Credential

Market Insights | MONTHLY

Month in Review

For the month ended February 29th, 2016

Overall Highlights

- **S&P/TSX higher.** Despite a rocky start to the year, Canada's primary equity market saw its first monthly gain of 38 points in February to close at 12,860, a rise of 0.3%. Gains in commodities and resources helped lift the index higher, as investors saw buying opportunities. In addition, a late-month reserve cut by China's central bank also helped boost markets higher.
- **Loonie soars.** After falling to 13-year lows, the Loonie rebounded in February surging 3.2% to end at US73.90 cents, an increase of two and 32/100ths cents. This is the highest the dollar has reached in 2016, as the economy begins to show positive signs, albeit small, after oil's decline.
- **Gold shines.** As the safe-haven asset, the yellow metal benefited from the market and commodity instability, ending the month at US$1,239.60 per ounce, a surge of 10.9% or US$122.30. As volatility continues with a lack of direction of the global economy and pockets of weakness seen in some countries, investors still sought the safety of gold.
- **Oil gains.** West Texas Intermediate (WTI) managed a gain in February edging higher by US$0.50, or 1.5%, to end at US$33.86 a barrel. Lower production from OPEC countries during the month helped lift the commodity higher while a move by China revitalize their economy added an extra boost to oil that has been stuck in a supply glut for over a year.
- **Inflation rises.** A rise in food, transportation, and gasoline prices pushed annual CPI to its highest level since October 2014.
- **Rise in unemployment.** The nation's jobless rate rose in January to 7.2% as the country shed 5,700 positions, all of a part-time nature.
- **Manufacturing PMI rises.** The RBC Manufacturing PMI index that measures the manufacturing sector contracted for a sixth consecutive month despite a sharp rise.
- **Retail sales decline.** December was not a merry month for retailers as sales fell at its fastest pace in five years.
- **U.S. Q4 GDP revised upward.** U.S. economic growth regressed in the 4th quarter, but at a slower pace than initially thought.
- **Fed remains firm with interest rates.** Despite recent turmoil in the stock markets and concerns about global growth, the Fed remains firm on its interest rate policy.
- **U.S. consumer sentiment drops slightly.** The University of Michigan consumer sentiment index fell slightly in February but was better than economists expected.
- **Euro-zone Q4 GDP growth positive.** The 19-member bloc posted a modest growth in Q4. Quarter-on-quarter, the GDP grew by 0.3% in Q4, matching economists' forecasts.
- **China cut reserve ratio again.** People's Bank of China (PBOC) announced further cut to its reserve requirement ratio (RRR), which was a bit of a surprise to the market.
- **Japan GDP contracts in Q4.** Japanese economy contracted an annualized 1.4% in Q4 2015, as consumer spending declined. Economists forecast Japan's GDP to shrink by 1.2% in the fourth quarter.

Index/Commodity/Currency		
Close	**MonthChange**	**YTDChange**
S&P/TSX Composite		
12,860.35	38.2	-149.6
	0.3%	-1.1%
BMO Nesbitt Burns Small Cap		
655.71	31.3	5.5
	5.0%	0.9%
Dow Jones Industrial Average		
16,516.50	50.2	-908.5
	0.3%	-5.2%
S&P 500		
1,932.23	-8.0	-111.7
	-0.4%	-5.5%
NASDAQ Composite		
4,557.95	-56.0	-449.5
	-1.2%	-9.0%
MSCI-EAFE Index		
1,558.17	-33.3	-158.1
	-2.1%	-9.2%
WTI Crude Oil (per barrel, in $US)		
33.86	0.5	-3.2
	1.47%	-8.7%
Gold (per ounce, in US$)		
1,239.60	122.3	179.1
	10.9%	16.9%
Canadian Dollar (¢ per US$)		
73.90	2.3	1.7
	3.2%	2.3%

