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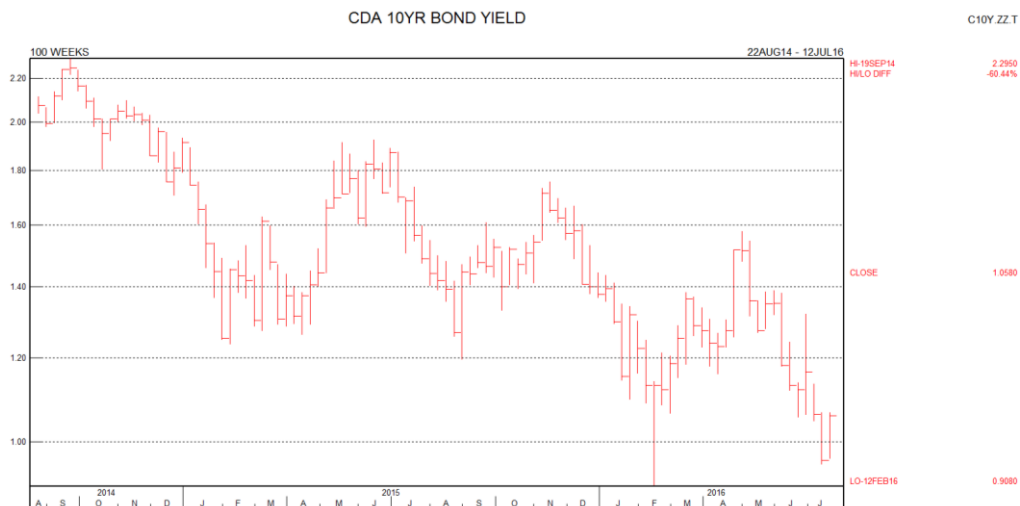
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Monday, July 11, 2016

Second Quarter 2016

One of the charming things about investing is that about every quarter there is a new piece of jargon. In the second quarter the hands down winner is “Brexit”. You like I are probably bombarded with punditry so I’ll restrict my comments to the direct effects that the Brexit Surprise had on our investments.

Immediately after the referendum result, stocks went down for a couple of days and we did far too little buying. I thought they might go down more and for longer as the enormity of the uncertainty became known. Bond yields plunged with the 10 year Government of Canada yield breaking below 1%. Much lower interest rates for much longer became the rallying cry.

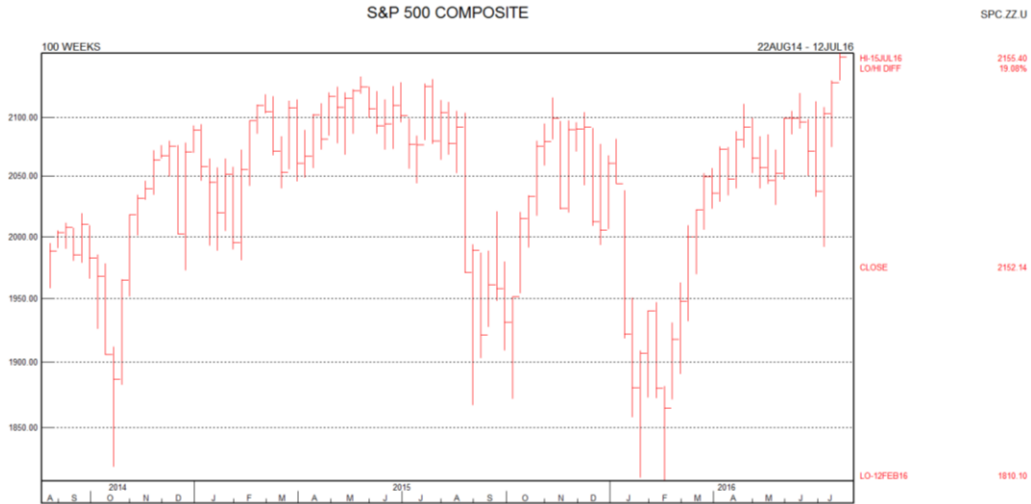


Graphic obtained from Trend & Cycle (July 13th, 2016)

Now, some 40% of the developed world’s governments bonds, \$7 trillion worth, yield less than zero. That is something I just can’t get my head around. About three quarters of the developed world’s government bonds yield less than 1%. Many companies have dividend yields on their stocks that are higher than the interest rate on their bonds. Investors are stuck between a rock, ultralow bond yields and, a hard place, lagging corporate profits.

