Davidson Professional Wealth Management

of RBC Dominion Securities

Market Commentary

June 13th, 2012

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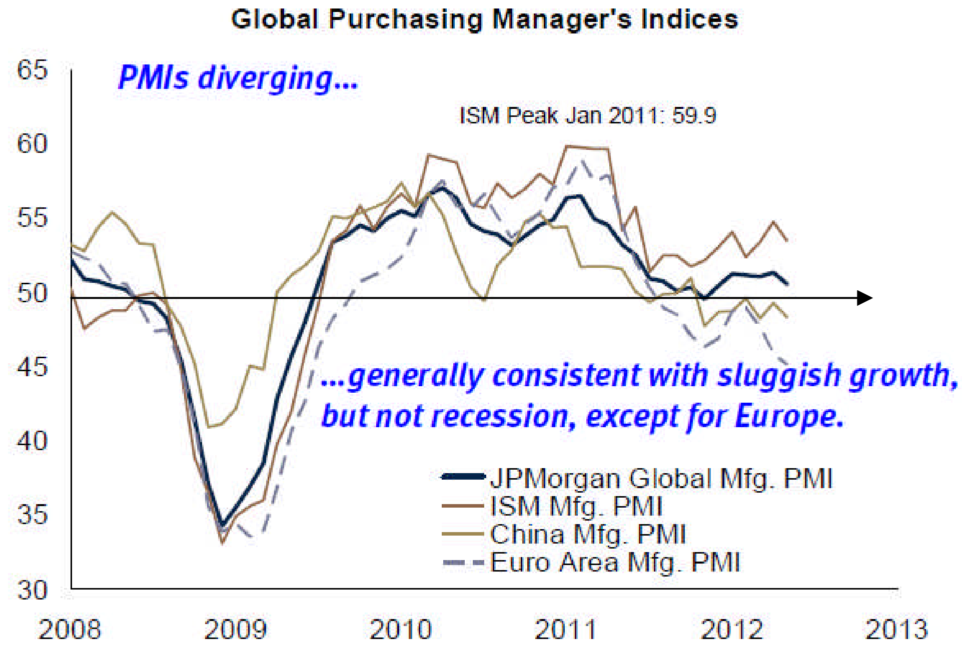
Global Economic Overview

➢ The Eurozone crisis has pushed the Continent into recession. The purchasing manager's index (PMI) chart on the right highlights the effect the crisis is having on manufacturing in Europe. Despite this the US economy continues to expand albeit at a modest pace. Data points above 50 indicate economic expansion.

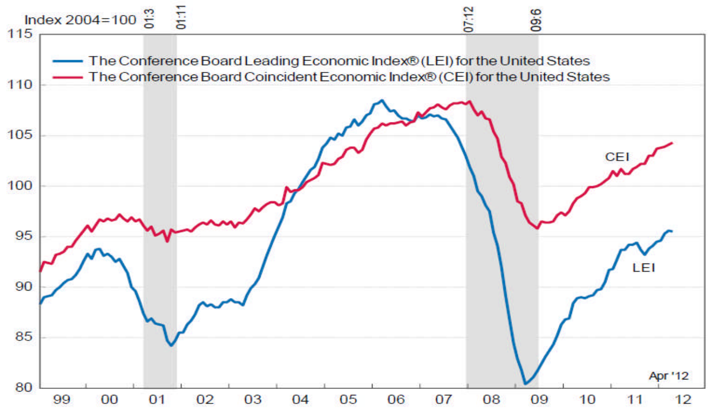


Source: Haver Analytics, RBC GAM

➢The lack of European political will is something that we've become accustomed to over the last several years. European leaders seem willing to play political chicken until the 11th hour when ultimately they come to some form of agreement. As a result equity valuations remain very low as investors wait on the sidelines for clarity.

