SEAMARK

THE LATEST

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38 Years in Industry

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CIO Commentary / Q4 2017

With the turn of a new year, it is time to take pause and survey the investment landscape.

2018 will mark the ninth year of an economic recovery in the United States. Although impressive in duration, the recovery has been anemic when compared to growth rates of prior economic expansions. The recovery required a bigger dose of stimulus, more for longer, causing the federal debt to double under President Obama's term. However, the breadth of the U.S. economy should not be underestimated. An important new engine of growth has revved up over this period, with the U.S. moving toward becoming a self-sufficient energy producer.

That development has had repercussions for the Canadian economy. Our financial service companies fared much better than most during the financial crisis of 2008/9, but we cannot escape the fact that Canada is a commodity based economy, particularly joined at the hip to the energy sector. So, while the U.S. was able to navigate a steady recovery since 2009, the Canadian economy found itself foundering along with the collapse of oil in 2015/16.

The U.S. route to self-dependency on energy has started to hurt Canada at many levels. A reduction in demand from our biggest customer is just the tip of the iceberg. For most of 2017, Canadian 'spreads' for oil have seen discounts from the WTI North American benchmark price of crude range from $10-$15 US per barrel. This discount has recently widened out to exceed $20. Well- funded pipeline protests by U.S. interests have largely focused their efforts on Canadian projects, and have succeeded in locking-in our energy production. In sum, U.S. self-sufficiency in energy has delivered a strong blow to the Canadian energy-rich economy.

With that as a background, what lies ahead for the U.S. and Canadian economies? The path to growth appears to be more assured and on a stronger footing in the U.S., than in Canada. Since assuming office, President Trump has set in motion many business-friendly initiatives, including the roll-back of regulations and most recently, significant corporate tax reform. U.S. corporations will no longer be taxed on a worldwide basis, an approach that had in effect led to double taxation, and trillions of dollars of profits being 'stranded' offshore. Moreover, the U.S. corporate tax rate is also being reduced, to better compare to tax rates of other countries that domicile corporations that compete with U.S. corporations. U.S. Corporate tax reform is expected to add about 5% to S&P 500 earnings in 2018.

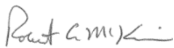
Along with organic growth of over 5%, U.S. corporate earnings may see double digit gains in 2018. Just like the energy story, U.S. corporate tax reform has a downside for Canada. No longer will Canadian companies have a significant tax advantage over their U.S. counterparts. That changes the business economics, making it more difficult to attract U.S. companies to establish in Canada, and making it harder to keep U.S. plants open north of the 49th parallel.

And then there is NAFTA. The not so behind the scenes talk is that there is a lot of concern about the state of negotiations. It is hard to see Canada coming out ahead, especially if Donald Trump were to withdraw the U.S. from the current agreement.

Interest rates on both sides of the border appear poised to rise further in 2018 on the strength of extended economic growth. The direction is clearly higher, the only debate is how many hikes of 25 basis points will be enacted. The wild card is inflation, which has been unusually tame this far into an economic cycle. Curiously, the U.S. may be about to experience demand-pull inflation, based on its underlying economic strength. Canadian inflation has the potential to be driven more by cost-push inflation, as employers seek to recover higher costs due to rising minimum wage levels across many parts of the country. Even with a modest pick-up in CPI, we expect returns for long dated bonds to be negative in 2018.

Notwithstanding that the economic prospects look very strong for the U.S., all the non-money considerations remain a concern. So far, the market has chosen to completely ignore Washington's antics and a host of geo political factors. It has now been a couple of years since the market had even a hint of a correction. Investors shouldn't be surprised when markets eventually deliver the needed pause that refreshes.

Sincerely,



Robert G. McKim, CFA | Chief Investment Officer

Bubbles

By the end of 2017, it is fair to say that many investment classes were considered to be in the formation of a bubble. A bubble occurs when the price of the asset is well above its normal valuation and no one seems to care, so prices continue to soar. One could point to the rapid rise in the price of Bitcoin, housing prices in Vancouver and Toronto, and share prices in the U.S, that had risen for 14 consecutive months, as three prominent examples. A sober view would ask: Are investors being greedy? When should they be fearful?

