

PALOS

The Palos - Mitchell Report

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The Markets - December

What a strange month. December 24th brought us the worst Christmas Eve in the history of the Dow Jones Industrial Average, and by a wide margin. Hot on the heels of this, Boxing Day brought us the largest single-day point gain ever! Finally, on December 27th, we saw the largest intra-day recovery in 10 years. So, you are probably wondering, what the heck is going on?

The 10-year bull market in U.S. equities, that began in March of 2009, has been one of the longest in history. Since the late September peak, we have seen a spike in volatility and a correction of approximately 20 percent. While it is never easy to weather a correction, it was the velocity of the most recent one that left investors feeling edgy.

Now would be a good time to remind ourselves that market corrections are normal. They should be **expected**. Further to this point, may I dare suggest they should be **welcomed**? I harken back to one of the most important truths about investing; returns are directly related to what you pay and ultimately, when and at what price you sell. If your time horizon is long-term, short term fluctuations should be viewed as nothing more than 'white noise'. Let us take some sage advice from Warren Buffet, one of the world's most astute long-term investors. Mr. Buffet is widely renowned for his investing acumen and his disciplined approach - *buying assets when they're 'on sale'*. I subscribe to this philosophy.

Where do we go from here?

As we don't live in a vacuum, we can't help but be inundated with media reports purporting that '*a bear market is upon us*' or that '*a recession is coming*'. My suggestion would be to take such opinion with a grain of salt. Keep in mind that market turmoil will turn many '*talking heads*' into expert prognosticators. This includes many Wall Street analysts who are paid to voice their opinions publicly. In recent days, I've repeatedly heard that '*the worst is yet to come*'. While this is certainly possible, it has been my personal experience that tying your strategy to '*expert prognosticators*' who try to predict the future is a fruitless endeavor. Remaining diversified, keeping a clear head while others panic, and using volatility to seize upon tactical opportunities – following these common-sense principles offers a much greater likelihood for success.

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Goodbye 2018!

While markets were quick out of the gate last January, the rally was short lived. A spike in volatility accompanied by a late January sell-off brought U.S. equities into the red by February. Over the ensuing months, broad optimism led U.S. markets to new highs by September. However, with a combination of White House turmoil, Trump's trade wars, and a hawkish Fed bent on raising interest rates, the gains could not be held. In the final quarter we witnessed a sharp decline that led most global markets into negative territory for the year (see table on page 4). In Canada, the TSX Composite finished 2018 with a similar sell-off that resulted in a decline of 11.6% (TSX Composite Index). Of interest to Canadians, was the ferocity of the decline in energy stocks. Obviously, the swift and unanticipated decline in oil prices led oil stocks lower. After a year in which we saw extended periods of low volatility, things had quickly changed. Volatility was back.

Volatility - is this the new normal? Or just normal?

What is stock market volatility? Volatility, or '**vol**' as it's called in market circles, is a measure of the price range of a security, or market index, over a given period. When stock prices are stable, volatility is low. When prices rise and fall sharply over a short period of time, as we have recently witnessed, the '**vol**' increases. Spikes in volatility are often viewed by the public as the equivalent of higher risk. While higher volatility can be unnerving, it also offers tremendous opportunity. Volatility is normal.

As an active manager, I am constantly in search of opportunities to buy assets when others irrationally sell. Conversely, I capitalize on exuberant or over enthusiastic buying by reducing or selling positions in order to reduce risk or lock in gains. This strategy forms the essence of what I have done over my thirty-year career as a professional trader and portfolio manager. In my opinion, active management offers far superior risk mitigation and wealth enhancing opportunities than more traditional '*buy-and-hold*' or index-following strategies.

Can volatility can be your friend?

Remember, markets are comprised of individual stocks that are characterized by sector or industry, classification (growth or value), size (market capitalization), and geographic location. All stocks are not the same. In times of uncertainty, sectors such as consumer staples, healthcare and utilities will attract buyers as these sectors are viewed as safe havens. When investors are willing to assume greater risk, capital will be allocated to higher growth sectors like technology, consumer discretionary, materials and industrials. Moving capital from one sector to another is called **sector rotation**. Buying or selling of individual stocks is called **tactical management**.

