BCV Asset Management Inc.

The Blue Chip Report
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What if a Recession Comes?

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First let me preface, on behalf of the entire Investment Team at BCV, that we do not know when an economic contraction will arrive. We do know that sooner or later a growing economy does slow down and from time to time, it declines or contracts.

Ever since the Great Depression of the 1930s, policy makers such as Federal Governments and central banks have tried to disrupt the natural economic cycle. Federal Governments have used deficit spending as a tool to shorten the duration and severity of an economic downturn. Central banks have used interest rate policy and adjustments to the supply of money to achieve a similar objective. This combination of expansionary monetary policy and loose fiscal policy has reduced the number of expected economic recessions and the magnitude of their decline over the past four decades. Having said that, business cycles still exist, and recessions will very likely remain a part of our economic landscape.

Investors still have a clear memory of the great recession of 2008 & 2009. It was the worst economic and financial crisis since the 1930s. With some assistance from the media, we let our fears lead us to the conclusion that a forthcoming economic recession will be just as severe as the last one. Economic and financial conditions today do not resemble the conditions of 2008. Banks do not have the ability to take on the same level of financial risk or use the same amount of leverage and the United States housing market is much more balanced. There is no sign of inflation.

The most important aspect of a recessionary event is the direct impact it has on securities such as stocks and bonds. The stock market is not the economy, but they are connected. Stocks usually decline about six months before a recession begins and generally start to recover at the worst point of the economic downturn. We are not concerned that stock prices may decline in a recession, since stock prices fluctuate every day. Our main interest is on the long-term permanent impact that a recession may have on a portfolio of securities. History has left us with some important clues on this matter. The last two severe economic downturns occurred in the late 1990s (Tech Bubble) and in 2008 - 2009 (Financial Crisis). Here are what investors need to consider:

- **Stay Invested.** All equity securities will drop in an economic recession. The Royal Bank of Canada dropped by 50% in late 2008 and into early 2009. The difference is that high quality, profitable businesses recover faster and fully, so remain in your positions.

- **Stick with Quality.** The risky ones sometimes never recover. Lehman Brothers Holdings Inc. went bankrupt in 2009. Great companies will recover their value. The Royal Bank of Canada increased over 100% from its low point in March 2009. The stock closed at $27.07 on February 15th, 2009. In late September 2019 it traded at $107.96, an all-time high. Apple Inc. is another example of a high-quality company that recovered quickly after its decline.

- **Own Dividend Paying Stocks.** High quality stocks keep paying and increasing their dividends. Since BCV's inception, we have witnessed only one dividend cut in all the stocks that we have owned for client portfolios. Many of them kept increasing their dividend, even during the great recession.

- **Do: Buy Buy Buy.** Economic contractions create opportunities to buy great stocks at low prices, compared to their true long-term value. Once a recession ends, these stock prices will seem cheap. In the last recession, Canadian National Railway was trading at $20 per share, now in late September 2019 it is $120 per share. Shareholders need to think in terms of being a business owner forever and take advantage of the opportunity to own high quality-operating businesses at discount prices. A company's long-term value is usually different (and sometimes much higher) than its current stock price.

- **Don't: Sell Sell Sell.** We never support selling stocks just because one believes that a recession is near. If investors require capital or periodic income for consumption purposes, the capital should be raised well in advance of its need and when the capital markets and the economy are strong.

- **Reduce Taxes.** Selling stocks because a recession is near will also create unnecessary capital gains taxes. The payment to the Canada Revenue Agency permanently reduces capital that can never be used again for future compound growth.

- **Avoid Market Timing.** Selling a security in anticipation of a recession also requires one to have accuracy and precision on when to exit and re-enter capital markets. Knowing when to sell is difficult and knowing when to re-purchase is even more difficult, since it requires a purchase decision when the economic and financial headlines are still negative. Capital markets bottom well before economic data turns positive.

- **Have Emotional Strength.** Investing at its core is driven by two primal emotions: Fear & Greed. Rising stock prices make us feel great and falling stock prices bring on unnecessary anxiety. Economic recessions are part of capital markets and the investing process. Keeping one's emotions in balance, both high and low can be difficult. Those that can maintain balance with their emotions will be rewarded more than those that cannot.

Whatever the future holds for Capital Markets, clients should be comforted in knowing that they have a team of professional investment staff at BCV that care about each and every client investment portfolio. We have a fiduciary duty to act in the best interest of our clients, and we strive to make the best investment decisions for our clients. As a result, our process will not change, whether an economic recession occurs or not. Thank you for your continued trust and support in BCV.

