18 AM Balanced Strategy Highlights

The 18 AM Balanced Strategy is designed to provide growth and capital preservation at a low cost, using both active and passive management. For our actively managed Canadian equity allocation, we believe a focus on company fundamentals and a style diversified portfolio provides an attractive opportunity to add value. For our passive asset class allocations, we utilize carefully selected index funds to represent chosen asset classes. In addition, the strategy utilizes currency hedging based on set policy parameters to manage the overall portfolio risk. The 18 AM Balanced Strategy is delivered via a separate account solution. This allows us to provide a low-cost, globally diverse portfolio customizable to each client's investment policy risk and return objectives.

Performance of the asset classes included in the strategy is displayed in the table below.

Asset Class Performance *			
		18 AM Balanced Strategy	
Asset Class		Q4	1 Year
Equities	Canada	-11.0%	-8.0%
	US	-9.1%	2.9%
	International	-11.8%	-10.1%
Fixed Income	Canada	1.4%	1.2%
	US	1.4%	-0.9%
	International	1.1%	1.3%
Cash & Equivalents		0.4%	0.2%

*The chart depicts performance data for the asset classes and is for information purposes only. Returns are stated in Canadian dollars.

Highlights of the fourth quarter:

- As can be seen in the table above, all major equity markets declined in the quarter, driving the bulk of the losses in the strategy in Q4.
- The strategy's actively managed allocation to Canadian equities was down 11.0% in Q4, slightly behind the benchmark TSX index. Within that allocation, the Offence style (growth and momentum) lagged the Defence style (income and low risk) in the period. The relative underperformance of the Canadian equity allocation was impacted primarily by security selection in the Energy sector.
- The Bank of Canada executed one additional rate hike of 0.25% in October, causing fixed income allocations to decline in the month. However, bonds rebounded during November and December to post a positive return for the quarter, in stark contrast to equity performance. The low correlation of bonds to equities in the period is a reminder of the benefits of prudent asset allocation.
- Currently, the strategy has currency exposure solely on the US Equity allocation as all other non-domestic currency exposures are hedged. The US dollar appreciated 5.7% versus the Canadian dollar in Q4, benefitting the return of this allocation.

**Performance is shown gross of all fees and is stated in Canadian dollars unless otherwise noted. Performance data is historical and not indicative of future performance. Returns are annualized for periods greater than 1 year. The benchmark is a linked index consisting of monthly rebalanced blend of S&P/TSX Composite Index / MSCI World Index (Net) / FTSE TMX Canada Universe Bond Index / FTSE TMX Canada 91 Day TBill Index. This document is for information purposes only. Data sources: Thomson Reuters, Standard & Poors, Morningstar/CMPS and 18 AM.*

Market Overview

Equities

The final quarter of 2018 saw declines across most major equity markets globally. Downward performance was significant enough to more than wipe out positive (and in some markets, record) returns during the first three quarters of the year. The final days of the year saw several significant daily performance swings, both upward and downward, causing volatility levels to rise sharply and setting the stage for further uncertainty in the new year.

For Q4, the TSX Index was down 10.1%. 7 of 11 sectors were down, with Energy and Financials, the two largest sectors in the index having significant declines. From a style (factor) perspective, be it value, growth, low volatility or high dividend, many strategies targeting factor exposure experienced negative returns. Despite heightened uncertainty, precipitated by an unstable political climate impacting global trade and interest rate policy, as well as ongoing concerns over consumer debt and housing, the attractiveness of the fundamental profile of the Canadian market has remained firm. Positive momentum of reported earnings and earnings surprise and 12% estimated year over year earnings growth provides support for continuing strength of TSX earnings. Recent market weakness has only served to improve the valuation profile of the overall market. Currently, the current price to earnings (“PE”) ratio of the TSX is attractively priced at 12.3 times, versus 15.3 times at the start of the year.

The S&P 500’s Q4 total return was -13.52% in USD. In CAD, the S&P500 was down 8.6%. Several factors contributed to the US market decline: escalating trade tensions between the US and China, the threat and then actual occurrence of government shutdown over the border wall dispute and a sharp drop in oil prices after the murder of a Saudi-American journalist. As to stocks, 85% of stocks in the index had Q4 losses. As to industry sectors, 10 of the 11 industry sectors in the S&P 500 experienced declines in Q4. Despite the market turmoil, underlying fundamentals such as Earnings growth remain strong in the US. Earnings in the last four reported quarters are up over 27% versus the earnings of the preceding four quarters. Wall Street analysts are expecting a 9% increase in earnings for fiscal 2019 over 2018. There are oft cited concerns about the market’s valuation levels. However, the S&P 500 is trading at a PE multiple of 15.6 times using 2018 expected earnings and 14.3 times using 2019 expected earnings. These valuation levels compare favourably to the 25-year average PE for the S&P 500 of 16.1 times, suggesting that the market is not critically overvalued at present levels.

The MSCI EAFE index represents 85% of the market capitalization of developed markets in Europe, Australia, Asia and the Far East. Overall, the regions represented by this index averaged double digit losses of -12.2% in their local currencies. In CAD, the index was down -6.1%. The index’s 4 largest exposures comprise 60% of the index and endured large losses including Japan down 14.1%, UK down 11.3%, France down 13.7% and Germany down 15.2%.

Fixed Income

The FTSE/TMX Canada Universe combines both government and corporate investment grade bonds over a range of maturities from 1 to 25 years. This index's return was up 1.8% in the period. The representative benchmark in Canada for short-term bonds is the Bloomberg Barclays Global Aggregate Canadian Government/Credit 1–5 year Float Adjusted Bond Index. The short-term index had a 1.3% return in Q4.

The representative US bond index includes over 8000 investment grade bonds with an average maturity of approximately 5 years. The representative global bond index includes almost 9,000 investment grades bonds with an average maturity of approximately 9 years. Both US and International fixed income allocations appreciated in Q4, in line with Canadian Universe bonds.