

# Market Matters

## Q1 2015 HIGHLIGHTS

- During the quarter diverging monetary policies around the world contributed to volatility and uncertainty within equity and fixed income markets.
  - In Canada, the Bank of Canada broke its four-plus year hold at the 1% interest rate level, and surprised investors with a 25 basis point cut to 0.75%.
  - The U.S. Federal Reserve toyed with its script for 'forward guidance' and seems poised to begin raising rates later this year.
  - The European Central Bank set its quantitative easing (i.e. asset-purchasing) program in motion in March.
- For the fifth straight quarter both US and Canada 10-year government bond yields declined, leading to strong returns for the fixed-income markets. The Canadian FTSE TMX Canada Universe Bond index returned a very healthy 4.2% year-to-date.
- North American equity markets experienced very modest gains.
  - The S&P/TSX Composite index rose 1.8%, aided by outsized gains in the health care sector, but held back by a weakened earnings outlook for companies affected directly and indirectly by low oil prices and the anticipation of a soft patch for the Canadian economy.
  - The S&P 500 was range bound for the quarter, ending the period with less than a 1% gain. Uncertainty around US Federal Reserve action and softer than anticipated economic data contributed to the lack-luster results for the index.
- Aided by easing monetary and fiscal policies, Japan, France, Germany and China each booked double digit returns for the first quarter of 2015.
- The US dollar was anything but range bound, as the USD index broke out to the tune of nearly 9% during the quarter. The currency exchange accounted for significant gains for US holdings when converted back to Canadian dollars.

### AT HOME

Bank of Canada (BoC) Governor Poloz caught investors off guard with a 25 basis point central bank rate cut on January 21st to 0.75%, stating the need for 'insurance' against the economic impact of low oil prices on the Canadian economy, and breaking the four-plus year hold at the 1% interest rate level.

With shaken trust in the BoC's forward guidance, the 'will he/won't he cut again' debate ensued with vigor. By late February Governor Poloz seemed to shift back to a more neutral stance, but volatility has continued as markets try to find their footing amid the uncertainty around the BoC's next move.

Table 1 Summary of major market developments		
Market returns*	March	YTD
S&P/TSX Composite	-2.2%	1.8%
S&P 500	-1.7%	0.4%
- in Canadian dollars	-0.4%	9.6%
MSCI EAFE	0.9%	10.1%
- in Canadian dollars	-0.6%	13.7%
MSCI Emerging Markets	0.0%	4.6%
FTSE TMX Canada Universe Bond Index**	-0.3%	4.2%
FTSE TMX Canada all corporate bond index**	-0.1%	3.6%

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

Table 2 Other price levels/change			
	Level	March	YTD
CAD per USD exchange rate	\$0.788	-1.4%	-8.4%
Oil (West Texas)*	\$47.60	-4.3%	-10.6%
Gold*	\$1,184	-2.5%	-0.3%
Reuters/Jefferies CRB Index*	\$211.86	-5.5%	-7.9%

\*U.S. dollars

Table 3 Sector level results for the Canadian market		
S&P/TSX Composite sector returns*	March	YTD
S&P/TSX Composite	-2.2%	1.8%
Energy	-0.9%	-2.0%
Materials	-10.3%	2.8%
Industrials	-1.2%	1.2%
Consumer discretionary	-1.1%	5.6%
Consumer staples	-0.6%	3.1%
Health care	4.2%	45.1%
Financials	-1.5%	-1.1%
Information technology	-3.4%	8.5%
Telecommunication services	-3.4%	-1.0%
Utilities	-1.6%	2.4%

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

Bond prices benefited from the rate cut in January, expectations for an economic soft patch in Canada, and the continued high demand for yield products. Within the global context of an ultra low-yield environment, North American bonds remain a relative bargain if compared to sovereign bonds in other countries where yields are at historic lows or even negative yield levels. Compare Germany's 10 year bunds which are yielding 0.18% with an equivalent 10-year Government of Canada bond yielding 1.36% at quarter-end. Investors have been drawn to the west in search of 'relatively' richer yields, keeping downward pressure on North American bond yields.

The Canadian equity market (See Table 1) managed a modest gain, with seven out of ten sectors putting up positive numbers for the quarter. Exceptionally, the Health Care sector experienced a 45% gain – the result of (very) positive investors' response to Valeant Pharmaceutical's (now more than 4% weight in the index) acquisition announcement of Salix Pharmaceuticals. The Materials sector got a lift from gold companies whose valuation levels had been depressed. The bounce-back from over-sold conditions helped the mid-cap Canada index (+2.3%) outperform the broad market in the first quarter of 2015. To the downside, weak employment growth data and low oil prices' effect on the Canadian economy contributed to the energy sector experiencing the largest absolute drop, followed by the financial sector whose earnings outlook weakened in anticipation of a soft patch for the Canadian economy. The more defensive (and primarily dividend-paying areas) of the market, such as the Telecommunications and Utilities sectors, have underperformed this year after a strong 2014.

## DOWN SOUTH

For most of the quarter the S&P 500 plodded sideways as investors showed varying degrees of patience around what the U.S. Federal Reserve would have to say on the future direction of interest rates. You know things are getting off kilter when the experts engage in discussions and debates around weighty economic topics ...like whether Fed Chairman Janet Yellen would (or would not) cut the word 'patient' from her speech!\* In the end, the Fed surprisingly tempered its growth expectations for 2015 and effectively pushed out its timeline for rate normalization (i.e. easy money for longer), but the Fed also became one of the only central banks expected to move to a tightening bias in the near future. \*She cut - the word, not rates!

The S&P 500 ended the quarter with less than a 1% gain. The laggards included the Utilities sector (down 6% this quarter, after strong gains in 2014), followed by the Energy and Financial sectors. To the positive side the Health Care sector led the way, followed by Consumer Discretionary. Of interest, without the strong performance of Apple, whose cap-size exceeded \$700B in the quarter, the S&P 500 would have finished the quarter in negative territory.

The US dollar has been anything but range bound so far in 2015. The US dollar's rise versus the Canadian loonie accounted for a near 10% appreciation of the S&P 500 when converted to Canadian dollars.

## AND ABROAD

European stock markets staged a substantial rally year-to-date as Europe benefitted from improving economic trends and the start of the European Central Bank's (ECB) quantitative easing (QE) program. The ECB surprised and pleased investors with the size and scope of their QE program. Having said that, Europe remains susceptible to setbacks, as exemplified by the volatility caused by another round of Greek debt (re-)negotiations. In China, despite some weak economic data, the Shanghai Composite leapt nearly 16%. Speculation and anticipation of further easing measures by the People's Bank of China are noted as contributors to the sharp rise. Likewise, expectations of continued monetary and fiscal stimulus in Japan helped the Nikkei 225 index rise over 10% in the quarter.

## ENTHUSIASM FOR 'EASY MONEY'

Enthusiasm for 'easy money' (i.e. accommodative & stimulative monetary policy) played out in many corners of the world, but with it (and globally diverging monetary policies) has come volatility and uncertainty within equity and fixed income markets. For your own investment plans, the term 'easy money' sounds too good to be true. After all, earning money takes work. But we do believe there is an 'easier' way for your money to work for you within a long-term investment plan.

- Diversify your assets (which will reduce volatility).
- Stay within your personal risk tolerance (which will reduce your stress when volatility happens).
- Match your investment time horizons with your financial goals (which will increase the chances that the money will be there when you need it).

Of course, there are harder ways to meet your investment goals too. The good thing is, you get to pick.