Market Matters

JANUARY 2014 HIGHLIGHTS

- Financial markets performed more spins and turns than a Russian ballet in January. Few market watchers anticipated such a start to 2014:
    - Best January since 2008 for bond markets.
    - Worst January since 2010 for equity markets.
    - The gold price, having been pounded down for more than a year into a mere leaf of its former self, caught a bounce. Canadian gold stocks rose 17%.
    - Canadian dollar fell below 90 cents USD.
    - Fiscal and political problems roiled emerging markets, their financial markets and their currencies.
- And if that didn't put a chill in your bones, winter sure did! *(Talk about Cold Wars! Winnipeg just had the coldest Dec/Jan in 64 years with 21 days of -30C° temperatures!)*
    - Natural gas prices benefited from the coldest Canadian winter in recent memory and rose 15% in January.

AFTER THE NEAR FLAWLESS ROUTINE…

After delivering a gold medal worthy performance in 2013, the S&P500 managed to post a new all-time high on January 15th, but succumbed to an Achilles heel injury in the form of a disappointing Chinese manufacturing report. The news sparked worry over the pace of global growth and investors saw it as an opportunity to sell off some of 2013's equity gains.

While the S&P/TSX Composite was also affected, it managed to stay in positive territory and ranked among the strongest performing indices of developed nations, helped in large part by the materials sector (see Table 3). Also making headlines and headway for the S&P/TSX Composite in January was Valeant Pharmaceuticals International Inc (up 21%) and Blackberry (up 33.5%, albeit from a much lower position). Valeant's acquisition plans were well received by investors and optimism around the new management team at Blackberry is being viewed as a 'Ray of Light' (a Sochi Olympic mascot) for the beleaguered company.

Emerging market equities and currencies were weak in 2013, started 2014 off poorly, and then worsened after the Chinese manufacturing report.

Table 1
Summary of major market developments

Market returns*	January	2013
S&P/TSX Composite	0.5%	9.6%
S&P 500	-3.6%	29.6%
- in Canadian dollars	***0.8%***	***38.4%***
MSCI EAFE	-3.4%	23.5%
- in Canadian dollars	***0.3%***	***27.6%***
MSCI Emerging Markets	-4.6%	0.9%
DEX Universe Bond Index**	2.6%	-1.2%
BBB Corporate Index**	3.0%	1.2%

*local currency (unless specified); price only
**total return, Canadian bonds

Table 2
Other price levels/change

	Level	January	2013
CAD per USD exchange rate	$0.899	-4.5%	-6.6%
Oil (West Texas)*	$97.49	-0.9%	1.0%
Gold*	$1,241	3.0%	-25.4%
Reuters/Jefferies CRB Index*	$283.31	1.1%	-6.8%

*U.S. dollars

Table 3
Sector level results for the Canadian market

S&P/TSX Composite sector returns*	January	2013
S&P/TSX Composite	0.5%	9.6%
Energy	-0.1%	9.9%
Materials	9.1%	-30.6%
Industrials	-1.0%	34.9%
Consumer discretionary	-0.4%	39.5%
Consumer staples	1.6%	21.4%
Health care	18.2%	71.7%
Financials	-3.6%	19.1%
Information technology	6.6%	36.2%
Telecommunication services	1.8%	8.1%
Utilities	3.5%	-8.6%

*price only
Source: Bloomberg, MSCI Barra, NB Financial, PC Bond

Investor demand drove bond prices higher in spite of the U.S. Federal Reserve announcing additional tapering of their asset-purchasing plans. The uncertainty surrounding emerging markets and volatile equity markets sparked a flight-to-safety trade that helped bonds post the best monthly gain in five years. January served as a healthy reminder of the value of fixed-income investments within a diversified portfolio during periods of equity market volatility.

Along the same track, it is worthwhile noting that a pull-back in equities after such a strong run can be a good thing - moderating overblown expectations and consolidating profits. For now, the underlying fundamentals remain supportive as fourth quarter corporate earnings reports have been strong and economic data remains on track with expectations for ongoing recovery.

EMERGING MARKET ANGST

The real angst in the global markets this January was focused on emerging markets, where equities, bonds, and currencies were under pressure. Currencies in countries like Russia, Argentina, India, Brazil, Turkey and South Africa have been particularly hard hit. A combination of slowing growth, rising inflation, U.S. Federal Reserve tapering, current account deficits and political unrest are the causes to varying degrees and significance in each country.

Money started leaving these regions last year, and continued in January. Emerging markets benefited from the U.S. Federal Reserve's cheap money policy over the past six years. Now that the Federal Reserve has begun a staged withdrawal from its monthly bond purchases, credit conditions are tightening as American interest rates are poised to rise. Many emerging market economies are running large deficits and require large capital inflows to maintain stable currencies. While on the radar for those tracking global economic growth forecasts, developed markets are still seen as having some distance from the developing world's fiscal problems, with the U.S. recovery remaining the driving force for global equity markets in 2014.

REMEMBER TURIN, ITALY?

Back in 2006, when Turin, Italy hosted the Winter Olympics, the Canadian dollar hovered comfortably below 90 cents USD. The Canadian dollar has fallen sharply over the past few weeks back to sub-90cent levels. In mid 2007, as the financial crisis took hold, the Canadian dollar was regarded as a safe haven currency. However that podium position has been given up as investors' safe haven demand for the Canadian dollar has dwindled. The economic growth momentum is now with the U.S., and our dollar's tie to commodity prices has further weakened the position. While Canadian travellers seeking refuge from Canada's winter may be upset, many are cheering the weaker loonie – including the Bank of Canada. A weaker Canadian dollar is considered just the ticket to help boost Canada's exporting industries and our overall economic performance. That said, it is expected to be a couple of years before those benefits filter through to export and import volumes, industry output, employment and personal income.

GO CANADA GO!

Russia welcomes the world in February with the Sochi XXII Olympic Winter Games! A record 88 countries will be participating in 15 sports for 98 medal events, including first time participation by Zimbabwe (men's slalom skiing) and Togo (women's slalom skiing). As the Games unfold, we know the medals presented to the athletes will be priceless - representing not months, but years of hard work, dedication, achievement and sacrifice, and dwarfing the value of the metals within the medals (see Table 4).

Well over 200 Canadian athletes will be competing in Sochi and with every skate, lap, end, run, jump and game, we wish them success and share our pride in their commitment to their sport and to representing Canada.

Table 4 – Priceless metals

	Vancouver, Canada 2010	Sochi Russia 2014	Increase in value (2010-2014)	Annualized rate of return (2010-2014)
Gold/ oz	$1,081.20	$1,244.55	18%	3.6%
Silver/ oz	$16.21	$19.19	15%	4.3%
Bronze/ lbs	$2.80	$2.99	9%	1.3%

Source: Bloomberg
All values shown in U.S. dollars as of January month-end of Olympic year.
Price of Bronze was estimated by a mix of 90% copper and 10% zinc.

GOOD LUCK! BONNE CHANCE! УДАЧИ!

(Russian pronunciation: oo-DAH-chee)