RAYMOND JAMES | Steele Wealth Management

Second Quarter 2017

"From Paris with Love"

Favourable French Election Results Push International Markets Higher and Booming Global Economy Paves Way for Interest Rate Hikes

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Market Cheer France's Macron; Central Banks Around the World Want to Hike

- The S&P/TSX Composite Total Return Index lost 1.6% during the 2nd quarter of 2017.

- The consumer discretionary, consumer staples, health care, industrials, telecom, IT, real estate and utilities sectors led the S&P/TSX Index while the energy, materials and financials sectors trailed.

- The S&P 500 returned 3.1%, exceeding the return of the S&P/TSX for the second quarter in a row.

- The price of oil was ~US$46 (WTI) at end of the quarter, down from ~US$51 at the end of Q1. Oil prices fell despite high supply cut compliance by OPEC members and non-OPEC nations as well as an agreement between OPEC and non-OPEC producers to extend the oil supply cuts by nine months to March 2018. The key reasons for oil price weakness was higher than expected US oil production, lower than expected demand growth, still near record global oil inventories and a revival of Libyan oil production which has more than tripled since August 2016, offsetting much of the OPEC supply cut. Libya and Nigeria remain the key wildcards with respect to global oil supply as the countries are exempt from the OPEC agreement and operate amidst political and social turmoil that could see production decline rapidly in short order. Oil production is currently lower than oil demand but it will take several months to whittle down oil inventories from record levels. It appears only a rise in Libyan or Nigerian tensions and violence could result in much higher oil prices in the near-term.

- Long-term US interest rate expectations fell significantly in the quarter even though the US Federal Reserve increased its key interest rate by 0.25% in June. Investors attribute a very low chance of a rate hike until December 2017 and are currently pricing in only a ~50% probability of a rate hike in December. US employment growth data has been lumpy and inflation data was lower than expected in Q2 and was negative for the month of May. Given the Federal Reserve's mandate to support employment and control inflation, it is natural for the market to expect little change in Federal Reserve policy any time soon. On the flip side, interest rate expectations in Canada spiked in mid-June as the Bank of Canada (BoC) began to hint at the possibility of a near-term hike given strong GDP growth so far in 2017, the Canadian economy generating the most jobs over the past year than any other twelve month period in the past five years and inflation remaining fairly close to the BoC's 2% target. Subsequent to quarter end, the Bank of Canada raised its key interest rate by 0.25% to 0.75%. The market is pricing in meaningful odds of an additional rate hike in 2017.

- The European election parade plodded along in Q2. Despite fears of a Trump-like underdog victory in France and to a lesser extent the UK, the centrist and safe bet Macron was the victor in France and the incumbent Conservative party leader May won in the UK, albeit losing her outright majority. Markets cheered the Macron victory with the MSCI All-Country World Index reaching an all-time high after his first-round victory and hitting another all-time high after beating Le Pen by a wide margin in the second round. The concern that brewed following the UK election never reached beyond the UK shores, as the British pound and FTSE stock market suffered but global markets mere shrugged. In order to keep her Brexit plans in place, May began negotiations with the Democratic Unionist Party (DUP) of Northern Ireland to support a Conservative minority government. While a coalition or confidence and supply arrangement will allow the Tories to continue Brexit negotiations with the support of a party with similar economic views, the union will be shaky given the DUP's nationalist and far-right social views.