For over 35 years, we have lived in an environment of falling interest rates. This period has yielded an entire crop of financial advisors, along with many of their clients, who have never experienced the impact of inflation and rising interest rates. Both bonds and equities have benefitted from this environment, but as we approach the tenth anniversary of the financial crisis of 2008, the days of central bank accommodation appear to be over. Both the U.S. Federal Reserve and Bank of Canada imposed two interest rate hikes in 2017, and the Fed has telegraphed additional increases for 2018. Rising rates make all things less affordable, so demand is reduced, and prices eventually adjust. Consider for example, that a person who can just afford a home mortgage at today's rates, may have to default on payments if rates went up by only 1%.

As this economic transition nears, investors should begin to transition their investment objectives from enhancing their capital, to preserving it.

During bubble periods, prudent approaches to building wealth are often disregarded. Investors throw caution to the wind to chase the apparent easy returns in asset classes that show positive momentum. And thus, the building of a bubble. As risk managers, we fear that in searching for better returns, investors are swapping one type of risk for another, often taking on additional, less understood risks. Private assets such as real estate, may appear to be less volatile than publicly traded assets, simply by virtue of the fact that there is little price transparency until actual trades are recorded. Unlike the market for publicly valued assets, liquidity in private assets is significantly lower, and may be disrupted for much longer during any new crisis.

The proliferation of Exchange Traded Funds (ETFs) in recent years has served to accentuate the run for most asset classes. It is our view that ETF buyers think primarily top-down, making simpler decisions based on thematic or momentum considerations. Traditional money management has a higher component of bottom-up thinking, that is, looking at the valuation of the specific company before investing. The top down participant thinks that it is a stock market, the bottom up practitioner sees it as a market of stocks.

ETFs that are designed to mimic the performance of market averages typically invest more dollars in the largest companies, creating a top-heavy phenomenon that the non-discerning buyer may not be fully aware of. So far, this has been a one-way street, with U.S. indexes making successive new highs, month after month. It concerns us that ETF buyers may not be fully aware of what they are buying, or what they are paying for. Further, many ETFs contain derivatives that help the product mirror its underlying index. A market shock would prompt these strategies to programmatically sell into weakness, causing a disorderly unwinding of investments and violating the number one rule of investing - buy low and sell high.

To conclude, our concern is that investors may not appreciate the level of risk that comes with high valuations for multiple asset classes. Money can still be made through discerning securities selection, however momentum strategies should be pared back or avoided. We urge investors to take stock of their risks and to pro-actively manage them, rather than wallowing in the pleasure of daily upward marks to market.

Don Wishart, CPA, CMA, CFA | President

A Year-End Note to our Private Clients:

Did you know… SEAMARK can manage your registered accounts, such as your RRSPs (Registered Retirement savings Plans) and TFSAs (Tax-Free Savings accounts)?

RRSPs – The deadline to contribute to your RRSP for the previous tax year is 60 days following the year-end. So, for the 2017 tax year, the deadline is March 1, 2018. For the 2017 year, your RRSP contribution room is the lower of 18% of the earned income you report on your tax return in the previous year, up to a maximum of $26,010. Note that if you are a member of a pension plan, your pension adjustment will reduce the amount that you can contribute to your RRSP. Don't forget, you can carry forward unused contribution room from previous years.

TFSAs – A Tax-Free Savings Account allows your investments to grow tax-free. That means you will not be required to pay taxes on interest, dividends, capital gains and any withdrawals, at any time. As of January 1st, 2018, a new year began for your TFSA contribution limit. You can now contribute to the 2018 limit of $5,500. If you have never contributed to a TFSA, your limit space is now $57,500. The TFSA program began in 2009 and from the age of 18, your contribution room has accumulated annually, and carries forward indefinitely. Another point to remember is that if you make any withdrawals, you regain that contribution space in the next calendar year.