Compounding: The Snowball Effect

Michelle Smith, CFA

Portfolio Manager

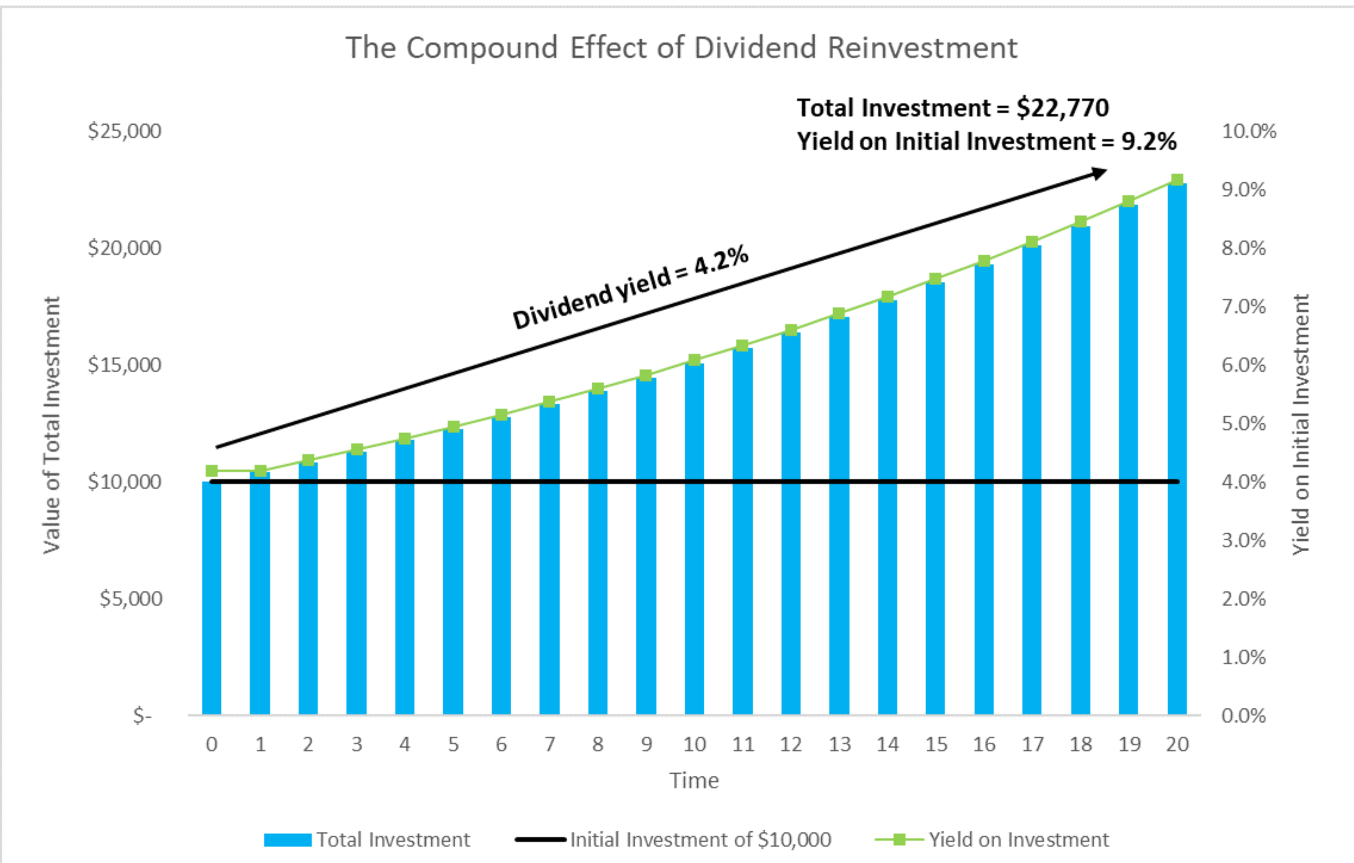
BCV Asset Management offices are located in Winnipeg, Manitoba. In Winnipeg, we are known for our NHL hockey team; the Winnipeg Jets, pesky mosquitoes, and most of all, our grueling Winters. Each year, our short Summer fades into an even shorter Fall and before we know it, Winter is here. We don't just welcome Winter, we put on our parkas, mittens, and boots, and embrace it. Winnipeg Winter is filled with experiences like the Festival du Voyageur, a skate down the frozen river trail (one of the world's longest), and the snow turns our city into a Winter wonderland! The cold doesn't slow us down and the snow makes for a more enjoyable season with skiing, tobogganing, and snowballs for kids of all ages. However, snowballs are not limited to Winnipeg Winters. In fact, every BCV client is building their own snowball year-round; a portfolio comprised of dividend paying and dividend growing companies.

