

Market Matters

APRIL HIGHLIGHTS

- Strong earnings results from American companies were overshadowed by broader global growth concerns as waning investor confidence in the economic outlook for global growth dampened equity market returns.
- The Canadian bond market (DEX Universe Bond Index) results were flat for the month, with lower long-term bond yields helping to offset higher short-term bond yields and a slight widening in corporate bond spreads.
- Weak gold company results weighed down the Canadian Materials sector.

MACRO MATTERS

Macro-economic concerns once again trumped capital market fundamentals, and stock market results soured in April after a strong run in the first quarter.

Better than anticipated U.S. corporate earnings results (albeit clearing a bar that was recently lowered by analysts' downward revisions) were not enough to keep equity markets in the black, as the global fiscal and economic concerns threw a wet blanket on equity market results and increased volatility in the markets.

BESTED BY BONDS

Global equity markets (see Table 1) were modestly negative in April, with Euro nations (in particular Spain) the laggards among their global peers. China was a notable exception as the Shanghai Composite index outperformed over the past month (up 5.9% in local currency) in spite of resurfacing concerns about slowing Chinese economic growth.

The Canadian bond market (DEX Universe Bond Index) bested the S&P/TSX in April. While shorter term yields rose slightly over the course of the month, yields on 10 and 30 year Government of Canada bonds did what many a headline had reported as inconceivable...they declined even further from historically low levels (albeit only slightly) to 2.03% and 2.61% respectively. For those who've continuously reported (for several months now), that 'yields cannot possibly go any lower', therein lies a subtle reminder that predicting short-term capital market behaviour (even bond market behaviour) is a mug's game.

Table 1
Summary of major market developments

Market returns*	April	YTD
S&P/TSX Composite	-0.8%	2.8%
S&P500	-0.7%	11.2%
- in Canadian dollars	-1.9%	8.0%
MSCI EAFE	-3.2%	5.8%
- in Canadian dollars	-3.5%	4.3%
MSCI Emerging Markets	-0.9%	9.3%
DEX Universe Bond Index**	0.1%	-0.1%
BBB Corporate Index**	0.2%	2.2%

*local currency (unless specified); price only

**total return, Canadian bonds

Table 2
Other price levels/change

	Level	April	YTD
U.S. dollar per Canadian dollar	\$1.0125	1.1%	2.9%
Oil (West Texas)*	\$104.82	1.6%	5.8%
Gold*	\$1,660	-0.2%	5.4%
Reuters/Jefferies CRB Index*	\$305.95	-0.8%	0.2%

*U.S. dollars

Table 3
Sector level results for the Canadian market

S&P/TSX Composite sector returns*	April	YTD
S&P/TSX Composite	-0.8%	2.8%
Energy	1.0%	-0.2%
Materials	-6.1%	-6.1%
Industrials	2.0%	4.8%
Consumer discretionary	1.4%	14.8%
Consumer staples	3.6%	10.7%
Health care	5.9%	22.3%
Financials	-0.4%	9.4%
Information technology	-3.5%	3.9%
Telecom services	-1.1%	-3.2%
Utilities	1.5%	1.4%

*price only

Source: Bloomberg, MSCI Barra, NB Financial, PC Bond, RBC Capital Markets

On the Canadian market front Health Care and Consumer Staples sectors extended their 2012 strength, while the Financial sector (still up 9.4% so far this), gave away its leadership in the latter half of the month.

Within the Materials sector, the gold and precious metal stocks continued to underperform their respective

underlying commodities as concerns over rising operating costs grew. The Energy sector managed to stay afloat as oil prices wavered between the opposing forces of weakening global growth prospects and elevated geopolitical concerns. Should we see a leveling off of oil prices, this will be good news from a consumer spending point of view - leaving more money in the wallet of consumers after each visit to the gas pumps.

PHILOSOPHICAL GAP

European debt concerns emerged again in April. Spain in particular earned the unwanted spotlight. Viewed by many as too big to fail and too big to bail, Spain's worsening fiscal backdrop and struggling banking system heightened investors concerns and will likely necessitate further action from the European Central Bank.

Investors concerns were further exacerbated by political upheaval across the Eurozone. While hard to imagine, the current political landscape in the Eurozone is making the U.S. presidential election process seem clear-cut, efficient and collegial in comparison. Over the last several weeks, European voter dissatisfaction over their government's austerity programs – both those implemented and those proposed – has raised the level of uncertainty across world markets. Unfortunately, the inability of governments to implement financial restraint and cost cutting is doing little to bridge the philosophical gap between those nations needing financing, and those nations providing the financing. We expect to see ongoing market volatility until a sustainable plan for greater financial stability of the Eurozone nations can be put in place. The process will be slow, but at this point we remain hopeful that further progress can be made.

DEALING WITH UNCERTAINTY

Currently stock market valuations (as measured by price/earnings ratios) in both Canada and the U.S. are well below historical averages, while corporate earnings results continue to be strong. To paraphrase, on a 'what you get for what you pay for' basis – today's stock market looks like a darn good deal.

In contrast, the fundamental picture for fixed income investors is much more muted. With current interest rates at very low levels, we acknowledge that the time for investing in bonds for capital appreciation purposes may be coming to an end.

With this backdrop, why are so many investors continuing to shy away from equities and overweighting their portfolios with bonds?

Uncertainty is the greatest single issue working against equity markets at the moment. Investors can live with negative news and less than rosy outlooks, adapting remarkably quickly to new realities, but too many uncertainties will diminish their confidence and stand in the way of investors comfort with forward-looking investment decisions. This can make it difficult for the rational mind to over-power the less rational, more emotional mind. For today's long-term investor, we believe that establishing a well diversified portfolio is the most rationally compelling and emotionally comforting option. By including equities (with greater long-term upside potential) and fixed income (with a tendency to mitigate volatility and outperform when equity markets don't) you can feel confident that you hold offsetting asset classes to smooth out volatility on route to your financial destination. It's a sustainable option that can put a lot more certainty back into your financial security plans.

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