

OUR 41ST YEAR

This licensed producer of medical marijuana believes that seniors will like their product. Page 6.

The latest acquisition by this IT and business process services company is a catalyst for growth. Page 7.

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THE MONEYLETTER[®]

STRATEGIES FOR SUCCESSFUL INVESTING

MARKET WISDOM

The Tremors

PORTENT OF A QUAKE?

Elvis Picardo

DO THE VOLATILITY TREMORS portend a major market quake?

For us denizens of the West Coast, it seems inevitable that a major earthquake will occur in the region at some point in time. The difficult part is in trying to forecast when this will occur – will it be a year from now, 10 years, or 50?



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Impossible to predict, but meanwhile, we live with the occasional tremors and temblors, hoping that the Big One isn't around the corner.

The recent surge in market volatility feels similar, albeit on a smaller timescale. Was the huge spike in volatility in the first week of February a natural corollary to the unusual calm of 2017, or was it an early indication of a major market quake within the next couple of years?

At the time of writing, although stocks have recouped part of their losses from a week of gut-wrench-

ing volatility, the market's gyrations could indicate that the January barometer might not be as reliable this year as it usually is, in our opinion. The January barometer holds that the performance of the S&P 500 in January sets the tone for the rest of the year – a positive January means that the S&P 500 will have an up year, and a negative January implies a down year. This is especially true when the S&P 500 advances more than 5 per cent in January. According to Fidelity Investments, of the 13 times that the S&P 500 has gained more than 5 percent in January since 1945, it has advanced in the remaining 11 months of the year 85 percent of the time.

A Fallible Barometer

But the barometer is not infallible, especially when January is negative. One need look back no further than 2016, when the S&P 500 finished the year up 11 per cent despite being down 4 per cent in January. Will 2018 prove to be a year when the index is unable to build on its 5.6 per cent January gain, the 11th-best since 1945?

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Elvis Picardo, from Page One

Certainly, the speed with which market sentiment unraveled after U.S. equity indices reached record highs on January 26 was quite astonishing. At their February 9 lows, U.S. indices had tumbled about 12 per cent from their peaks; this was the fastest the S&P 500 had plunged into a 10 per cent correction since 1950.

Prices Plunge, Yields Rise

The market rout commenced on February 2, after a triple-whammy of “threes.” A robust U.S. jobs report showed wages in January rose almost 3 percent from a year ago, the fastest annual pace since 2009. Such strong wage growth spurred speculation that the Federal Reserve would need to boost its benchmark rate more than the three times this year that was factored in by investors. As a result, bond prices plunged and the yield on the 10-year Treasury rose to a four-year high of 2.85 per cent, inching closer to the 3 per cent threshold that bond guru Jeff Gundlach and others have identified as a level that would signal a bond bear market.* If bond prices plunge, spiking yields could imperil the second-longest equity bull market in history.

On February 5, the Dow Jones Industrial Average plunged intraday by 1,600 points, the biggest point drop in history. It closed the day down 1,175 points and endured another 1,000-point drop on February 7. Overall, the week ended February 9 was the worst one in two years for U.S. equities, with the S&P 500 losing 5.2 per cent for the week.

Despite the significant decline and upsurge in volatility, most Wall Street strategists continue to advocate the “buy the dips” strate-

gy that has served investors so well since 2009. A Bloomberg article** notes that since the start of the current bull market in 2009, U.S. and global equities have experienced nine distinct selloffs and have bounced back every single time. In addition to the aforementioned January 2016 selloff, other notable dips include the August 2015 plunge caused by China’s shock devaluation of the yuan; the correction of the summer of 2011, that was triggered by Standard & Poor’s lowering of the U.S. government’s credit rating; and the 16 per cent slide in 2010, from April to July, a period that included the “Flash Crash” on May 6.

Europe and Japan Look Good

Each of those episodes could have spelt an end to the bull market, but it recovered and lumbered on. However, it may not be as easy for the markets to post a sustained recovery this time, because the era of cheap money is coming to an end, at least in North America.

Since the Bank of Canada and the Federal Reserve are both poised to push up benchmark interest rates substantially this year, we recommend increasing equity exposure to regions where monetary policy is still accommodative. Two such regions are the Eurozone and Japan, the biggest of the advanced economies, excluding the United States. Europe is enjoying an economic resurgence as it grows at the strongest pace in a decade, underpinned by healthy domestic demand and rising corporate profits. Japan is finally emerging from its prolonged economic slump, with GDP growth estimated by the IMF at 1.8 percent in 2017, helped by stronger international trade and fiscal stimulus.

