F&A
FOSTER & ASSOCIATES

Quarterly Report

Second Quarter Report 2019

One must weigh not only the risk of ruin, but also the risk of being on the sidelines.

When we think about investing, it's important to not just focus on "What if?", but to also think about "What if not?"

The media never seems to run out of things to worry us about. We are constantly inundated with nightmare scenarios that are also potential market disruptors; from "What if we go into a trade war?", (or an actual war), to "What if President Trump's foreign policies create a global melt-down?"

To that, we would respond, "What if... Not?" That's right, what happens if none of these things happen? To be sure, there are a large number of scary awful things that could befall us. But what happens when the world collectively comes to the conclusion that it's once again safe to aggressively invest in the businesses of North American and abroad?

This is more than just a philosophical question. Suffering through a period when the value of your investments gets marked down because of some calamity is certainly unpleasant. And if there's little prospect of better times ahead, staying cautious is the better course.

But instead of calamity, what if there is a chance of the boom times continuing? This possibility of ruin must be weighed against the suffering you will feel if you aren't fully invested during a meaningful market melt-up. (A market "melt-up"? Yes, a market rise that makes the plunge of late last year feel like a distant memory.)

What could bring about a melt-up? Well, nobody is arguing that the stock market is offering gate-crasher specials right now. Depending which market you look at, we are up 10% to 20% so far this year, and we've still got half a year left. So, it's not likely going to be value-shoppers scooping up stocks that propels us to higher and higher levels.

But how about monetary policy? While I realize that in the post-Greenspan era, monetary policy has been about as interesting as the inside of your eyelids, if you're going to have a surprise, it can only come from a surprising place.

If you're listening to nerdy economic podcasts, or following the fringes of central bank thinking, you will be aware of Modern Monetary Theory (MMT).

		2019 Q2	12 Month Returns
S&P/TSX*	16382	1.7%	1.9%
S&P 500	2942	3.8%	8.2%
Dow Jones	26600	2.6%	9.6%
Nasdaq	8006	3.6%	6.6%
$CAD	$0.7637	1.9%	0.3%
Crude Oil (WTI)	$58.47	-3.5%	-20.8%
Gold	$1,409.50	9.1%	12.5%

** The S&P/TSX, the S&P500, the Dow Jones and Nasdaq indices are not investable indices, and as such are not a direct comparison to any investment product available at Foster & Associates Financial Services Inc, and therefore should therefore be considered hypothetical in nature and for illustrative purposes only.*

In very simple terms, MMT seeks to legitimize the idea that governments can spend more than they take in WITHOUT increasing borrowing. That is, it recognizes there are circumstances where just printing money for the government's needs is recommended.

We refuse to pass judgement on this idea, but the fact that it has moved from the economic fringes into the campaigns of certain US Democratic Presidential candidates, is worth mentioning. Also worth mentioning perhaps is the chance that President Trump's constant haranguing of Fed Chair Powell to lower interest rates might actually work to some degree.

What does this mean? Well, it means that maybe we aren't really in the early stages of a series of interest rate hikes. This would be great news for the stock market, and something you wouldn't want to miss.

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The prudent investment advisor will tell you that it's okay to underperform the market when things are booming, and they're right. But it's what happens after that can cause the real damage.

Really, really underperforming, especially when it happens to a self-directed investor, can leave a lasting mark. In the business, we call that getting off-track, and the train analogy is a good one. Once you jump off the rails, it's very hard to get back on. Deciding to get cautious is an easy decision. Deciding you made a mistake is much harder.

Every Bay Street veteran has seen investors refuse to get back into the market after misplaying their hand, even years later, and even after declining prices would give them a good opportunity. True, they have averted ruin, but they could be committing themselves to a lifetime of under-performance.

The 12-Month Market Outlook

Stocks (U.S.)	▲
Stocks (Canadian)	▲
Bonds (US)	▼
Bonds (Canadian)	▼
Canadian dollar	--
Crude Oil	▼

This table represents the way the firm is leaning in particular market sectors over the next 12 months. It does not represent a trade recommendation, nor does it play a major role in our portfolio construction, which involves much more than having a view on a particular market index, currency or commodity.

ADVISOR INTERVIEW with John Suske, MBA, Investment Advisor speaking to our readers about one of his top holdings.

JOHN SUSKE

Canoe EIT Income Fund

Symbol:
TSX: EIT-U

Price, June 28/19:
$11.08

Price, YE 2018,
$10.10

Market Cap:
$1.3 bil

John, I see a number of your clients have been long-standing owners of the Canoe EIT Income Fund. Can you explain what you like about the fund?

JS: The Canoe Income Fund has a proven, long term track record of consistent, stable and recurring dividends (0.10 per unit, per month). My family and clients have owned this fund for over ten years.

This is a closed-end fund. For our clients that may have less experience with these products, is a closed-end fund like an exchange-traded-fund (ETF)? Or is it like a mutual fund?

JS: The Fund trades on the exchange at a slight premium to its Net Asset Value (NAV) which is a strong endorsement of the safety of its monthly dividend. The units have always traded in this manner. They are a true image of the value of the securities it holds. As a result, the units represent a true proxy on the North American stock markets with an attractive dividend as a bonus. In other words, the units are paying you to wait.

The fund pays a very high dividend. Is this a fund for people that require steady income? Do you feel that the dividend is sustainable?

JS: The dividend is extremely tax-efficient with approximately 50% of the dividend proceeds treated as capital gain or dividend income and 50% treated as Return of Capital (ROC) which is non-taxable.