PIMG Model Benchmarking Disclosures

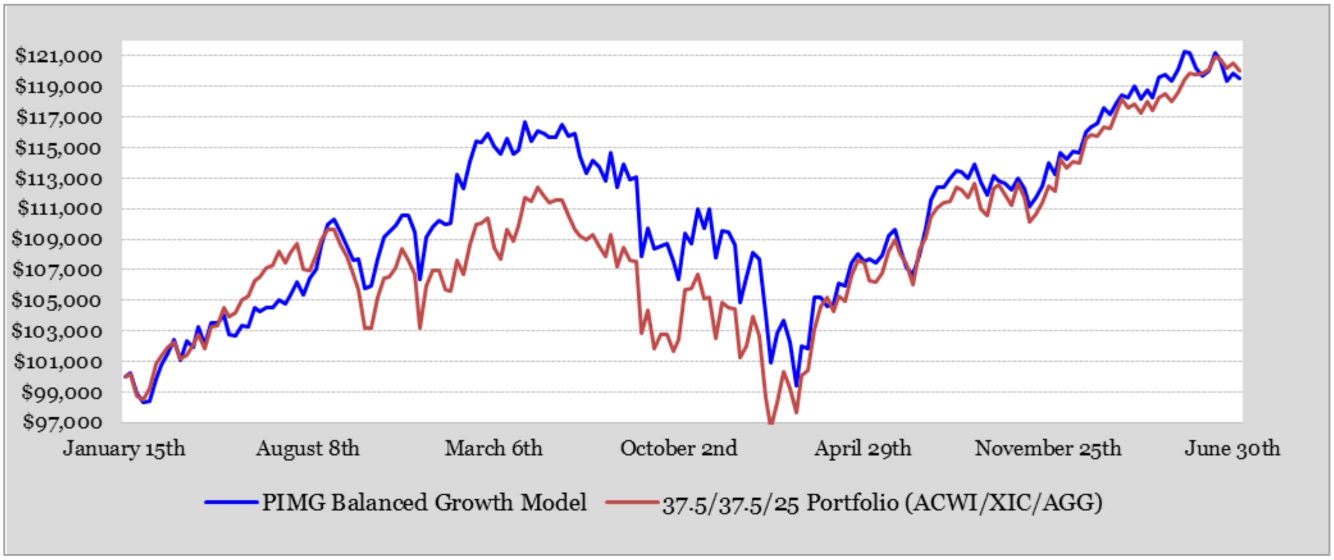
- The numbers presented on the following two pages reflect those of our two models, Balanced Growth and Balanced Income. As a client of Steele Wealth Management, you may or may not have your account linked to one or both of these models. In our discussions prior to signing your PIMG documentation, we outlined which model(s), if any, your accounts would be linked to. If you are unsure whether your account is linked to one or more of these models, please let us know and we can clarify this for you.
- Model returns presented are those of two individual accounts whose returns fully reflect that of the model's holdings and transactions and are not impacted by deposits or withdrawals that could impact return calculations. The accounts we use to reflect model performance incur a 1% annual investment management fee, charged monthly, which is also subject to 13% HST, charged monthly, for a total cost of 1.13% annually. Your individual account performance may deviate from the model account based on any differences in fees charged relative to the model account, differences in account holdings relative to the model account as well as any deposits or withdrawals made throughout the reporting periods outlined.
- On January 15, 2014, we materially changed the composition of our two model portfolios. We renamed our Tactical Taxable and Tactical Registered models to Balanced Growth and Balanced Income and made major changes to model allocations and exposures. The Tactical Taxable and Tactical Registered models were invested in 80%-85% common equity and 15%-20% preferred equity and our exposure was virtually 100% in Canadian dollars and Canadian companies. The Balanced Growth model has an asset allocation of ~75% common equity and ~25% fixed income, of which half is invested in preferred equity, and roughly 40% exposure to non-Canadian securities. The Balanced Income model has an asset allocation of ~50% common equity and ~50% fixed income, of which a third is invested in preferred equity, and roughly 30% exposure to non-Canadian securities. With these changes, our two models now reflect a more universally appropriate choice, in terms of asset allocation and risk, for the vast majority of our clients and investors in general. As a result, we expect these new models will remain in force for the foreseeable future.
- As a result of the model changes outlined above, we also changed our benchmarks to reflect the new asset allocations and exposures. Benchmark information is detailed in the disclosures at the bottom of the following two pages.

