Market Update

PRIVATE CLIENT SOLUTIONS

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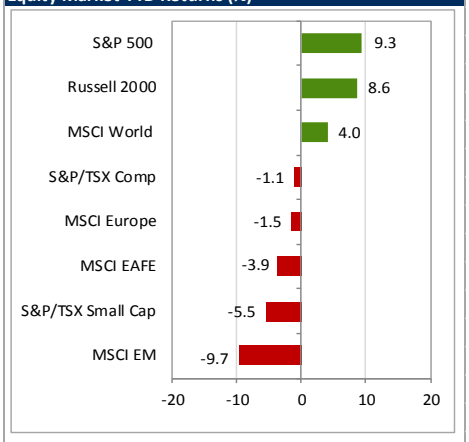
USMCA

The new US-Mexico-Canada Agreement (USMCA), while having minor economic impacts, does remove a significant overhang on the Canadian market. The diminished risk should allow risk sentiment to improve in the coming weeks, although it may take some time for foreign investors to regain confidence in the Canadian marketplace. The finalized deal that Congress still must sign off on could serve as one of the catalysts to allow Canadian equities to outperform over the next 6 months. Another significant development this week is Royal Dutch Shell's announcement that it will proceed with the $40 bln Kitimat LNG project. In the future, we have the NEB's Trans Mountain expansion review, which will conclude in Q1/19. We view the positive news on the trade and pipeline front as positive catalysts to free up any investment projects that had been delayed due to the investment uncertainty, providing a tailwind for Canadian equities.

With trade at the forefront, this week we identify the most significant alterations to NAFTA and potential winners/losers; although, we have to admit not a lot has changed other than the name of the agreement.

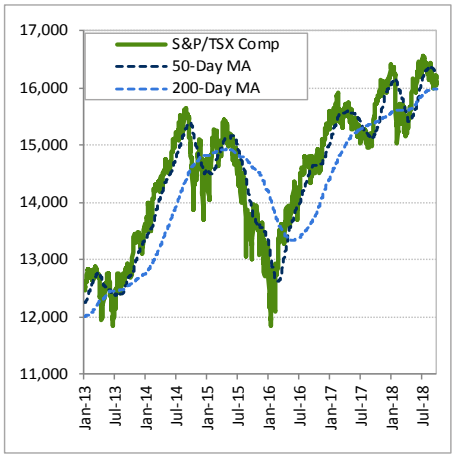
Issue	Comment	Winners	Losers
Dispute Settlement	The New trade deal does not make major changes to current Chapter 19 trade dispute settlement mechanism, which gives the three countries the right to challenge each other's anti-dumping and countervailing duties in front of an expert panel with members from both countries involved in a dispute.	The US was looking to water down this mechanism so we could say Canada and Mexico are the winners and the US a loser.	
Autos	The agreement imposes a vehicle export quota of 2.6 million vehicles that could be exported to the US tariff free or near tariff free. Above this threshold tariffs may apply; however, 2.6 million units annually is ~40% above current levels. ▪ 75% of content must originate in the US and Mexico (up from the current 62.5%) ▪ 40% of a car to come from workers whose pay averages more than US$16 per hour.	Auto/auto parts. The agreement removes the threat of tariffs, allowing equity market valuations to recoup their losses.	Consumers will end up paying more for the end product as increased costs (associated labour, domestically, sourced materials) are passed on to the consumer.

Equity Market YTD Returns (%)



Canadian Sectors	Weight	Recommendation
Consumer Discretionary	4.4	Market weight
Consumer Staples	3.4	Underweight
Energy	19.3	Overweight
Financials	34.0	Market weight
Health Care	2.0	Market weight
Industrials	10.6	Overweight
Technology	4.0	Market weight
Materials	10.3	Overweight
Communications	5.2	Market weight
Utilities	3.7	Underweight
Real Estate	3.0	Market weight

Technical Considerations	Level	Target
S&P/TSX Composite	16,038	17,650



Source: Bloomberg, Raymond James Ltd.
Sectors are based on Bloomberg classifications

Please read domestic and foreign disclosure/risk information beginning on page 4

Dairy	Canada has granted US farmers access to around 3.5% of our dairy market.	Canadian consumers may benefit from increased competition and lower prices.	Canadian Dairy industry. As the dairy industry is small accounting for just 1% of Canadian GDP the increased access will have limited impact to the overall Canadian economy. Further, the Federal government has already pledged its support for the dairy farmers which will limit any negative impact felt by the industry.
Online Shopping	Canadians buying US goods online will be able to buy more duty-free: ▪ Items under $150 will not be subject to customs duties (up from the current $20) ▪ Items under $40 will be exempt from sales taxes.	Marginal positive for Canadian consumers. The US had pushed for $800 limit, which would have been meaningful, but at $150 it's unlikely to result in any significant savings.	Canadian consumer's online purchases tend to be concentrated on clothing, travel and household products. Canadian clothing and household product retailers may be negatively impacted; although given the limit level the impact will not be meaningful.
Pharma	Canada will lengthen patent protections term on pharmaceuticals to 10 years.	US & Canadian Pharmaceuticals	Consumer. Canada has resisted increasing pharma protections in order to keep drug prices low and help its own generic drug industry. Extending patents will limit generic competition and increase prices.

