Credential

Market Insights | MONTHLY

Month in Review

For the month ended August 31st, 2016

Index/Commodity/Currency		
Close	**MonthChange**	**YTDChange**
S&P/TSX Composite		
14,597.95	15.2	1,588.0
	0.1%	12.2%
BMO Nesbitt Burns Small Cap		
830.16	-3.2	180.0
	-0.4%	27.7%
Dow Jones Industrial Average		
18,400.88	-31.4	975.9
	-0.2%	5.6%
S&P 500		
2,170.95	-2.7	127.0
	-0.1%	6.2%
NASDAQ Composite		
5,213.22	51.1	205.8
	1.0%	4.1%
MSCI-EAFE Index		
1,685.57	-3.5	-30.7
	-0.2%	-1.8%
WTI Crude Oil (per barrel, in $US)		
44.77	3.3	7.7
	8.04%	20.8%
Gold (per ounce, in US$)		
1,311.60	-46.3	251.1
	-3.4%	23.7%
Canadian Dollar (¢ per US$)		
76.24	-0.4	4.1
	-0.5%	5.6%

Sources: Bloomberg, PC Bond

Overall Highlights

- **S&P/TSX sees a gain.** The TSX Composite managed a small gain for the month amidst volatility in commodity and resources, and weak economic data. On the close, the Index rose 15 points or 0.10%, to end at 14,598, as investors looked to the Federal Reserve for a signal on interest rates and indicators from the markets which are perceived as becoming increasingly overvalued.
- **Q2 GDP plummets.** Not since the Financial Crisis has Canada's economic output been so weak; second quarter GDP contracted 1.6%, wiping out the majority of Q1's revised 2.5% growth. The reading should not come as much of a surprise as May's Alberta wildfires was responsible for 1.1% of Q2's loss, as reported by StatCan. Quarterly growth would have been worse had June's monthly GDP gain of 0.6% not offset the loss in May by the same amount.
- **Canada loses jobs.** The Canadian economy shed 31,200 jobs in July, a lot higher than the 10,000 reductions estimated by economists. The unemployment rate increased from 6.8% to 6.9%. 71,400 full-time positions were lost, the largest one-month decline since October 2011. Job market was also tough on young workers as 28,000 jobs were cut for workers between the ages of 15-24. British Columbia was the lone bright spot in the report, gaining 12,000 jobs, while most other provinces saw decline.
- **Dollar lower.** The Loonie was mostly positive in August until the final day of the month, when Q2 GDP growth disappointed. At month's end, the Canadian dollar trimmed by 35/100ths of a U.S. cent, or -0.5 %, to close at 76.24 U.S. cents. Working against our currency was the resurgence of the U.S. greenback; it strengthened on the rising probability of a rate hike in September following comments from the Fed.
- **Gold drops.** The rush towards this safe-haven asset following the Brexit vote was short-lived. The yellow metal fell steeply in August as the U.S. economy continues to remain strong, and a rate hike seems likely. For August, gold shed US$46.30 an ounce, or -3.4%, to close at US$1,311.60.
- **Oil moves higher.** News of coordinated output cuts from global producers generated optimism for crude, but was followed by renewed pessimism of lower demand, and as a result, oil moved up and down during the month. As the month drew to a close, crude was on the downtrend as U.S. inventories were higher than expected. Regardless, a barrel of West Texas Intermediate (WTI) still ended higher than the previous month, at US$44.77, an increase of 8% or US$3.33.
- **Canada Inflation falls.** The cost of a notional basket of goods was cheaper in July as CPI fell 0.2% from the month earlier.
- **FOMC Minutes Release.** The Federal Reserve kept its benchmark interest rates unchanged in July.
- **Yellen speaks at Jackson Hole summit.** Yellen said that the Federal Open Market Committee "continues to anticipate that gradual increases in the federal funds rate will be appropriate over time to achieve and sustain employment and inflation near our statutory objectives."
- **U.S. Q2 GDP growth revised down.** U.S. second quarter GDP growth was revised down slightly to 1.1% from the first estimate of 1.2.
- **Euro-zone GDP growth slows.** GDP growth within the 19-member economic zone slowed to 0.3% in Q2.
- **Japan approves fiscal stimulus.** In an attempt to jump start the sluggish economy, Prime Minister Shinzo Abe announced the approval of a 28 trillion yen fiscal program including 7.5 trillion yen in new spending over the next two years.
- **China's inflation eases.** China's consumer inflation slowed down in July, easing to 1.8% in July year-over-year, a drop off from June's 1.9% increase.