Benchmark of iShares XIC/ACWI/AGG (37.5%/37.5%/25%)

vs

The PIMG Balanced Growth (BG) Model

January 15, 2014 (Inception of BG Model) to June 30, 2017



01/15/2014 – 06/30/2017	PIMG Balanced Growth Model	37.5% XIC / 37.5% ACWI / 25% AGG	iShares XIC	iShares ACWI	iShares AGG
Cumulative Return Since Inception	19.49%	20.00%	21.85%	21.99%	11.00%
Compound Annual Return	5.31%	5.44%	5.91%	5.95%	3.08%
Standard Deviation	8.40%	8.39%	11.87%	12.44%	3.27%
Sharpe Ratio	0.28	0.29	0.25	0.24	0.02
Largest Monthly Gain	4.16%	5.04%	5.45%	7.66%	2.22%
Largest Monthly Loss	-3.99%	-4.25%	-4.31%	-6.81%	-2.56%
Number of Up Months	25	27	26	26	25
Number of Down Months	17	15	16	16	17
Correlation with Balanced Growth	--	0.89	0.87	0.82	-0.27

PIMG Balanced Growth Model	3 month	6 month	9 month	12 month	3 year	5 year	10 year	Inception
	-0.09%	4.19%	5.88%	10.62%	4.37%	n/a	n/a	5.31%

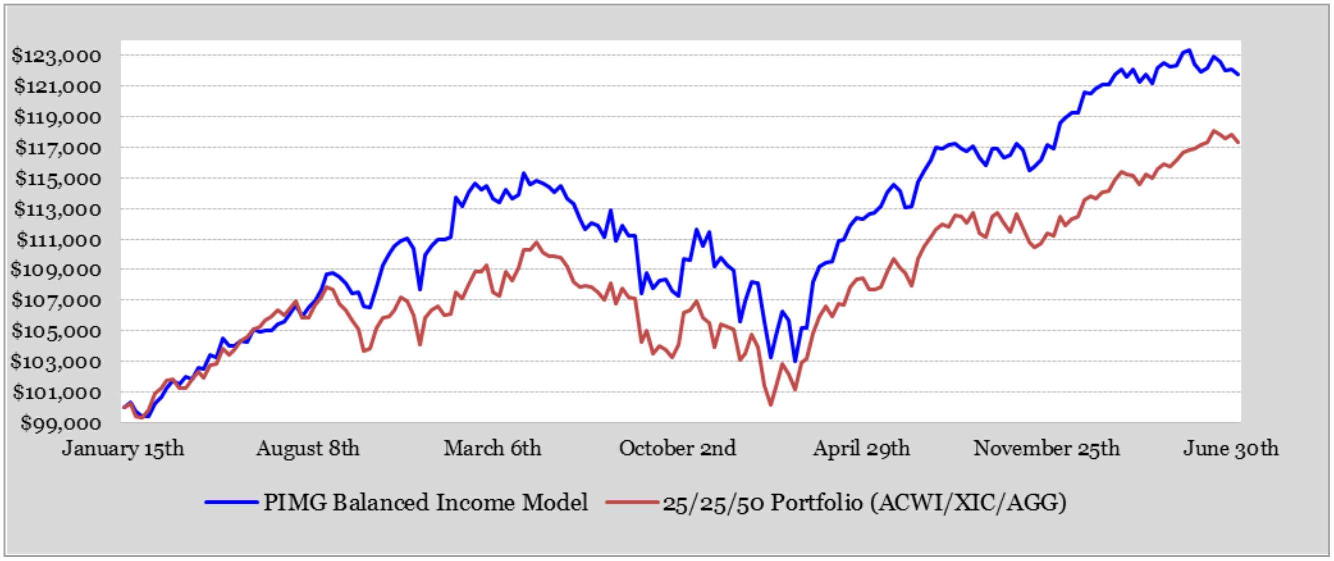
We have assumed a 1% investment management fee plus 13% HST when calculating the returns for our PIMG models. To the best of our knowledge, the ETFs used as benchmarks track the indices they represent though material tracking error and misrepresentation can occur which is beyond our control. The 37.5% XIC / 37.5% ACWI / 25% AGG index is an index consisting of 37.5% iShares XIC (S&P/TSX Compositie Index ETF), 37.5% of iShares ACWI (All-Country World Index ETF) and 25% iShares AGG (Barclays Aggregate Bond Fund). Volatility and correlation data are calculated from weekly returns. For the purpose of calculating Sharpe ratios, a risk-free rate of 3% is assumed. All returns presented for the PIMG Models and the ETFs used for comparison are in Canadian dollars. Data used to calculate returns are derived from Market-Q (for ETFs) and Dataphile (for the Models). All returns presented are "total returns", meaning they include all dividend payments & interest payments. All return numbers beyond 12 months are annualized numbers.

