RAYMOND JAMES® | CHRIS RAPER & ASSOCIATES

The Opportunity Update – Tuesday, September 11th, 2018

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Track #1: Introduction – The Skinny

Hi, this is Chris Raper, Senior Vice President & Portfolio Manager, Private Client Group of Raymond James Ltd. & co-founder of **The Dividend Value Discipline™**. Welcome to **The Opportunity Update**, which is being recorded for you in Victoria BC on Tuesday, September 11th, 2018. Here is what we are going to cover today.

You are now listening to **Track #1: The Introduction**, where I give you the skinny on what I am going to talk about.

On **Track #2: The Markets – Trump, A Mid-term Perspective**, we will start out with a discussion on the pending U.S. midterm elections and how that is impacting the current NAFTA negotiations, then dip our toe into Trump global (his geopolitical influences worldwide) and give you our perspective on how that is influencing the markets. Then we will follow our usual course – updating you on our favourite leading economic indicators: the price of copper, which is down like an elevator from our last recording, the wobbling semiconductor index and the oil complex, then close out with a brief commentary on the Canadian dollar.

On **Track #3: The Dividend Value Discipline™ – Innovation and Transformation**, I will report on the two new companies that we have added to the program since our last recording. First up will be 3M, the founder of Post-it® notes and about 60,000 other things. Then we will turn our attention to Accenture, a global consulting firm that helps the world's largest companies and governments transform and adapt to an increasingly complex and technologically dependant world. I will speak to the culture of both firms, how that has helped expand their competitive advantage, and why we believe that bodes extremely well for future rent cheque growth, which in our minds is the ultimate driver of stock prices.

On **Track #4: The Wrap Up – Why Your Investor Behaviour Matters**, I will wrap it up, giving you the key takeaways from each track and then speaking to a potentially challenging topic, and yet one that is apropos given our strong year-over-year results to the end of August and the hopefully soft markets coming our way through the upcoming midterm elections.

Track #5: Postscript I is where I walk you through our core investment program, **The Dividend Value Discipline™**, its methodology, return objectives, and all-in costs. This track is primarily for the benefit of potential clients who are being introduced to us by way of this recording. By the time you are done listening, you will know what makes the process unique vis-à-vis our competition and whether or not you are interested in pursuing it any further. Not interested, not interested right now, and let's talk further are all perfectly acceptable answers.

Track #6: Postscript II is again for the benefit of prospective clients. It will give you some insight on what to expect during our initial meeting, where we both want to answer the question: "Is there a fit between our services and your needs?"

In terms of legal requirements, there are three things to note:

1. The opinions that are expressed on this recording are mine. They may differ from those of Raymond James Ltd.

2. Raymond James Ltd. is a member of the Canadian Investor Protection Fund. That is a good thing. If you are interested in those details please ask me or any one of our relationship managers the next time we speak.

3. This recording/transcript provides links to other Internet sites for the convenience of users. Raymond James Ltd. is not responsible for the availability or content of these external sites, nor does Raymond James Ltd endorse, warrant or guarantee the products, services or information described or offered at these other Internet sites. Users cannot assume that the external sites will abide by the same Privacy Policy which Raymond James Ltd. adheres to.

I also want you to recognize that some of the things I am going to say today are going to be proven wrong. It is an inevitable part of this business. It is also important to recognize that you don't have to be right all the time to do well. You just have to be more right than most or, conversely, less wrong than most.

Finally, regarding investment jargon, when I say I am bullish, it means I expect things to go up. When I say I am bearish, it means I expect things to go down. Likewise, north means up and south means down. When I speak about rent cheques, I am speaking about income, primarily dividends. You will also hear me using the term disruptor, which is our moniker for those companies that are disrupting or re-inventing the way business is done in their particular market and are thereby able to grow at rates far faster than those of the economy. Think of Wal-Mart twenty years ago and Amazon today. You will also hear me use the term aggregator, which is our moniker for those companies that have a systemized approach to acquiring smaller competitors as a means to fuel their growth. That growth is the path to increasing dividends or in our language, growing rent cheques. If you catch me using industry jargon beyond that, I invite you to call me out. Send an email to the office and the team will let me know, usually with considerable gusto!

That’s a wrap on the skinny, and off we go to Track #2.

