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Commentary & Outlook

U.S. Economy Still Chugging Along

The economy South of the border continued to look positive during the month of August and now into the better part of September. This is despite continued political drama. Jobless claims are down, and job creation is up along with consumer confidence.

The GDP (Gross Domestic Product) numbers for the U.S. also came in strong. An economy is considered to be in a recession or economic slow down after 2 quarters of declining GDP. Strong numbers are a positive sign that the U.S. economy is still chugging along.

Investors demonstrated their confidence by pushing S&P 500 to all time highs, breaking the record as the longest running bull market in history.

A point that is not lost on our management team as Croft Portfolio Managers continue to cautiously take advantage of the trend.

Canadian equities had a tough August as trade concerns between the U.S. and China impacted the materials sector, while the overturn of the Trans Mountain Oil Pipeline expansion weighed heavy on energy.

Oil as a commodity finished the month of August about where it started after some volatile swings and currently remains with in the 67 to 69 range.

Gold hit a recent low of $1170.00 but rallied quickly to settle back above $1200.00. This trading behavior continues to be heavily influenced by the swings we have seen in the U.S. Dollar as of late.

Fund Performance

TCG 531 Equity Growth Fund

In August, the Equity Growth fund finished positive 3.27% while its benchmark, TSX Total Return Index was negative 0.82% for the month.

Year to date, the Equity Growth fund is up 8.32% with the TSX TR benchmark trailing at 2.27%

With Canadian banks reporting at the end of August, and given expectations for interest rate increases, the Canadian Financials index approached a six-month peak near the end of August. The Investment Review Committee took the opportunity to re-evaluate the Canadian bank holdings and decided to close out a position in National Bank of Canada (NA.TO). Although this company had performed well in the past, according to lead manager Alex Brandolini, research confirmed that earnings quality has been weak, and the upside on the financial stocks is limited. Given that view, we decided there would be better places to deploy the capital.

Over the month of August, the momentum factor continued to provide opportunities in Canada and the United States. Canada Goose Holdings Inc (GOOS.TO), a Canadian Consumer Discretionary stock, was added to the portfolio during the mini-momentum correction. This company exhibits supernormal growth and has a history of beating expectations, but also doesn't trade on a lot of volume. When a significant holder of shares in a company that trades on low volume chooses to exit the position, it often creates large moves to the downside and an opportunity to get in at a more favorable price. Given the fundamentals of the company, its factor exposures and future prospects, we took the opportunity to buy the company on a pullback.

TCG 534 Income Fund

Our Income fund finished the month of August up 2.27% compared to the Real World Index Income benchmark, which was up 0.39%. Year to date, the fund shows gains of 6.20% compared to its benchmark, which trails at 1.28% for the year so far.

Lead manager Mark McAdam suggests that the strong returns in the fund can be attributed to the acquisition of Enercare (ECI) by Brookfield Infrastructure Partners for a 52% premium. We've also seen strong, active trading returns on Constellation Brands Inc. (STZ).

Overall, the fund continues to overweight the Technology sector while reducing exposure to the Consumer Discretionary sector.

In addition, some exposure to the Telecommunication sector was introduced. According to Mark's analysis, valuations in this sector are attractive and many companies feature high dividend yields.

Equity exposure has also been reduced in an effort to lower the risk of the Pool, and put options on the S&P 500 remain in place as part of our ongoing hedging strategy.

TCG 539 Option Writing Fund

Our Option Writing Fund is designed to drive cash flow using income generating option strategies regardless of market direction.

The fund finished August positive with a 2.26% gain, beating its benchmark, the Montreal Exchange Covered Call Writers index, which finished the month positive 0.30%.

Year to date, the fund sits positive at 4.44% compared to its benchmark, which trails slightly at 3.60%.

Lead manager Richard Croft confirms that as highlighted last month implied volatility remains at short-term lows and continued to contract in the month of August. This continued contraction has reduced the premiums collected from our option writing strategies. In response, Richard has continued to shorten the terms to expiry of these options, with a current average term to expiration of 26 days. The objective of writing option contracts with shorter terms until expiration is to benefit from the accelerated time value erosion characteristic of these options.

Richard continues to maintain a balance between Value and Momentum stocks. The fund currently has a 48% exposure to value stocks, 36% exposure to momentum stocks and 16% cash.

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The current exposure to the U.S. Dollar is approximately 35% which Richard notes, depending on the outcome of the NAFTA negotiations, could be volatile relative to the Canadian Dollar over the short term.

Current Outlook and Expectations

The length of the current bull market, now officially the longest on record for U.S. equities, concerns some investors. According to Investment Review Committee consensus, what's different about the new high on the S&P 500 achieved in August, relative to the peak we saw in late January is that valuation multiples look much better this time around.

Much of the volatility over the last month was sparked by risks within Emerging Markets. Historically, weakness in Emerging Market stocks has not spilled over into U.S. markets without a significant surge in the U.S. dollar and a significant drop in oil prices. While the U.S. dollar has strengthened this year and the price of oil has come off its peak, neither are anywhere close to the magnitude associated with previous U.S. market downturns.

To summarize, economic fundamentals continue to support a positive view on the markets. Both macroeconomic models and bottom up forecasts, which focus on company fundamentals, indicate this bull market continues to have legs to run.

That said, although we plan to continue to be fully invested while the overall outlook remains positive, we will continue to re-evaluate and adjust as market conditions change.

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Investment Review Committee

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