Benchmark of iShares XIC/ACWI/AGG (25%/25%/50%)

vs

The PIMG Balanced Income (BI) Model

January 15, 2014 (Inception of BI Model) to June 30, 2017



01/15/2014 – 06/30/2017	PIMG Balanced Income Model	25% XIC / 25% ACWI / 50% AGG	iShares XIC	iShares ACWI	iShares AGG
Cumulative Return Since Inception	21.82%	17.33%	21.85%	21.99%	11.00%
Compound Annual Return	5.90%	4.76%	5.91%	5.95%	3.08%
Standard Deviation	6.34%	5.52%	11.87%	12.44%	3.27%
Sharpe Ratio	0.46	0.32	0.25	0.24	0.02
Largest Monthly Gain	4.87%	3.65%	5.45%	7.66%	2.22%
Largest Monthly Loss	-3.06%	-2.95%	-4.31%	-6.81%	-2.56%
Number of Up Months	27	27	26	26	25
Number of Down Months	15	15	16	16	17
Correlation with Balanced Income	--	0.86	0.88	0.80	-0.19

PIMG Balanced Income Model	3 month	6 month	9 month	12 month	3 year	5 year	10 year	Inception
	-0.34%	2.11%	4.21%	6.14%	4.94%	n/a	n/a	5.93%

To the best of our knowledge, the ETFs used as benchmarks track the indices they represent though material tracking error and misrepresentation can occur which is beyond our control. The 25% XIC / 25% ACWI / 50% AGG index is an index consisting of 25% iShares XIC (S&P/TSX Compositie Index ETF), 25% of iShares ACWI (All-Country World Index ETF) and 50% iShares AGG (Barclays Aggregate Bond Fund). Volatility and correlation data are calculated from weekly returns. For the purpose of calculating Sharpe ratios, a risk-free rate of 3% is assumed. All returns presented for the PIMG Models and the ETFs used for comparison are in Canadian dollars. Data used to calculate returns are derived from Market-Q (for ETFs) and Dataphile (for the Models). All returns presented are "total returns", meaning they include all dividend payments & interest payments. All return numbers beyond 12 months are annualized numbers.

PIMG Balanced Growth Model

Lost 0.1% during the quarter (April 1 to June 30).

The model's asset allocation as of June 30 was 9.2% cash, 17.7% bonds, 7.1% preferred equity and 66.0% common equity.

Top five outperformers in Q2 were:
- Sandvine Inc. (IT/Communications Equipment) at +40.09%
- SNC-Lavalin Group (Industrials/Engineering & Construction) at +9.32%
- Nintendo Co (IT/Video Games) at +9.04%
- Chipotle Mexican Grill (Consumer Discretionary/Restaurants) at +8.60%
- Corus Entertainment (Consumer Discretionary/Media) at +6.60%

Top five underperformers in Q2 were:
- AIMIA Preferred C (Preferred Share/Fixed Reset) at -36.14%
- Sprott Energy Fund (Mutual Fund/Energy) at -23.54%
- Open Text Corp (IT/Enterprise Software) at -13.40%
- AMC Networks (Consumer Discretionary/Media) at -11.21%
- Cara Operations (Consumer Discretionary/Restaurants) at -10.37%

During Q2, we bought:

- iShares 1-3 Year Treasury Bond ETF (SHY): We rolled the proceeds from our US dollar sales into iShares SHY to maintain our US dollar exposure for redeployment at a later date.

- TFI International (TFII): We added to our position in TFI International. After the election of Donald Trump, TransForce shares benefitted from improving North American economic sentiment. Trump's "America first" policies should boost U.S., and potentially Canadian, economic activity and this is positive for trucking margins and volume. TransForce also announced a highly accretive acquisition in October which caused the shares to rally 12% in two days. This acquisition shows that TransForce is back to making smart acquisitions when the opportunities arise. TransForce currently trades at its historic valuation of ~14x trailing earnings when incorporating its recent acquisition of XPO Logistics. This is roughly in line with trucking peers. We believe TransForce should trade at a premium to peers given expected synergies from its recent acquisitions. Further, most industrial companies trade at a 10%-30% premium to their historical multiples and we think the truckers should trade at a premium to historical multiples as well. The trucking sector remains highly fragmented and with advances in self-driving technology the pace of consolidation should accelerate leaving TransForce, the leading acquirer in the sector, with plenty of opportunity to grow through acquisition.