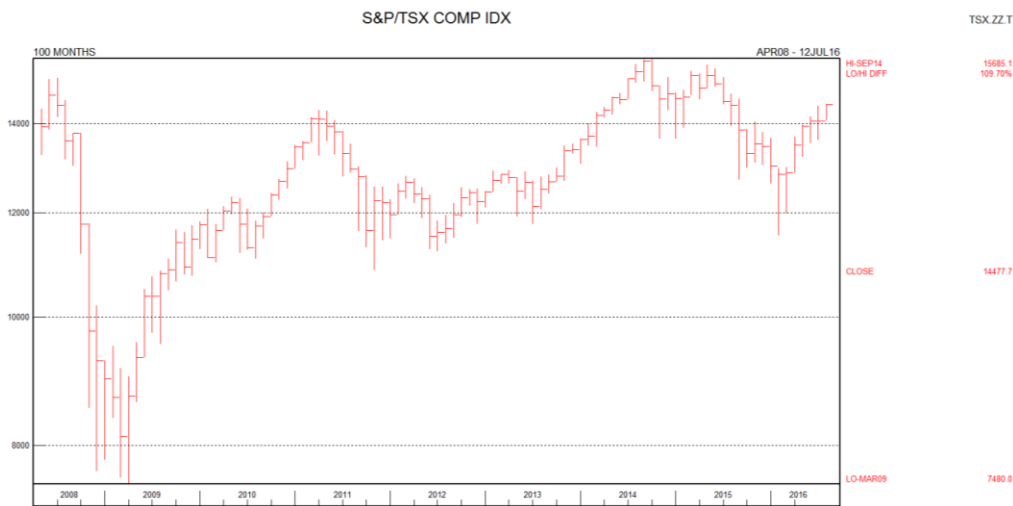


U.S. stocks have been going sideways for two or three years.



Graphic obtained from Trend & Cycle (July 13th, 2016)

Canadian stocks have been going sideways for ten years but have been very strong over the last 6 months as the price of oil nearly doubled from the low of \$26 in February.

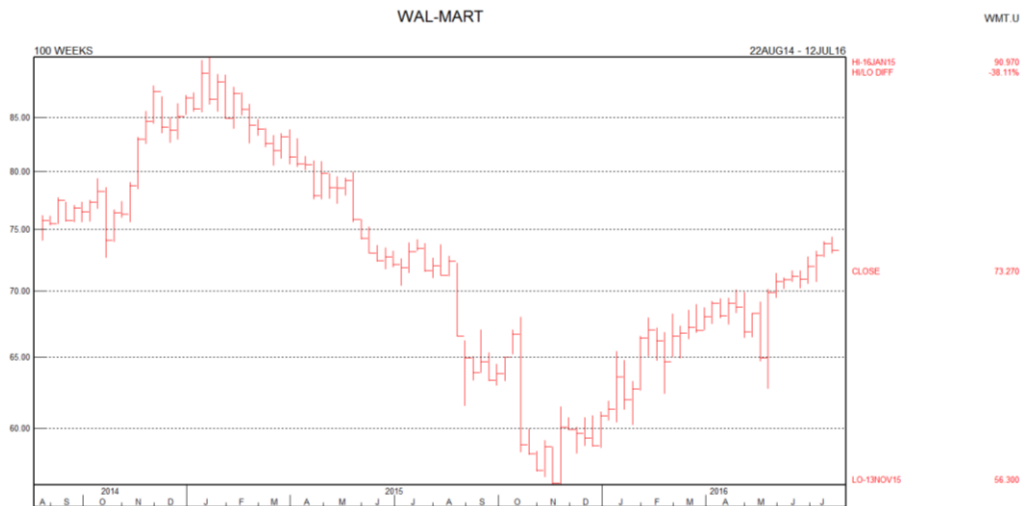


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Thinking of bond yields versus stock yields reminds me of Charlie Munger's take on the perennial question of what is the right asset mix between stocks, bonds, and cash. For himself, Charlie says he nearly always has nearly all of his money in stocks but, he chooses better stocks than most people. That's more or less how I feel.



Selling stocks can be hard and I don't like to admit I was wrong. I try to position our portfolios ahead of long term societal trends so I don't have to make frequent decisions. My favorite stocks to invest in are companies that make things that I can touch and understand and which, perhaps, Amazon, or other retailers, sell. But we have been invested in three retailers, Dollarama, which is a local company, sells things that are unlikely to be bought online and shipped. Loblaw's fresh food is nice to touch and smell before buying and Loblaw's Shoppers Drug Mart offers the expertise of a Pharmacist. The third retailer we were invested in was Walmart, which I have sold. Although Walmart is the second largest online retailer, Amazon has such a huge lead that I've concluded that it is going to cost Walmart a lot to catch up.



Graphic obtained from Trend & Cycle (July 13th, 2016)

I sometimes regret selling old favorites and the stocks usually go up afterwards because we usually invest in soundly profitable companies, but I have to make choices.

I hope you enjoy plenty more good weather this summer.

Sincerely,

George Stedman, CFA
Portfolio Manager, Vice-President
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