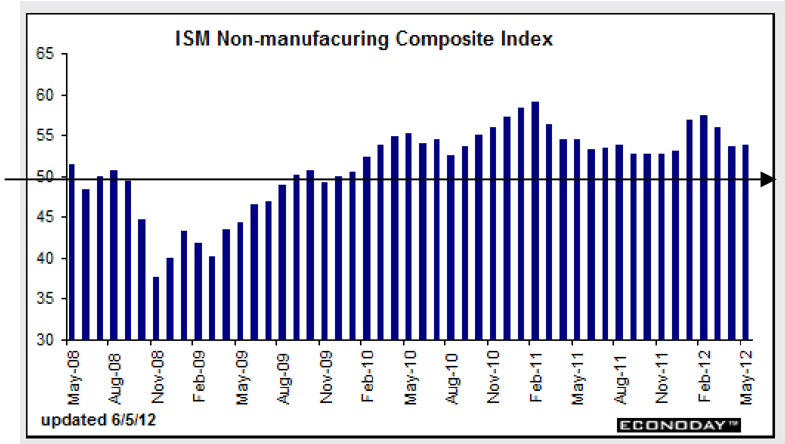
US Economic Indicators Show Resilience

➢Leading economic indicators have taken a pause in May, the medium term trend is still positive so there is a low probability of US recession at this point. We'll be watching these charts closely throughout the summer as they are an excellent indicator of the health of the economy.



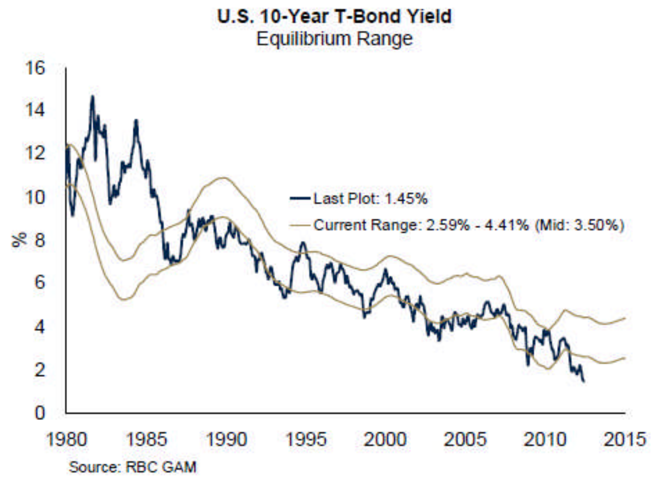
Latest LEI Trough March 2009, Latest CEI Trough June 2009
Shaded areas represent recessions as determined by the National Bureau of Economic Research.
Source: The Conference Board

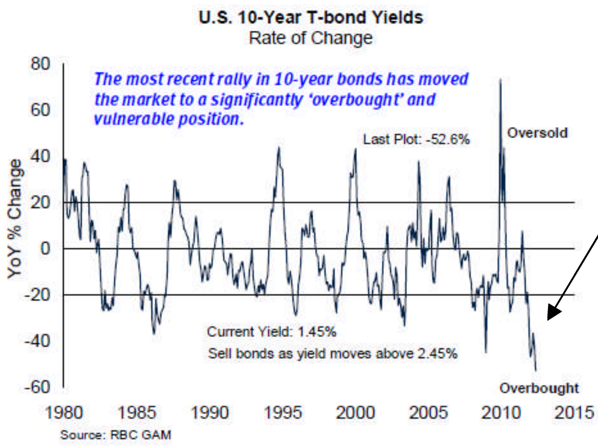
➢Growth in the non manufacturing sector in the US continues despite the problems in Europe and China. Data points above 50 represent growth in the non manufacturing sector which represents over 80% of the economic activity in the US.