- Open Text Corp (OTEX): We added to our position in Open Text. Open Text trades at 11.5x forward EV/EBITDA, a discount to its peers which trade at greater than 14x on average. On the surface, all things equal, this discount could be reasonable due to Open Text's higher debt load. That said, Open Text's earnings have been relatively depressed over the past year due to its above average exposure to currency fluctuations and relatively unfavourable product cycle timing. Open Text has stated that it looks to deploy US$3 billion for acquisitions over the next few years and Open Text's track record as an acquirer is best in class. After a period in which the company made only a few minor acquisitions, we can see an acquisition renaissance on the horizon following four $100M+ acquisitions in the past eight months. While we believe Open Text's future revenues and earnings could be lumpy due to new product rollouts/updates and continued currency volatility, and that this could result in above average stock price volatility, we believe Open Text's updated product offering and expected future acquisitions should result in much higher than average long-term revenue and earnings growth and in turn result in much higher than average returns for equity holders.

- SNC-Lavalin Group (SNC): We purchased a position in SNC. SNC recently announced its intention to purchase Atkins, a diversified UK-based engineering and construction (E&C) company that will boost SNC's revenues by 40%. SNC continues to trade at a material discount to peers as result of the 2011-2012 bribery scandal in which SNC and SNC management was charged with offering bribes in Libya. We believe SNC's recent acquisition of UK-based Atkins will help the company regain its premium valuation as Atkins is a well-respected company and it makes more sense for SNC shares to trade at Atkins shares' middling valuation than for Atkins shares to trade at SNC shares' industry low valuation. The absorption of Atkins will mean the addition of new high quality management that has investor respect and approval, further reason why SNC should see its valuation revert to historical levels. After removing the value of SNC's interest in the 407 ETR, SNC's E&C business trades at a ~25% discount to peers looking two years out on an EV/EBITDA basis, based on analyst estimates. SNC historically traded at a 10%-30% premium to E&C peers so SNC has plenty of upside should it shake off its bad reputation.

<u>During Q2, we sold:</u>

- Nintendo Company (NTDOY): We sold our position in Nintendo following an announcement that its Switch console set a U.S. sales record in March and is expected to sell over 7 million units globally this year. We believe the ultimate number of Switch consoles sold will be limited given its fairly poor consumer reception and lack of novelty. Nintendo will still likely trade in the 40-60x earnings ex-cash range, despite being in a major console launch year. As a result, the shares looked quite overpriced.

- Chipotle Mexican Grill (CMG): We sold our position in Chipotle as the stock rallied in response to a third party report that stated its sales growth would handily beat sales growth expectations. This came after several quarterly sales misses and marked a major shift in investor sentiment for the shares/company. Rallying almost 40% from its lows, we thought the stock got ahead of itself considering the rally was based on a third party report and not a tangible improvement in the company's operations. At the time of sale, the stock was trading at the high end of its historical valuation based forward two-year analyst consensus earnings, which assumed normalization in the company's outlook and margins. Subsequent to selling the shares, while the company did beat sales expectations, management noted extreme food cost pressures as well as labour cost pressures due to minimum wage hikes across North America that would hurt profit margins for the foreseeable future.

- Apple Inc (AAPL): We sold our position in Apple. The stock appeared overvalued trading at ~17x trailing normalized earnings relative to a historical average of ~14x trailing earnings. While Apple has announced its intention to enter high growth market segments like self-driving technology and artificial intelligence, we think Apple has a lot to prove before any value can be attributed to their efforts in these areas. Further, we view these burgeoning new market segments as a direct threat to Apple's legacy phone business so failure to dominate these markets like they dominate the phone business will likely impact margins going forward.

- BMO Tactical Global Equity ETF Fund (GGF70217): We sold our position in BMO Tactical Global Equity as the position had failed to keep up with the broad US market. The bulk of the return since we purchased the position was the result of currency gains.

