American consumer and raising inputs costs for American businesses. Foreign governments pleaded with Trump for exceptions and vowed tariffs on US products in retaliation if exceptions were not provided. To that Trump tweeted "trade wars are good and easy to win". The Trump administration eventually relented, providing temporary exceptions to NAFTA trading partners, Canada and Mexico, as well as key political and economic allies including the European Union, South Korea, Australia, Brazil and Argentina. It is clear that China is the main target of these tariffs and China has since responded in kind, applying tariffs to $3 billion in US imports of wine, fruit, pork, steel pipe and over 100 other products. The European Union stated that it remains on track to impose tariffs on a slew of US imports. Subsequent to quarter end, the US unveiled proposed tariffs on $50 billion worth of Chinese robotics, information technology and aerospace imports. China responded within a day with tariffs on $50 billion worth of US imports, notably soybeans and civilian aircraft.

The broad consensus is that cooler heads will prevail and the world will avoid a tit-for-tat trade war similar to the one experienced in the 1930s. Introducing new taxes via tariffs, hindering global trade and increasing political tensions could have a meaningful impact on global economic growth and equity market valuations. As the dollar value of tariffs rises, the likelihood of a negative shift in economic, interest rate and market expectations also rises.

NAFTA Negotiations

NAFTA negotiations are ongoing. At the end of the fourth quarter of 2017, tensions were high and very little progress had been made. Some progress appears to have been made in the first quarter of 2018 as the US reportedly softened its requirement of 50% American content requirement for US autos. The dialogue appears to have shifted slightly from "How much can we take from our NAFTA partners?" to "How much can we take from non-NAFTA partners, and how can we split that pie?" While NAFTA negotiators are adamant that a new agreement is not expected any time soon, any perception of agreement among negotiators is seen as a major improvement in the situation and could boost business sentiment in North America. We still think that NAFTA uncertainties are a

major risk to the Canadian economy and equity market but are somewhat more concerned with the deterioration in trade relations between the US and non-NAFTA economies.

Oil Price Summary and Outlook

The price of oil continued to climb higher during the first quarter, finishing the quarter at ~US$65 (WTI) versus ~US$60 (WTI) at the end of 2017. The oil market continued its march toward balance in Q1 with US oil inventories now sitting at their five year average. Economic instability continues to suppress Venezuelan oil output and is helping more than offset some of the non-compliance of non-OPEC members vis-à-vis the agreed upon production cuts. Compliance with the global deal to curtail oil supply hit a new record in February, with OPEC and non-OPEC allies achieving 138% of pledged output reductions. The current oil supply deal is in place until the end of 2018. Reuters reported that Russia and Saudi Arabia are in discussions to curtail production for a period of ten to twenty years which would establish a floor under the price of oil for quite some time, assuming compliance remains high. A ten or twenty year deal would be unprecedented and would likely be seen as transformative for the energy markets.

So long as economic growth appears robust, we remain constructive on energy prices and energy stocks. We believe the deals to curtail production currently in place, and future potential deals, will boost energy prices enough to greatly benefit energy stocks. This is particularly true for energy stocks outside of Canada.

As for Canadian energy stocks, the caveat is energy transportation. The oil price spread between Canadian Western Select (CWS) and WTI has narrowed since the end of 2017 but remains near US$25 per barrel in March. Cenovus, which accounts for almost 20% of Canadian oil production, announced in March that it will reduce production rates and store excess barrels of oil in its reservoirs as a result of a critical lack of crude oil export capacity in Western Canada. While it is expected that oil-by-rail transportation capacity will grow and reduce the oil price differential to a more reasonable level, the ramp-up in oil-by-rail capacity has been slow. Cenovus also noted a lack of pipeline capacity as a major driver of its decision. The spat between Alberta and British Columbia over the Trans Mountain pipeline heated up in the first quarter. Politicians in British Columbia blocked the project and forced the issue to be resolved by federal lawmakers and the Supreme Court of Canada. Albertan politicians condemned British Columbia's stance against the Trans Mountain pipeline and temporarily banned British Columbian wine in response. While the oil-by-rail and pipeline issues are likely to be resolved in due time, the headlines do not make Canadian energy companies particularly attractive relative to foreign counterparts.

Trader's VIX

In early February, equity markets sold off rapidly alongside a rapid increase in the, bear with us, implied volatility of S&P 500 options, or the Chicago Board Options Exchange Volatility Index, or colloquially the VIX. The VIX measures perceived equity market risk. Between February 1 and February 6, the VIX rose almost 300% from ~12.5 to ~49. For perspective, the only time in recent history that the VIX hit 49 was near the peak of the 2008 financial crisis. Seeing as the S&P 500 "only" fell ~10% during this period versus the 50%+ in 2008, something was amiss.