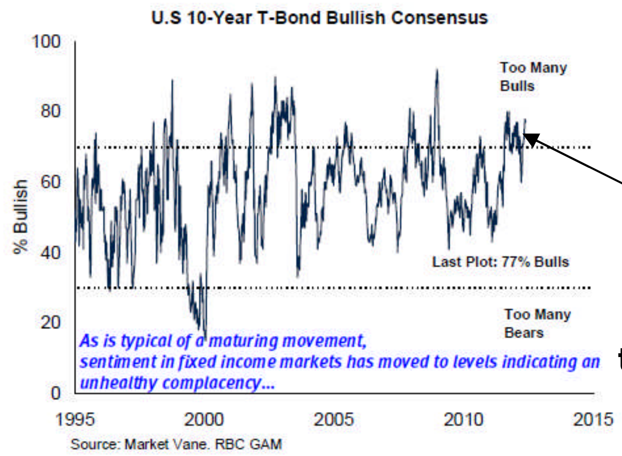
Bond Investors Beware

- Investors continue to be fearful of the potential economic fallout of the Eurozone crisis, resulting in a very expensive bond market that sits well outside of its equilibrium range. When the Euro crisis moves toward resolution the fear trade should diminish, driving bond yields higher and bond prices lower as interest rates move back towards equilibrium. This has the potential to hurt investors who hold long dated bonds and may be unaware of the potential risks.





Bond yields have plunged



The bond trade is very crowded and is vulnerable to a correction

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Like a Tax Cut!

The recent drop in the price of oil by more than 20% amounts to a tax cut for many businesses. This will help companies to reduce their costs and increase their profitability which should be a positive for shareholders at some point in the near future.

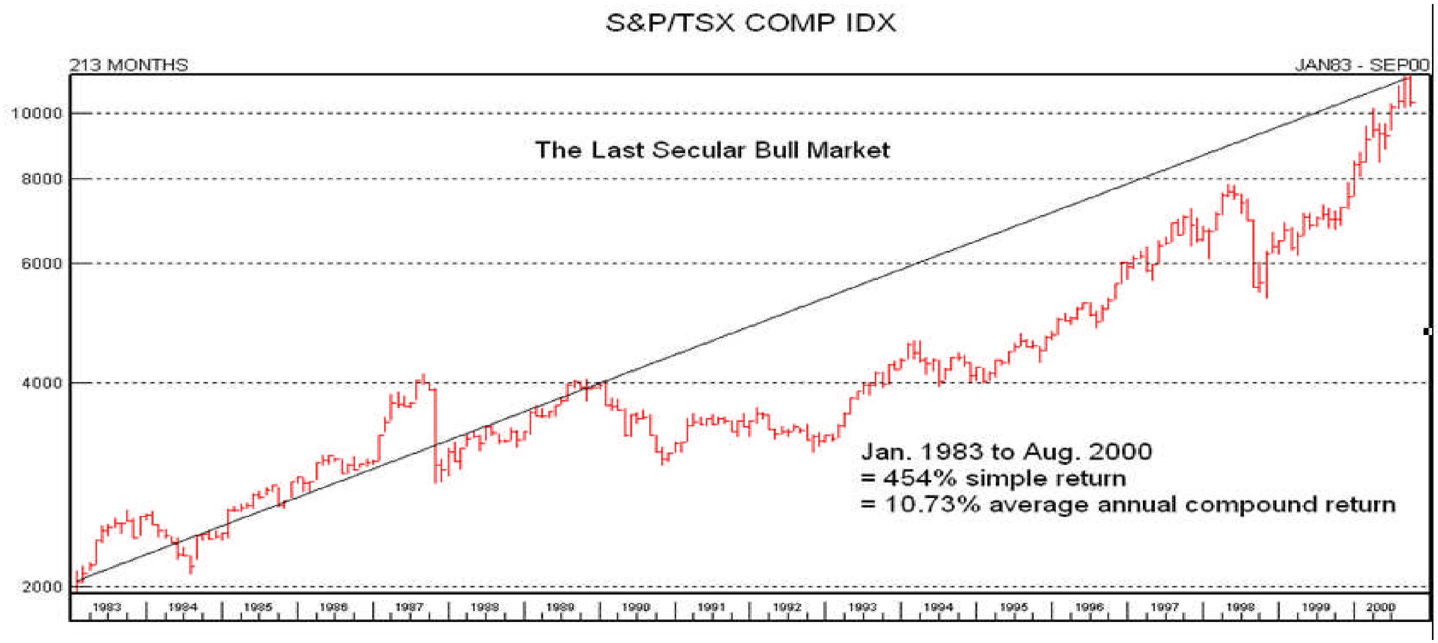
Source: RBC Dominion Securities & Reuters Thomson One

This also extends to gasoline prices which will provide some much needed relief for consumers. This will allow them to allocate these dollars elsewhere, which should be a positive for both consumer sentiment and retail sales.

