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## EXECUTIVE PERSPECTIVE

Mark Arthur, CEO  
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A little more than three months have elapsed in 2016, and yet one may not be faulted for thinking that a year's worth of financial market developments have already played out. The quarter started off on the downside — one of the most negative New Year launches for equities in decades. Investor sentiment across the board was infectiously negative.

However, as we write, investor sentiment has shifted to the opposite extreme around the world. In fact, some equity markets even registered positive returns for this past quarter.

Normally, we are nonplussed by short-term market gyrations, given our preference to focus upon long-term Supertrends. However, we do see recent trends validating our expectations. Conditions are in flux. As such, while long-term portfolio returns should amply exceed short-term bank deposits, they will be subject to the unevenness of above average market gyrations.

In this issue of Global Thinking, we interview a long-time investment executive, Russell Lindsay. You'll be interested to hear his perspectives.

Also, Tyler Mordy, President and CIO, reflects on the sweeping and profound changes that are defining a new era. And, finally, the Portfolio Update outlines some of our key investment strategies — where the rubber hits the road, so to speak. This feature is found on the back page.

We hope that you will find the Spring edition of Forstrong Global Thinking informative. Please feel free to provide us with any feedback that you may have.

Sincerely, Mark Arthur, CEO

### What's New at Forstrong

Please visit our new "Global Thinking" section of our website [forstrong.com/global-thinking](http://forstrong.com/global-thinking) for all Forstrong interviews, videos and articles. You can also view regular video updates on topical investment issues on our YouTube page.

Forstrong has recently achieved compliance with the Global Investment Performance Standards (GIPS). What that means is that Forstrong investment performance reporting has been verified by an external auditor and met the standards of the CFA Institute.

Clients can expect to receive an invite to our new Virtual Symposium later this month. This digital format now allows us to present in real-time to all of our clients across Canada.

### Last Quarter's Highlights

- Above-average volatility continued to characterize global financial markets this past quarter. Nevertheless, patient investors were rewarded for holding the course. Following steep declines earlier in this period, strong recoveries played out over the second half of the quarter.
- Investors in Canada, after years of disappointing results, experienced a reprieve. Not only was the Canadian equity market one of the strongest performing amongst developed countries this past quarter, a rising Canadian dollar also kicked in further upside for most foreign investors.
- Generally, market rebounds were registered in higher-risk assets, from commodities (including petroleum), to emerging markets, to Russian rubles. We are not convinced that recent recovery trends will persist at the pace witnessed to date. Nevertheless, it is becoming probable that the lows in various commodity prices and the Canadian dollar will already have been set.
- The Canadian dollar (CAD), after plummeting against the U.S. dollar 19.3% in 2015, finally found a recovery launch point at the multi-year low of \$0.68.5 USD/CAD, rallying as much as 12.5%. For the quarter, the CAD rose 6.7% against the USD. A rising CAD dollar, however, generally detracts from foreign market returns.
- Canadian equity markets returned 4.5% in the 2015 first quarter. Foreign equity markets, after many quarters of strongly outperforming Canada, logged negative returns in CAD terms. To illustrate, the MSCI EAFE Index (representative of most developed-country equity markets) declined 8.52% in CAD terms.
- Fixed income markets enjoyed a quarter of positive returns, viewed in local currencies. Canada's bond market (FTSE TMX Canada Universe Bond Index) returned 1.39%. U.S. fixed income markets (Barclay's U.S. Aggregate Index) also enjoyed positive returns locally, however, were a negative 3.3% in CAD.
- World financial conditions continue to be marked and challenged by tepid economic growth, disinflationary trends, active currency competition and experimental new monetary policies such as negative interest rates and Quantitative Easing (QE). Ongoing developments suggest that financial markets will continue to "see-saw" for some time as markets remain dependent upon central bank actions.



### GLOBAL INSIGHT

#### Explaining a Rollicking New Era

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Here we share perspectives from our recent investment strategy sessions. As the working document that captures all our actionable strategy views is 25-plus-pages long, we can only focus on the most topical of these. And, without a doubt, the most mind-boggling of these factors for

most observers would be the strange phenomenon of negative interest rates. Lately its spread has been as if a global epidemic, though not yet arriving in Canada.