Over the past several years, fund managers and amateur investors increasingly bet against volatility or the VIX. This bet was wildly successful if expected volatility declined and was even successful if expected volatility was stable due to the mechanics of how investors bet against volatility – a concept that is beyond this commentary. Many of these investors likely thought that they could exit

the trade well before a spike in the VIX resulted in major losses – this had been the case for the entire history of the VIX. The VIX and equity markets have historically been highly negatively correlated and the idea was that market declines take time and increases in the VIX will take time. As we now know, if too many investors bet against the VIX and almost all of these investors want to exit the trade if the VIX begins to rise, the previous relationship between the VIX and the S&P 500 will break down and the VIX's rise will be far greater than the decline in the S&P 500.

There are a couple of theories about why equity markets declined in response to these VIX-related shenanigans. Firstly, VIX is seen as an investor fear gauge and if it rises significantly in a short period of time, this may trigger some investors to sell some of their equity holdings almost as a golden rule. Secondly, as the VIX rises, the cost to insure your portfolio against losses goes up and investors may be more inclined to sell some of their equity holdings outright to reduce risk. Lastly, and most importantly, the rapid rise in the VIX may have pushed some traders, fund managers and amateur investors to sell some of their equity holdings to cover margin calls related to their bets against volatility or the VIX.

Ultimately, the repricing of expected volatility and perceived risk could have a lasting impact on equity market valuations. It is still too early to tell whether the spike in the VIX was an anomaly and will normalize in the coming months or if the spike in the VIX was preamble to further equity market downside and volatility.

Manufacturing

After hitting a five year high in December, the global manufacturing economy as measured by the JP Morgan Global Manufacturing PMI hit a five month low in March. Activity remains more robust than most of the post-2008 economic cycle. Concerns about a global trade war as well as NAFTA negotiations are key factors affecting business confidence. The downshift in economic activity could result in falling economic growth and interest rate expectations going forward.

Housing

The new mortgage rules have taken a bite out of the Canadian housing market with sales activity falling to the slowest pace since Q1 2013, a pace that is more in line with historic norms. The new rules require that all new mortgage borrowers (i.e. those originating a new mortgage as well as those refinancing their mortgage with another lender) must show that they could handle mortgage payments using a greater of the contractual mortgage rate plus 2% or the five-year benchmark rate published by the Bank of Canada which currently sits at 5.14%. The rule is expected to reduce buying power by roughly 18%. In response to the reduction in buying power, first time home buyers have markedly shifted to buying condos over single family homes. Condo prices are positive year-over-year versus marked declines for single family home prices.

Politicians in British Columbia have pulled out all the stops to lower housing prices. BC politicians look keen on finalizing a 0.5%-2% speculation tax on secondary homes in many metro areas in the fall. This is in addition to increasing the foreign buyer tax to 20% (from 15%) and expanding its geographical coverage. We will learn more about Ontario politicians' housing market intentions as they rollout their platforms for the June election.

The days of rapid price appreciation are likely over as governments at all levels look to restrict buying power and impose new taxes. Further, if interest rates rise as broadly expected, this will further pressure household finances.

PIMG Balanced Growth Model

Lost 2.3% during the quarter. Performance figures for other periods are in the Appendix.

During the quarter, we bought new positions in Brandes Emerging Markets Value Fund (BIP571), Telus Corp (T), CIBC (CM) and Manulife Financial (MFC) and added to our position in iShares 1-3 Year Treasury Bond ETF (SHY). Please see the reasoning for our purchases below.

Brandes Emerging Markets Value Fund (BIP571)
We saw mid-January as a good time to add core emerging markets exposure to better diversify the portfolio and improve long-term expected returns. The severe cyclicality of emerging market economies and stock markets promote value investing over growth investing. Brandes has shown to be the most consistently value oriented and one of the best performing emerging market value managers over time. Value-oriented stocks began outperforming growth-oriented stocks in late 2016 after underperforming for the previous six years. This value over growth outperformance was predominantly in developed markets as interest rate expectations rose in these markets pushing financial sector valuations much higher. We think that emerging markets will see this same value outperformance as interest rate expectations rise globally and begin to boost the earnings of value-oriented companies. Value stocks outperform growth stocks about 80% of the time so this shift could indicate the start of a long period of outperformance for value stocks.

