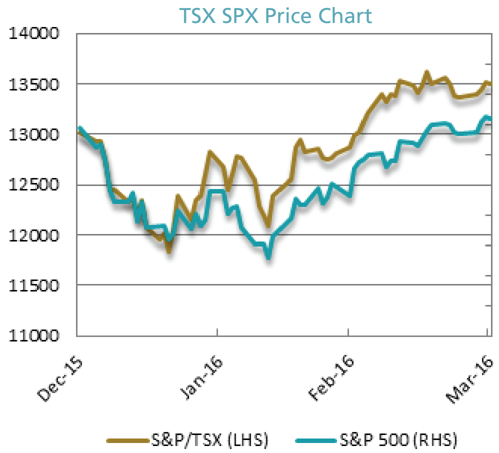
GROW TOGETHER

CWB Wealth Management Newsletter Q2 2016

President's Message *by David Schaffner*

February 11th: "Global markets are collapsing", Business Insider

March 31st: "Dow posts biggest quarterly comeback since 1933", CNBC.com



Stock markets got off to a rocky start in 2016 (see chart), generating sensational negative headlines in the media, only to more than fully recover. During the down times in the market, immersed in all the doom and gloom, our brains are wired to avoid taking risk which can delay our investing, or worse yet, lead us to sell at the most inopportune times. Thankfully we have a way to deal with this, and the cure is twofold.

The first thing we need is a financial plan; a roadmap to our long term goals that incorporates a disciplined approach. Nobody likes to lose money, and it is hard to stay the course in the face of the jarring headlines. How many people decided to wait it out this latest round of volatility? As you can see in the chart, when the markets rebound, they can move quickly. That is where the value of the plan comes in, with the focus on the right asset allocation and contribution schedule to take advantage of the ups and downs.


David Schaffner

Managing investments across multiple asset classes takes a lot of resources. You need a team of people on your side that have the knowledge, experience, and temperament, along with a process that is consistently applied over time. Is it any wonder why, most people realize the second cure is to leave the investing to the professionals?

With the CWB Onyx Portfolio Series, our advisors can match a client's financial plan and risk profile with the right solution. The Onyx funds are managed by the professionals at our partner companies, Adroit Investment Management and McLean & Partners, whose independent research has emphasized fundamental analysis and risk management for many years. You don't need to worry about being disciplined through the market volatility – the Onyx funds do it for you.

In this issue:

CWB WEALTH MANAGEMENT

Europe & China: Road to Recovery

by McLean & Partners Wealth Management

The European Central Bank (ECB) announced important initiatives in the March 10th policy meeting that will stimulate its still-sluggish economy, reaffirming our confidence in Europe's economic recovery. The ECB said it will:

1) cut the refinancing rate from .05% to zero;

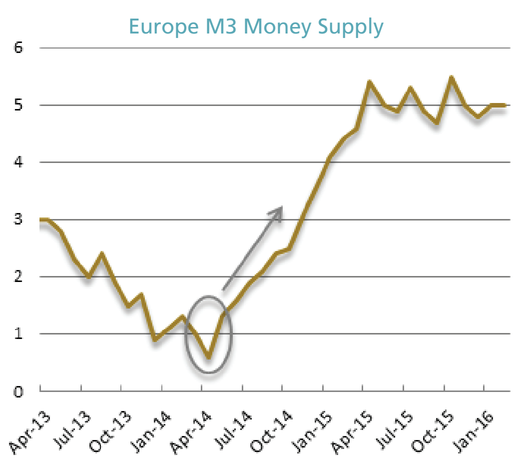
2) reduce the rate paid to commercial banks on overnight deposits from -0.3% to -0.4%;

3) increase its quantitative easing (QE) program by EUR$20B/month to EUR$80B;

4) extend QE bond purchases to include investment grade private-sector issues; and,

5) introduce a second tranche of targeted long-term refinancing operations (TLTROs) under which commercial banks can borrow up to 30% of the book value of their non-mortgage private loans at 0% to -4% interest over four years.

These moves demonstrate the resolve of ECB president Mario Draghi and show that the bank still has tools that it needs to boost the economy and fight deflationary pressures. These initiatives are expected to continue boosting the M3 money supply (cash in circulation plus large liquid assets), improve GDP growth and support European stock markets. The figure below demonstrates ECB policy has already been successful in increasing the money supply from trough levels in April 2014.



Source: Bloomberg

As for China, while some observers predicted uncontrolled currency devaluation and a hard landing for the economy, thus far neither has materialized. In fact, the Chinese economy continues to outperform expectations. Recent economic data suggests that China is in a recovery phase. The March Caixin manufacturing PMI jumped to 49.7 from 48.0 in February, much stronger than the expectation of 48.3. Meanwhile, the official manufacturing PMI rose to a nine month high of 50.2 in March from 49.0 in February, with estimates at 49.4. Similarly, the official non-manufacturing or services PMI came in at 53.8 in March up from 52.7 in February. So far in 2016, the value of the renminbi has remained constant and January market tremors have subsided. Capital outflows have dramatically abated, while foreign exchange reserves that are needed to defend the renminbi remain safely above $1.5-1.7 trillion, this is widely viewed as the required level to keep the currency stable.

Since mid-February, four developments have strengthened the emerging markets:

1. China has improved its communication with regards to its monetary policy;
2. China and India have become more active in using fiscal policy to stimulate their economies;
3. The Fed has dialed down its rhetoric on interest-rate normalization (higher rates) leading to a lower U.S. dollar; and,
4. There's increased awareness that many emerging nations are net importers of raw materials and benefit from lower commodity prices.