What is the story behind negative interest rate policy (NIRP)? It remains the era of the Central Bank, we believe. While many investors rightly recognized unsustainable global imbalances and the reality of slow economic growth, they also respected the “central bank put” (meaning down-side protection). As such, recent years, reputations of central bankers have come close to deity-like status. But how long can this reverence for the world’s monetary priests last? And, is the new monetary toolkit of policies a work of divine brilliance or are they “making it up as they go along”? Nothing lasts forever (this including the infallibility of central banks) and, yes, desperation is proving to be the mother of invention as far as introductions of unorthodox policies are concerned.

Recently, there is growing sentiment that the “Quantitative Easing (QE) bubble” has come to an end and that “NIRP” is ineffective. To many, QE is viewed as benefitting only the wealthy (i.e. capital owners who profit from rising asset prices). NIRP is also widely viewed as highly problematic particularly for the banking sector. Recent under-performance of European and Japanese banks reflect this concern. Banks are reluctant to pass on negative interest rates to their retail customers. A negative charge on deposits acts as an effective tax on the banking sector, squeezing their net interest margins.

But what about moving beyond QE and NIRP? Could the world’s central banks attempt even more radical policies? These are the type of questions we now often hear from clients. This leads us to “People’s QE” (PQE) — a catchy phrase originating from the UK, where a number of respected academics and the new Labour leader Jeremy Corbyn are pushing the idea. The basic argument is that central banks should provide money to the public with no expectation that those funds are repaid: in other words, a permanent, money-financed fiscal expansion.

PQE could take several forms. The simplest would be for central banks to deposit cash directly into household bank accounts. This would be similar to a tax cut, except that there is no deterioration in the government’s fiscal position (no new debt) because the operation would be funded by the creation of new money. Alternatively, the central bank could directly fund infrastructure and public works spending. For example, the government could use money provided freely by the central bank to invest in highways, bridges, etc. It would fund itself by selling bonds (which never have to be repaid).

The growing supporters of PQE claim it would be more effective than QE because money would be immediately directed into the real economy. In contrast, existing QE works only through indirect channels, by raising assets prices and lowering interest rates. People’s QE could be less dangerous for financial stability because it would not over-inflate asset-price bubbles. PQE could even fight inequality as it boosts income growth, whereas QE mainly helps the wealthy who tend to hold financial assets. Given the right platform for PQE, the public would likely enthusiastically embrace the concept.

Central banks have become the lead sponsors of rising asset prices, effectively becoming victims of their own success. Attempts to cushion financial volatility always end up creating instabilities in the future. Yet, seven years after the financial crisis, not much has been achieved in terms of boosting economic growth. The central issue is that policymakers have not yet resolved the deficiency of world demand. That means we may have only scratched the surface in terms of possible unorthodox policy.

The next stage will likely see central bankers endorsing People’s QE: direct consumer cheques, higher budget deficits to sponsor infrastructure projects, central-bank funded tax cuts ... etc. Economists in favour of these policies are often just fiscal stimulus advocates (perhaps hoping to use the central bank to stealthily push through quasi-fiscal measures). To be sure, money-financed fiscal expansions carry a stigma, often associated with the Weimar hyperinflation of the early 1920s. However, PQE is gaining support. Indeed, it may yet be a few years before full-fledged PQE-type policies are actually put in place. However, as already witnessed, financial markets stand to remain very volatile throughout the transition period

It has been more than 10 years since both the Star Wars franchise’s last major installment and a lift in interest rates by the US Federal Reserve. Both streaks were broken in December 2015. There

arises one additional factor that has added gyrations to financial markets — the recent policy differences of the world’s major central banks. While the Bank of Japan and the European Central Bank have put in place deeply negative interest rates, in America the direction has been very different.

Markets remain obsessed with trying to guess the precise timing of further interest rate increases in the US. Rather than speculating about the Fed’s timing, it is far more useful to ponder the implications of a worldwide policy convergence. This is likely as policymakers realize that competitive policy wars have not raised to global economic growth.

In a much-celebrated quote on his 50th birthday, the late David Bowie boldly declared to an audience at Madison Square Gardens “ ... I don’t know where I’m going from here, but I promise it won’t be boring.” Recent and expected financial markets carry echoes of those immortal words. In the opening months of 2016, action has been anything but boring. Investors cannot be faulted for feeling disoriented. To be sure, financial markets have and are reacting to legitimate macro fears.