Track #2: The Markets – Trump, A Mid-term Perspective

Much of what I am going to share with you regarding the U.S. midterm elections came from my latest discussion with Stuart J. Sweet of Capitol Analysts Network. Regular listeners may recall that I featured Stuart's insights on the Trump agenda on the September 2017 edition of this recording. Suffice to say, he was a lot more right than wrong. If you are interested in Stuart's background, you can find out more at www.capitolanalysts.com – in a nutshell, his entire career has been devoted to the Hill in Washington D.C. and thus is in a great position to offer likely outcomes.

You may be aware that the U.S. House of Representatives and roughly one third of the Senate will face an election this November, and that is the true litmus test for the Trump agenda amongst the U.S. electorate. Today, both houses are controlled by the Republicans. According to Stuart, the chance of the Republicans retaining control of the House of Representatives is only about 40%, whereas they have about a 70% chance of keeping the Senate.

To state the obvious, Trump wants the Republicans controlling both and he wants to win a second term in 2020. If he has any chance of making that happen he has to:

1. Keep the economy humming because ~20% of the U.S. electorate have little to no ideological bent – they will swing from Democrat to Republican and back again based on how they feel about their personal circumstances. A good job and improving prospects means you vote for the incumbent. This year's massive corporate tax cut was designed to boost the economy, as is Trump's ongoing work on deregulation which simply acts like another tax cut. Look for further easing of U.S. banking regulations in the coming months in an effort to "lend baby lend", again boosting the economy and maintaining full employment.

2. Maintain his base and get the vote out among the former rust belt Democrats that put him in the Whitehouse, so look for the China trade wars to last longer because they are popular amongst the rust belt democrats. On the same objective but opposite tact, the NAFTA deal almost certainly gets done before the midterms because if he loses the House, getting NAFTA done will be a lot more complicated, and the current concessions from Mexico are seen as a win amongst his base.

Stuart also shared some interesting insights on the Trump global agenda. His sources in the Pentagon see North Korea as a far bigger threat than most people realize. "Rocket Boy" has a hydrogen bomb and missiles that can reach the U.S. Couple that with a regime that has a history of saying one thing and then doing the opposite, and the odds of a military conflict before Trump's term expires in 2020 get very real. Add to that phenomenon his pressure on the NATO allies to up their military spending and you can see that defence contractors will continue to do well. Finally, assuming that the Democrats take control of the House of Representatives this fall, we can expect a raucous session in 2019 as the impeachment proceedings will start shortly after the swearing in ceremony. This will only amp up Trump's global agenda as he tries to distract the public.

All in, the second half of this presidency is apt to be far rockier than the first, and that is quite a statement when it comes to Trump. My intention is to have some dry powder to take advantage of any market swoons and you can help me with that, a point I will speak to later.

Moving on to our favourite leading economic indicators, copper has taken it on the chin since our last recording, and that's important because copper goes into just about every manufactured good you can think of. So weaker prices point to weaker demand, and it suggests a slowing economy especially as it relates to the developing/manufacturing economies. On the June edition, copper was pegging in at $3.20 per pound. Today it is within spitting distance of a new 52 week low at ~$2.63 per pound, leaving us in the quandary – is it a tell of untoward things to come or merely a reaction of the China U.S. trade spat? Either way, it leans bearish.

Turning to our other favourite leading indicator, the raw material of developed economies, semiconductors, the Philadelphia Semiconductor Index (symbol $SOX) pegged in at 1423 on the June recording it was at 1327 today – I would rate that still strong, but wobbly.

Turning to our ancillary indicators, the world's Purchasing Managers Indices has moderated yet again for the month of August and that leans bearish, albeit only slightly.

Oil-wise, it is important to recognize that we are in a seasonal lull. Over the winter months we are biased to the upside on global prices, but given the slowing we are seeing in some of the economic data my conviction on that statement is not high. Even if we do get higher prices, it will not necessarily point to an upside in Canadian energy producers. The latest Trans-Mountain decision screams to the world that Canada is not a safe place to invest, and it follows that investors will take their money elsewhere, just as we have done via our oil exposed U.S. based ETFs. That is a net negative for the Canadian dollar, where the wild card for our loonie is NAFTA. If it gets done this month, I do expect our loonie to rally on the news, so if you are snowbird bound this winter that may be your chance to buy your U.S. dollars a little cheaper. Today a U.S. dollar on the wholesale market will cost you $1.3127, or if you are like me and you think about it in the other direction a Canadian dollar will cost you $0.7616.

