

Taking Stock with Steele

Your Monthly Newsletter

The purpose of this newsletter is to share insights and expertise. Our goal is to ensure that our clients are well-informed of changes affecting local business decisions and our investment recommendations.

We believe Knowledge Pays and we want our knowledge to help pay for you.

MARKET COMMENTARY INTEREST RATES AND THE PREFERRED SHARE MARKET

The preferred share market has been unusually volatile since the Bank of Canada cut its key interest rate by 0.25% on January 21st. As the rate cut resulted in falling yields across the yield curve, particularly in the short-end of the curve (i.e. 1-5 year yields), those preferred shares with reset yields based on the 5-year Government of Canada (GoC) bond yield experienced rapid price decline. Other types of preferred shares, like perpetual and retractable, weathered the interest rate cut well.

What's the Best Strategy? Avoid Fixed-Reset Preferred Shares with Low Reset Rates

Fixed-reset preferred now make up 60% of the total preferred share market. Knowing which ones to invest in is essential to being a successful preferred share investor. A fixed-reset preferred share's expected volatility and expected returns are entirely based on its reset rate.

If a fair reset rate for Royal Bank fixed-reset preferred shares is currently the 5 year GoC rate plus 2.5%, Royal Bank preferred shares with reset rates less than that are unlikely to be called (i.e. bought back) at \$25. Instead they will likely trade below their issue price of \$25. Because the fair reset rate changes over time, it is important to own fixed-reset preferred shares with high reset rates to increase the odds that the shares will be called at \$25 at the reset date. Most companies will call a preferred share if its reset rate is well above the fair rate at the time of reset as it can simply issue a new share at the fair rate. **Preferred shares with high reset rates tend to act more like bonds**, which is what we are trying to achieve when buying preferred shares.

The preferred shares we feature in the 'Riding The Curve' section below are typically preferred shares with high reset rates.

RIDING THE CURVE A CATALOGUE OF OUR MONTHLY FIXED INCOME FAVOURITES

Manulife Preferred H (MFC.PR.H)

- Manulife is one of the largest life insurance companies in the world
- The shares are callable or reset at 3.13% + the 5-year GofC bond on March 19th, 2017
- At \$25.82, the issue has a yield-to-call (soft) of 3.10% and is rated Pfd-2H

RioCan REIT Preferred C (REI.PR.C)

- RioCan is Canada's largest REIT focused exclusively on retail real estate
- The shares are callable or reset at 3.18% + the 5-year GofC bond on June 30th, 2017
- At \$25.18, the issue has a yield-to-call (soft) of 4.12% and is rated Pfd-3H

Current Rates & Data

Govt of Canada

90 day	0.51%
1 year	0.45%
2 year	0.42%
5 year	0.73%
10 year	1.44%
30 year	2.06%

U.S. Treasury

90 day	0.01%
1 year	0.22%
2 year	0.64%
5 year	1.51%
10 year	2.00%
30 year	2.58%

Canada Prime Rate

2.75%

U.S. Prime Rate

3.25%

Exchange Rates

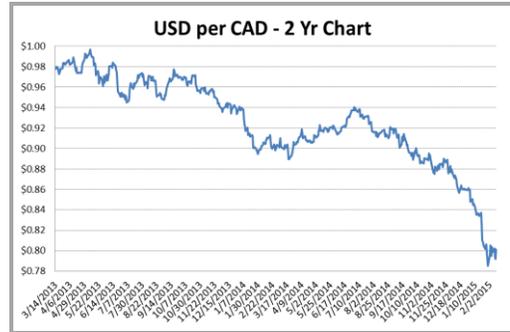
CAD/USD	0.801
USD/EUR	1.138
JPY/USD	119.2

ECONOMIC TIDBITS *GREEK ELECTIONS COULD ROCK EUROZONE & OIL'S SECOND-ORDER EFFECTS*

- The far-left Greek political party Syriza won the Greek elections that took place in late January. Their key platform piece was to **reject the EU-mandated austerity and bailout program** initiated in 2010. Greek politicians are hoping the specter of Greece exiting the EU, and potentially destabilizing the common currency, will allow them to win concessions from their EU counterparts.



- The Bank of Canada's interest rate cut took the market by surprise. Poor Canadian economic data confirmed a bleak short-term outlook soon after. In late January, the Canadian yield curve inverted, signaling a **high risk of recession in Canada**. Currently, the interest rate swaps market assigns a ~60% probability of another rate cut in March. All of this is bad news for the Canadian dollar.



LE JIT A "JUST-IN-TIME" RUNDOWN OF OUR CURRENT INVESTMENT THEME

Consumer Staples Seasonally Strong Period Begins in April; Several Bargains to be Had

- EcoLab (ECL)** and **Sysco (SYY)** are two investment ideas related to this theme.
- EcoLab** provides water, hygiene and energy technologies and services worldwide, primarily serving the foodservice, hospitality, education and healthcare industries. Ecolab is the largest and most trusted name in foodservice sanitation products in North America and faces minimal competition on its home turf. The international growth opportunity is immense as emerging market consumers demand more robust and proactive food handling techniques and improved sanitation in general. EcoLab trades at 26x trailing earnings and is one of the fastest growing U.S. consumer staples stocks having realized earnings growth of 25%+ for the past three years.
- Sysco** is North America's #1 food distributor and it is currently attempting to purchase U.S. Foods, North America's #2 food distributor. Though the deal is far from certain due to antitrust issues, it would significantly add to the attractiveness of the Sysco story. Sysco currently trades at ~24x trailing earnings and would trade at ~15x trailing earnings if it can achieve the expected cost synergies associated with the acquisition. Further, Sysco has no net debt and if it levered up its balance sheet to match that of its peers or the broad market, it would trade at 11-13x trailing earnings, a major discount to the broad equity market and companies with a similar risk profile.
- Feel free to ask a member of our team for more information on these securities.

JEANNINE'S TIP O' THE MONTH RRSP CONTRIBUTION DEADLINE

The RRSP contribution deadline is March 2nd for the 2014 tax year. Make contributions early to avoid the stress!

This newsletter has been brought to you by Steele Wealth Management

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