LEE, TURNER & ASSOCIATES INC.
INVESTMENT QUARTERLY

REVIEW January 2020

2019 was a banner year for financial markets the world over. As you review your enclosed annual performance reports, you will notice that your rates of return over the past year seem outsized and unusually high. Rest assured that these figures are very much real. There are a couple of reasons for last year's strong performance. First, despite a few hiccups, economic conditions were mostly favorable over the greater part of the year, so investors responded by bidding up stock prices. Second, stock markets had the benefit of starting off the year at a sharp cyclical bottom, which by the properties of arithmetic alone bolstered the performance calculations. In reviewing the global economy of the past year, we found that it had a fairly smooth sailing despite a few instances of perceived threats, ones that were quickly extinguished. The best example of a threat neutralized was the resolution of trade tensions between the US and China reached in December. On the monetary front, the Federal Reserve made 3 cuts to its interest rates, 25 basis points each time, and announced its commitment to foster US economic growth. The Bank of Canada did not cut its interest rates as it deemed our economy to be firmly on track for growth and stability. Investors were pleased with what they heard and saw as evidenced by the fact that almost every major stock market index in the world hit all-time highs before year end. The final year over year tally for the stock markets was a 25.3% advance in the Dow Jones Industrials Average and a 22.9% rise in the S&P/TSX Composite Index. The bond market was strong as well. Canadian bonds had a 6.9% total rate of return. Gains were weak for the short to medium maturity bonds but grew stronger as maturities lengthened.

FORECAST

Our 2020 economic forecast is moderately optimistic. We see most of the past year's economic growth inputs carrying over into the first half of this year. The impending end to the US and China trade dispute should stir further investor confidence and the equities markets. The impeachment of the US President and the ensuing political theatrics might seem like a tempest brewing in a crucible but really is much ado about nothing as far as the economy and the markets are concerned. The soon to be ratified free trade agreement for North America is just a lightly tweaked version of its replacement, again it is much ado about nothing. The Canadian economy should see some stability on its fiscal front as our newly re-elected minority government will likely abstain from making major changes to its fiscal direction. Closer to home, the Trans Mountain pipeline expansion appears poised for completion sometime next year, a much-needed salve for Canada's beleaguered energy industry. Unfortunately, this pipeline will likely be the last such project in Canada for a very, very long time as future infrastructure developments will no doubt be mired in decades-long legal, environmental, and/or regulatory obstacles. While our economic forecast is optimistic, our expectations for the financial markets in 2020 are tempered. We do not anticipate a repeat of last year's strong rates of return. Financial markets are expected to benefit from a stable economic environment, but double-digit rates of returns will be hard to come by.

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INCOME STRATEGY

Bonds

The threat of negative bond yields spreading to North America receded in the last quarter of 2019. Bond yields moved slightly higher in December to signal the bond markets' slow return to normality. Central Bankers were right to have proactively defended their economies with accommodative policy actions last year. But going into 2020, we see them shifting towards a somewhat more neutral stance where no further interest rates cuts should be expected. They will, however, stay their course of maintaining low and steady interest rates because North American GDP growth rates and inflation rates will likely remain soft throughout the year. Consequently, we expect very little movement in bond yields, just a slight steepening in the shape of the yield curve. We see bond yields confined to under 2% over the course of the year, so we will leave bonds out of our portfolios for the time being.

Income Trusts

Real Estate Income Trusts (REIT's) had the wind, courtesy of Central Bankers, at their backs last year. Looking ahead, low interest rates will play a smaller role in driving the REIT's valuation process. Economic growth, vacancy rates, and population growth will be the more significant factors when we assess the REIT's investment merits. Our view on the REIT's continues to be positive. For now, we are very content in holding our positions.

EQUITY STRATEGY

Equities are currently trading well within their normal valuation range. Investors have assigned a good balance of optimism and caution towards the stock markets. After nearly a decade of economic growth spurred on by fiscal and monetary stimuli, we still see some cause for optimism in the equities markets going forward. However, we also see developments that warrant our caution today. We are quite concerned over consumers who, as a group have been egged on by cheap and easy credit, added massive amounts of debt to their already swollen personal balance sheets. Should interest rates rise in the near future in any pace other than slow and measured, then debt laden consumers will be hit with debt servicing costs that just might prove to be unmanageable. Under such a scenario, an ensuing widespread contraction in consumer spending could potentially seed a recession. Canadian banks and companies in the consumer discretionary industries will be the first to feel this consumption crunch while the balance of the economy and the stock markets will feel the knock-on effects shortly thereafter. We will be watching the Central Bankers' every move with great attention.

ANNOUNCEMENT

We are extremely excited and pleased to announce that Trevor Lee, BA, MSc, CFA, has joined our firm as a Senior Associate. He comes to us after 6 years of increasingly senior roles in Business Intelligence at BCLC. Prior to that, he was a Strategist at a brand consultancy working with some of the world's largest consumer goods companies. Trevor earned his Bachelor of Arts degree from the University of Waterloo and his Master of Science degree from the Cranfield School of Management. As well, Trevor holds the Chartered Financial Analyst designation and is a regular member of the CFA Society Vancouver. He is very much looking forward to meeting and working with all our clients.