HugganWhite Wealth Management

Protect Capital. Manage Risk. Provide Income.

First Quarter 2017

Much to the surprise of many investors and market participants, the first quarter of this year proved to be relatively favourable. Heading into the quarter, the majority of the attention was focused on the official inauguration of Donald Trump and the fear of the unknown with an unconventional leader now at the helm. In addition to the drama surrounding the new administration on this side of the pond, European markets were also riddled with their own political uncertainty as elections in both Germany and the Netherlands moved to centre stage. Despite the perception that recent politics can be major market moving events (I don't underestimate that they can), so far investors have shrugged off their suspicions and have preferred to focus more on fundamentals and real data. Indeed, this is a wise approach and a strategy that we have supported for many years.

Looking at closing figures for the quarter, the S&P 500 was up 6.1%, the Dow Jones Industrial Average posted a gain of 4%, while our Canadian based TSX Composite managed a small gain of 1.7%. European markets also saw strength, with indices such as the German DAX, French CAC40 and Spanish IBEX 35 gaining between 5% and 11%, an indication that their economies are showing much improvement. Digging deeper into the sector level, the groups that were believed to most benefit from the "Trump" trade, such as industrials and financials, ultimately gave up some of their early 2017 gains, as large cap names in technology, discretionary and healthcare showed better performance. This is possibly a sign that investors are rotating from more cyclical names and building their exposure to more defensive names, a possible emerging trend we are watching closely. Moving forward, we believe further gains will likely be predicated on the success of the new administration to advance their agenda which is focused on deregulation, infrastructure spending, corporate tax reduction and more favourable fiscal policy. With the failure of repeal and replace Obamacare, as voted down by Congress in late March, we also believe that the uphill battle Trump faces has now become a reality. The CEO of a private corporation is much different than the CEO of a "publicly traded company" who is responsible to the shareholders. In this case, the shareholders are Congress, Senate and the American People.

As mentioned above though, for the here and now, markets are more focused on data such as growth and earnings. Economic indicators seen throughout the quarter continued to show signs that the U.S economy is improving or at the very least "holding the line". A few of the most widely followed indicators such as employment, manufacturing and business optimism all showed resilience and in some cases produced their best readings pre-financial crisis 2008/2009. Inflation does appear to be trending higher, with energy prices contributing largely to the increase in headline CPI in response to a ~100% pickup in crude oil prices from a year earlier. Thus, the Federal Reserve in the U.S. raised rates another 25 basis points, the second increase in three months. They also noted that they may look to raise rates two more times in 2017, but those decisions would be data dependant. Here in Canada, there is little or no chance of a rate hike by the Bank of Canada in 2017, as our economy continues to muddle through and the "hangover" effect from the oil collapse of 2015 continues to weigh on a few key contributing provinces. Further to this, we believe the Bank of Canada is closely watching Canadian debt to income levels, which are now at all-time highs and a reflection of a real estate market that has driven lending to historic proportions. Thus, the Bank (and the Canadian economy) has essentially backed itself into a corner and any consideration of increasing rates will have to be managed carefully and prudently. We view this as a key risk. Overall, the U.S. 10 year treasury finished the quarter essentially flat at 2.40%, while the Canadian 10 year bond closed at 1.62%.

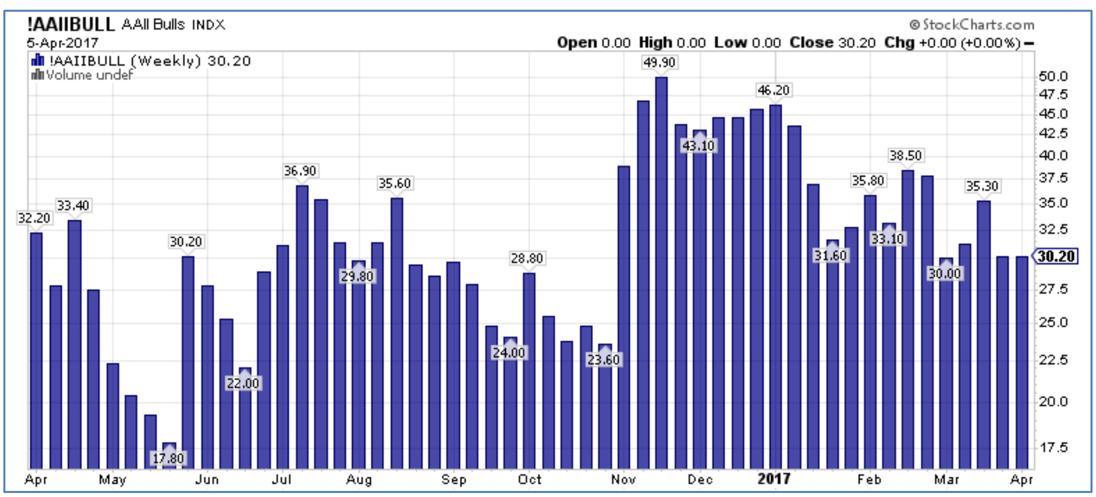
12-Month Earnings per Share

	Operating Earnings (estimates are bottom-up)	As Reported Earnings (estimates are bottom-up)
2018	**$146.98**	**$132.18**
	$142.94	$129.62
	$139.04	$127.59
	$134.93	$124.32
2017	**$130.66**	**$120.43**
	$124.00	$114.68
	$118.82	$108.38
	$112.49	$102.09
2016	**$106.86**	**$96.76**

Source: Standard & Poor's, Raymond James Research. Data as of February 16, 2017.

