

# Market Matters

## JANUARY HIGHLIGHTS

- Global equity markets were broadly positive in January, buoyed by:
  - improving economic conditions in the U.S.;
  - supportive fiscal and monetary policy action in the U.S., Europe and China;
  - signs of progress for Eurozone debt issues;
  - strong corporate earnings across North America; and
  - improving investor sentiment.
- Bond markets weakened, but were ultimately bumped into positive territory at month's end on the U.S. Federal Reserve (Fed) announcement that they expect rates to remain low until at least 2014.
- Gold bullion prices soared, aided by a number of factors such as:
  - a bounce back from fourth quarter weakness in bullion prices;
  - a weaker U.S. dollar (further to the Fed's 'low for longer' announcement);
  - sentiment support for the hard asset as global economic conditions remain fragile.

## YEAR OF THE DRAGON

January marks the start of 'the year of the Dragon' in many Asian cultures. Whether the fire-breathing beast will serve as friend or foe to capital markets this year remains to be seen, but at the start of 2012 the dragon clearly ignited the risk appetite of investors – at long last appearing willing to give equities another chance.

## EVEN THE TALLEST TOWER STARTED FROM THE GROUND.\*\*

Global equity markets experienced broad strength, both from developed and developing nations, in January. Investors found reason for optimism in the slow, but steady, progress on Eurozone debt issues, and modest, but significant, improvements in U.S. economic indicators (see Table 1). Overall, world equity markets gained \$1.8 trillion (USD) in January, cutting the 2011 loss of \$3 trillion (USD) by 60% in one month.\*

As January's market results unfolded, a near mirror image of 2011 results appeared. In general, what went down in 2011 went up in January 2012, and vice versa. The cyclical sectors, like Materials and Energy, had positive results while the defensive sectors, like Utilities and Telecommunications, sold off in January (see Table 2).

| Market returns*       | January | 2011   |
|-----------------------|---------|--------|
| S&P/TSX Composite     | 4.2%    | -11.1% |
| S&P500                | 4.4%    | 0.0%   |
| - in Canadian dollars | 3.1%    | 2.2%   |
| MSCI EAFE             | 3.8%    | -14.8% |
| - in Canadian dollars | 4.0%    | -12.9% |
| MSCI Emerging Markets | 7.3%    | -14.9% |
| DEX Bond Universe**   | 0.5%    | 9.7%   |
| BBB Corporate Index** | 1.3%    | 8.7%   |

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

|                                 | Level    | January | 2011  |
|---------------------------------|----------|---------|-------|
| U.S. dollar per Canadian dollar | \$0.9959 | 1.2%    | -2.2% |
| Oil (West Texas)*               | \$98.46  | -0.6%   | 8.4%  |
| Gold*                           | \$1,731  | 9.9%    | 11.1% |
| Reuters/Jefferies CRB Index*    | \$321.31 | 2.3%    | -8.3% |

\*U.S. dollars

| S&P/TSX Composite sector returns* | January | 2011   |
|-----------------------------------|---------|--------|
| S&P/TSX Composite                 | 4.2%    | -11.1% |
| Energy                            | 3.5%    | -12.3% |
| Materials                         | 10.3%   | -21.8% |
| Industrials                       | 2.6%    | 2.0%   |
| Consumer discretionary            | 3.3%    | -17.9% |
| Consumer staples                  | -0.2%   | 4.8%   |
| Health care                       | 4.1%    | 49.6%  |
| Financials                        | 2.6%    | -6.6%  |
| Information technology            | 6.4%    | -52.6% |
| Telecom services                  | -2.5%   | 19.0%  |
| Utilities                         | -1.2%   | 1.6%   |

\*price only  
 Source: Bloomberg, MSCI Barra, NB Financial, PC Bond, RBC Capital Markets

Likewise, after having experienced a very strong year in 2011, bond markets followed the inverse pattern into negative territory for much of the month. However, shortly before month-end, the Federal Reserve announced its expectations to keep its central bank rate unchanged until at least 2014 – re-assuring fixed-income investors who kept demand for bonds up and helped returns move back into positive territory.