Where to from here? It is useful to revisit the role of the portfolio manager. They certainly do not have powers of clairvoyance. Rather, it is to anticipate probable risks, prepare for opportunities and, importantly, not to lose our proverbial “heads” when everyone else has lost theirs in times of emotional upheaval. Expressly, that requires a disciplined approach that can extract emotion from the process.

## *Attempts to cushion financial volatility always end up creating instability in the future.*



**What do you think?**

**Share your thoughts with us on Twitter!**

@tylermordy or @ForstrongGlobal

## CLIENT PERSPECTIVE

# Russ Lindsay

Russ Lindsay is a retired accountant who describes himself as a “boring guy” but there’s nothing boring about how he’s now using his broad based business background to help others. This lifelong Montreal Canadians fan wanted to share his new calling with us and why he’s also become a little bit of a Forstrong fan.

### Why did you decide to become an accountant?

I was always good with figures and math came fairly easily to me so accounting was sort of a natural choice. However, earlier in my career while I was an accountant with a large brokerage firm I was pretty sure that I didn’t want to be an accountant any more. In fact, it was a bit of a crisis for me so I undertook some serious aptitude and career counselling. But in the end, all of the results indicated that I was best suited to be an accountant. Needless to say, I was very disappointed.

### So tell us how you’re now using that early “disappointment” as a force for good.

When you retire, you have all of this valuable experience and expertise that you’ve cultivated over many years and it would be a shame to let it languish. I no longer wanted to work all day every day but I didn’t want to do nothing either. Aside from helping numerous friends, family members and former colleagues with their financial planning and tax strategies, I’m now involved with a couple of not-for-profits. One is called Neighbourhood Information Post and I am their volunteer President. One of their services includes doing income tax returns for low income people. A group of professional accountant friends (some of us are not yet retired), dedicate four Thursday evenings each March to doing tax returns for people who otherwise wouldn’t have access to that type of expertise. Even though our purpose is to help others deal with a task that they find complex, the benefit for us is the overwhelming gratitude that comes back. That is the lesson I really wanted to impart to other Forstrong clients; just because you’re retired doesn’t mean that you have to let your valuable skillset atrophy. There are so many ways in which you can volunteer your time to help others and create a greater sense of meaning in your retirement.

### Where did your strong work ethic come from?

I grew up in Montreal and my father died when I was quite young. My mother was overwhelmed with the responsibility of raising a young family alone so we moved in with my grandmother who was a huge influence in my life. Whenever I asked my grandmother for money, she would give me an opportunity to earn it by doing something around the house like paint a fence. That taught me the value of money at an early age and that you had to earn it. As a result, I always had part-time jobs throughout high school and university. Working was just a natural part of my life.

### Do you recall your first experience with investing?

The very first investment I ever made was to purchase 10 shares of Bank of Montreal stock. This was a very positive experience for me and I immediately fell in love with investing. I tend to become very engaged in whatever I’m interested in so I was investment literate in a relatively short period of time. Even though I had success picking stocks over the years, I’ve come to realize with experience that asset allocation and not individual stock selection is the key to investment success. That’s why my money is with Forstrong because I believe that

the macroeconomic environment is the correct perspective from which to make the best asset allocation decisions. The way that I approach my personal finances now is that I’m in the business of sustainably managing my lifestyle and my estate. From a financial planning and tax perspective, I know from experience that how one harvests their assets in retirement has a huge effect on sustainability and peace of mind.

### Anything else you want to share with our readers?

GO HABS (maybe next year).



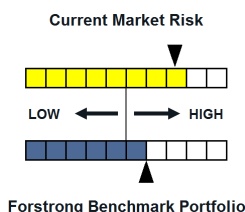
## Notable Quotes

*“THERE HAVE BEEN THREE GREAT INVENTIONS SINCE THE BEGINNING OF TIME: FIRE, THE WHEEL, AND CENTRAL BANKING.”*

— WILL ROGERS

*“THERE ARE LIMITS TO MONETARY POLICY.”*

— BEN BERNANKE



## Current Portfolio Strategy

Over the past few quarters, investors have chosen to view global financial affairs cautiously. As it was, there was no shortage of factors serving to heighten fears. Indeed, investment markets have been transitioning to a new regime. Symptomatic of such shifts is above-average volatility and investor indecision. This has been evident over the past year as well as the opening months of this year. Market downdrafts in January were sharp, as commodity prices weakened. Yet, portfolios have experienced rapid recoveries since that point.

