Lincluden

Quarterly Investment Review

December 31, 2017

Economic Commentary

Fourth Quarter 2017

U.S. Fed Follows Through on Rate Hikes

The U.S. Federal Reserve raised interest rates by 25 b.p. at its meeting in December. The move was widely anticipated by the market. This was the third rate hike during the year and marked the first time in several years where the actual moves made by the Federal Reserve matched the forecasts outlined at the beginning of the year. Over the past couple of years, the number of interest rate hikes that occurred were lower than what was forecast. For 2018, the expectations are for the Fed to raise interest rates three times, although many economists are beginning to feel that four hikes may be more appropriate. The December meeting was the last meeting chaired by Janet Yellen as she turns over control to incoming Fed Chair Jerome Powell.

Mixed Messages from the BoC

The Bank of Canada did not change its overnight interest rate at either of its two meetings in the fourth quarter. BOC Governor Poloz, however, did send out mixed messages following the December meeting, indicating that the bank will take a cautious approach toward future interest rate hikes. Poloz has downplayed the significance of providing forward guidance to the markets. This stance, which differs from other major central banks, can often result in volatile reactions by market participants to comments that are made. Poloz is increasingly confident that the economy will need less monetary stimulus going forward as the economy approaches full potential. There are still uncertainties in the market which may prevent the Bank from aggressively raising rates, including the negative impact of lower oil prices. As a result, the path of future rate hikes in 2018 by the Bank of Canada, currently projected at two, will lag the expected moves in the U.S.

The Canadian economy exhibited signs of a slowdown following a stellar start to the year. After leading the G7 countries for the first half of the year, Canadian GDP growth rates have subsided during the second half of the year. Third quarter GDP grew at a 1.7% annual pace, following a Q1 reading of 3.7% and a Q2 rate of 4.5%.

Job Market Tightening

Employment rates in major countries continue to trend down indicating improved economic conditions around the world. However, inflation pressures to-date have remained modest, with inflation rates remaining below the 2% target in most countries. There is also little in the way of upward pressure in the form of wage growth occurring. Inflation will be a key economic indicator to watch in 2018 as any signs of a significant pick-up could result in more aggressive monetary policies being adopted by major central banks.

ECB Extends QE at Reduced Pace

At its October meeting, the European Central Bank announced that it would extend its quantitative easing program. However, beginning in 2018 the level of monthly purchases will decrease from 60 billion euros to 30 billion euros. The program will be extended from an original completion date of March 2018 to September 2018.

Key Metrics

Indicator	Value	Chg Q3	Chg 1Y
S&P/TSX Composite	16,209.13	4.4%	9.1%
S&P 500 (USD)	2,673.61	6.6%	21.8%
MSCI EAFE (USD)	2,050.79	4.3%	25.7%
FTSE TMX Universe Bond Index	1,036.84	2.0%	2.5%
USD/CAD	$0.80	-0.8%	6.9%
WTI Crude ($/bl))	$60.42	15.7%	6.2%
GoC 10Y Bond	2.05%	-5.4 bp	+32.4 bp
GoC Deposit Rate	1.00%	0	+50 bp
Cdn CPI YoY	2.1%	0.5%	0.6%
US 10Y Treasury	2.41%	+7.2 bp	-3.9 bp
Fed Funds Rate	1.50%	+25 bp	+75 bp
USD CPI YoY	2.2%	0.0%	0.1%