Source: RBC Dominion Securities & Reuters Thomson One

Investment Strategies for Bear Markets

For those investors who were fortunate enough to be investing in the 1980's and 1990's consistent double digit returns were the norm.



Source: RBC Dominion Securities & Trend & Cycle

Characterized by low inflation, accommodative tax policy, falling interest rates, greater use of leverage, strong and relatively consistent economic growth, support from developed world demographics, productivity gains as a result of technological advances, a benign environment conducive to lower risk premiums and higher P/E multiples. It was the perfect wave for investors.

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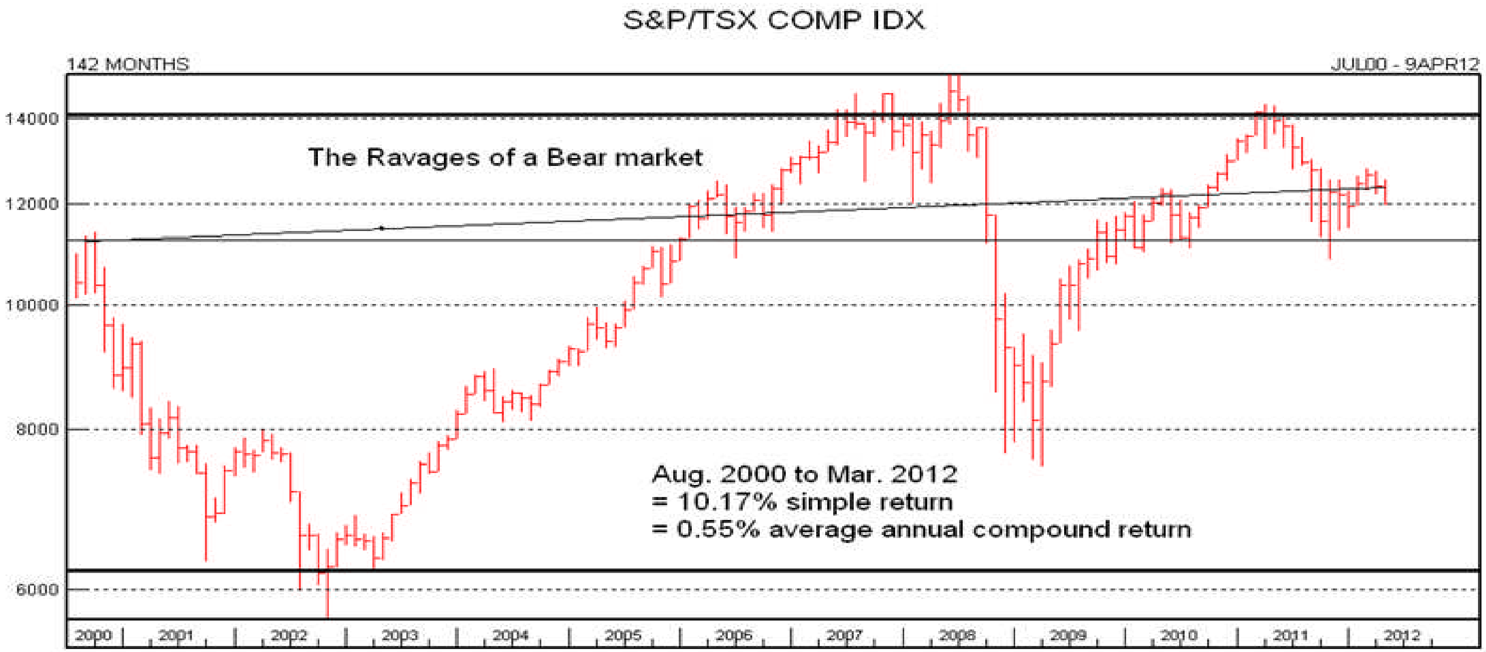
Memories of those years have faded following the poor equity market returns of the 2000's leaving investors disillusioned with equity and bond markets.