What defines the new era? Certainly, wide-spread negative interest rate policies (known as NIRP, whether viewed in inflation-adjusted terms or nominal) are unprecedented. More than a trillion dollars of assets are bearing negative yields (a concept hard to understand for many).

As well, geopolitical tensions are high and countries are warring for their share of economic growth through competitive monetary and fiscal policies. The long-running trend of globalization has shifted into reverse.

Central banks continue to remain key actors at this time. With global economic growth rates still well below pre-crisis levels, monetary policymakers are very attuned to downside risks. If they are to err in their policies, they will prefer to do so on the side of caution and over-stimulus. A consensus is growing that policies of quantitative easing and NIRP are running against the limits of effectiveness. As such, we expect a third wave of monetary heterodoxy to occur. Pressures are mounting to introduce “helicopter money” policies, though these may yet take some time to come to fruition.

Despite the increased volatility and monetary competition that defines this transition phase, we are still forecasting long-term portfolio returns to be significantly above cash returns. Of course, it should be noted that portfolio returns are random over the short-term and can be highly variable for any given year.

Economic growth, while slow, is still positive (2% GDP growth is the “new bullish”) and recession risk for the U.S. economy is low. Furthermore, we still identify good higher-yielding opportunities around the globe. In a world of continuing NIRP, these stand to perform well.

We remain of the view that the U.S. dollar (USD) is near its peak (versus the rest of the world’s major currencies). The outlook for Canada remains negative as we anticipate commodity prices to remain in a low range for some time.

Some selected investment shifts and themes that describe our

current strategies are highlighted next.

**Asset Mix Shifts Away From Low Yield.** Cash levels have been raised to neutral for core portfolios and modestly overweight in income mandates. Fixed-income allocations have been reduced to underweight. Ultra-low interest rates are simply not attractive, returning significantly less than equity market dividend yields. Equity exposure, therefore, has been raised modestly to a further overweight. Our asset mix nevertheless remains reasonably diversified, and therefore ideally suited for above-average market volatility.

**Regional Preferences Steady.** While equity market exposure is overweight relative to our benchmarks, the equity allocation to the U.S. remains underweight. Exposures to Europe, Asia and selected emerging markets are overweight. Allocations to Canadian equities remain at a neutral level.

**Income, Income, Income.** A major and enduring investment theme that we continue to emphasize is a “global income crisis.” A world of NIRP only exacerbates the chase for income and yield. As such, all of our portfolios, including the more aggressive opportunity assets, have yields well above their benchmarks.

**Opportunity Strategies.** Of the holdings in this category, current strategies emphasize selected emerging markets equities, emerging market local-currency bonds, higher growth countries, and high-yield investments. All core portfolios have an allocation to this opportunity set of holdings.

**Currency Protection.** Should the U.S. dollar begin to decline (especially so against the CAD) preservation strategies are required for international asset positions. We had begun to phase in hedges to protect against a U.S. dollar decline vs. the CAD the previous quarter. Due to the recent counter-rally in the Canadian dollar, hedges are maintained.

The objective of our ETF Managed Portfolio strategies is to achieve stable, positive returns over the long-term without assuming excessive risk. We believe that the best approach in today’s atypical investment climate is to build portfolios that are globally diversified across many asset types, informed by a concerted focus upon a variety of common and unique risk factors.

2nd Quarter 2016			Investment Stance	
Net Asset Mix	Versus Benchmark			Change from previous quarter
	Under	Neutral	Over	
Cash		■		↑ Increased
Total Equity			■	↑ Increased
Total Fixed Income	■			↓ Decreased
Opportunity		■		● Unchanged
<b>CDN Investments</b>				
Bonds	■			↓ Decreased
Stocks		■		● Unchanged
<b>US Investments</b>				
Bonds		■		● Unchanged
Stocks	■			↑ Increased
<b>INTL Investments</b>				
Bonds	■			↓ Decreased
Stocks			■	● Unchanged

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