

Market Research #001

This is the first in a monthly series of Independent research produced by the Murray Wealth Group Research Team. The purpose of this series is to provide insight into our portfolio construction and how our research shapes our investment decisions. We welcome any feedback or questions you may have on these monthly commentaries.

The Lost Decade: How to Make Money in Canada? *Answer: Diversify Away from It.*

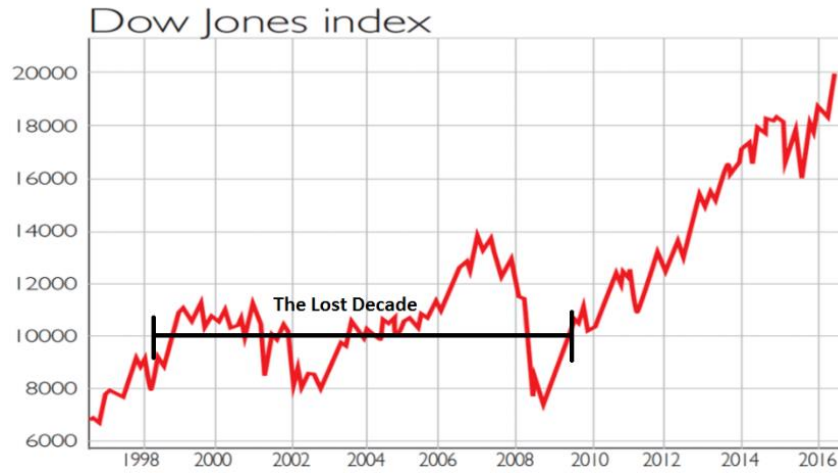
In late 2008 and into the first quarter of 2009, global stock markets suffered great losses when the U.S. housing bubble burst. The accompanying collapse of the mortgage market and associated leveraged financial instruments led to the failure of the banking sector in the U.S. and several European countries, including Iceland, Ireland, Spain, Italy and, particularly, Greece. The situation was salvaged by unprecedented financial intervention led by the U.S. Secretary of the Treasury, Hank Paulson, the Federal Reserve and other affected central banks and governments.



Everybody takes credit for prosperity.

Photo: Richard Grasso, NYSE Chairman & New York City Mayor Rudy Giuliani sport their Dow 10,000 hats in 1998

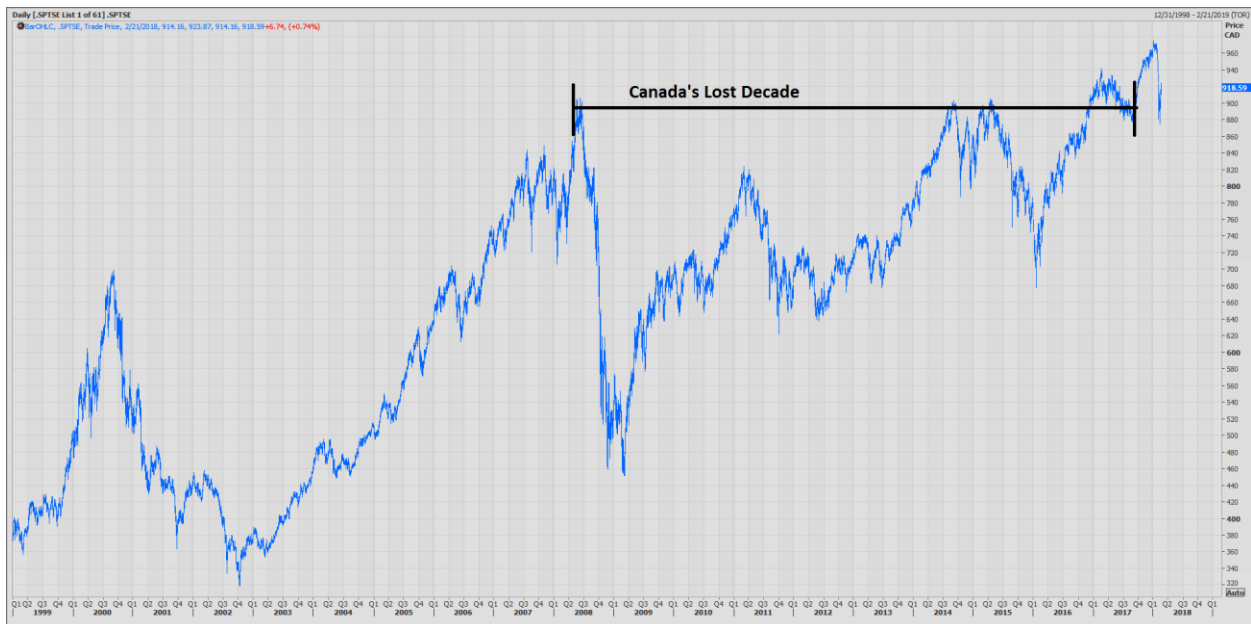
In October 2008, the Dow Jones Industrial Average fell below the 10,000-point level, stoking memories of the Dow's initial charge above 10,000... ten years earlier, in 1998, during the technology bubble. At that time, the talk on business television was of a lost decade for equity investors (although, including dividends, the return would have been approximately 3% per annum). While U.S. investors may have been justifiably disheartened by their meagre returns at that time, the subsequent 291% return from the bottom in the spring of 2009 has not brought about a material change in confidence as indicated by the vast sums of cash (\$3.1 Trillion at Dec 31, 2017) held in money market funds alone on the sidelines. The current market capitalization of the S&P 500 is about \$24 Trillion.