Sources: Bloomberg, PC Bond

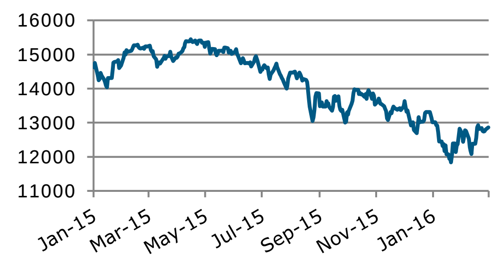
Canadian Markets

- **Inflation rises.** A rise in food, transportation, and gasoline prices pushed annual CPI to its highest level since October 2014. For the month of January, inflation rose 0.2%, doubling earlier estimates, and helped move annual inflation to 2%, midway of the Bank of Canada's target band of 1-3%. Core inflation, which excludes volatile components, also rose for the month by 0.3% raising that rate to 2% annualized.
- **Rise in unemployment.** The nation's jobless rate rose in January to 7.2% as the country shed 5,700 positions, all of a part-time nature. The falling price of oil was to blame as Alberta led the provinces in declines and pushed its unemployment rate above the national average for the first time since 1988. The labour market is expected to continue to see weakness as low oil valuations make their way through the broader economy.
- **PPI gains.** For the first time in six months, producer prices rose on greater demand for cars and their parts. In January, PPI rose 0.5%, 1.7% annually, as 18 of the 21 sectors tracked increased. Energy and petro products were the laggard for the month falling 7.3%.
- **Manufacturing PMI rises.** The RBC Manufacturing PMI index that measures the manufacturing sector contracted for a sixth consecutive month despite a sharp rise. For January, the index was 49.3, an improvement from the previous month, but sentiment still remained poor for the sector; an overall deterioration in business conditions led to lower output.
- **Manufacturing sales higher.** Output from factories rose in December rising 1.2% for the month on sales of $51.6B. This was the second straight monthly gain, which provided hope of ongoing momentum for a sector that still remains below pre-2008 levels eight years later. Most of the increase came from autos, wood products, chemicals, and transportation; however, manufacturing sales saw its first annual decline of 1.5% not seen since the financial crisis.
- **Wholesale sales gain**. For a second consecutive month, wholesale trade topped expectations on strength in the automobile and parts. For December, wholesale sales rose 2.0%, bettering estimates of 0.2%, as four of the seven sectors tracked gained, led by motor vehicles and parts (+10.6%) followed by the food, beverage, and tobacco sector at 1.3%.
- **Retail sales decline.** December was not a merry month for retailers as sales fell at its fastest pace in five years. For the month, sales were lower by 2.2%, more than the -0.4% expected by economists, with receipts tallying $43.2B. Most of the decline can be attributed to lower vehicle sales, but also the shifting of retail activity into November, to coincide with the U.S. Black Friday.
- **Canada housing news:**
  - **Housing starts fall**. Fewer new homes broke ground primarily in Quebec and Western Canada. For January, 165,861 units were started on an annualized basis, down from December's 172,533. Multi-home dwellings fell 5.3% for the month, while the single-detached segment declined by 1%.
  - **Building permits higher**. Following an almost 20% decline in new home applications in November, building permits bounced back in December rising 11.3%. An increase in multi-family units in Quebec, B.C., Ontario, and Alberta were the month's drivers of the 16.3% rise in the residential sector. Non-residential intentions rose as well by 2.5%.
  - **New home prices edge up.** The price of a new home rose in December by 0.1%, Statistics Canada reported. Prices in Toronto and Vancouver continued to move the national average higher, where prices are 1.6% higher compared to a year earlier. Seven of the 21 cities tracked remain unchanged. Of the three decliners, Calgary's housing market was hit hard due to the slump in oil.
  - **Existing home sales higher.** Low supply and high demand continue to drive the real estate market, especially in Toronto and Vancouver. For January, sales of existing homes bounced back from a December decline, rising 0.5%, compared to a year earlier, where sales have risen 8%, based on a non-seasonally adjusted basis.