- Power Corp Preferred D (POW.PR.D): We sold part of our position in Power Corp Preferred D as the shares were temporarily trading well above $25 and at a major premium to comparable perpetual preferred shares.

- AIMIA Preferred C (AIM.PR.C): We sold our position in AIMIA Preferred C following the announcement that Air Canada will not be renewing its contract with AIMIA which expires in 2020. AIMIA common shares fell ~65% and approached the $2 level at which the preferred shares are convertible to common shares. We see the risk of much greater losses as high now that the common shares are close to the $2 conversion price. We were able to exit the position with a tolerable loss given the risk associated that is now associated with the position. Subsequent to selling the shares, AIMIA suspended dividends on both its common and preferred shares and AIM.PR.C fell over 50%.

- WSP Global (WSP): We sold our position in WSP Global. WSP traded roughly in line with peers but we think its days of growing through acquisition, as it has done in the past, are numbered as it is now the largest publically traded pure play engineering company in the West.

PIMG Balanced Income Model

Lost 0.3% during the quarter (April 1 to June 30).

The model's asset allocation as of June 30 was 3.2% cash, 25.3% bonds, 4.1% convertible debentures, 8.2% preferred equity and 59.2% common equity.

Top five outperformers in Q2 were:
- SNC-Lavalin Group (Industrials/Engineering & Construction) at +9.32%
- Corus Entertainment (Consumer Discretionary/Media) at +6.60%
- WSP Global (Industrials/Engineering) at +5.87%
- Telus Inc. (Telecom/Diversified) at +4.87%
- Fortis Inc. (Utilities/Diversified) at +4.35%

Top five underperformers in Q2 were:
- AIMIA Preferred C (Preferred Share/Fixed Reset) at -36.14%
- Sprott Energy Fund (Mutual Fund/Energy) at -23.54%
- Cara Operations (Consumer Discretionary/Restaurants) at -10.37%
- Enbridge Inc. (Utilities/Diversified) at -6.20%
- Jean Coutu Group (Consumer Staples/Pharmacies) at -4.31%

<u>During Q2, we bought:</u>

- SNC-Lavalin Group (SNC): Same reasoning as the Balanced Growth Model.

- Sun Life Financial (SLF): We purchased a position in Sun Life. Sun Life trades at 11.2x trailing earnings versus peers Manulife Financial and Great West Lifeco at 15.4x and 12.9x respectively. The valuation gap between Sun Life and Manulife is the biggest in recent memory. We see little reason why Sun Life should trade at a material discount at this point. It makes little sense that Sun Life trades at its pre-Trump rally level and a major discount to peers given Sun Life's higher earnings sensitivity to changes in interest rate expectations. Sun Life has experienced above average policyholder "usage" but this is likely to be one-time and any ongoing increase in policyholder "usage" would affect all life insurance companies, not just Sun Life. We believe there is a good chance that Sun Life outperforms Manulife and Great West by 10%-30% over the next 12-18 months.

- TFI International (TFII): We purchased a new position in TFI International with the same reasoning as the Balanced Growth Model.

- Open Text Corp (OTEX): We purchased a new position in Open Text with the same reasoning as the Balanced Growth Model.

<u>During Q2, we sold:</u>

- BMO Tactical Global Equity ETF Fund (GGF70217): Same reasoning as the Balanced Growth Model.

- Manulife Financial (MFC): We sold our position in Manulife as a result of its apparent valuation premium relative to Sun Life.

- Power Corp Preferred D (POW.PR.D): Same reasoning as the Balanced Growth Model.

- AIMIA Preferred C (AIM.PR.C): Same reasoning as the Balanced Growth Model.

- WSP Global (WSP): Same reasoning as the Balanced Growth Model.

Going Forward:

As mentioned in our last quarterly commentary, we are currently working to rearrange our models. We have started to reallocate the portfolios to reflect the slight change in strategy. The change involves holding fewer ETFs and larger positions in our preferred blue chip equities. The change will reduce overall investment management fees and allow for greater exposure to our best ideas.