Source: Money Week Magazine

Recently, those that have invested solely in Canadian equities have been experiencing a similar dissatisfaction with their investment returns. The TSX 60 Index, which is comprised of Canada’s largest public companies (i.e., banks, telecoms, oils, mining, grocers, utilities and some tech/manufacturing names), has returned just 2% (not per annum, but in total!), excluding dividends, from its 2008 peak, prompting Canada’s own lost decade.

The TSX 60 Index



Source: Thomson Reuter Eikon

If investors were smart enough or lucky enough to diversify out of Canada, they would have enjoyed the frothy returns provided by international markets. A depreciated Canadian dollar (C\$) would have further

buoyed those returns. The table below contains Canadian dollar adjusted returns as at Feb 14, 2018 for the periods in question.

C\$ Adjusted Return as of Feb 14, 2018 (Month End Values for all period)					
	2007/08 Peak	2009 Bottom	2014 YE	2016YE	2017 YE
TSX 60	2%	84%	5%	0%	-6%
SP 500	34%	366%	40%	8%	-1%
NASDAQ 100	149%	541%	100%	31%	4%
MSCI World (\$USD)	5%	256%	31%	7%	-2%

Source: Thomson Reuter Eikon

The Canadian equity returns are particularly muted in the periods from year-end 2014 and year-end 2016. But the fact remains that even backing out currency effects, Canada has not been investor friendly over the past few years. We do not expect this to change given the following three factors:

- 1) **Heavy reliance on energy and materials:** Lower energy and metal prices will continue to depress returns. We note that for energy stocks, poor geographic proximity and infrastructure restrictions are causing further underperformance of Canadian-based energy assets. While global oil markets are closer to balancing, we do not foresee a prolonged period of price growth given new low-cost supplies and a trend line of slower growth in demand.
- 2) **Increasing taxation disparity:** Canada’s taxes have increased for businesses and corporations as well as individuals at both the federal and provincial level. In contrast, U.S. competitiveness is improving with the recent passing of the Trump administration’s Tax Cuts and Jobs Act.
- 3) **Increasing social burden:** Whether it is through increased regulation, higher minimum wage or increased environmental taxes such as carbon tax (Alberta) or green energy (Ontario), Canadian businesses are facing increased obstacles to profit growth.

Unlike the United States in 2008, where returns following the lost decade were historically strong, **we do not believe Canadian Equities will outperform over the next decade.** Our MWG Global Equity Growth Fund continues to hold a concentrated basket of 37 high growth equities and stable compounding companies, with 80% of the portfolio invested in U.S. and international companies. Our Income Fund holds mostly Canadian equities, but that is a function of better dividend tax treatment here in Canada (foreign dividends must pay withholding taxes). In our MWG Income Fund, we have focused on higher yielding equities to provide a greater return in a low-price growth environment. We believe this asset allocation will best serve our clients in the long run.

Our performance in both funds has surpassed the returns of Canadian dollar-adjusted indices with the exception of the NASDAQ, which is a technology-weighted Index, in 2017.