The BMO MSCI EAFE Hedged to CAD Index ETF (TSX: ZDM) or the unhedged version (TSX: ZEA) provide exposure to both these regions. Both these ETFs track the MSCI EAFE index, which represents the performance of more than 900 stocks across 21 developed markets in Europe, Australasia and the Far East. The ETFs’ geographic diversification makes it worthy of consideration for Canadian investors, whose investment portfolios tend to be concentrated in North America. The biggest stock weights in ZDM and ZEA are household names such as Nestle, HSBC Holdings, Novartis, Toyota and Roche.

Our investment thesis for ZDM and ZEA is that since Eurozone and Japan are much further behind in the economic recovery cycle than North America, their stock markets may have more room to run. ZDM gained 6.5 per cent in 2016, 16.1 percent in 2017 and was up 1.6 per cent in January; corresponding figures for ZEA were -1.9 per cent, 17.1 per cent, and 2.1 per cent.

On the fixed income side, where the environment is growing increasingly more challenging, we like the First Asset Enhanced Short Duration Bond ETF (TSX: FSB). This ETF aims to provide positive absolute returns over any 12-month period with very low volatility and steady monthly distributions regardless of the interest rate or credit environment. FSB primarily focuses on U.S. and Canadian corporate bonds. The average duration on the ETF’s holdings is 0.4 years, well below its maximum of two years. The ETF currently pays a monthly distribution of 2 cents, for an indicated yield of 2.4 percent. It is also available in a U.S. dollar version (TSX: FSB.U).

Overall, it would be safe to assume that market volatility will continue to be markedly higher this year than it has been in the last couple of years. The tug-of-war between bulls and bears will likely be more pronounced this year, in our opinion, as positive factors such as accelerating global growth and strong corporate earnings are offset by rising bond yields and fears of a more hawkish Fed. Market action over the next few months will determine whether the “buy the dips” mantra is finally turning into “sell the rallies.” Should that happen, it may be a sign that the Big One in the markets is closer than most investors currently assume. ▼

* *Bloomberg (February 1, 2018)*
- *Pimco views 3% yield as an opportunity where others see bear signal.*

***Bloomberg (February 8, 2018)*
- *Far from unprecedented: Nine selloffs like this, and nine rebounds*

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STOCK STRATEGY

Notes from Underground

ALL THAT GLITTERS

Stephen Bernhut

IAMGOLD CORP. REPORTED A strong 2017 finish, say CIBC Capital Markets analysts David Haughton and Terry Tsui. The analysts add that the gold company gave upbeat guidance for 2018, which should garner further positive sentiment. (IMG-TSX, \$7.60; IAG-NYSE, US\$6.07)

“IAMGOLD presents reasonable value with improving operations and near-term production growth,” Messrs. Haughton and Tsui state. They maintain their Outperform recommendation and 12-18 month target price of US\$7.50 per share.

IAMGOLD reported preliminary 2017 production of 882,000 ounces of gold, at the higher end of earlier company guidance, and above the analysts’ estimate of 875,000 ounces. They cite strong fourth-quarter performance at the Essakane, Rosebel and Sadiola sites, in West Africa and Suriname, as the reason for beating expectations. The company stated 2017 average total cash costs will be at the midpoint of guidance (from

US\$740 to US\$780 per ounce).

The company’s 2018 production guidance of 850,000 to 900,000 ounces is in line with the analysts’ expectations of 896,000 ounces. They predict total cash costs for 2018 will be stable compared with 2017, and relatively in line with their forecast of US\$773 per ounce.

GOLDCORP

Following a two-year period of restructuring and optimization of assets at Goldcorp Inc., Credit Suisse analysts Anita Soni, Robert Reynolds and Mark Llanes upgrade their recommendation for it from “neutral” to “outperform” and increase their target price to US\$19 a share from US\$15.50 per share. (G-TSX, \$16.70; GG-NYSE, US\$13.34).

The analysts assert that the company boasts an “achievable and attractive growth profile” from 2018 through 2020. They comment further, “Goldcorp has re-established a good operational track record by achieving 2016 and, we expect, 2017 production,

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