S&P/TSX Composite Index
Sector Snapshot

Sector	Month Return	YTD Return	Weight (%)
Energy	-1.53	-1.05	18.50
Telecoms	3.31	6.94	5.90
Industrials	1.44	-1.75	8.20
Consumer Staples	3.81	5.69	4.80
Utilities	-5.15	0.32	2.30
Financials	-2.65	-4.24	37.00
Consumer Discretionary	3.22	-3.49	6.70
Health Care	-23.30	-30.43	2.20
Materials	17.80	15.46	11.20
Information Technology	0.92	-2.74	3.20

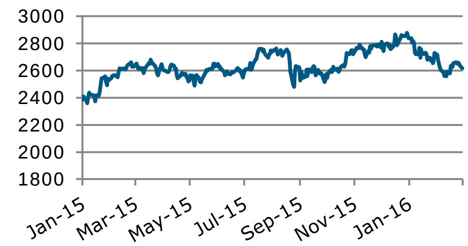
S&P/TSX Composite - 1Y Return



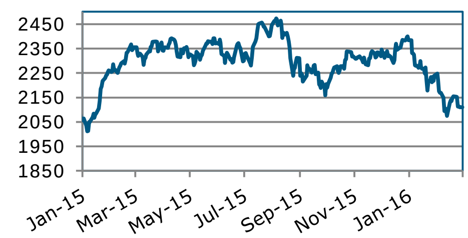
U.S. Markets

- **U.S. markets stabilize after big dive in January.** After a bad start to the year in January, the U.S. stock market stabilized in February on crude oil prices and the Chinese yuan currency. The broad-based S&P 500 index dropped slightly by 0.4%, closing the month at 1,932, while the Dow Jones Industrial Average posted a small gain of 0.3% to end at 16,517. The Nasdaq, however, fell the most among the three, declining by 1.2%, closing the month at 4,558.
- **U.S. Q4 GDP revised upward.** U.S. economic growth regressed in the 4th quarter, but at a slower pace than initially thought. The Commerce Department released its second estimate of the Q4 2015 economic growth rate reporting growth by 1% in the 4th quarter, which was higher than the first estimate of 0.7%, and way better than economists' forecast for a revised-down 0.4%. The improvement came mostly from inventory investment which was reported to be $68.6 billion in the first estimate and was revised up to $81.7 billion in the second estimate.
- **Fed remains firm with interest rates.** Despite recent turmoil in the stock markets and concerns about global growth, the Fed remains firm on its interest rate policy. In her testimony to the Congress, Fed Chairwoman Janet Yellen believed that the U.S. economy will continue to grow which would allow the Fed to pursue its plan of gradual rate hikes this year. Yellen kept the options open though "I think we want to be careful not to jump to a premature conclusion about what is in store for the U.S. economy. I don't think it is going to be necessary to cut rates."
- **Job growth slows but unemployment rate drops.** According to the Labor Department, U.S. non-farm payrolls increased by 151,000 in January, less than the 190,000 gains estimated by economists. However, the unemployment rate dropped to 4.9%, the lowest level since February 2008; economists forecast the unemployment will stay at 5%.
- **U.S. consumer sentiment drops slightly.** The University of Michigan consumer sentiment index fell slightly in February but was better than economists expected. The sentiment index was reported to be 91.7 in February, lower than January's final reading of 92.0 but was better than economists' estimate of 91.0.

S&P 500 - 1Y Return (CAD)



MSCI EAFE – 1Y Return (CAD)



