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Market Matters
Summary for January 2019

Highlights

- All global equity markets rebound from December lows. S&P 500 has best January return in 32 years.
- U.S. Federal Reserve pauses rate hikes and signals a more accommodative stance.
- Canadian oil prices finally find relief and Canada's energy stocks rally.
- Fixed-income investors benefit from a rare synchronized rally alongside equity investors.

Best January return since 1987 brings market back to pre-December levels

All major global equity markets rebounded in January, charting a near perfect 'V' by climbing back from the sharp correction at the end of 2018. While the S&P 500 set a record by booking the best one-month start to the year in 32 years, it was bested by the S&P/TSX Composite that outperformed the S&P 500, all the European bourses and emerging markets. A strengthening Canadian loonie dampened foreign investment returns when translated back to Canadian dollars. Contrary to common convention, fixed-income investors were able to join in on the equity party with a positive monthly return of their own. As can often be the case in volatile market conditions, the pendulum of price swings and investor sentiment tend to overshoot on both the down and upside. As a result, while we welcome the relief from what we believed was an overdone price drop in December that erased most gains for 2018, we caution against believing January's upmarket trend is here to stay. Consider that an 8.5% (January's S&P/TSX Composite return) is a decent equity market return for an entire year, let alone for a month! Since we neither foresee the markets flatlining for the next 11 months, nor moving in a straight line up, **we expect volatility and modest price give-back in the near term**.

What changed? Not as much as you'd think.

Beyond a modest recovery from the December lows, we don't see enough justification for the exuberant optimism from investors as to warrant such a large gain as January delivered. Investors may recall that December's descent was precipitated on the fear of a slowing global economy, as well as a number of geopolitical issues creating uncertainty and challenging investor confidence. Specifically, the U.S. government shutdown, Brexit and

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Canadian Fixed Income[1]	Month	YTD
FTSE Canada Universe Bond Index	1.3%	1.3%
FTSE Canada All Corporate Bond Index	1.7%	1.7%

Canadian Equities[2]	Month	YTD
S&P/TSX Composite	8.5%	8.5%

	Month		YTD	
Global Equities[2]	**Local**	**CAD**	**Local**	**CAD**
S&P 500	7.9%	4.1%	7.9%	4.1%
MSCI EAFE	5.4%	2.7%	5.4%	2.7%
MSCI Emerging Markets	7.1%	4.9%	7.1%	4.9%

Currencies and Commodities (in USD)	Level	Month	YTD
CDN $	0.762	4.0%	4.0%
Oil (West Texas)	53.79	18.5%	18.5%
Gold	1,322.07	3.2%	3.2%
Reuters/Jeffries CRB Index	179.64	5.8%	5.8%

Canadian Sector Performance[2]	Month	YTD
Energy	10.6%	10.6%
Materials	6.7%	6.7%
Industrials	7.4%	7.4%
Cons. Disc.	10.6%	10.6%
Info Tech	10.0%	10.0%
Health Care	43.2%	43.2%
Financials	8.0%	8.0%
Cons. Staples	3.4%	3.4%
Comm. Services	4.5%	4.5%
Utilities	6.1%	6.1%
Real Estate	7.7%	7.7%

Local currency unless otherwise stated.
[1]Total return [2]Price only return
Source: Bloomberg

U.S./China trade disputes were top of mind. In January, as markets were rising, each of these issues remained present and of significant concern.

Some measure of (temporary) relief from the U.S. government shutdown and positive indications on U.S./China trade issues did arrive later in the month supporting some of the gains. But slowing global growth expectations haven't changed much. Better than expected economic data (e.g., U.S. job creation) emerged and, since investors may have been fearing a 'hard landing' for economic growth, the recent picture of 'better than feared' results lifted a weight off the shoulders of fretful investors. However, broadly speaking, signs still point to a moderating growth picture for global economies and estimates of economic growth and 2019 corporate earnings growth continue to be revised down in the early days of 2019.