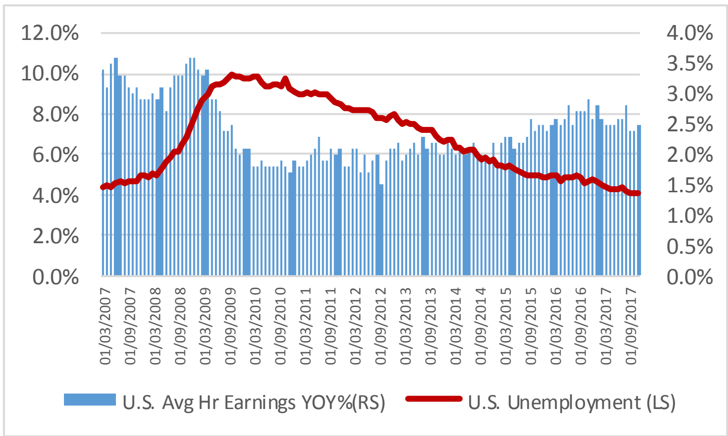
Top Themes

U.S. Fed hikes rates for 3rd time this year

Canadian economy slows after hot start

Unemployment falls, but wage pressures remain modest

Top Chart: U.S Unemployment vs. Wage Growth



Source: Bloomberg, Lincluden

Portfolio Highlights Q4 2017

Ticker	Security	Sector	Commentary
BMO	BANK MONTREAL QUE COM	Financials	Shares in the bank appreciated on the back of good quarterly results. The Canadian segment performed well supported by growth in it's commercial segment.
CM	CDN IMPERIAL BK COMM TORONTO O COM	Financials	Shares in the bank appreciated on the back of strong quarterly results which came ahead of consensus expectations. The bank's Canadian segment, wealth management business, and it's private bank operations in the U.S. performed well. This was also the first quarter following the closure of the Chicago-based PrivateBancorp acquisition.
CVE	CENOVUS ENERGY INC.	Energy	Cenovus declined in price along with the broader sector. Canadian oil prices declined versus global benchmark prices due to a supply glut in Western Canada caused by a temporary shutdown in one of the main pipelines.
ESI	ENSIGN ENERGY SERVICES INC.	Energy	Ensign was negatively impacted during the quarter by energy prices which has curtailed it's customers drilling and well servicing activities.
HCG	HOME CAPITAL GROUP	Financials	Home Capital has been hard at work since the liquidity crisis in the first half of the year. Following the Berkshire Hathaway equity injection, the new management team led by the recently hired CEO has been able to further solidify it’s capital base to the point where investors felt comfortable rejecting a second tranche of equity financing from Berkshire. With capital concerns behind them the company is on the path to recovery. The new strategic plan will look to optimize Home Capital's operational processes with the goal of returning new mortgage originations back to their previous levels.
HSE	HUSKY ENERGY INC.	Energy	Shares in Husky appreciated due to several reasons. The company has exposure to international operations which benefited from rising global oil prices. Also the company released its capital expenditures for 2018 which came in lower than consensus. Furthermore the company is expected to reinstate its dividend early next year due to a stronger free cash flow profile.
IIP-U	INTERRENT REAL ESTATE INVESTMENT TRUST	Real Estate	InterRent REIT and its apartment REIT peers have benefitted from affordability issues in the housing market. This has lead to an increase in people renting and for longer. InterRent has benefitted from the repositioning of its assets, and from growth in the Hamilton area. We continue to hold the position and see more upside.
MFC	MANULIFE FINL CORP COM	Financials	Shares in the insurance company appreciated on better than expected results. Both the Canadian and U.S. segments reported higher fee income, while the wealth management division had strong earnings growth.
RY	ROYAL BK CDA MONTREAL QUE COM	Financials	Shares in the bank appreciated on the back of good quarterly results. The bank's capital markets division, wealth management business, and it's U.S. operations via City National Corp. performed well.

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TCN	TRICON CAPITAL GRP	Financials	Tricon Capital contributed to performance as the integration of Silver Bay Realty is running ahead of schedule. This purchase of a U.S. single family rental REIT has helped create many synergies and is performing well as many families in the U.S. are choosing to rent as opposed to purchasing due to affordability issues.
ARYN SW	ARYZTA AG	Consumer Staples	The shares performed strongly in the quarter after announcing the hiring of a new CEO after a lengthy process. Quarterly earnings were inline with expectations which demonstrated stability after several declining quarters. The valuation is attractive and new senior management provides opportunities for strategic improvements.
BAC	BANK OF AMERICA CORPORATION COM	Financials	With rising interest rates and solid third quarter results, the company was a positive contributor during the period. The bank's credit quality and capital position remains strong and the company announced a material increase to its share buyback program. Valuation in the stock remains reasonable and the risk/reward looks positive in light of an improving U.S. economy and rising interest rates.
BBBY	BED BATH & BEYOND	Consumer Discretionary	Upon conducting a full review, we decided to exit the position. Quarterly earnings were below expectations and operating performance continues to deteriorate with same store sales declining mid-single digits and compressing margins. While their online sales are growing, it remains a very small component of overall revenues and further investments are required to increase capabilities, which will further depress free cash flow.
BHF	BRIGHTHOUSE FINANCIAL INC	Financials	Brighthouse is a pure-play variable annuities business that was recently spun-out from Metlife. After the initial fall from the spin-out, the stock had rallied ~20% and we used that as an opportunity to exit the small position as we had several concerns for the company. Given the low level of rates, there is limited demand for variable annuities, with significant competition, and potential for regulatory reform. The company is launching as a new brand, and will require significant investment to build its awareness in the market, all while trying to grow its capital and earnings low ROE's. There is no dividend and capital return to shareholders is unlikely over the next several years. Despite a valuation that looks attractive, this is inline with it's more established peer Voya.
CSCO	CISCO SYSTEMS INC.	Information Technology	Shares in the company increased as they reported a growth in revenue after a long period of decline. Guidance for the next quarter reflects further growth and was ahead of expectations. The company's transformation is gaining traction as subscriptions become a larger portion of revenues and new products are seeing positive demand. The valuation remains attractive as the earnings profile transitions to a steadier recurring base.

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GSK	GLAXOSMITHKLINE PLC SPONSORED ADR	Health Care	Despite solid earnings results, concerns that the company will conduct an expensive acquisition (Pfizer's consumer health business) drove sentiment negative and led to the shares detracting from performance in the quarter. The valuation is depressed and represents an attractive risk/reward.
SNY	SANOFI SA ADR	Health Care	The stock was a detractor to the performance. The company reported results that were below expectations driven by softer results in its Diabetes franchise that is facing increased competition from generic competitors. The valuation is depressed and represents an attractive risk/reward as potential new drug approvals could improve sentiment.
DG FP	VINCI SA	Industrials	The stock was a strong contributor to performance during the period. The company reported solid quarterly results and held an investor day that demonstrated opportunities for continued growth in its concession businesses and margin targets that exceeded expectations across all assets. The improving French economy continues to be a positive driver.
WBA	WALGREENS BOOTS ALLIANCE	Consumer Staples	The stock was a detractor to the performance due to fears that Amazon will be entering the retail pharmacy business. Despite those concerns, the company reported strong third quarter results and operating momentum remains positive. The valuation is very attractive for this high quality company and we believe it has the scale to compete if Amazon did enter the market.
WMT	WAL-MART STORES INC.	Consumer Staples	The shares contributed strongly to the performance during the quarter after it reported stronger than expected sales trends that demonstrated the company is having success growing both its online and in-store sales. Recent investments in online initiatives are paying off and is showing that the company can compete successfully with Amazon.
WPG	WASHINGTON PRIME GROUP (WP GLIMCHER)	Real Estate	The company saw some sales pressure in its secondary mall portfolio. The market has been very concerned about the effects of ecommerce on retail real estate, and as such the stock detracted from performance over the quarter. The stock is trading at one of the largest discounts to NAV we have ever seen, and we remain holders and collectors of the dividend as we wait for the situation to play out.