The fund holdings have a price-to-book ratio of 1x (versus the emerging markets benchmark at 1.7x), price to future earnings ratio of 9.6x (versus the emerging markets benchmark at 12.1x) and a dividend yield of 3.5% (versus the emerging markets benchmark at 2.4%).

Telus Corp (T)
Telecom stocks had been weak for the prior two months as investors shift from defensive stocks to cyclical stocks in response to improving global manufacturing data and the US tax bill. That said, telecom operators are actually more cyclical than defensive so we think the recent weakness will be temporary. Telus now traded at 17x trailing normalized earnings and should continue to experience 2%-3% organic growth over time as mobile phone growth tracks population growth and as data usage per user grows over time.

CIBC (CM)
CIBC is the most Canada-centric bank with above average exposure to the Canadian housing market, interest rates, consumers and businesses. Canadian financial stocks are depressed as a result of international investors' poor outlook for the Canadian housing market and its effect on the broader Canadian economy. As a result, the Canadian financial sector has not responded to rising interest rates to the same degree as international markets. The housing market appears to be weathering mortgage rule changes well. We think the worst is over for rule changes and any future changes will likely be stimulative to the housing market. CIBC trades at a 20%-30% discount to peers due to its above average Canadian exposure. We think this discount is excessive. That said, our bull case for CIBC would be tarnished if regulators applied measures similar to BC's speculation tax more broadly. We think this is unlikely for now.

Manulife Financial (MFC)
We switched from Sun Life to Manulife. Sun Life outperformed Manulife substantially over our holding period. Sun Life went from trading at a ~15% discount to Manulife to a ~10% premium,

based on a combination of earnings and book value. Sun Life is more sensitive to Canadian interest rates than Manulife. We see a much faster pace of interest rate hikes in the US than Canada and we think Manulife should trade at a premium to Sun Life as a result. Manulife currently has a dividend yield of 3.6% versus Sun Life at 3.3% and has a lower payout ratio leaving it with more cash flow to use for investment. This is the first time in years that Manulife has had a higher dividend yield than Sun Life. In addition to interest rate related investment gains, we think Manulife ultimately has better growth opportunities than Sun Life due to its greater presence in Asia and strong foothold in the US. Finally, Manulife's US businesses should see a material boost from the US tax changes that came into effect in 2018.

iShares 1-3 Year Treasury Bond ETF (SHY)
This ETF is an income generating place holder for US dollar cash.

During the quarter, we sold our positions in Jean Coutu Group (PJC.A), Algoma Central (ALC), Corus Entertainment (CJR.B), AMC Networks (AMCX) and Sun Life Financial (SLF). Please see the reasoning for our sales below.

Jean Coutu Group (PJC.A)
We sold our position in Jean Coutu as it had agreed to be acquired by Metro Inc. We saw little chance of Jean Coutu receiving a higher bid and thought we could find more upside potential elsewhere.

Algoma Central (ALC)
We sold out of Algoma as its outlook was somewhat less favourable than when we purchased it. Algoma has sold most of its real estate properties and used the funds to buy ocean-faring ships, one of the key reasons we purchased the stock. However, the supply glut of ocean-faring ships continues to persist and the glut is unlikely to go away anytime soon given the long-term outlook for trade has worsened under the Trump administration. Labour costs continue to be an issue for Algoma, and have worsened since we initially purchased the stock, as the company is experiencing difficulty hiring skilled mariners who are in short supply and are likely remain in short supply. We still think Algoma is attractively priced when compared to railway companies, which face many of the same issues that Algoma faces, but we are unsure whether this valuation gap will ever close.

Corus Entertainment (CJR.B)
The global media stock selloff that began in early 2015 has intensified. At the time of sale, Corus traded at only ~8x trailing earnings. In Canada, cord cutting has slowed significantly, most likely due to a relatively weak over-the-top offerings Canada. Netflix and Amazon offer much less content than in the US and there is no strong TV-operator backed competitor like Hulu in Canada. While Corus now faces an enviably stagnant TV subscriber base and has a good chance of maintaining the status quo over time, it has recently been affected by reduced TV advertising spend. Advertisers are gravitating to social media advertising irrespective of the neutral TV subscriber trend in Canada. While our initial forecast of the Canadian TV market was for cord cutting to slow due to the weak over-the-top offering in Canada, therefore allowing Corus to eventually return to a more normal earnings multiple of 15x-20x earnings, we did not fully recognize the risk of a long-term shift in advertiser budget allocations to TV, irrespective of subscriber trends. We sold our position in Corus as there is a fair chance that TV advertisers will continue to cut back on TV ad spending despite improving TV subscriber trends. We were driven to sell Corus when we did as it had held up well relative to the broad market during the February market decline and we are concerned about how Corus shares would perform in an economic downturn due to the company's large debt load.

