

Market Matters

JULY HIGHLIGHTS

- Stocks, bonds, the dollar and commodities all gained in July as global markets reacted to expectations that the U.S. Federal Reserve and the European Central Bank will take steps to stimulate the flagging economy.
 - The energy sector led the gain in the S&P/TSX composite index while defensive sectors of the North American stock markets continued to outperform cyclical sectors.
 - The Canadian dollar gained amid rising prices for oil and metals.
- Data for second quarter U.S. gross domestic product recorded its weakest pace since the third quarter of 2011 and Canada's GDP showed equally passive performance.
 - In June the rate of new-home construction in the U.S. rose to its highest level since October 2008. But just when the housing market is showing signs of finding a bottom, a sluggish U.S. economy is muddying the ground.

VOLATILITY DOMINATES

July was another volatile month for global markets with eurozone debt issues continuing to dog investors. Europe's debt crisis has weighed on markets for more than two years now. While Greece, Portugal and Ireland were forced to seek bailouts, the crisis has recently moved to Italy and Spain, which have been paying surging bond yields in order to finance their debts. Market sentiment was given a boost in July following a commitment from the president of the European Central Bank to protect the euro and pledges from European leaders to preserve the union of the 17 countries that use the euro. Whether the eurozone debt crisis has finally turned a corner remains to be seen.

Markets have also been stung by disappointing revenue reports with companies citing production shortfalls, higher operating costs, weaker demand and a stronger dollar. While expectations may have to be marked down, positive earnings growth should continue this year.

| Market returns* | July | YTD |
|--|-------|-------|
| S&P/TSX Composite | 0.6% | -2.4% |
| S&P 500 | 1.3% | 9.7% |
| - in Canadian dollars | -0.3% | 8.2% |
| MSCI EAFE | 1.4% | 3.5% |
| - in Canadian dollars | -0.5% | 0.4% |
| MSCI Emerging Markets | 1.4% | 4.7% |
| <hr/> | | |
| DEX Universe Bond Index** | 0.7% | 2.7% |
| BBB Corporate Index** | 0.9% | 5.1% |
| *local currency (unless specified); price only | | |
| **total return, Canadian bonds | | |

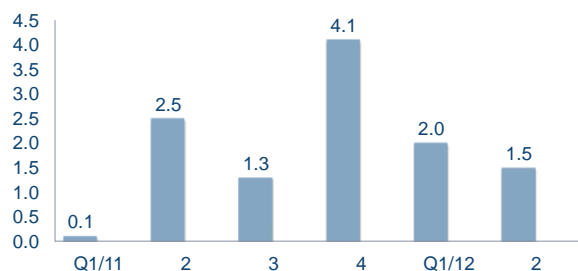
| | Level | July | YTD |
|---------------------------------|----------|------|--------|
| U.S. dollar per Canadian dollar | \$0.998 | 1.6% | 1.4% |
| Oil (West Texas)* | \$87.58 | 3.2% | -11.6% |
| Gold* | \$1,621 | 1.5% | 3.0% |
| Reuters/Jefferies CRB Index* | \$299.51 | 5.4% | -1.9% |
| *U.S. dollars | | | |

| S&P/TSX Composite sector returns* | July | YTD |
|---|-------|--------|
| S&P/TSX Composite | 0.6% | -2.4% |
| <hr/> | | |
| Energy | 4.3% | -5.2% |
| Materials | -3.6% | -14.4% |
| Industrials | 2.4% | 6.2% |
| Consumer discretionary | -0.3% | 11.2% |
| Consumer staples | 1.9% | 9.9% |
| Health care | -3.2% | 7.6% |
| Financials | -0.3% | 3.1% |
| Information technology | -4.7% | -15.6% |
| Telecommunication services | 2.8% | 2.2% |
| Utilities | 1.2% | -0.6% |
| *price only | | |
| Source: Bloomberg, MSCI Barra, NB Financial, PC Bond, RBC Capital Markets | | |

GROWTH SLOWS

Weak retail sales resulting from high unemployment held U.S. growth to an annual rate of only 1.5 per cent in the second quarter, down from 2.0 per cent in the first quarter. Growth for the second half of the year comes into question as a U.S. budget crisis and Europe's financial difficulties continue to curtail business investment and consumer spending despite historically low interest rates.

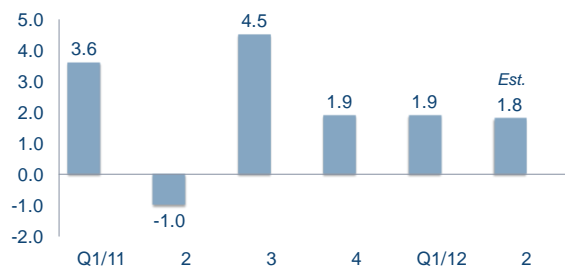
United States Real GDP Growth
Quarterly Annualized (%)



Source: U.S. Bureau of Economic Analysis

Canada too seems headed along a path of sub-par growth with the economy growing at only 0.1 per cent in May and forecast to grow at perhaps an optimistic 1.8 per cent in the second quarter. On the upside, Canadians are still willing to spend—retail sales increased for the third straight month in May—and employment is still trending higher.

Canada Real GDP Growth
Quarterly Annualized (%)



Source: Statistics Canada

Encouraging news out of the U.S. includes an increase in housing starts in June to its highest level in four years and a second quarter rise in exports of 5.3 per cent. Housing starts in Canada remain solid although Canada Mortgage and Housing Corporation tightened its mortgage insurance rules in July, which are expected to contribute to a slowdown in the housing market.

BEARS REPEATING

Global equity markets did not respond bearishly to bearish news in July. The bull market remains intact with all markets gaining in the month and the S&P 500 index up a healthy 9.7 per cent year-to-date. Most other major global indices have also gained this year. Lagging its global peers due to a greater leverage to resource stocks, the S&P/TSX composite index has declined 2.4 per cent year-to-date.

REMAIN FOCUSED

The Canadian Olympic Committee has a strategy. They are focused on ensuring that high-priority sports develop depth, so that every hope for a medal doesn't come down to one athlete. A well-diversified investment portfolio builds depth, so that every expectation for growth doesn't rest on one asset class. By including equities (with greater long-term upside potential) and fixed income (with a tendency to take the edge off volatility and outperform when equity markets don't), you can feel confident that you hold offsetting asset classes to smooth out volatility as you aim to achieve your financial goals.

GROSS NATIONAL HAPPINESS INDEX

The tiny, remote Himalayan kingdom of Bhutan has a GNH index that measures gross national happiness. Instead of relying on GDP (gross domestic product), which is based on a nation's economic activity, Bhutan considers GNH, a measure of its people's sense of being well-governed, their relationship with the environment, satisfaction with the pace of economic development, and a sense of cultural and national belonging.

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