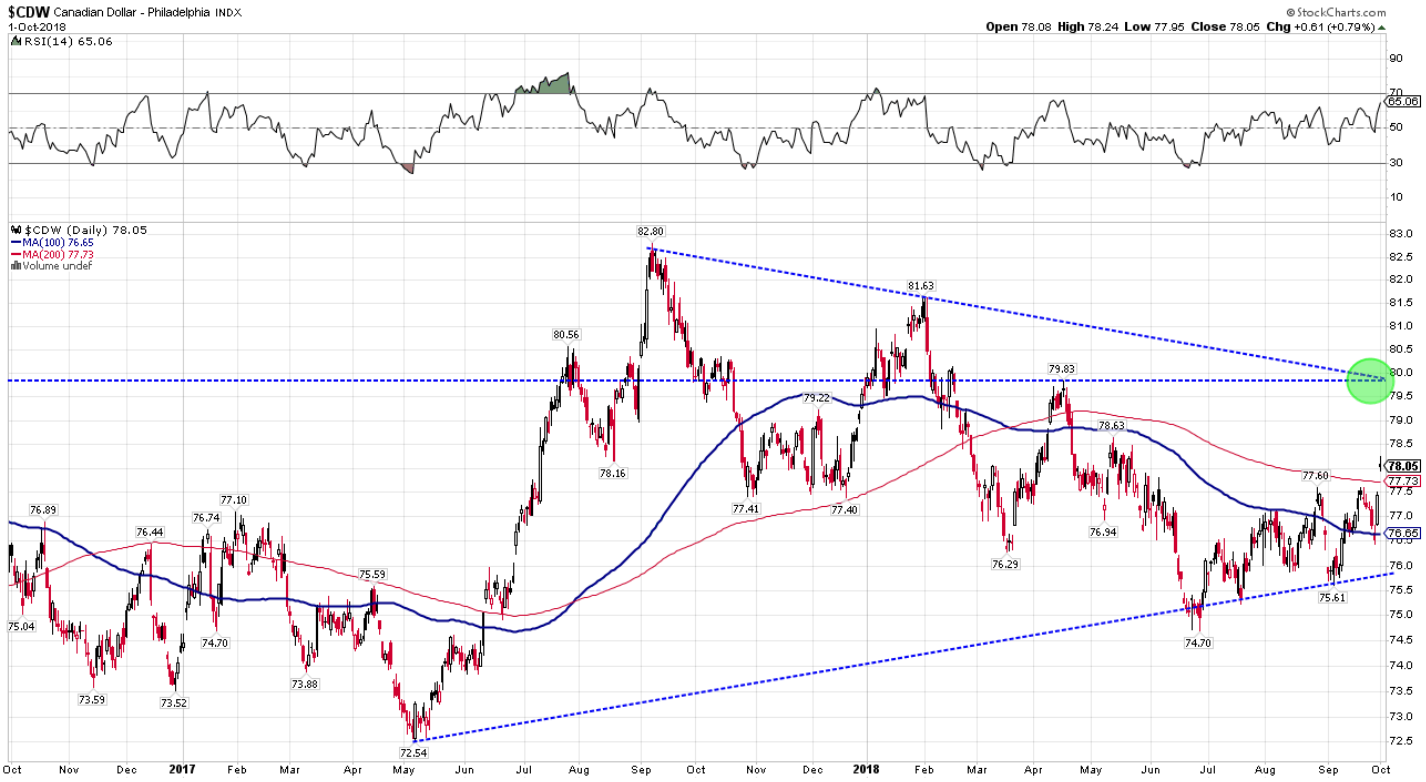
Investment Implications

From an investment perspective, USMCA will have varying degrees of impact on Autos, Dairy and Pharmaceuticals companies. However, the most obvious impact will be on the Canadian dollar. The Loonie has been under pressure for the past year and a half, the ongoing uncertainty surrounding trade removes this overhang and is a clear positive for the currency. Additionally, the Bank of Canada will no longer need

to guard against the potential fallout from NAFTA being terminated. As such, the BoC may become more aggressive in raising short term interest rates. The market is currently pricing in a hike in October and the probability of a January hike increased from 45% to 60% this week. This should further support Loonie strength.

Our initial call earlier this year for CADUSD for H2/2018 was for the pair to eventually retrace back into the familiar $0.76-0.80 range. Following the USMCA announcement the pair has clearly moved into our target range and we anticipate $0.80 to be the next level of resistance for the currency pair.

Loonie Set to Test Prior Resistance



Source: Stockcharts.com, Raymond James Ltd.

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