The annual TFSA limit has fluctuated since its inception and breakdown as follows:

Year:	Annual Limit:	Total Limit:
2009	$5,000	$5,000
2010	$5,000	$10,000
2011	$5,000	$15,000
2012	$5,000	$20,000
2013	$5,500	$25,500
2014	$5,500	$31,000
2015	$10,000	$41,000
2016	$5,500	$46,500
2017	$5,500	$52,000
2018	$5,500	$57,500

Contact one of our Portfolio Managers for more information at information@seamark.ca or by calling 1-888-303-5055 and to see how SEAMARK can help manage your registered accounts.

2016 Pooled Fund Capital Gains Tax Deferrals

	Tax Loss Carry Forwards*
SEAMARK Pooled U.S. Equity Fund	$ 22,058,047
SEAMARK Pooled Total Equity Fund	$ 17,700,378
SEAMARK Pooled Low Volatility Equity Fund	$ 4,933,560
SEAMARK Pooled Canadian Equity Fund	$ 4,999,362

*Audited Financial Statements, as at December 31, 2016

Some of these tax loss deferrals are significant compared to the assets in the respective Pools.

Please contact Danielle MacLeod for more information:
902-423-1172 dmacleod@seamark.ca

Composite Performance Update[1]

December 31, 2017

	One Quarter	Six Months	Nine Months	One Year	Two Years	Five Years	Inception Returns	Inception Date
SEAMARK Balanced Composite	**2.97**	**3.05**	**2.06**	**4.89**	**6.83**	**9.70**	**8.13**	12/31/2009
Balanced Benchmark*	3.59	4.20	4.54	7.38	7.57	8.27	7.36	
SEAMARK Low Volatility Equity Composite	**3.05**	**2.83**	**3.30**	**6.68**	**9.50**	**12.77**	**11.14**	12/31/2010
S&P/TSX Composite Index	4.45	8.30	6.52	9.10	14.92	8.63	5.76	
SEAMARK Canadian Equity Composite	**3.50**	**5.39**	**3.61**	**5.20**	**12.27**	**9.56**	**7.96**	01/31/2011
S&P/TSX Composite Index	4.45	8.30	6.52	9.10	14.92	8.63	5.68	
SEAMARK Total Equity Composite	**3.62**	**4.36**	**2.53**	**5.90**	**9.02**	**13.23**	**13.43**	09/30/2011
Total Equity Benchmark**	5.49	7.83	7.71	12.07	12.62	13.83	13.65	
SEAMARK Fixed Income Composite	**1.76**	**0.53**	**1.15**	**2.58**	**2.18**	**2.84**	**3.13**	04/30/2012
FTSE TMX Canada Universe Bond Index	2.02	0.15	1.26	2.52	2.09	3.01	3.31	
SEAMARK U.S. Equity Composite	**4.39**	**3.78**	**0.59**	**3.41**	**8.53**	**16.64**	**15.78**	04/30/2012
S&P 500 Index (CAD)	7.21	7.72	8.16	13.84	11.18	21.29	19.45	

*5% FTSE TMX 91 Day T-Bill Index, 40% FTSE TMX Canada Universe Bond Index, 30% S&P/TSX Composite Index, 25% MSCI World (ex-Canada) Index
**50% S&P/TSX Composite Index, 35% S&P 500 Index, 15% MSCI EAFE Index

Links to Q4 2017 Pooled Fund Profiles

Balanced | Canadian Equity | Low Volatility Equity | Canadian Bond | U.S. Equity | Total Equity

Stay in Touch!

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[1]Performance data is calculated on an actual basis for periods of less than one year, and on an annualized basis for periods of one or more years. Performance data assumes the reinvestment of all distributions and does not take into account management fees or income taxed (except for withholding tax, if any, on foreign income) payable by any unitholder that would have reduced returns. Past performance is not necessarily indicative of future returns. For GIPS® presentation please email information@seamark.ca