Where we do take comfort is in the fourth quarter of 2018 corporate earnings results. With 333 S&P 500 companies and 41 out of 239 S&P/TSX Composite companies having reported so far, 60% of S&P/TSX and 72% of S&P 500 companies' earnings have beat analyst estimates, and year-over-year earnings growth is currently tracking at 5.7% and 14.3% respectively.

Later in the month, the U.S. Federal Reserve (Fed) signalled a change in their rate hiking plans, moving toward a more accommodative stance. This has spill-over implications for our own Bank of Canada that resulted in a decline for bond yields that gave fixed-income investors a much better result than they might have expected for the start of 2019. The FTSE Canada Universe Bond Index increased 1.34% in January, and corporate bonds led the charge, buoyed by confirmation from the Fed on January 30 that it would not do anything to spoil the party in the capital markets. In a change from expectations, the Fed pressed the pause button for rate hikes and signaled it's prepared to be flexible with its balance sheet winddown. This move placated investors' fears that the Fed's path to rate 'normalization' would slow economic conditions such that it could lead to a recession.

The Canadian stock market: Pot stocks get lit. Black gold rises.

Canada's high-performing sectors were exciting to watch in January. The health care sector produced an eye-popping 43.2% return as pot stocks were hot once again. The sectors' roller coaster ride continues with this the third major upswing (>40%) amongst three major downdrafts (>-30%) over the past 12-months. It is worth keeping in mind that the sector remains but a tiny component of the S&P/TSX Composite (~2%) and as such, their weighted contribution to total returns has less impact than the headlines merit (only 0.69% out of the 8.5% total return). The primary driver of the strong returns for the S&P/TSX Composite came from Canada's large energy and financial sectors. Canadian oil prices experienced a significant recovery, both in absolute terms and relative to their global oil price counter parts as differentials between Canadian Western Select and West Texas Intermediate oil prices narrowed substantially from US$50 back in October to the $US10 range now. This relief for Canada's energy patch comes on the heels of the Alberta governments decision to curtail production; not the ideal backdrop for a price recovery, and the longer-term solution of greater export capacity remains fraught with uncertainty. Canadian bank shares moved higher, rebounding from the -12.7% drubbing of Q4 2018. Buoying bank shares are the twin reliefs brought about by the move in bond yields. Lower bond yields bring some relief to the outlook for borrowing conditions in Canada and the yield moves also arrested the straight-line decline in the yield curve to one where it is now moving sideways and even a slight steepening. It's not the greatest environment for lenders, but the theme amongst many of the equity moves in January was one of a move away from the brink, toward one of 'less bad' than originally thought, or at least 'less bad' than the December lows had portent.

恭禧發財 Gong Xi Fa Cai – Year of the Pig to bring good fortune and luck. We hope so!

As China celebrates the year of the pig (a year of good fortune and luck), there's optimism growing around the current tone of U.S./China trade negotiations, and a new Chinese central bank program aimed at strengthening their banking system and a shift in fiscal and monetary policy toward a pro-growth mode. Every global expansion since the financial crisis has come in concert with a reflating Chinese economy, but these current events, while positive, are in their early stages and tenuous at best. With North America, Europe and Japan all appearing to be entering a slowing phase, the timing couldn't better for China's economy to exit its slowdown sooner rather than later. Unfortunately, it remains wishful thinking to expect the timing to line up that conveniently.

How the Chinese economy responds in the coming quarters of 2019 could mean the difference between a risk-on view of global growth (i.e., a solid global equity market performance) or a risk-off stance (i.e., a solid performance from bonds). So, while we enjoy the opportunity to celebrate the optimism that comes with the Chinese New Year celebration, we're keeping a close eye on these events as it relates to our expectations for global growth and capital markets.

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VP Marketing and Communications, has more than 15 years of investment industry experience and has been writing the monthly Market Matters for over 10 years.