Source: RBC Dominion Securities & Trend & Cycle

A confluence of factors have combined to create one of the most challenging and volatile investment environments in recent memory. Housing, technology and commodity bubbles, credit crises, bank failures, European debt issues to name a few have all at various times fomented investor greed and fear over the past 12 years.

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We've been here before, on more than one occasion. The chart below illustrates the tendency for equity markets to go through alternating bull and bear phases that last many years. These are know as secular phases, lasting anywhere from 14-18 years.

Long-Term Market Cycles 1925-2012

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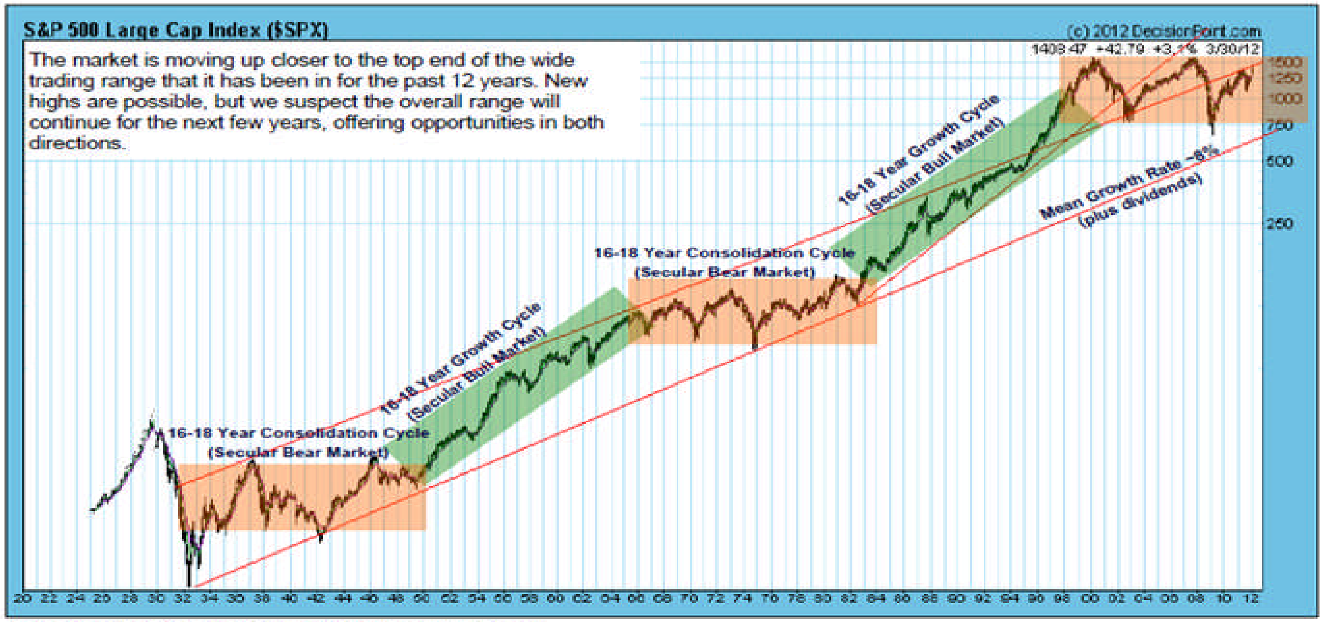
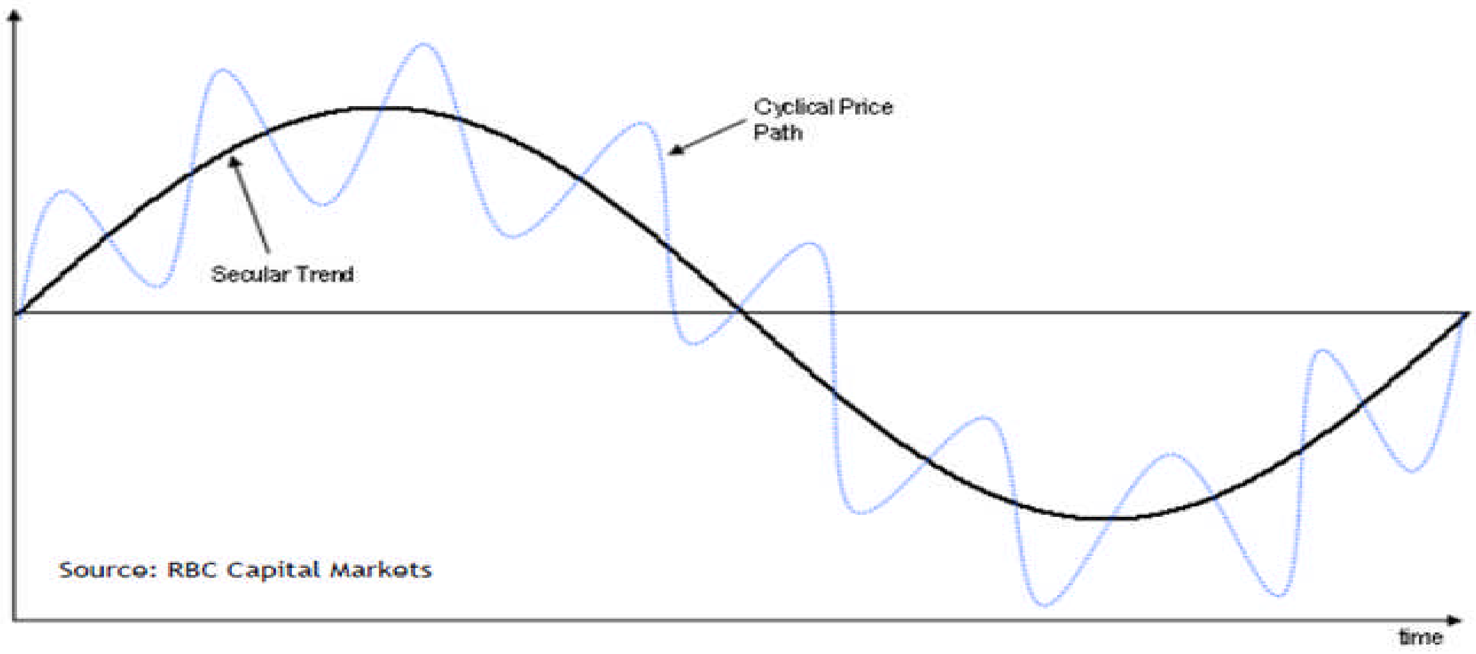