So...I have thrown a lot at you, most of which is in the good to know category. How do I take all this information and weigh it when it comes to making investment decisions? Here is the most important point – even if everything that concerns me comes true, and that's unlikely, it will have very little impact on how fast the rent cheque grows at say Starbucks, Charles Schwab or any one of the other great companies that we own over the next five to ten years. Trying to guess the date of the next recession or a North Korean/U.S. conflict and make investment decisions around those issues is a mug's game. What we can do is be prepared to add money during such events, so please think about that in advance. In essence, help me help you. What you are going to do if you are presented with such an opportunity? Will you send money or ask for it back? Making up your mind ahead of time is a lot easier than in the heat of the moment.

With that we are off to track # 3.

Track #3: The Dividend Value Discipline™ – Innovation and Transformation

We have added two new companies to the program since the June recording so what follows is a synopsis of our research and thinking as we made those acquisitions. We continue to seek out those companies that evidence great corporate culture, and that are disrupting and/or aggregating their way to higher growth rates, in sales, earnings and yes dividends, or rent cheques as we like to call them. We see those metrics as the ultimate driver of higher stock prices and in the interim, we like the regular income as we wait for that eventuality.

Without further ado, we purchased **The 3M Company** ("MMM") back in early August, a company we have long admired. Most listeners will recognize the name from its household products like Scotch® tape and Post-it® notes. What you might not know is that if you go to 3M.com, you will find over 22,000 listed products and I am told there is another 40,000 speciality products that are not listed. The most exciting point to me is that almost one third of those products did not exist five years ago. That is a lot of research and development that very few companies can compete with.

When you study 3M you quickly realize that it is the culture of innovation that spawns so many products and enables them to register ~4,000 patents per year. Employees are actively encouraged to devote 15% of their time working on innovative ideas that excite them – collaboration is part of the corporate DNA. When we went through our "culture scorecard" we were able to tick pretty much all of the boxes. The current CEO is a 30 year veteran of the firm and most of the executives at 3M have tenures that are even longer. Promotion from within and talent development are easily identifiable, and the incentives are aligned with shareholders. ~90% of executive compensation is variable, and the CEO makes less than 2x the next highest employee, which is rare in this era. Meaningful insider stock ownership is also evident. In fact, 3M scored amongst the best we have seen in five years.

What we find especially attractive about this company is that it has all the hallmarks of a long term hold – hopefully decades, not just years. Our forward earnings yield at the time of purchase was just over 5% and we expect those earnings and the corresponding dividends to grow at double digit rates for the foreseeable future, which implies a doubling approximately every seven years. Of course we expect that performance to be reflected in the stock price over long periods of time, and we also expect to look quite foolish from time to time when investors turn bearish en masse. During those times, it helps to reflect on why you bought 3M – it just might give you the courage to buy more.

While 3M may be the big kahuna of innovation in the product space, our next acquisition, **Accenture** ("ACN") just might be big kahuna of innovating/adapting new business systems and I have to confess, that description falls well short of their capabilities. They provide consulting services to 95 of the Fortune Global 100 companies and over three quarters of the Fortune Global 500 companies. The current CEO, Pierre Nanterme, puts it this way: “Accenture works at the intersection of business and technology to help clients improve their performance and create sustainable value for their stakeholders.” Their moat is the intellectual know how they bring to the table with their 400,000+ employees. They are on the leading edge of helping companies, governments and institutions harness the power of things like artificial intelligence and block chain technology. Here is an example close to home – in May of this year, Payments Canada, the Bank of Canada, the TMX Group and ACN worked together to demonstrate an instantaneous settlement using distributed ledger technology, commonly known as block chain. That process takes two days today and is far less secure. In a nutshell, ACN is shaping the future to come. As such, we can easily identify disruptor status – it has over 6000 patents and patents pending across 44 countries. They also have a track record of accretive acquisitions which complement their existing businesses and thus are aggregators as well.

