Market Matters

OCTOBER 2016 HIGHLIGHTS

- US Election (November 8th): The run up to the US election was red hot with scandal, media focus and narrowing polls. In the early hours of November 9th Donald Trump was declared US President-elect.
- In October, stock market results were mixed in the lead-up to the election. Developed markets (including the US) were weighed down in part by the political uncertainty, while emerging markets fared better as global growth forecasts improved.
- Global bond yields moved higher in October and sent bond prices lower, resulting in losses for bond investors for the month.
- During the month, the Canadian dollar dropped on lower oil prices and a soft economic picture.
- Early in October the British pound sterling declined to a 31 year low against the US dollar following UK Prime Minister May's announcement that she would give official notice of separation from the EU in March 2017.
- Oil prices were volatile. Uncertainty remains over the ability of OPEC to successfully negotiate a production quota among its 12 members, along with other key non-members as well.

AMERICA'S CHOICE

Americans cast their vote on November 8th, 2016 and Donald Trump will be the 45th President of the United States. This US electoral season has been like no other in its divisive outcome, its personal insults and nasty rhetoric. It will take time for America to heal from the bruising fight.

The immediate response included a flight-to-safety market reaction that was quickly tempered. As was the case for the unexpected Brexit result, history tells us that after initial reactions, a measure of reasonability and composure returns to capital markets over time – often a necessary step to put money on the sidelines back to work, and help corporations move forward on decisions and investments in people, products and development.

For specific comments on the market reaction to the November 8th U.S. election results, please see **GLC's commentary on the US Election results (November 9, 2016)**, which can be found on GLC's LinkedIn page and GLC's website (www.glc-amgroup.com).

SCARIEST MONTH OF THE YEAR

In spite of October's reputation as the scariest month of the year, this past October's market results were relatively muted, and the tricks and treats were not equally distributed. Emerging markets were a treat - continuing their upward path for 2016. Meanwhile, developed markets tricked and delivered weak market results.

Table 1
Summary of major market developments

Market returns*	October	YTD
S&P/TSX Composite	0.4%	13.7%
S&P 500	-1.9%	4.0%
- in Canadian dollars	***0.2%***	***0.8%***
MSCI EAFE	1.1%	-3.0%
- in Canadian dollars	***0.0%***	***-5.9%***
MSCI Emerging Markets	0.6%	9.7%
FTSE TMX Canada Universe Bond Index**	-0.9%	4.3%
FTSE TMX Canada all corporate bond index **	-0.4%	5.2%

*Local currency (unless specified); price only
**Total return, Canadian bonds

Table 2
Other price levels/change

	Level	October	YTD
CAD per USD exchange rate	$0.746	-2.1%	3.2%
Oil (West Texas)*	$46.86	-2.9%	26.5%
Gold*	$1,274	-3.3%	19.9%
Reuters/Jefferies CRB Index*	$186.28	0.0%	5.8%

*U.S. dollars

Table 3
Sector level results for the Canadian market

S&P/TSX Composite sector returns*	October	YTD
S&P/TSX Composite	0.4%	13.7%
Energy	0.8%	24.5%
Materials	-1.0%	47.2%
Industrials	-0.3%	14.8%
Consumer discretionary	-2.4%	4.6%
Consumer staples	1.8%	10.1%
Health care	-17.8%	-75.4%
Financials	2.2%	10.3%
Information technology	-1.3%	3.7%
Telecommunication services	-0.2%	14.0%
Utilities	1.3%	15.8%
Real Estate	-3.2%	2.0%

*Price only
Source: Bloomberg, MSCI Barra, NB Financial, FTSE TMX Global Debt Capital Markets Inc.

In fact, October is not the worst performing month of the year for stock markets. September has earned that honour over the past 80+ years. Having said that, there have been infamous frights (i.e. market drops) that occurred in October 1929, 1987, and 2008.

In October, scandals plagued both candidates, polls narrowed and markets faced the headwinds of political uncertainty. Beyond the US election noise, bond yields and corporate earnings results were big capital market drivers this October.

Bond yields continued to march upward across developed markets, moving in anticipation of a December rate increase by the US Federal Reserve and encouraged by improving (or better than anticipated) economic growth results out of the US, the UK, and stronger 2017 global growth estimates from the International Monetary Fund (estimated at 3.4%, up from the estimated 3.1% for 2016). Ten year Government of Canada bond yields rose 20 basis points in October; 10-year Treasury yields rose 23 basis points; Germany, France, Italy and UK 10-year sovereign bonds experienced even larger jumps (28, 28, 48 and 50 basis points respectively). The rise in yields drove bond prices lower for the month.

U.S. corporate earnings came in strong during the month of October. Broadly speaking, retail sales results were stronger than expected and gave hope that the American consumer continues to spend. Importantly, results were strong enough to ease fears that stock prices had gotten ahead of themselves (i.e. the fear that prices were unsupported by good corporate fundamentals). Looking forward to the end of the year, the strong earnings results, combined with greater political certainty in the US, bode well for investor and corporate confidence.

For both the S&P 500 and the S&P/TSX Composite indices, the financial sector led October's results. Financial companies benefited from higher interest rates, and stronger conviction for a December rate hike decision by the US Federal Reserve. Conversely, the 'bond proxy' real-estate sector (newly spun-off from the financial sector) was hampered by rising yields.

The energy sector was volatile, as were oil prices. Rumours and promises of a potential OPEC production freeze and OPEC's ability to work out a deal with non-OPEC members (most notably Russia) has oil prices swinging from headline to headline. Continued volatility of the oil price and for stock prices within the sector is likely to continue as the November 30th OPEC meeting approaches.

The health care sector lagged strongly in October. Drug pricing policies continue to come under scrutiny, and news that the cost of Obamacare would increase 25% in 2017 didn't help.

STRONGER TOGETHER

October saw a record number of US merger and acquisition announcements ($489 billion for the month). The marriage proposals include:

- A blockbuster deal by AT&T vying for Time Warner ($85 billion);
- British American Tobacco's $47 billion offer to take full control of Reynolds American, a move that would create the world's largest listed tobacco company;
- Qualcomm's intention to purchase NXP Semiconductors for $39 billion, the second-largest pure technology deal of all time;
- CenturyLink's $34 billion acquisition of Level 3 Communications; and,
- General Electric's deal to combine its oil and gas division with Baker Hughes.

There were deals with a Canadian twist as well:

- Oil refiner HollyFrontier said it had agreed to buy Suncor Energy Inc's Petro-Canada lubricants unit for $1.13-billion;
- TD Bank (40% owner of TD Ameritrade) is helping TD Ameritrade buy privately-held US discount broker, Scottrade, for US $4 billion and separately TD has made a $600-million offer to buy Richardson GMP.

FEELING TRUMPED?

It may be some time before the US election news subsides. As the current situation moves past the acute stage, we expect to see stocks and sectors return to responding to their fundamental outlook. We caution against knee-jerk reactions, as much regret can come from decisions made on emotion and haste.

At GLC we have clear, defined investment processes in place which help us apply a disciplined approach to seeing through the market noise and media hype. We will weigh the new realities and circumstances affecting the stocks and bonds we hold, and focus on recognizing and acting on opportunities as they present themselves. During periods of market volatility, when it can be difficult to remove human emotion and personal bias from decision making, the merits of GLC's disciplined investment processes shine through.

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