- **U.S. retail sales better than expected.** Consumer spending regained some momentum in January. The Commerce Department reported that overall retail sales increased by 0.2% in January, the same pace as it was in December and was higher than economists' estimated rise of 0.1%. The core retail sales, which excludes automobiles, gasoline, building materials, and food services increased by 0.6% in January after a 0.3% fall in December.
- **U.S. durable goods orders jumps.** Durable goods orders rebounded from December's decline, posting the strongest increase in 10 months. The Commerce Department reported that January's durable goods orders rose by 4.9%, reversing December's decline of 4.6%; economists forecast durable goods orders to rebound by 2.5% only in January. Core capital goods orders, which excludes aircraft, rose 3.9% after tumbling by 3.7% in December.
- **U.S. wholesale inventories drop.** Wholesale inventories fell for the third straight month in December as businesses continued to reduce unsold items in storage. The Commerce Department reported that wholesale inventories dropped 0.1% in December after a 0.4% drop in November. Economists expected a 0.2% drop in December. A record inventory accumulation in the first half of 2015 had weighted heavily on manufacturing.
- **U.S. core CPI increases.** The overall consumer price index (CPI) remained unchanged in January but the core CPI posted its largest gain in 4-1/2 years. The Labor Department reported that CPI remained unchanged from December, but the core CPI, excluding food and energy, increased by 0.3%, the biggest gain since August 2011. Economists estimated the core CPI to move up by 0.2% only. Year-on-year, overall CPI rose by 1.4%, and core CPI increased by 2.2%, the biggest rise since June 2012.
- **U.S. manufacturing sector remains in contraction.** According to the Institute for Supply Management (ISM), U.S.'s manufacturing sector continued to be in contraction mode, but was shrinking at a slower pace as compared to the previous month. The ISM index of national factory activity rose from November's 48.0 to 48.2 in December, slightly better than economists' projection of 48.1. A reading below 50 indicates that the sector is in contraction.
- **U.S. housing news:**
  - **U.S. housing starts fall.** Housing starts unexpectedly fell in January, but it may be due to bad weather. The Commerce Department reported that starts fell 3.8% in January to a seasonally adjusted annual pace of 1.099 million units, lower than economists' estimate of a 1.17 million-unit pace and a drop from December final number of 1.143 million-unit rate. It was believed that part of the decline was due to the snowstorms hitting the northeast region last month.
  - **U.S. building permits dip.** Building permits dropped by 0.2% to a seasonally adjusted 1.202 million-unit pace in January. The number was above economists' forecast of a 1.200 million-unit pace. Permits for single-family home fell 1.6%, but permits for multi-family building increased by 2.1%.
  - **U.S. new home sales dive.** New single-family home sales tumbled in January as sales in the West region dove. The Commerce Department reported that single-family home sales dropped 9.2% in January to a seasonally-adjusted pace of 494,000 units after big jump in December; economists expected sales to slip to a 520,000-unit pace. Sales in the West plunged by 32.1%, the biggest percentage decline since May 2010.
  - **U.S. existing home sales increase.** Existing home sales unexpectedly jumped to a six-month high in January, according to the National Association of Realtors. Existing home sales increased by 0.4% to a seasonally adjusted annual pace of 5.47 million units, the highest level since July. Economists had expected sales to decrease by 2.9% to an annual pace of 5.32 million units. Year-over-year, sales were up 11% in January.
  - **U.S. home prices rise.** Home prices in U.S. continued to rise in December, despite at a slower pace than expected. The S&P/Case-Schiller 20-City Home Price Composite moved up 5.7% year-over-year in December, slightly missing economists' estimate for a rise of 5.9%. The highest year-over-year gain continued to come from Portland, Oregon (11.4%), San Francisco (10%), and Denver (10%).

European Markets

- **Euro-zone Q4 GDP growth positive.** The 19-member bloc posted a modest growth in Q4. Quarter-on-quarter, the GDP grew by 0.3% in Q4, matching economists' forecast; year-on-year, GDP grew by 1.5%, also in line with economists' estimate. Germany remained the economic locomotive of the region, whereas Greece and Finland's economy contracted in the final quarter of 2015.
- **ECB will take action if required.** ECB's president Mario Draghi assured the market that the ECB will act to make sure its monetary policy will reach the real economy. Of particular concerns lately for Mr. Draghi include the turmoil in the European stock market, especially the bank sector, and the continuous decline in energy prices, which has been a drag on prices. Mr. Draghi said in his speech to the European Parliament "if either of these two factors entail downward risks to price stability, we will not hesitate to act."
- **Euro-zone unemployment falls.** Euro-zone labour market conditions continued to improve in December, dropping to a 4-year low. The region's jobless rate fell to 10.4% from the 10.5% reported for November, according to Eurostat. Economists predicted the jobless rate to remain at 10.5% in December. December's unemployment rate was the lowest level recorded since September 2011.
- **Euro-zone price level falls.** Price level within the 19-member bloc fell in February, providing further support for another round of policy easing by the ECB on March 10. Headline inflation was reported to be -0.2% in February, a drop from 0.3% reported in January and missed economists' expectations for unchanged prices. Core inflation, which excludes food and energy, dipped 0.8%, which could be an indication that the stubbornly low oil prices were feeding into the price of goods and services.