Culture-wise, the current CEO is a 35 year veteran and the median management tenure is an outstanding 34 years. The top dog’s compensation is reasonable at only 1.5x the next highest paid officer – again, something not normally seen in this day and age. Succession planning is readily evident with the top five executives being hired from within. Executive compensation is 81% variable and most is tied to long term total shareholder return. All in, we scored them at 79% which is at the high end of the range of our proprietary culture scale, although not as high as 3M.

Rent cheque-wise, the last increase was a 10% bump, and that was an acceleration over the previous two years. We expect the double digit increases to continue, implying a double every seven to eight years, and we fully expect the stock price to reflect that growth in the fullness of time…and I am sure that there will be times when investors “lose their marbles” and part with the stock in a panic downturn as well. I just hope we have additional cash at the ready to take advantage of such times.

We are off to track # 4.

Track #4: The Wrap Up – Why Your Investor Behaviour Matters

First, the takeaways:

Track #1: Introduction – The Skinny: A reminder that the opinions that are expressed on this recording are mine. They may differ from those of Raymond James Ltd. Please recognize some of what I told you is going to turn out to be wrong and when it becomes evident we are wrong, our intent is to acknowledge it quickly and adjust accordingly. The strategy is to keep the inevitable losses small and let the winners run.

Track #2: The Markets – Trump, A Mid-term Perspective: The biggest takeaways from the Trump agenda in my mind are as follows: NAFTA gets done before we get to the midterms, and deregulation continues regardless of the midterm outcomes. Trump has the authority to do so on his own and he wants the economy at full steam heading into the 2020 election, and believe it or not, the second half of this presidency is going to get even more raucous than the first. Add to that a longer trade war with China (which is undoubtedly contributing to weaker copper prices, a wobbly $SOX and perhaps a military conflict), and it is not hard to see how we may be in for a significant market correction…but it doesn't have to happen. If it does and you can take advantage of it by sending us cash, please do so. If the prospect of a 10% market correction has you fearful, it is time to call Erika, Larissa or Ryan for a review appointment. Let's get to it before such an event happens. I can't tell you when, but it will happen sooner or later.

Track #3: The Dividend Value Discipline™ – Innovation and Transformation: The takeaway here is that we continue to seek out and find great culture companies that are disrupting and aggregating their way to faster growth. The fact that one third of 3M's products did not exist five years ago speaks volumes to the strength of this industrial juggernaut. Moving from product to service, you can see Accenture is helping the world's most valuable companies adapt the technologies of tomorrow, be that artificial intelligence, block chain technology or mundane things like data veracity. Both firms have displayed great culture and have proven themselves to be tough competitors. We expect that to continue and that bodes well for our rent cheque growth and in the fullness of time, stock price appreciation.

Track #4: The Wrap Up – Why Your Investor Behaviour Matters

As we wrapped up August, most of the accounts within The Dividend Value Discipline™ balanced mandate pegged in at ~6% year-to-date, and the year-over-year return was closer to 10%. That got me thinking about investor behaviour and how it influences your personal returns. Thinking back to August of 2017 when I was getting client calls to "get me out", some of our clients were skittish because the

Trump/ North Korean rhetoric was amped up and markets had pulled back. We were say -3% on a year-to-date basis at the time. Thankfully, we were able to convince all of our clients to hold the course, but then I had the audacity to ask those who I spoke to to send us money. While some replied, "let me think about that" others just flat out told me, "Chris, that is not going to happen!" The sad part of this story is nobody sent us money and yet here we are a year later up almost 10% on a balanced portfolio. Fast forward to August 2018, performance is up and the money has been trickling in. If there was only one thing I could do as an advisor, it would be to reverse that behaviour. I get that it is not easy to do, but if this process of acquiring great companies that have demonstrated their ability to earn and grow their dividends at double digit rates makes sense to you, maybe it really is in your best interest to step up when the world is fearful. I will leave you to ponder that as we approach the midterm elections and I am sure the volatile outcomes thereof.

With that, I will close. A reminder, if you are being introduced to us by way of this recording then tracks #5 & #6 are for you. If the approach make sense to you, may I suggest a telephone or face to face meeting is in order.

