CLIENT

NEWSLETTER

DECEMBER 31, 2016

Message from the Managing Director, Private Client

As we enter 2017, it is timely to reflect on the year just past and look forward to the New Year. 2016 was another successful year for the Highstreet team and its investors. As we reflect on the year it is fair to say that it was one of surprise and transition. The key surprises of 2016 included; the US Federal Reserve softening their rate hike stance to start the year; Britain's exit from the European Union; Trump's presidential victory; OPEC's production cuts; and at its peak, $13 trillion of negative yielding debt worldwide. The key investment theme in 2016 was a transition towards Value stocks and away from Growth stocks. All are substantial events when taken independently, let alone together in one calendar year.

A Year of Surprise

At the end of 2015, the US Federal Reserve raised its key interest rate for the first time in ten years. Markets sold off to start 2016 amid expectations of tightening monetary policy, and concerns over the slowing Chinese economy. The Shanghai Composite Index fell 7% on the first trading day of 2016 and equity markets worldwide were not spared as the S&P 500 and TSX Indices were down around 10% in January. The Fed was quick to back away from raising rates further, and suggested a much slower pace of rate hikes for the rest of the year. The Fed maintained their dovish tone through the year, further reinforced by a surprisingly weak payroll report in May dashing hopes of a summer rate hike. Instead of raising rates four times in 2016 as initially projected, the Fed raised rates only once in December.

The surprise result of the "Brexit" vote, where British voters chose to leave the European Union, saw global equity markets selling off for the second time in 2016. Market volatility, caused by uncertainty around the impact of the vote, dissipated quickly as Central Banks worldwide assured investors with their commitment to accommodative monetary policy and as investors sought to gain a better understanding of what the result meant for Britain and Europe.

Despite numerous polls to the contrary, Donald Trump became the US president-elect in November. Market reaction was initially negative and investors braced for the third major equity market sell-off in 2016. However, markets soon took on a more positive tone and focused on the stimulative effects of the Trump administration's pro-growth policies, and equity markets rallied.

December saw both OPEC and non-OPEC countries committing to production cuts in an effort to raise oil prices, representing unprecedented coordination by oil producers to stem oversupply in the oil market. The oil price was supported by this decision and ended the year at ~$54/barrel, up from its February lows of $26/barrel.

Bond markets experienced sharp moves through the year in response to uncertainty and equity market volatility. Following a sharp decline at the start of the year, bond yields came under renewed pressure around the events of Brexit, with the US 10-year yield reaching all-time lows and some European yields turning negative. In fact, investors held over $13 trillion of negative yielding debt at its peak right after Brexit[1]. The surprise result of the US election ultimately led to higher growth and inflation expectations causing a sharp increase in bond yields worldwide. As of the end of the year almost no negative yielding debt was held.

A Year of Transition

The sharp sell-offs followed by sharp rallies caused an overall trendless market. From a factor perspective, buying stocks which performed well in the previous months (traditionally a winning strategy called "momentum"), hurt investors in most months of 2016 as investors struggled to navigate through various periods of market uncertainty.

The year also saw a transition in style and sector leadership as the typical Growth sectors, such as Consumer Discretionary, Consumer Staples, and Health Care, turned lower, while the typical Value sectors such as Energy, Materials, and Financials began to turn higher. This has benefitted regions with a larger focus in the Value sectors such as Canada and Latin America relative to the US.

[1] http://www.wsj.com/articles/germany-sells-10-year-debt-at-negative-yield-1468410101

Despite a challenging investment backdrop, most major equity markets had positive returns with Europe being the exception. Most of Highstreet's investors are holders of the Balanced Fund and 2016 marked the 5th consecutive year of strong returns.

Fund awards

At Highstreet, researchers and portfolio managers collaborate to develop a disciplined and repeatable investment process to provide our investors a compelling product offering. Through blending quantitative and fundamental investment styles, Highstreet's investment team is well-equipped to navigate a wide variety of market conditions. As a result, the Highstreet Balanced Fund, the Highstreet Canadian Equity Fund, and the Highstreet Dividend Income Fund have received the Fundata FundGrade A ratings so far this year. These grades are awarded to funds that have had outstanding performance over a period of time. This is a testament to the strength of the investment team and process, and we remain squarely focused on delivering on our performance objectives for our clients.

Outlook for 2017

After the worst start to a calendar year ever, equity markets climbed to new highs in 2016, defying broad market consensus around events such as the early market sell-off, Brexit, and the US election. The economic backdrop continues to be supportive of global growth and governments are beginning to tap into other forms of economic stimulus, such as fiscal policy. As we look to 2017, we believe that the transition to Value should continue through the year and, as we have learned from 2016, we are likely to see more surprises along the way. The theme of Value should also find support from a stabilizing oil market, improving Chinese manufacturing prospects, which increases demand for commodities and improved inflation expectations. Our models have highlighted opportunities outside of the US and in Value in the long term, and we continue to monitor these developments.

From all of us at Highstreet, we thank you for the opportunity of serving you over the past year and look forward to working with you going forward. We also take this opportunity to extend our best wishes to you and your families for a healthy and prosperous 2017.

Michael Hodgson

Opening doors at Highstreet

Since our founding in 1998, one of the best sources of new clients has been our existing client base. In this context, we often are asked, *"what is the minimum amount needed to become a private client at Highstreet?"*

Recent regulatory changes allow us to take on younger family members of existing clients who are still in a wealth building stage in their lives or someone whose main wealth is invested in their private company or farm operation and are not yet in a position to set aside significant sums for investment in financial assets.

Please contact your relationship manager if you think we may be the right fit for someone you know.

Congratulations

Tingting Lu has moved from Senior Analyst to Associate Portfolio Manager. Since joining Highstreet two years ago, Tingting spearheaded research in the field of asset allocation, market risk forecasting and FX hedging. Congratulations to Tingting on her recent promotion!

In the Community

This quarter, the Highstreet team participated in the annual United Way Boot Drive. Through the help of Highstreet along with other businesses in the community, the United Way was able to collect a total of 750 pairs of boots!

Telephone: 519 850 9500
Toll Free: 877 850 9500
Facsimile: 519 850 1214
Website: www.highstreet.ca