Asian Markets

- **China cut reserve ratio again.** People's Bank of China (PBOC) announced further cut to its reserve requirement ratio (RRR), which was a bit of a surprise to the market. The PBOC announced to cut its RRR by 50 bps after the stock market close on February 29th to maintain ample supply of liquidity in the system. It was the fifth time that the PBOC cut the ratio since February 2015; with the last cut on October 23rd.
- **China's CPI and PPI diverges.** China's consumer price index (CPI) rose, but producer price index (PPI) posted back-to-back decline, a continuing divergence that might reflect a structural change in China's economy. CPI quickened to 1.8% year-on-year in January, compared to 1.6% posted in December and economists' estimate of 1.9%. PPI fell by 5.3% in January year-on-year, a drop from December's 5.9%; it was the 47th consecutive month PPI posted a decline.
- **China's exports and imports worse than expected.** China's trade data in January disappointed, adding to worries about the health of the world's second largest economy. Year-on-year, exports was down 11.2%, a lot worse than the 1.8% decrease expected by economists. The decline was broad-based ranging from developing countries to developed countries. Import felt 18.8% from a year ago, also way below the 3.8% decline economists were expecting. As a result of the big dive in imports, China's trade surplus jumped to a record $63.3 billion.
- **China's manufacturing PMI rises, but remains below 50.** The most recent Caixin China manufacturing purchasing managers' index (PMI) indicated that China's manufacturing sector remained in trouble. January's manufacturing PMI was reported to be 48.4, a slight improvement from December's 48.2. It marked the 11th consecutive month that the private gauge was below the 50-mark, meaning the sector remained in contraction mode. Caixin's data also showed that China's manufacturers have been in layoff mode for 27 months.
- **Japan GDP contracts in Q4.** Japanese economy contracted an annualized 1.4% in Q4 2015, as consumer spending declined. Economists forecast Japan's GDP to shrink by 1.2% in the fourth quarter. Private consumption, which makes up 60% of GDP, declined 0.8% in Q4, higher than economists' estimate for a decline of 0.6%.
- **Japanese government bond yield below zero.** Japan 10-year benchmarks bond yield fell below zero for the first time. The 10-year yield touched -0.05% on Tuesday as investors sought shelter for their money with the existing market conditions. With safe-haven buying pouring into the Japanese Yen, this pushed the Yen to its 15-week high, which contrasted the Nikkei 225 index, which dropped 5.4% on the same day.

Key Take-aways:

- The Canadian dollar has rebounded to becoming one of the best performing currencies in 2016 so far, up over 8% since touching a 13-year low in January. Following oil's precipitous decline, starting in late 2014, the weakness of the U.S. dollar, along with improvements in our economy, have renewed investor confidence to move back towards Canada. The currency, however, still remains highly correlated to the price of oil and will continue to see volatility going forward.
- Annual inflation is sitting comfortably within the target range preferred by the Bank of Canada. However, this not necessarily good news, especially if inflation continues to rise. The Central Bank's main weapon against inflation is increasing its key interest rate, which was lowered twice in 2015 to spur economic growth. The Bank of Canada's next meeting on rate policy is scheduled for early March.
- The manufacturing sector is starting to see some recovery after difficulty in gaining any growth momentum as Canada's economy continues to slump on low commodity and resource valuations. We see the sector's recovery being long and drawn out despite a low interest rate environment and weak Canadian dollar, which should promote business investment and increasing exports.
- Gold is anticipated to continue to be the "Go-To" asset as long as market volatility persists. The metal remains a safe-haven asset since its value cannot be manipulated by interest rate policies and has traditionally been considered a hedge against inflation.
- Following the remarks by Fed Chairwoman Janet Yellen, the U.S. central bank will likely take a wait-and-see approach to its monetary policy given the rout occurring in global markets. While a few of the world's central banks have taken the position of enacting negative interest rates, essentially charging banks to hold cash in reserves, it's too early to know if the Federal Reserve is even considering this path - given it just raised its key rate for the first time in almost a decade.
- Chinese trade continues to be weak, as the latest data from January on exports and imports were lower than the previous month's. China is expected to maintain strong growth relative to the rest of the world, but at a slower pace than in the past.

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