Thank you for taking the time to listen. On behalf of the entire team here at Chris Raper & Associates, please accept our best wishes for a great autumn season. This is Chris Raper bidding you good day and may God bless from Victoria BC on Tuesday, September 11th, 2018.

Track #5: Postscript I – The Dividend Value Discipline™ Methodology

The first thing to note is that **The Dividend Value Discipline™** is core to everything we do – meaning if we were approached by a prospective client and we determined that our core investment process did not fit with their investment philosophy or their need, then we are not the right advisors for that particular client – there is no fit.

While it is not our only offering, the lion's share of our client assets are allocated to the program and that includes our most senior people, my family, and me. The takeaway is that my team and I have huge vested interest in ensuring the success of **The Dividend Value Discipline™**.

The process is discretionary, meaning we make the entire buy and sell decisions and report to you after the fact. Post a new purchase, our normal course is to send an email outlining the background of the company and the rationale for the decision, five business days after it settles to your account. When we close out a position, we also send an email outlining the result and our rationale.

Our objectives for the program are:

- Income every month – that can be paid out or reinvested;
- An acquisition process where we buy only those securities which become attractive on a "go forward" basis;
- Absolute returns of 8%+ over any investment cycle, which we would describe as peak to peak or trough to trough. If you are looking for a time frame in terms of years think 5+ years, but please understand investment cycles have a wide range of timeframes.

Long term performance-wise, we started **The Dividend Value Discipline™** in the fall of 2002, and the average annualized return for all of the accounts that were opened that year (that are still in operation) is +7.46%, net of fees, as at the end of 2017. Throughout the course of our 15 calendar year history, we have had 14 years of positive returns and 9 years where we met or exceeded the +8% objective. The original accounts opened in 2002 have net to client compound annual growth rates ranging from a low of 6.8% to a high of 8.9%. Why the big discrepancy? Part of the differential is due to the timing of money in and money out, but when you really drill down, the high number is a result of intelligent investor behaviour. The client with the absolute best performance sends us money when others are ready to fire us. There is a valuable lesson therein – for your sake, please don't overlook it.

Those results have been achieved by focusing on three keys objectives, so let's walk through this with the illustration of a three legged stool.

The First Leg is Dividends

Every security that we buy must provide some form of income. We do that because income makes portfolios inherently less volatile, i.e. less chance of loss. The analogy I like to use is that of an apartment block versus a piece of raw land – it is a lot easier to hold onto the apartment block in a tough real estate environment when you are getting a rent cheque every month. Income drives stability and absolute returns.

The Second Leg is Value

Our research function is in-house. We were one of the first private client teams in the industry to have a dedicated analyst on staff and we add additional resources every year. Our objective was (and still is) to get to the truth. We do not want to depend on any outside analysts that we have little or no contact with. One of the great things about having an in-house investment team is that I can ask questions until I am satisfied that we have the right answers. We spend an inordinate amount of time studying the corporate culture. If you are interested in what that looks like, read ***Good to Great*** by Jim Collins – that is the yardstick we use to measure potential investments against. Another yardstick is the importance of wide economic moats. You can hear more on that subject by archiving the September 2013 edition of this recording on our website. We believe that the focus on great corporate culture and wide economic moats gives us an edge. Anecdotally, we can provide you with lots of evidence to support that. I remain convinced that having your own people who are totally dedicated to the investment process adds a lot of value not available at most other private client focused groups.

The more recent development in our strategy has been tackling the growth problem. History buffs will note that when we started the program in 2002, we had 5-year GICs yielding 5%, much better economic growth, and stocks benefiting from decreasing interest rates, whereas today we have 5-year GICs yielding only 3%, subpar economic growth, and the headwinds of rising interest rates. In short, the 8% is tougher to come by.

Accordingly, we spent late 2015 and 2016 tackling the "growth problem". We need to find companies that are growing far faster than the economy. As you would expect, we start within the normal confines of "has to pay a rent cheque, score well on the corporate culture front, and have some sort of strategic advantage (the moat) that makes the company difficult to compete with". We then focus on those companies that have demonstrated their ability to grow their dividends at double-digit rates as a primary indicator of growth and capital gain potential. As we searched, we found that most such companies fell into one of two themes. They tend to be disrupting the existing marketplace with a better way of doing things, or they tend to be aggregating their way to growth by buying smaller tuck-in acquisitions. More detail on our "disruptors and aggregators" themes can be found on the May 2016 edition of The Strategist which is archived on our website. I am happy to report we are currently bearing the fruit of those efforts.