The **Balanced Growth** model underperformed its benchmark in the second quarter due to our underweight exposure to international markets and Europe in particular. Posited as the most significant event and greatest source of political risk in 2017, the French election could not have gone more smoothly. The centrist, business friendly and pro-EU Macron decisively beat Le Pen two-to-one which not only boosted the outlook for French and European economic growth but soothed investors' concern as the election was seen as a proxy for the French populace's attitudes toward the European Union.

While we expected a favourable result in the French election, we did not think it would have such a materially positive impact on European markets. A Macron victory was widely expected but perhaps due to the recent election upsets in the US and the UK and the extremely negative implications of a Le Pen victory meant that some investors hedged their bets anyway resulting in a strong post-election rally as hedges were unwound.

Canadian interest rates rose substantially throughout the quarter with the 5-year Government of Canada bond yield rising to 1.4% at the end of Q2 versus 1.1% at the end of Q1. Our interest rate sensitive positions in the telecom and consumer facing sectors performed well despite this spike in interest rates. We think these positions can continue to weather gradual increases to Canadian interest rates. Strangely, our remaining fixed reset preferred share, ENB.PF.E, did not outperform. We believe there is opportunity for fixed reset preferred shares to trade substantially higher given the paradigm shift in Canadian interest rate expectation and interest rate expectations around the world. Counterintuitively, we think rising interest rates will help all preferred shares, even interest rate sensitive perpetual preferred shares, as rising interest rates indicates healing the general economy and narrowing credit spreads should more than offset negative effects related to rising interest rates, at least initially.

Our newfound optimism (as of Q4) about the long-term trend in oil prices was tested in Q2. We are still very much underweight the energy sector relative to our benchmark. We were tempted to add to our energy market exposure but the rapid recovery in Libyan oil production and the increasing efficiency of US shale production is concerning. While we think the energy sector looks attractive relative to other sectors, it is difficult to see what the next major catalyst is for oil prices. It was supposed to be as good as it gets following the major deals between OPEC members and non-OPEC nations. Now that those deals are well underway and will likely begin to fall apart over time, oil price risks will gradually accumulate as time passes. We believe this growing risk is already reflected in the price of oil and will look to add to our energy sector weighting following the next oil supply shock which is most likely to be caused by political upheaval in Libya or Nigeria.

We remain underweight the materials sector as we believe the unwinding of the commodity supercycle remains in force and that these sectors remain in a long-term downtrend. The sector performed poorly throughout Q2 as lackluster Chinese demand pressured base metals prices and rising interest rates around the world pressured precious metals prices.

Sandvine is currently the target of a bidding war between two private equity firms. We will likely tender the shares in Q3 and walk away from the position with a respectable gain, though it took more than three years to achieve it. This is the greatest challenge with value investing. Finding value isn't the hardest part, as Tom Petty says, the waiting is the hardest part and how long you wait isn't up to you. Without a catalyst on the horizon, luck plays a big role in how long you wait. In this case, Lady Luck took her time but at least she didn't stand us up!

The **Balanced Income** model underperformed its benchmark during the quarter for mostly the same reasons as the Balanced Growth model. Balanced Income is somewhat more interest rate sensitive but the model held up well given the rapid rise in interest rates over the first half of the year. As we continue to rearrange our models, we expect Balanced Income to become somewhat less interest rate sensitive as we further diversify the model's equity holdings by sector.

US interest rate expectations fell during the quarter, with the market only pricing in a 50% chance of another US interest rate hike in 2017, down from nearly 100% odds at the end of Q1. Elsewhere, interest rate expectations shifted. In Q1, investors attributed almost a 0% chance of a Canadian interest rate hike in 2017. At the end of Q2, the odds of at least one Canadian interest rate hike in 2017 sit at close to 100%. A similar but less significant change occurred in Europe. We believe this shift in interest rate expectations is paramount and could mark a paradigm shift in how investors should position themselves. Going overweight non-commodity linked cyclical stocks and financials and going underweight defensive and interest rate sensitive stocks seems like the obvious play. While we will implement this change somewhat we wish to remain well diversified as rate hikes will eventually drag on economic growth and worsen the outlook for cyclical and financial stocks.

As at the end of Q2, the models yield 2.6% (Balanced Growth) and 3.4% (Balanced Income) in line with 2.6% and 3.4% yields, respectively, at the end of Q1.

Sincerely,

Steele Wealth Management