

# INVESTORS' JOURNAL

December 2017

CAPSTONE  
ASSET MANAGEMENT™

## BACK TO BASICS

With the New Year comes a time of reflecting on the past and setting goals for the year ahead. We often go so far as to write down our goals (or voice them on social media) alongside a plan for how we will achieve them. While goals may include changes we hope to make in our health, relationships or finances, we believe that a good underlying theme, one which we intend to embrace this year, is that of becoming a better steward.

At the heart of it, stewardship recognizes God's sovereignty as the Creator of the Universe and all that is in it, right down to the fine details of our finances.

*Psalm 24:1 "The earth is the Lord's, and everything in it, the world, and all who live in it;"*

This may come as a shock for some and a relief for others. We hope it is the latter. For many, the realization that we are not ultimately in control brings great freedom.

Being an effective steward is not about how much or how little we have but about how we take care of what has been entrusted to us.

With this approach, we can serve the Lord with a grateful heart and lay up for ourselves treasures in heaven so that God will one day say, "Well done good and faithful servant."

*Matthew 6:19-21 "Do not store up for yourselves treasures on earth, where moths and vermin destroy, and where thieves break in and steal. But store up for*

*yourself treasures in heaven, where moths and vermin do not destroy, and where thieves do not break in and steal. For where your treasure is, there your heart will be also."*

May you be blessed and be a blessing to others in 2018 and beyond.



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A new year means new opportunities to contribute to your registered accounts. If you would like to contribute to your TFSA, RRSP or RESP, please email us at [info@capstoneassets.ca](mailto:info@capstoneassets.ca).

## ARE WE INVESTING IN A REAL ESTATE BUBBLE?

When clients learn of the Canadian Real Estate Holdings within our Capstone Non-Traditional Equity Pool some express their reservations. While they may have seen success in their own homes appreciating over the years, there is concern as to whether we are entering a 'bubble'.

For this reason, we'd like to highlight two Canadian Real Estate Ventures within the Pool which we view as having tremendous potential to contribute significant performance.

<i>Project Location:</i>	Markham, ON
<i>Type of Residential Housing:</i>	Luxury high-end townhome complex
<i>Estimated Completion Date:</i>	End 2018-Early 2019
<i>Current Status:</i>	100% Sold
<i>Target Rate of Return:</i>	19% Preferred Dividend Rate

This project is led by a developer with a long-standing track record for excellence. This specific project caters to clientele wishing to live in the Markham area and features large, luxury townhomes of approximately 3000 square feet.

<i>Project Location:</i>	Saskatoon, SK
<i>Type of Residential Housing:</i>	Entry-level townhomes
<i>Estimated Completion Date:</i>	End 2019-Early 2020
<i>Current Status:</i>	Sales still in progress, currently about 20% sold
<i>Target Rate of Return:</i>	10-15%

This is a real estate sales opportunity with additional opportunities in the rental market. To further enhance performance, a portion of the townhomes are being moved into a rental structure to take advantage of low vacancy rates in the area as well as progress the project.



Beyond a certain stage, we receive capital back and the rental projects become self-sufficient. These entry-level townhomes play very well into this particular area and are in high demand.

Certain segments of the Canadian Real Estate market are indeed frothy and expensive to enter. However, in both the instances above, we have taken advantage of opportunities arising from changing market conditions while maintaining flexibility by working directly with developers each of whom have decades of experience and previous successes.

Capstone Non-Traditional Equity Pool is a Limited Partner in both of these developments.



If it has been more than a year since your last meeting with our office, or if your circumstances have materially changed, please be in touch with your Portfolio Manager directly.

## ADDRESSING THE HYPE: CRYPTOCURRENCIES

Blockchain technology has existed for a while now but it is only recently that a lot of cryptocurrencies, especially Bitcoin, have somewhat dramatically taken center stage. And so, while we don't necessarily buy into the hype, we'd like to take some time to illuminate our opinion on an interesting subject which has become a hot topic in the media and among some of our clients.

