ISSUE 102 | DECEMBER 2019

Taking Stock with Steele

Your Monthly Newsletter

The purpose of this newsletter is to share insights and expertise. Our goal is to ensure that our clients are well informed of changes affecting local business decisions and our investment recommendations. We believe Knowledge Pays and we want our knowledge to help pay for you.

MUTUAL FUNDS IN AN EXCHANGE-TRADED WORLD

As part of our charitable draw, a participant inquired,

"ETFs (exchange-traded funds) seem to be all the rage compared to mutual fund as they are a very cost effective way to diversify your investments. So why do mutual funds still exist and who is buying them?"

We love this question. Business news has covered the rise of ETFs and the demise of mutual funds for years. The ETF v. mutual fund bout is the investing world's Ali v. Foreman. But like Foreman, mutual funds have stood their ground through time and remained a venerable contender. Canadian mutual fund holdings are still ~9x the size of ETF holdings. No word yet on a mutual fund endorsed grill but you never know.

We can understand why some investors, especially those who no longer use mutual funds, cannot understand why mutual funds are still around. *There are several not-so-noticeable reasons why mutual funds have maintained relevance.* Here they are…

1. Industry Structure: MFDA (Mutual Fund Dealers) v. IIROC (Investment Dealers)

Some financial organizations are "mutual fund dealers" and are members of the Mutual Fund Dealer's Association of Canada (MFDA). MFDA advisors can only recommend mutual funds. Clients of these firms would therefore only be able to invest in mutual funds. Raymond James Ltd. is an investment dealer and is a member of the Investment Industry Regulatory Organization of Canada (IIROC). IIROC advisors can recommend a variety of investment products depending on an advisor's licenses.

2. Investment Landscape and Products Available

Until very recently, mutual funds were the best way to access smaller or more complicated market segments such as fixed income and international markets. Even IIROC advisors like us use mutual funds to round out fixed income and international allocations. ETFs have since caught up and are now worth considering in these areas.

3. Relative Pricing Between Mutual Funds and ETFs

In their early days, passive ETFs were notoriously low cost relative to active mutual funds. Mutual fund fees have become more competitive with passive ETFs. These days, many active mutual funds are launched with a matching active ETF. While passive ETFs are still cheaper than active ETFs and mutual funds, the difference is not much more than the historical excess returns generated by active portfolio managers.

4. Do-It-Yourselfers May Rely on the Familiarity of Mutual Funds

Investing is still an intimidating and potentially complicated process and many who opt to do-it-themselves tend to rely on product companies and product names they have entrusted their money with in the past – i.e. mutual funds.

Current Rates & Data

Govt of Canada

90 day	1.64%
1 year	1.73%
2 year	1.68%
5 year	1.64%
10 year	1.65%
30 year	1.74%

U.S. Treasury

90 day	1.55%
1 year	1.53%
2 year	1.62%
5 year	1.70%
10 year	1.87%
30 year	2.30%

Canada Prime Rate

3.95%

U.S. Prime Rate

4.75%

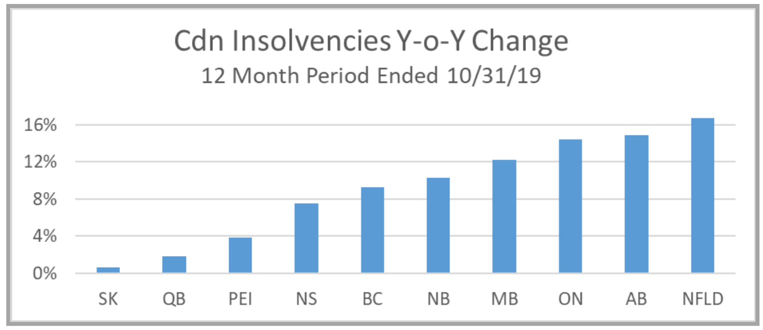
Exchange Rates

CAD/USD	0.758
USD/EUR	1.111
JPY/USD	109.3

ECONOMIC TIDBITS US DELAYS TARIFFS SET FOR DEC 15 & CDN CONSUMER STRUGGLING

- US-China trade negotiations have become more amicable. Slow global growth looks to have motivated both parties to seal a deal. To date, the best solution is a "phase one" trade deal whereby China pledges to buy US agricultural products, reform its intellectual property laws and open up its financial sector in exchange for lower US tariffs. That said, there is nothing binding the parties to comply.

- Canadian personal insolvencies hit the highest level in a decade in October. This spike came as a surprise as employment growth was strong in the first half of 2019, though the data has since turned negative. In Q4, many Canadian banks raised their loan loss provisions for the next year. Ontario and Alberta saw big spikes in insolvencies while in Quebec insolvency growth was muted.



LE JIT A "JUST-IN-TIME" RUNDOWN OF OUR CURRENT INVESTMENT THEME

Canadian Beverages for Cheap, Just In Time for the Holidays!

- <u>**Lassonde Industries (LAS.A)**</u> and <u>**Corby Spirit & Wine (CSW.A)**</u> are two ideas related to this theme.
- **Lassonde** is one of North America's largest fruit and vegetable beverage producers with products marketed under brands such as Oasis, Rougemont and Fruite. Lassonde also operates packaged food and wine businesses. Lassonde shares have fallen ~50% from the June 2018 highs as higher transportation costs ate into profit margins. A shortage in North American truckers caused a temporary spike in labour costs that should normalize over time. Lassonde's profitability will likely recover as transportation costs come back down. Lassonde shares trade at ~7.7x trailing EV/EBITDA, well below US packaged food peers at ~12x trailing EV/EBITDA on average, despite Lassonde's more "on-trend" business.
- **Corby** produces and sells brands like J.P. Wiser's whiskey and Polar Ice vodka and is the Canadian distributor for Pernod Ricard's brands including Jameson Irish whiskey, Glenlivet and Chivas Regal scotches, Beefeater gin and Absolut vodka. Pernod Ricard owns 46% of Corby's shares outstanding. Corby shares trade at ~7.7x trailing EV/EBITDA, well below global spirits producers at ~20x, though a meaningful discount is required due to Corby's limited growth opportunities and lack of geographic diversification.

  Key risk points: Both stocks are Canada-centric businesses that would come under pressure if Canadian consumers reduced consumption. Both stocks have low trading liquidity so the stocks may be more volatile than larger peers, especially around news events.

JEANNINE'S TIP O' THE MONTH TFSA Limit for 2020 is $6,000

The TFSA annual contribution limit for 2020 is $6,000. The total cumulative contribution room available will be $69,500 as of January 2020 for those who have never contributed and been eligible to contribute to a TFSA since 2009.

Those who have used TFSAs in the past may have more room depending on contribution and withdrawal activity. You can check MyCRA to confirm your contribution room if you are unsure. Start planning now for TFSA contributions in early January!

This newsletter has been brought to you by Steele Wealth Management

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