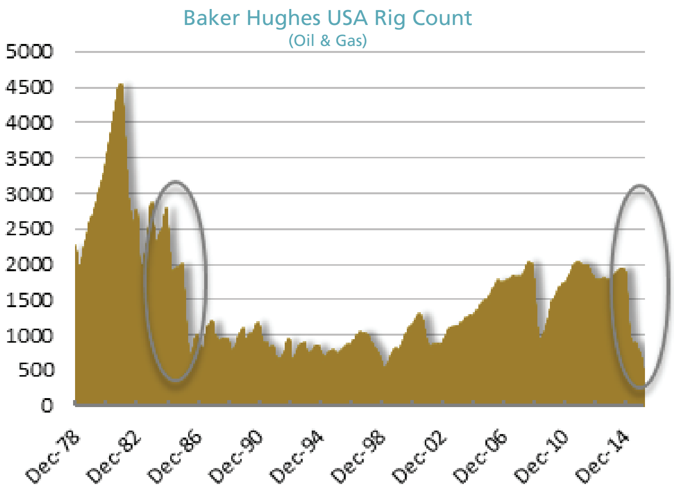
We continue to view the risk/reward in both Europe and China positively. Recent sell-offs in both regions provided compelling opportunities to add to some of our existing positions at very attractive entry points.

Oil Price Bottom…"Are we there yet"?

by Adroit Investment Management

Over the past three decades there have been four major declines in the price of crude oil that occurred in 1986, 1997-1998, 2008 and 2014 to present. The recent decline is most similar to the 1986 price shock where Saudi Arabia abandoned its role as the global 'swing producer', driving the price of oil down 75% from its June 2014 peak. The oil industry is now crying "uncle" and investors are asking the question "are we there yet"?

One way to search for an answer is to look at the drilling rig count, as they won't be 'turning to the right'[1] if the underlying commodity price is not high enough to generate an economic return on investment.



Source: Bloomberg, Baker Hughes, Adroit

When Saudi Arabia 'turned on the taps' in 1986 the world had growing oil production at a time of weak oil demand growth and prices dropped almost 70% – a situation similar to today. As shown in the chart this grueling downturn (left oval) took the rig count down about 75% in a few months establishing a multi-year low. In the current decline (right oval) the number of rigs working[2] is at 443, again setting a new all-time low. By this measure one may conclude that history is suggesting we are close to a bottom in the oil price cycle and in the number of rigs working.

Looking at the oil & gas world through the lens of a drilling rig is admittedly a 'simplistic view' since one needs to have a deeper look into some of the recent structural changes that have occurred in the oil business such as horizontal drilling and multi-stage fracking. These technological changes have enabled the USA to almost double its oil production by adding about 4.5 million b/d of supply since 2008 from a previously uneconomic resource called shale oil. Another important factor is that shale oil production declines[3] quickly, typically in the 50-70% range after one year of production. With lower prices, producers have been forced to cut spending which will result in lower production in the USA and Canada in the next year or two.

Offsetting production declines is the return of additional barrels of oil from Iran and worries of weakening global demand growth. Furthermore, back to our lens of the drilling rig, almost 1,500 drilling rigs have been idled since 2014. When prices recover we know that many of these efficient rigs will go back to work and the industry has demonstrated the ability to add oil production quickly with them 'turning to the right'.

So – "are we there yet" and have we seen the bottom at $26 oil in February, 2016? Looking at drilling rigs working it appears that we may have, but only time will tell. In the meantime let's hope that as oil prices find their new trading range it doesn't take 10+ years like last time (after 1986) for the next up-cycle!

1 Common term used to describe a working rig, as rotary rigs operate in a clockwise fashion.
2 Baker Hughes Rig Count as at April 8, 2016.
3 A decline rate measures the rate at which oil production declines in a period, typically after 1 year. A well with a 70% decline rate would be producing at 30% of the initial rate after 1 year.

Changing Times — The 2016 Federal Budget Update

by CWB Wealth Management

On March 22nd the Federal Liberals tabled their first budget labelled *Growing the Middle Class;* the budget included a number of tax and policy changes that will have an impact on many Canadian families and investors. The key changes are:

- Tax rates for individuals: A reduction in the tax rate from 22% to 20.5% for income between $45,281 and $90,563 will create a savings of up to $670 for each tax filer. However, there is now a new tax bracket of 33% for any income over $200,000.
- Elimination of Family Tax Cut: Previously, qualified families with high income from one individual were able to split a portion of this income with a lower income spouse. This has been cancelled for 2016.
- Reduction in OAS and GIS age eligibility to 65 years: Previously, depending on birth year, an individual would have to wait until the age of 67 in order to be eligible for Old Age Security. This has been reversed back down to the age of 65 for all Canadians.
- Small business tax rate: Many small business owners were looking forward to a reduction in the rate, which was announced during the recent campaign. Unfortunately, this will remain at the current level of 10.5% for 2016.
- Elimination of tax deferral on switches within corporate class mutual fund investments: Previously, investors holding corporate class mutual funds were allowed to move from one fund to another fund (in the same class) without triggering a disposition. From October 1st onward, these switches will now realize a capital gain or loss.
- Tax Free Savings Account: (Previously Announced) The annual savings limit for the TFSA has been reduced from $10,000/individual (set in 2015) back down to $5,500. The cumulative personal TFSA contribution amount is now $46,500.

These tax and policy changes, along with others made at both the Federal and Provincial levels, have created both challenges and opportunities for Canadians. At no point in recent history has there been as many material changes to the personal and corporate wealth environment as there is now.

Put our expertise to work for you - reach out to one of our Wealth Management Specialists to learn how a financial plan with integrated tax strategies, can help you achieve your vision of the future. Visit cwbwealth.com/approach for direct contact information.

Disclosure: The information above is general in nature and should not be construed as specific legal, lending or tax advice. As with all planning strategies, you should seek the advice of a qualified tax advisor.

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