The Third Leg is Discipline

Here I refer to the buy/sell decisions. We often identify extremely attractive value propositions and then delay the buying decision, why? Because if you are the only guy in the world that sees it as undervalued, you can wait a very long time for the market to recognize that value – in other words, the stock price doesn't rise or worse, it goes down! Those are not comfortable situations so we try to avoid them. We buy when it is apparent that the market is starting to recognize the stock as undervalued. One of the most helpful indicators is positive relative strength – i.e. is the security in question starting to outperform its peer group and the market? Because if it isn't, there is little incentive in owning it. Sell decisions can be triggered by a number of things – when the company fails to materialize as expected, when a company's stock price exceeds what we believe it to be worth, negative relative strength, or when we find a better opportunity elsewhere. In reality it tends to be a combination of those factors.

Perhaps the most important part of the buy/sell discipline is the way we operate the program – we call it "The Buys Only Mandate". Unlike our competition, we only buy those securities which become attractively priced on a go-forward basis, meaning if you start today and your brother starts three months from now, your portfolios are going to be different in the short-term, and more closely aligned the longer you are in the program together. As rational as that might seem, most people do the exact opposite. Every time you buy a mutual fund, you buy a pro-rata share of an existing portfolio – by definition, you got the buys, the holds and the near sells. To us, that is not rational. Would Warren Buffett buy 100 companies in a single day? Were they all great value propositions? You should also be aware that most third party money management programs work exactly the same way – they buy the basket. Our objective is the protection of your hard earned money and we believe that the buys only mandate is consistent with that objective.

Other key points to the program: a fully invested account would normally have 20 to 25 positions in it, so we are relatively concentrated. Our fees are 1.75% per annum plus the GST or HST – it is tax deductible for non-registered accounts. Our target return is 8%+, net to you.

You should also know that when I buy for you, I buy for me. When I sell for you, I sell for me – same time, same price – and that statement also applies to our most senior people as well. Furthermore, every person on our team participates in our profit sharing plan, which means they have a vested interest in looking after you.

Generally speaking, we are looking to establish new relationships with new clients that have north of $1 million in investable assets. That said, I'm a lot more interested in where you are going than where you are. If you have a credible plan to get to that number say within a three to five year period, we are very interested in meeting with you.

To conclude this track, if income and absolute returns are attractive to you, and you think that there may be a fit between your objectives and those of **The Dividend Value Discipline™,** then I would suggest a face to face meeting is in order. You can check out what to expect during that initial meeting by moving to Track #6 – "Is There a Fit", and that is where we are going right now.

Track #6: Postscript II – "Is There a Fit?"

Our objective – and presumably yours – during the first meeting is to figure out whether or not we have a basis for an ongoing relationship. In essence, can we work together? If so, will it be mutually beneficial? Job one is to get your tough questions off the table, so we encourage people to ask whatever is on their mind. Our responsibility is to be forthright with our answers, regardless of what it is that you might want to hear.

Before we enter into any new relationship, one of the biggies we ask ourselves is, "can we add significant value?" To answer that question we need to learn some things about you, your family, your finances and what your ideal future looks like. If you are not really sure on the latter point, we have some thinking exercises that will take us through that process.

Next we will walk you through an a la carte menu of our services that are most applicable to you. We'll outline how we will report to you and who the key relationship people will be. You will also have a very clear picture of the costs involved.

Before you leave we'll outline how we see our program fitting with your situation, or not. We will not ask you for a go/no go decision at the meeting and quite frankly, we don't want to be pressed for a decision that day either. We'll schedule a meeting of the minds call, say a week out, and then mutually agree on the best course of action from there.

At the end of the day, we are in the business of keeping our clients' most challenging financial decisions consistent with their life goals. Our mission is ongoing progress towards those goals, and the result we seek is appreciative clients who are increasingly confident about their future.

So...if that process sounds engaging, I invite you to call and book some time. If you'd like further information, including access to our quarterly communication pieces, you can check us out on the web at chrisraper.com and send us an email from there.

This concludes "Is There a Fit".