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Taking Stock with Steele

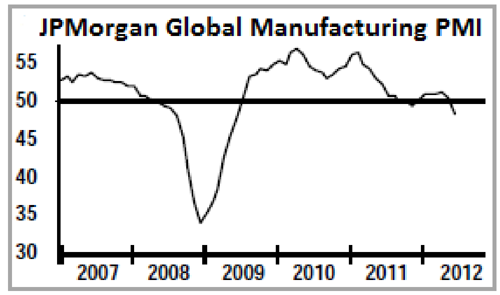
Your Monthly Newsletter

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.

ECONOMIC TIDBITS *AN INVENTORY OF NOTABLE DATA AND INFO*

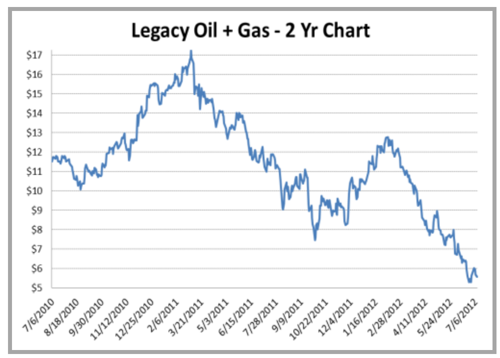
- Since our last newsletter, equity markets are modestly higher. A joint bank supervisory and recapitalization agreement by European Union policymakers temporarily eased market jitters but doubts about the implementation of the agreement continue to pressure the Euro currency as well as Spanish and Italian bonds. Manufacturing data continued to worsen globally sparking a round of monetary easing.
- Global manufacturing data as measured by the JPMorgan Global Manufacturing PMI slid to a three-year low in June. Data showed that the U.S. manufacturing sector was contracting for the first time since July 2009. Chinese manufacturing data indicated stagnation and Eurozone surveys showed that the Euro area continues to contract at the fastest pace since June 2009. Bucking the trend is Canada, where manufacturing data showed continued expansion. *See Fig. 1 for chart of JP Morgan Global Manufacturing PMI.*
- In response to deteriorating economic data and ongoing Eurozone uncertainty, central banks went on the offensive with the U.S. Fed extending Operation Twist, the ECB cutting its benchmark interest rate, the Chinese central bank lowering interest rates and the Bank of England increasing the size of its quantitative easing program.

Fig. 1



Data Source: JP Morgan, Markit; www.ism.ws

Fig. 2



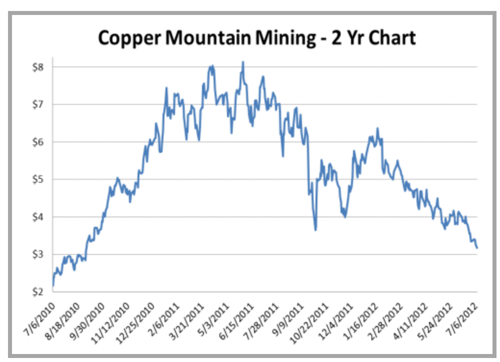
Data Source: Market-Q

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

Monetary Easing Makes Cyclicals More Attractive

- A global monetary easing cycle is underway with the large economies (the U.S., UK, Eurozone, China, Brazil) implementing easing measures
- Cautionary note: Monetary easing provides liquidity but fiscal stimulus will be needed to support a prolonged market advance
- **Legacy Oil + Gas (LEG)** and **Copper Mountain Mining (CUM)** are two investment ideas related to this theme:
  - Legacy engages in the development, exploration and exploitation of oil and natural gas in Canada. *See Fig. 2 for 2-year chart.*
  - Copper Mountain engages in the exploration, development and operation of a copper/silver/gold mine in British Columbia. *See Fig. 3 for 2-year chart.*

Fig. 3



Data Source: Market-Q

RIDING THE CURVE *A CATALOGUE OF OUR MONTHLY FIXED INCOME FAVOURITES*

Fortress Paper Debenture A Maturing on Dec. 31st, 2019 (FTP.DB.A)

- Fortress produces and sells specialty pulp and security papers worldwide
- This is a 7.5 year debenture with a conversion price of $31.00 (current: $15.75)
- This debenture yields 7.80% until maturity at a current trading price of $96

Great West Life Perpetual Preferred H (GWO.PR.H)

- Great-West operates insurance and investment management businesses worldwide
- At $24.54, the issue has a yield of 4.9% versus the yield on bank perpetuals of ~4.4%

PORTFOLIO PLANNING FINANCIAL REPRESSION AND A POOR MENU OF RETURNS

In today's environment of record low interest rates and historically high equity market volatility, investors are hard-pressed to achieve returns similar to those experienced in the past 20-30 years without markedly increasing portfolio risk. Many would say the conventional 60/40 portfolio is now a relic of times past, what our ancestors held.

Currently, the yields on 10-year Canadian and U.S. bonds are 1.65% and 1.51%, respectively. Considering inflation is expected to be 2% on average (Bank of Canada's inflation target), one can expect a negative real return when purchasing 10-year government bonds in a registered account (even worse in a non-registered account). As a result, most investors have ventured into the high yield bond, convertible debenture and preferred share markets in order to achieve a positive real return.

Unbeknownst to many investors, as these markets are made up of corporate issuances, they are highly correlated to equity markets and will decline (and rise) in tandem with equity markets. Substituting government bonds for corporate bonds, debentures and preferred shares results in greater portfolio volatility and increases the maximum drawdown of the portfolio (i.e. the ultimate expected low value).

It is important that clients understand the additional risk taken when investing in non-traditional fixed income securities and understand that the extra yield they receive on an ongoing basis comes at the cost of additional downside volatility. At the same time, it is important for clients to understand the risk of not taking on additional risk as locking in negative real returns will ensure that the financial goals that require positive long-term investment returns will likely go unfulfilled.

As investors adjust to a higher risk environment, it is important to focus on long-term portfolio returns and avoid establishing a myopic loss aversion bias by continually "marking your portfolio to market". Higher highs and lower lows can send your head spinning if you set yourself up to feel the brunt of every decline in portfolio value.

JEANNINE'S TIP O' THE MONTH *ENHANCING YOUR SWM EXPERIENCE*

Canada Revenue Agency for Individual Account Access – Sign up for online access to your CRA account at http://www.cra-arc.gc.ca/myaccount. Check your tax installments and refunds, TFSA info, RSP contribution limits, GST/HST credits, child benefit payments and more.

Current Rates & Data

Govt of Canada

90 day	0.86%
1 year	0.93%
2 year	0.97%
5 year	1.17%
10 year	1.62%
30 year	2.24%

U.S. Treasury

90 day	0.10%
1 year	0.18%
2 year	0.25%
5 year	0.63%
10 year	1.49%
30 year	2.57%

Canada Prime Rate

3.00%

U.S. Prime Rate

3.25%

Canada CPI Y-o-Y (May)

1.20%

U.S. CPI Y-o-Y (May)

1.70%

Exchange Rates

CAD/USD	0.986
USD/EUR	1.224
JPY/USD	79.22

This newsletter has been brought to you by Steele Wealth Management

Brian Steele | Jeannine Campbell | Laura Prust
Kelly Townsend | Matthew Bell | Keith Gummow

Phone: (519) 883-6030 Toll-Free: 1 (877) 642-6408

Email: steelewealthmanagement@raymondjames.ca

Address: 1001-20 Erb Street West | Waterloo, Ontario | N2L 1T2

Website: www.steelewealthmanagement.com

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