We are now entering first quarter earnings season of 2017, which as always, we will be watching closely. If analyst consensus can come in anywhere near the mark, we see the market as fairly valued. Current bottom up forward earnings estimates call for ~$130 for fiscal 2017, which at a current S&P 500 level of 2,375, this produces a P/E multiple of ~18x. This is marginally ahead of historical averages, but not expensive compared to previous market peak valuations. Earnings contribution is largely driven by financials, technology, healthcare and discretionary, sectors we will be monitoring to determine the accuracy of expectations. With energy prices firming up since the first quarter of 2016 and capital expenditures administered more frugally, earnings from this sector may help to provide a boost to the $130 estimate. At this time we are still cautious on the energy sector as rig count has jumped materially year over year and stockpiles are at/near record highs. West Texas Intermediate appears to be consolidating around the $50 dollar mark, but we are not yet willing to make an all-out bet on this commodity.

Turning over quickly to a few of the technical indicators we track, seasonality does favour the second quarter as it only trails that of the fourth quarter dating back to 1928 (see chart at the bottom of the next page). Bullish sentiment amongst investors did reach a high of approximately 39% earlier in the quarter, but has backed off to a level of 30% more recently as seen below. This is a positive development as excessive bullishness is a sign of increased optimism (and possibly euphoria if levels significantly spike) and is generally accompanied by an exhausted market (read:top). There is no indication of outright bullishness at this time based on consensus. Further confirmation of this can be seen in fund flows throughout the quarter, as net inflows continued to favour bonds over equities, a trend that has been in place for eight years (see chart at the bottom of the next page). Not only are retail investors skeptical of equities here in North America, but so are global fund managers as they stepped off the proverbial gas pedal, trimming their holdings of U.S. stocks to the lowest level since Fall of last year. And finally, the risk premium to own equities relative to fixed income continues to favour that of equities, as the earnings yield for the S&P 500 less the 10 Year Treasury shows a ~210 basis premium. These, along with a host of other indicators we track, continue to validate our belief that the longer term secular bull market for equities remains alive and well. We are cognizant that this can change at any time and will respond if markets or data flash any red lights. But based on our work at this juncture, allocations across portfolios will reflect our bullish tilt.



The transition of portfolios to our Private Investment Management Group (PIMG) has been a great success thus far. The feedback from clients, who have been introduced to PIMG, has been extremely positive as they also see the many benefits that this platform offers. The individual tailored asset allocation, greater transparency, individual tax planning, increased trading efficiencies and lower management costs are all highly beneficial and are "tools in the box" that we can utilize to further enhance our offering. Do recall though, that the change of individual positions will take time as we want to diligently manage that process and ensure that we are exiting or entering names when timing is best. With so many names/strategies already "best in class", we are looking to tweak portfolios and only introduce positions that will enhance return, without assuming undue risk. This was carried out throughout the quarter as we reduced exposure to a number of portfolios that had higher exposure to Canadian banks. Our research and analysis concluded that Canadian banks were trading at a significant premium to global peers, and thus we decided to trim select names. We also added names in the consumer staple and midstream energy infrastructure sector with additions such as George Weston, Jean Coutu and Gibson Energy. At this time, we are also looking to increase our global exposure and are considering a few different strategies that will likely be implemented in the near term.

In summary, we are very pleased with the positioning and performance of the portfolios over the course of the quarter as they all benefitted from the underlying strength of the market. Our focus going forward on the equity side will be on high quality, dividend paying names, while the fixed income component will be on shorter term, corporate issuances that carry a solid credit rating and offer attractive liquidity. As always, our main focus will be to protect your capital, manage the volatility and ensure that we provide an acceptable rate of return that compliments your risk tolerance and longer term objectives. Thank you for your trust and confidence in allowing us to manage your financial affairs. We will keep you updated moving forward.

Sincerely,

Craig White, CIM, FCSI
Senior Vice President | Portfolio Manager | Raymond James Ltd.
T: 250.979.3044 | TF: 1.877.979.2700 | F: 250.979.2749|
craig.white@raymondjames.ca
Suite 500, 1726 Dolphin Ave | Kelowna | BC | V1Y 9R9 | Canada

Net Flows into Mutual Funds + ETFs ($BN)

Year	Domestic Equity MF	Domestic Equity ETF	International Equity MF	International Equity ETF	Bond	Money Mkt
2009	-27.6	30.9	29.6	39.6	417.2	-539.1
2010	-81.1	46.7	56.7	41.5	262.0	-525.1
2011	-133.3	47.3	4.1	24.3	163.7	-124.1
2012	-159.1	80.9	6.4	51.9	358.5	-0.2
2013	18.1	104.1	141.4	62.8	-59.0	15.0
2014	-60.2	141.5	85.4	46.6	94.5	6.2
2015	-170.8	65.4	93.9	109.7	29.4	21.5
2016	-235.4	167.6	-24.5	20.1	190.1	-30.3
2017 YTD	-11.1	16.0	2.5	12.4	35.5	-48.1
TOTAL	-860.4	700.4	395.5	408.9	1491.9	-1224.2