AMC Networks (AMCX)
Like Corus, we purchased AMC at close to its lowest ever valuation and we sold AMC at its lowest ever valuation – roughly 7x trailing earnings. The kicker is that valuation declined over time. AMC's outlook was somewhat less rosy than Corus's due to AMC's US exposure and the rapid decline in US TV subscribers due to robust offerings by Netflix, Amazon and Hulu, among others. Similar to Corus, we sold AMC after it held up well relative to the rest of the equity market during the February market decline and we are concerned about how AMC shares would perform in an economic downturn due to the company's large debt load.

Sun Life Financial (SLF)
As described in the Manulife Financial buy commentary above, we sold Sun Life as it became seemingly overpriced relative to its peers.

PIMG Balanced Income Model

Lost 1.8% during the quarter. Performance figures for other periods are in the Appendix.

In line with trades in the Balanced Growth model, we bought new positions in Brandes Emerging Markets Value Fund (BIP571), Telus Corp (T), CIBC (CM) and Manulife Financial (MFC).

We also switched from BCE Inc. (BCE) to Rogers Communications (RCI.B) to bring the Balanced Income model in line with the Balanced Growth model. We prefer Rogers over Bell due to its limited exposure to the wireline segment and its superior mobile growth stats of late.

In line with trades in the Balanced Growth model, we sold our positions in Jean Coutu Group (PJC.A), Corus Entertainment (CJR.B) and Sun Life Financial (SLF).

Rogers Sugar Debenture D (RSI.DB.D) held in the Balanced Income model was redeemed by the issuer in March at par ($100).

Our View Going Forward

Going into Q1, equity markets, ex-Canada, fed off of the very optimistic economic environment that existed at the end of 2017 and early 2018. Since the market peak in January, economic growth expectations and interest rate expectations have ratcheted down, as have equity markets. Global manufacturing appears to have peaked at least temporarily, though this may be mostly the result of rising and potentially temporary trade tensions. As a result, equity market sentiment could be weak in the near-term. Longer-term, the picture is not so clear. While bear market indicators have been triggered (e.g. US Federal Reserve raising rates, earnings beats going unrewarded, price-to-earnings plus inflation greater than 20, excessive consumer and investor confidence, major spike in volatility) we have yet to see any sign of tightening credit conditions, worsening delinquency rates for credit cards or other debts and an inverted yield curve. Historically, all or almost all of these indicators were triggered prior to the start of an equity bear market. As a result, we are fairly confident that equity markets will continue to chug higher for the time being.

The one wildcard is a trade war. Subsequent to quarter end, major trade actions were followed by equity market selloffs so clearly we are not the only ones concerned. An escalating trade war could result in a business and consumer buyers strike and result in weak economic growth or even economic contraction. This would likely require tariffs that are much harsher than currently proposed and involve several different actors rather than just the US and China. We are fairly confident that, despite President Trump's seemingly brash approach, he is unwilling to single-handedly cause an economic downturn. Like his and his negotiators' approach to NAFTA, we believe the Trump administration will come out swinging against all the perceived trade wrongs committed by China but temper their approach over time in favour of smaller but more symbolic concessions.

Even after the recent equity market weakness, valuations remained stretched on a historical basis. That said, stretched valuation does not a market decline make. Valuations can remain stretched for quite some time.

Though we are value investors at heart and believe that owning value stocks is ideal in most market environments, we believe owning value is utterly essential at the current time. Growth stocks have been on fire since the recent economic upswing began in 2016. This upswing now appears to be petering out which could have a major effect on industrial, materials and consumer stocks. Further, technology stocks, the turbo boosted growth stocks of this market cycle, will be scrutinized severely by regulators following news that Facebook may have been too cavalier with user information. This shift in market momentum should benefit value-oriented and defensive stocks.

Our significant position in Canadian stocks has limited performance over the past quarter and for much of the past 12-18 months. We believe this trend of underperformance relative to international markets will end soon as NAFTA negotiations appear to be progressing, the outlook for oil prices has improved markedly over this time period (though the outlook for Canadian energy transportation has worsened) and the Canadian housing market appears to have normalized without too much ado. While we believe some discount is warranted for the Canadian equity market relative to international markets, we see that discount as excessive given Canada's stabilizing energy and housing sectors as well as Canada's close economic ties with a booming US economy. We added a core emerging markets position in the quarter as emerging markets, particularly value stocks in emerging markets, trade at a material and historic discount to developed markets, including Canada.