As a reminder, a dividend is a share of profit that management pays out to shareholders as a reward for their patience and trust by investing in the company. Generally, dividends are paid on a quarterly basis and increased annually. In order to sustain and grow the dividend, management must have confidence in the company's earnings power and growth prospects. Thus, dividends are often considered a signal of the company's future financial prosperity. All the companies that make up our client investment portfolios pay a dividend, and the majority also increase that dividend over time. This investment strategy helps investors build wealth efficiently and effectively over the long-term. Here's how it's done:

As dividends get paid into client accounts, they will accumulate until the cash balance reaches an investable level. Once this investable level is attained, cash will be reinvested in the market, buying more of those companies that pay and grow their dividend. Thus, the next time a company pays a dividend, the shareholder will be entitled to a greater amount of investment income based on (1) a greater number of shares in the company, and (2) an expected higher dividend. This is the snowball effect of dividend investing – or in financial terms, the compound effect. Compounding has a similar effect to a snowball rolling down a hill. The growth of the snowball starts off slow, gradually building on itself until it becomes enormous. The same effect is true for dividend investing. Over time, the impact of compounding can be astounding.

To better illustrate, consider an example. Assume you shape your snowball by investing $10,000 in shares of Manulife Insurance Company, a life insurance company paying investors an annual dividend of $1.00/ share or yielding 4.2% (dividend yield = dividend/share price). For simplicity sake, let's assume the share price and the dividend value are constant. At the end of the first year, you will have earned $420 ($10,000 x 4.2%) in dividend income, which you use to purchase more shares of Manulife for a total investment of $10,420. Over the next year, you remain disciplined by leaving your total investment untouched. At the end of year two, your investment will be worth $10,858 ($10,420 x 1.042). Effectively your investment earned growth on its previous growth – your snowball is starting it roll!

As time goes by, your snowball will pick up speed and size, as will your investment. Again, consider the same example as above over a 20-year time horizon. By the end of the first 10 years, you will have earned $15,090 ($10,000 x [1.042^10]). After 20 years, the investment will have grown to an astonishing $22,770 ($10,000 x [1.042^20]). Your patience will have literally paid off. Furthermore, this growth will be accelerated should both the share price and the dividend value increase over the same time horizon (which often happens in capital markets). Your snowball has grown into a snow-boulder!



The phenomenon of compounding is simple, but it is not easy. It requires time, patience, and discipline to truly make a material impact on the value of your investments. Like surviving a Winnipeg Winter, exercising all three will lead to a brighter (and warmer) future.

Recent Dividend Increases

Canada

First Quarter 2019:
Bank of Montreal: 100 cents (96 cents)
Brookfield Asset Management Inc.: 16 cents (15 cents)*
Brookfield Property Partners LP: 33 cents (31.5 cents)*
Canadian National Railway Company: 53.75 cents (45.5 cents)
Canadian Western Bank: 27 cents (26 cents)
Enbridge Inc.: 73.8 cents (67.1 cents)
Intact Financial Corporation: 76 cents (70 cents)
National Bank of Canada: 65 cents (62 cents)
Suncor Energy Inc.: 42 cents (36 cents)

Second Quarter 2019:
Bank of Nova Scotia: 87 cents (85 cents)
Canadian Imperial Bank of Commerce: 140 cents (136 cents)
Canadian Natural Resources Ltd.: 37.5 cents (33.5 cents)
Open Text Corporation: 17.46 cents (15.18 cents)*
Power Financial Corporation: 45.55 cents (43.3 cents)
Royal Bank of Canada: 102 cents (98 cents)
Sun Life Financial Inc.: 52.5 cents (50 cents)
Stantec Inc.: 14.5 cents (13.75 cents)
Toronto-Dominion Bank: 74 cents (67 cents)
TransCanada Corporation: 75 cents (69 cents)

Third Quarter 2019:
Algonquin Power & Utilities Corporation: 14.10 cents (12.82 cents)*
Bank of Montreal: 103 cents (100 cents)
Canadian Western Bank: 28 cents (27 cents)
National Bank of Canada: 68 cents (65 cents)

Fourth Quarter 2019 (Pending):
Canadian Imperial Bank of Commerce: 144 cents (140 cents)

United States

First Quarter 2019:
Analog Devices Inc.: 54 cents (48 cents)
AT&T Inc.: 51 cents (50 cents)
Home Depot Inc.: 136 cents (103 cents)
Wells Fargo & Company: 45 cents (43 cents)

Second Quarter 2019:
Apple Inc.: 77 cents (73 cents)
International Business Machines Corporation: 162 cents (157 cents)
Johnson & Johnson: 95 cents (90 cents)
UnitedHealth Group Inc.: 108 cents (90 cents)

Third Quarter 2019:
Bank of America Corporation: 15 cents (12 cents)
U.S. Bancorp: 37 cents (30 cents)
Wells Fargo & Company: 43 cents (39 cents)

Fourth Quarter 2019 (Pending):
U.S. Bancorp: 42 cents (37 cents)

Dividend Increases reported in domestic currency of common shares, except where noted.

* Dividend paid in USD.
Source: Bloomberg LP