The name of the fund makes it sound like it's all about creating steady income, but I notice there are some technology names among its top holdings. How would you describe the way they invest?

JS: By relying on the professional managers to provide diversification and proper sector weighting, the investor receives the comfort of market exposure and safety. In other words, the guesswork is left to the pros.

Do you have a type of client that is particularly well-suited to this fund?

JS: Not only is this a great solution for clients seeking steady, reliable monthly income, it is also suitable for clients looking for exposure to the equity market. By registering in the Dividend Reinvestment Program (DRIP), an investor can multiply his returns by receiving more units each month. This gives the investor the benefit of the magic of compounding. The Fund will wrap up in 2050 and as such an investor will receive in cash the Net Asset Value (NAV) at that time.

The views as articulated in this interview are those of John Suske alone and do not necessarily reflect the opinion of Foster, and do not constitute a solicitation to engage in any specific investment or strategy.

GOLD: A Brief Update

Briar Foster
is the founder and former CEO/Chairman of Foster & Associates Financial Services Inc (Foster), and remains a Board Member of FAFS Holding Corporation, the parent company of Foster.

Gold is used in medical science, dentistry and making jewelry, but the bulk of it is held as a currency reserve, taking up storage space in places like Fort Knox. Its reputation is impeccable, bringing with it notions of high value and great reliability.

Gold coins began circulation around A.D. 600 and went on to be the ultimate in liquid wealth until displaced by paper currencies. This triumph of paper started in 1971 when rising inflation made Richard Nixon take the United States off the gold standard (US $35 per troy ounce).

Over the next eight or so years the price of gold climbed to over $600, and it looked like paper money was losing the battle. But prices then consolidated for the next twenty-five years between $300 and $500 during that period, proving that paper money unmoored to gold was not the financial apocalypse it was feared to be.

Obviously, gold is not an investment. It pays no dividends and has a horoscope-level of price predictability. Nor is gold as useful as a man's suit, the price of which it is thought by some to mimic. On the other hand, the price movements can be huge as well as long-lasting, making it an attractive speculation. At times.

Is now one of those times? Traditionally, gold rises with rising inflation expectations. Yet, we live in a low inflation environment. On the other hand, our low-interest rates mean the economic cost of owning gold is less onerous than if investors could earn six percent on a five-year GIC.

The recent pop in the price of gold to over $1400 is likely related to currency uncertainties. The Chinese domestic debt situation and the lack of a trade agreement with the United States has weakened the outlook for the yuan. The lack of a clear outcome for Brexit has made the British pound a suspect storehouse of value. The future of the Euro faces uncertainty from the shaky finances of Italy and Greece, as well as a few of the major European banks.

The US dollar, on the other hand, remains strong. Despite President Trump or because of President Trump or because of so much uncertainty elsewhere, the US dollar has maintained its value well. Of course, if the US dollar were to weaken, almost by definition the price of gold would have to rise. This is what happened in the wake of the depression of 2007-09 when the US dollar fell. The price of gold rose to $1800 by 2011, but by 2015 had slid back to under $1100.

But that big move in gold wasn't a real loss of faith in the paper money system. Central banks, the really big potential buyers of gold are still not really piling in. They have increased their holdings slightly over the past 10 years, but it hasn't yet gathered steam. They still hold less in aggregate than they did when the US went off the gold standard more than 45 years ago.

Canada, for its part, despite being a significant producer of gold, has abandoned gold as part of Canada's currency reserves. In 1965 our central bank had 1,023 tonnes of gold. Now, after having sold all their gold bars more than 15 years ago, they have also disposed of all their gold coins, taking their reserves to zero. By way of contrast, The U.S federal Reserve holds 8,100 tonnes of gold.

Investors can be assured demand for gold is deep and that gold will remain a fixture of the investment scene. If central banks around the world push the panic button again and start printing money *en masse*, gold prices will surely rise. But now it seems the price of gold has become something of a simple barometer of uncertainty, not the stuff true gold bull markets are made of.

So, for now, while I confess to owning small positions in rather speculative gold companies - Eastmain Resources (TSX: ER), a gold exploration company, and Yamana Gold (TSX: YRI), a mid-size Canadian gold producer - my only gold bullion speculation will be to hold onto the gold cufflinks inherited from my grandfather.

Briar Foster, June 10, 2019

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Our core beliefs

What defines the culture of a firm is what stays consistent no matter what's going on in markets. Politics, market trends, and the business cycle will cause us to think different about the way we invest our clients' money. However, there are a few things you can count on from us, through good markets and bad, through recessions and buoyant recoveries:

Asset Allocation is Key.

While some individual securities will do well, and some less well, most of what will make or break your portfolio over time is asset allocation. Of course, we all remember our great buys, and mourn our missteps, but the key to how well you do in the markets will come from how much you owned of various asset classes, and when you owned them.

We Love Canada.

But it's not where we want to put all your money. The Canadian stock market is heavy on banks and resource companies, making true diversification hard to achieve. Venturing abroad can improve returns and lower volatility. You'll also find companies where Canada isn't as strong, such as in consumer staples and biotechnology.

Alternatives aren't that Scary.

Sure, some hedge funds can be dangerous, but there's more to the Alternatives space than hedge funds. There's private debt, real estate, infrastructure and market-neutral funds, all of which can provide a place of refuge during periods of excessive market volatility.

Costs matter a Great Deal.

Over time, even small increases in costs can significantly lower returns. If you pay us to manage your money, we will pinch your pennies for you.

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