Market Matters

MAY 2016 HIGHLIGHTS

- Most major developed equity markets continued to move in the right direction in May (see Table 1). May's equity market gains solidified the turnaround from the sharp decline at the beginning of the year:
  - S&P/TSX Composite declined 9.0% from January 1-January 20th, 2016 (note that Canada's recovery began earlier than many of its peers), followed by an 18.8% rebound to May 31st, 2016.
  - The S&P500 declined 10.5% from January 1-February 11th, 2016, followed by a 14.7% rebound to May 31st, 2016.
  - The MSCI EAFE declined 13.0% from January 1- February 11th, 2016, followed by a rebound of 11.8% to May 31st, 2016.
- Canadian bond markets had strong one-month returns, helped by a decline in yields across most terms.
- A largely 'risk-on' trade helped oil prices catch a bid (briefly trading above $50 USD during the month), while gold prices found themselves on the other side of the risk-on trade.

AT THE HUNDREDTH MERIDIAN (THE TRAGICALLY HIP: CANADIAN ROCK BAND/LEGENDS)

Canadian equities finished May in positive territory, helped by the energy sector which continued to benefit from recovering oil prices. Oil prices rose 7% over the course of the month and traded briefly above $50 USD in May, but ended the period down a buck from those highs (see Table 2). Nearly all of the Canadian market gains were erased by losses within the materials sector. Gold, the traditional safe-haven asset in times of economic concern, sold-off in May as investors favoured a more risk-on approach.

Canadian bond markets also posted positive returns in May. Yields along the Government of Canada yield curve initially rose early in the month, but soon turned around and began to drop. Canadian bond yields followed a general downtrend in global yields, but yields in Canada also felt the effect of some economic concerns (i.e. oil production loss and expected hit to economic growth) associated with the Alberta wildfires.

From a broad economic perspective, Canadian GDP looks rather unremarkable as sluggish growth is expected to come in around 1.5% this year, accelerating to around 2.1% in 2017. But at the hundredth meridian, where the great plains begin, there's a divide in our country's economic health forming.

Table 1
Summary of major market developments

Market returns*	May	YTD
S&P/TSX Composite	0.8%	8.1%
S&P 500	1.5%	2.6%
- in Canadian dollars	*5.9%*	*-2.8%*
MSCI EAFE	1.3%	-5.3%
- in Canadian dollars	*2.7%*	*-8.0%*
MSCI Emerging Markets	-1.0%	1.2%
FTSE TMX Canada Universe Bond Index**	0.9%	2.2%
FTSE TMX Canada all corporate bond index **	0.7%	2.7%

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

Table 2
Other price levels/change

	Level	May	YTD
CAD per USD exchange rate	$0.764	-4.1%	5.7%
Oil (West Texas)*	$49.10	6.9%	32.6%
Gold*	$1,215	-5.9%	14.4%
Reuters/Jefferies CRB Index*	$186.15	0.8%	5.7%

*U.S. dollars

Table 3
Sector level results for the Canadian market

S&P/TSX Composite sector returns*	May	YTD
S&P/TSX Composite	0.8%	8.1%
Energy	1.3%	15.6%
Materials	-6.7%	33.6%
Industrials	1.3%	5.7%
Consumer discretionary	3.2%	3.8%
Consumer staples	4.7%	5.5%
Health care	-6.7%	-65.0%
Financials	1.3%	5.9%
Information technology	8.3%	1.1%
Telecommunication services	3.5%	10.7%
Utilities	3.1%	10.4%

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

The impact of weak oil prices continues to ripple through Alberta and Saskatchewan with cutbacks in energy-sector capital expenditures alongside the economic and production loss associated with the wildfires scorching parts of both provinces. Meanwhile, central Canada (Manitoba, Ontario, Quebec) is benefitting from non-oil related industries, the weaker Canadian dollar and improved U.S. economy.

Atlantic Canada faces demographic challenges and fiscal restraint, but the region is expected to see some improvement; the exodus of younger workers toward the western oil-patches is expected to slow, and the weaker loonie/stronger US economy should provide a boost to tourism in PEI, forestry exports in New Brunswick, and shipbuilding in Nova Scotia.

At the far edges of Canada (British Columbia and Newfoundland & Labrador) distance and fortunes couldn't be further apart. Newfoundland & Labrador expect to see economic growth contract further as oil-related growth stalls, and heavy fiscal restraint measures get put in place. Meanwhile British Columbia is humming with a much more diverse resource base (natural gas, base metals, forestry and little direct exposure to oil), a rip-roaring housing market, and a strong export picture with good US demand and a weaker Canadian dollar.

SHOULD I STAY OR SHOULD I GO (THE CLASH: ENGLISH PUNK ROCK BAND)

The summer heat is certain to rise as a number of game changing decisions will shake up the status quo in the coming months.

Brexit: On June 23, 2016, the U.K. will hold its 'Brexit' vote – when the British electorate decide whether to stay in the European Union (EU) or go it alone. Pollsters and book-makers are currently placing the odds in favour of Britain remaining a part of the EU. Most recently this has helped to lift European markets and the British pound. As the vote nears and both sides intensify their campaigns, we anticipate the volatility of markets and the British currency to be relatively high.

U.S. Federal Reserve rate move: June and July will be decision time for the U.S. Federal Reserve (Fed). In May, Chair Janet Yellen raised expectations for a possible interest rate increase coming this summer, with the possibility of additional increases in September or December. In a change of heart, markets seemed ready to accept that it was, in fact, a sign of progress that interest rates should move up from their ultra-low, emergency levels (see Table 1). Of course the door was left open with the usual 'data dependent' wiggle-room statements allowing the Fed to continue to hold off on raising rates if need be. While recent data on U.S. housing looked good (or at least better than recent history), non-farm payrolls disappointed, dropping to their lowest levels since September 2010. The upcoming rate announcements will be on June 15th and July 27th.

U.S. Presidential election: Things have started to solidify around the presumptive presidential nominees for both the Republicans and the Democrats, but this has been anything but a predictable primary season. Both Clinton and Trump have some serious fence-mending and work to be done in unifying their party supporters. How successful they are at this will largely be on display at the upcoming national conventions. The Republican convention starts on July 18, 2016, in Cleveland, with the Democratic convention starting on July 25, 2016, in Philadelphia. If the conventions are anything like the primaries, expect fiery words and a few surprises.

AHEAD BY A CENTURY *(+20YEARS)* (THE TRAGICALLY HIP: CANADIAN ROCK BAND/LEGENDS)

The Dow Jones Industrial Average turned 120 years old on May 26, 2016. The iconic blue-chip microcosm of the U.S. stock market remains one of the most widely reported indices. It's only remaining issue from the original twelve constituents from 1896? General Electric (GE). What's a $100 USD of GE shares invested in 1896 (adjusted for stock splits) worth today? About $388,000 USD. Now that's a buy and hold story!