### *Firstly, how do cryptocurrencies work?*

A cryptocurrency is a decentralized digital currency designed to work as a medium of exchange (not unlike how precious metals were used in Biblical times). It uses cryptography otherwise known as encryption to secure its transactions, control the creation of additional units and verify the transfer of assets. It has become especially popular due to its relative anonymity in that it is difficult to trace transactions. Its decentralized nature also means that governments will have great difficulty regulating or restricting transactions as these are recorded on a dispersed network rather than one centralized server, another advantage many say. From a user's standpoint, owners of cryptocurrencies keep their digital coins in an encrypted virtual wallet. The first cryptocurrency to make headlines was Bitcoin but over a thousand different cryptocurrencies have since emerged including Ethereum, Ripple and Litecoin.

### *How are cryptocurrencies valued?*

In terms of valuation, things are tricky from the outset. Historically, a precious metal's intrinsic value lay in its physical value; (after all, gold was useful for its malleability, use in jewelry and other adornments). While it can be argued that cryptocurrencies utilize new technologies alongside their other characteristics, outside of their use as a medium of exchange, they have no utility. Hopefully it is easy to see how difficult it is to value cryptocurrencies with no apparent intrinsic value. Add in the increasing variety of cryptocurrencies and valuations become all the more complex and speculative.

Lastly, investing in cryptocurrencies is considered a zero-sum game, meaning that one investor's gain is another person's loss; no wealth is created. Said another way, the only way to make a profit is if you can sell to someone willing to pay more than the price for which you bought it; this is otherwise known as the greater fool theory.

### *What's the bottom line?*

We are not averse to new alternative forms of payment (yes, this old dog can learn new tricks) but as an investment we caution those entering this complicated market already trading at manic levels.

Disclaimer: Capstone does not currently hold Bitcoin in any of our Funds.



2 Corinthians 9:6 "Remember this: Whoever sows sparingly will also reap sparingly, and whoever sows generously will also reap generously."

## CAPSTONE'S POOLED FUNDS SUMMARY

Performance figures are those of Class I units as of December 31st, 2017

### **Capstone Mortgage Pool**

Diversified pool of construction and development mortgages  
(Launched April 30, 2012)

3 Month: 2.22%  
1 Year: 9.09%  
Inception: 9.52%

### **Capstone Fixed Income Pool**

Conservative, traditional and non-traditional income  
(Launched November 1, 2013)

3 Month: 0.83%  
1 Year: 4.70%  
Inception: 4.27%

### **MarshallZehr Mortgage Opportunities Fund**

Diversified pool of construction and development mortgages  
(Launched July 31, 2014)

3 Month: 2.10%  
1 Year: 8.60%  
Inception: 9.26%

### **Capstone Non-Traditional Equity Pool**

Diversified portfolio of non-traditional equity investment  
opportunities (Launched May 2, 2014)

3 Month: 2.34%  
1 Year: 8.03%  
Inception: 6.93%

### **Capstone Traditional Equity Pool**

Value-based approach to investing in traditional markets  
(Launched November 14, 2014)

3 Month: 4.23%  
1 Year: 2.94%  
Inception: 4.86%

### **MarshallZehr First Mortgage Fund**

Diversified pool of construction and development mortgages  
(Launched August 31, 2016)

3 Month: 1.42%  
1 Year: 5.57%  
Inception: 5.46%

Class I Funds are only available to Capstone's managed account clients and certain institutional investors.  
Performance is annualized for periods longer than one year.

## WHAT'S AHEAD IN 2018?

As we enter 2018 Canada appears to be in good shape. Unemployment is at a multi-decade low as job creation booms along with healthy hiring trends among corporations. Brent crude oil, considered to be the international benchmark for oil prices, broke \$70USD, its highest levels since December of 2014 and West Texas Intermediate (WTI) which we tend to use as our benchmark in Canada also reached a two-and-a-half-year high breaking \$60USD per barrel, another positive sign for Canada's oil-focused economy.

Canada may still come under some pressure in the year ahead but we believe the inflation and employment data (both heavily relied upon by the Governor of the BoC) will be rosy enough to warrant additional interest rate increases throughout the coming year.

Though the economy is well poised as we enter a 9<sup>th</sup> consecutive year of bull markets, we see continued downside risk in traditional markets. Although market expansions don't simply die of old age, there are several continuing risks including the consequences of synchronized global growth, the reduction of monetary easing by many central banks along with the dreaded 'black swan' events which one cannot know in advance. For these reasons and more, we believe that 2018 could be the year of 'peak growth' symbolizing the near end of a growth phase.

We continue to believe that caution is in order concerning stock markets, and a prudent investor should diversify into non-correlated assets.