This accommodative action taken by the U.S. Federal Reserve also weakened the U.S. dollar; in turn boosting gold bullion values (see Table 3). Gold continues to claim the interest of anxious investors who, so long as global economic uncertainties continue, are expected to support these strong values. Having said that, one has to be wary of the increasing risks of this traditional safe haven asset that has risen in value to the tune of +30% over the course of a year - giving it more in common with speculative assets than with 'safe haven' assets.

### **PATIENCE IS A TREE WITH BITTER ROOTS THAT BEARS SWEET FRUITS.\*\***

Economic momentum has improved in the U.S., creating a supportive backdrop for corporate America. In recent months we have seen the American job market continue on its path of improvement. The U.S. unemployment rate recently dropped to 8.3%, the lowest level since February 2009. Job gains have been made across a range of sectors, from manufacturing and construction to retailers. We've also seen signs of life in new housing construction, which is now a positive contributing factor to U.S. GDP. Furthermore, there has been a noticeable firming in discretionary consumer purchases, such as motor vehicles, furniture and clothing. This reflects the backlog of replacement demand that has built up since the recession began. Improved consumer balance sheets (i.e. Americans have been reducing their debt loads) and gradual improvement in the job market are now allowing replacement demand to surface.

In Canada, corporate balance sheets continue to exhibit healthy profiles. While the strengthening Canadian dollar will create a headwind for Canadian manufacturing companies, and a resulting tighter job market in those sectors, the accommodative stance by the Bank of Canada to keep rates low for the foreseeable future should support economic growth moving forward, albeit at a relatively slow pace.

In January, the American S&P500 index posted its best opening month in 15 years, tallying up a 19% rise from the early October, 2011 lows. Supporting both the Canadian and U.S. markets in January, were strong corporate earnings, an encouraging sign that is gaining traction with investors after having been ignored for much of 2011. In fact, stock price levels (as measured by price/earnings

ratios) have been weighed down by a lack of clarity and confidence in global economic growth and remain attractive. Seeing investors respond to the positive earnings results of companies is a good sign that markets may move away from their macro-driven environment into more of a stock-picker's environment, in which companies can differentiate themselves through good stewardship and good corporate results.

### **ORDER MOVES SLOWLY BUT SURELY DISORDER ALWAYS IN A HURRY.\*\***

Europe's sovereign debt crisis spiralled downhill in 2011, and will take years to repair, but efforts are at long last beginning to work. Recent favourable bond auctions from countries such as Italy and Spain have been a confidence builder as investors are gaining hope that refinancing of weaker countries' debt will be possible. Over the coming months the focus will be on the continued progress of European policy makers to work out a sustainable, longer-term plan.

Emerging market economies continue to hold up relatively well. China's economy expanded by 8.9% year-over-year, as reported for the fourth quarter of 2011. While this is still very strong growth, it was the slowest pace for China in two and a half years. Challenges in Europe and its contagion effect on global economic growth contributed to the slow down, but should be mitigated by China's recent actions toward more accommodative monetary policy and easing bank reserve requirements - the goal being a 'soft landing' to their rocketing economy and inflation concerns that remain at bay.

### **A SINGLE BEAM CANNOT SUPPORT A GREAT HOUSE.\*\***

The dragon, an apt symbol for power, strength and good fortune, is a legendary creature that relies on its diverse strength to ward off opponents – able to thrive on the ground, in the water, and in the sky. Because market leadership can change quickly, we tend to agree with the idea of diversifying your strengths. A diverse portfolio with a mix of fixed-income and equity, domestic and foreign holdings, can give your portfolio the strength to weather and prosper in changing market environments.

*\*Standard & Poor's*

*\*\*Chinese proverbs*

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