While we think it is prudent to eventually diversify further away from Canada, we believe now is not the time to do so provided current market valuations.

Corus Entertainment (since sold), Enbridge and Rogers Communications performed poorly during the quarter as they have high debt loads, and are therefore, interest rate sensitive and susceptible to economic sentiment. Corus and Enbridge face concerns about dividend sustainability and/or suffer from a weak dividend growth outlook as well. The energy sector was fairly weak in the first quarter and our position in Sprott Energy Fund underperformed as a result.

Cara Operations, TFI International and Sun Life Financial all outperformed as each company showed an improvement in profitability and growth. Our international value-oriented equity exposures (e.g. National Bank SmartData International Equity Fund and Brandes Emerging Market Value Fund) outperformed their relative benchmarks in the quarter as international value stocks had their day.

We continue to believe that the Canadian financial sector offers value relative to global peers but our optimism is more restrained relative to last quarter due to the BC government's notable actions against the housing market. Swapping Sun Life for Manulife is a symbol of this shift in sentiment.

At the end of 2017 we were keen to watch for bear market indicators and early warning signs as the economic outlook and investor sentiment appeared fairly extreme. While we have seen a few more warnings signs, we are not convinced there are enough to meaningfully change our positioning. This is especially true considering major equity markets are now already down 5%-10%. We would need to see a convincing confirmation of a persistently deteriorating economic picture before opting to sell when the equity market is well off its highs.

We have meaningful exposure to the industrials, financial and telecom sectors. We see these sectors offering the best value of all cyclical sectors, although telecom is partially seen as being defensive. We continue to avoid the materials sector and see it as a value trap. We think the risk to the materials sector has risen markedly as a result of the US-China trade war because any impact to global demand or trade will directly impact the materials sector. The energy sector is beginning to look enticing and we could see additional opportunities for investment in that sector in the second quarter. The energy sector is typically seasonally strong in the early part of the second quarter and most of the third quarter.

As at the end of Q1, the models yield 3.2% (Balanced Growth) and 3.4% (Balanced Income), from 3.1% and 3.6% at the end of Q4.

Sincerely,

Steele Wealth Management

The information contained in this report was obtained from sources believed to be reliable, however, we cannot present that it is accurate or complete. Information has been sourced from the RJL Bond Desk or RJ Private Client Solutions, unless otherwise noted. Index and sector returns represented in this commentary are measured using the S&P/TSX Total Return Index and S&P/TSX GICS Sector Indices as detailed in Raymond James Ltd.'s *Insights & Strategies: Quarterly Edition*. This report is provided as a general source of information and should not be considered personal investment advice or solicitation

to buy or sell securities. The views expressed are those of the author and not necessarily those of Raymond James Ltd. (Member Canadian Investor Protection Fund).

This Quarterly Market Comment has been prepared by Steele Wealth Management and expresses the opinions of the author and not necessarily those of Raymond James Ltd. (RJL). Statistics and factual data and other information are from sources RJL believes to be reliable but their accuracy cannot be guaranteed. The performance outlined in the report is net of fees. The client account performance may vary from the model portfolio due to several factors, including the timing of contributions and dates invested in model. The performance reported is that of the account that represents the model, not a composite. Performance calculation for the models may be different than the index used as a reference point. It is for information purposes only and is not to be construed as an offer or solicitation for the sale or purchase of securities. This Quarterly Market Comment is intended for distribution only in those jurisdictions where RJL and the author are registered. Securities-related products and services are offered through Raymond James Ltd.

Within the past 12 months, Raymond James Ltd. has undertaken an underwriting liability or has provided services for a fee in regards to the securities of Algoma Central Corporation, CIBC and Manulife Financial.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

Appendix

Model	3-mos	6-mos	1-yr	3-yr	Since Inception
Balanced Growth	-2.3%	0.2%	2.3%	2.1%	5.0%
Balanced Income	-1.8%	0.7%	2.6%	3.2%	5.6%

The above performance data is current as of March 31, 2018. The returns above incorporate a 1% annual investment management fee, charged monthly, which is also subject to 13% HST, charged monthly, for a total cost of 1.13% annually. Inception date for the Balanced Growth model and Balanced Income model is January 15, 2014. Performance figures for periods greater than 1-year are annualized.