Chart courtesy of Decisionpoint.com and RBC Wealth Management

April 2012

Many investors continued to make money through these bear markets but the investment strategies that worked in the Bull market of the 80's and 90's will not work in today's market.

Secular Trends and Cyclical Paths: Bears within Bulls and Bulls within Bears



As temporary as they are, the cyclical rallies within a bear market serve to give investors the impression that a new bull market is underway. Investors are drawn back into the market only to have their hopes and expectations dashed when the market inevitably rolls over.

Investors need to embrace the bear

- **Attitudinal considerations**:
  - Know your required rate of return and adjust your portfolio to take no more risk than is required.
  - Trying to hit home runs in your portfolio sets you up for trouble
  - Expect the next pullback before it happens; panic is an emotion for the unprepared.
  - Bear markets, more so than bull markets, need to be treated like a marathon and not a sprint

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- **Behavioural considerations:**
  - Investment strategies that worked during the last bull market have proven to be largely ineffective. Buy and hold, basic index investing, and pure growth investing are not particularly well-suited to bear markets.
  - Undertake rebalancing between asset classes which forces one to sell high and buy low will make the volatility work for you and serve to reduce portfolio volatility and enhance returns
  - Get used to buying the dips, it doesn't feel good at the time but is the right thing to do.
  - Whereas formerly the focus was on capturing as much upside as possible, investors today need to be more concerned about protecting the downside of their portfolios. Less exposure to cyclical and economically sensitive sectors, more exposure to traditionally defensive sectors is needed.
  - Keep an eye on investment management expenses: in a world of 5% - 6% expected average annual equity returns, a difference of 0.5% in the costs of investment management is material.