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My point is this. Without volatility in markets, the opportunities for tactical management are fewer. When volatility increases, irrational selling provides plentiful opportunity to buy stocks when they're 'on sale' and this is what we strive to do. So, if volatility is what provides us with opportunities to enhance performance, shouldn't we view higher volatility as a providing us with much welcomed opportunity? ***Volatility can be our friend.***

The Palos-Mitchell Alpha Fund – UPDATE

I'm pleased to announce that the Palos-Mitchell Alpha fund is approved and set to launch on January 9, 2019.

Documentation that contains information on the fund and how it is to be managed, will be available shortly. While holding your investments as units of a fund will appear differently than in separately managed accounts, the overall investing philosophy, securities held, and capital preserving strategy will remain unchanged. In fact, individual securities held at the time of transition will be migrated to the fund, effecting minimal change in the securities you currently hold.

Managing your portfolio as a fund rather than as separately managed accounts, has distinct advantages. These advantages are derived from our ability to focus full-time on managing the fund, reduced transaction costs, and greater ease with regards to implementing risk mitigation and income enhancing strategies. In addition, tax management and performance measurement will be simplified. Units of the fund are eligible for both registered and non-registered accounts.

TFSA contribution amount gets a boost

TFSA annual contribution limits will be going up in 2019, from \$5,500 to \$6,000. The cumulative amount will now be \$63,500. TFSA's offer a great way to invest as they offer tax-sheltered investing. A solid strategy is to contribute as much as you can to both your RRSP and TFSA accounts. However, there are differences between a TFSA and an RRSP.

- ✓ TFSA income and gains are non-taxable. (*RRSP withdrawals are taxable and must begin in the year you turn 71*).
- ✓ There is no age limit in a TFSA, so can continue to contribute. (*You cannot contribute to your RRSP after age 71*).
- ✓ You do not need earned income to contribute to a TFSA. (*RRSP's require income*).
- ✓ Beneficiaries will not be taxed on gains made in your TFSA (*only gains following death of the TFSA holder are taxed*).
- ✓ You can make a withdrawal from your TFSA at any time and re-contribute that amount as soon as the following calendar year. (*RRSP's withdrawals, once made, cannot be replaced*).
- ✓ TFSA's can be used for any investment goal, either to augment retirement income or for any other purpose.

If you would like to open a TFSA account, make a contribution, transfer your TFSA from another institution, or simply obtain more information, please send us email and we will respond promptly.

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Happy New Year!

I would like to take this opportunity to extend my heartfelt wishes for a healthy, happy and prosperous 2019.

Best Regards,

Bill

Markets at year-end, December 31, 2018.

Source: Thomson Reuters Eikon

	VALUE	YTD CHANGE	YTD Returns
Dow Jones Industrial Average	23,327.46	- 1,391.76	- 5.63%
S&P 500 Index	2,506.85	- 166.76	- 6.24%
NASDAQ Composite Index	6,635.28	- 268.11	- 3.88%
S&P/TSX 300 Composite Index (Canada)	14,322.86	- 1,886.27	- 11.64%
STOXX Europe 50 Index (Europe)	2,760.06	- 417.78	- 13.15%
Nikkei 225 Index (Japan)	20,014.77	- 3,491.56	- 14.85%
Shanghai SE Composite Index (China)	2,493.89	- 813.28	- 24.59%
U.S Dollar/Canadian Dollar	0.7332	- 0.61	- 7.75%
NYMEX - WTI Crude Oil	\$45.41	- \$15.01	- 24.84%
COMEX Gold	\$1,278.30	- \$28.00	- 2.14%

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We invest our clients’ money as we do our own. Our interests are aligned with yours.

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I am a portfolio manager at Palos Wealth Management based in Montreal, Quebec, Canada. My experience in the investment industry is extensive, having spent more than twenty-nine years analyzing, trading and investing in global financial markets.

At Palos, we are driven by our values. We believe in the principles of honesty, integrity and transparency. We subscribe to a strong work ethic and we have a passion for investing. The pursuit of excellence is our motivating force. We take our fiduciary duty to heart and we always act in the best interests of our clients.

If you have any questions about investing, our services, or becoming a client of Palos Wealth Management, please contact me at:

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