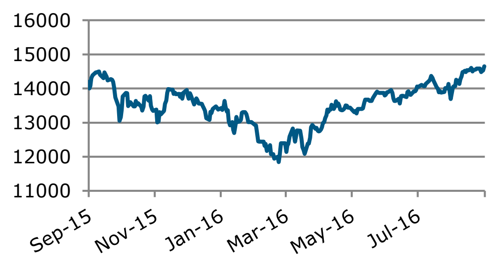
Canadian Markets

- **Canadian manufacturing sector grows.** Canadian manufacturing sector edged higher in July. The RBC Canadian manufacturing purchasing managers' index (PMI) rose from June's 51.8 to 51.9 in July. Domestic consumption helped offset the slowdown in exports. The index of new export orders dropped to 48.4 from 50.2 reported in June; weak demand from Asia explained the bulk of the slowdown.
- **Inflation falls.** The cost of a notional basket of goods was cheaper in July as CPI fell 0.2% from the month earlier. Fuel and clothing fell while consumers paid more for seafood. On an annualized basis, inflation fell to 1.3% from 1.5% and lower than the 1.4% expected from economists. Core inflation remained unchanged in July at 2.1%.
- **PPI gains.** The cost of goods leaving Canada's factories rose in July, driven by higher prices on metal products. For the month, the Producer Price Index gained 0.2%, bettering analyst expectations for a loss of 0.3%. The tracking of 21 sectors saw 13 posting gains particularly in gold and silver as the Brexit vote was seen as the reason for their demand. On an annual basis, PPI have fallen 1.3% from the same period last year.
- **Factory sales rise.** Manufacturing rebounded in June as factory sales rose 0.8%, bettering forecasts and reversing a 1.0% slump in May. Total sales were valued at $50.2B, led by machinery and transport equipment. Of the 21 industries followed, 15 saw gains as the surprise reading stoked hopes of growth momentum in the sector.
- **Retail sales slip.** Consumers were less inclined to spend as retail sales fell in June by 0.1% as seven of the 11 sectors tracked saw declines. Food, building material, and clothing were notable areas that saw decline as analysts had predicted a 0.5% gain for the month. Consumer spending is a large component of GDP expansion and its stalling may make its growth momentum more difficult.
- **Wholesale sales gain.** For a third straight month, sale receipts to entities other than the end consumer rose, providing some optimism for economic growth, albeit slow-moving. In June, wholesale sales rose 0.7% to $56.4B, higher than the 0.1% expected by analysts but slower than the 1.9% in the previous month. The data follows manufacturing sales numbers reported earlier and a glimmer of growth as wholesale volumes rose as well by 0.6%.
- **Canada Housing News:**
  - **Housing starts drop.** Housing starts fell in July, and the drop was broad-based. The Canadian Mortgage and Housing Corp reported that housing starts declined to a seasonally adjusted annualized rate of 198,395 units in July, a drop from June's 218,326 units. The value of building permits dropped in June, declined by 11.5% and 8.4% in British Columbia and Ontario respectively.
  - **Canadian housing prices increase.** House prices in Canada continued to climb. According to the Teranet-National Bank Composite House Price Index, prices rose by 2% in July nationwide when compared to June; year-over-year, prices were up 10.9%.
  - **Existing home sales lower.** In July, for the third straight month, homes sales fell by 1.3% nationally, with most of the declines coming in the Vancouver (-6.7%) and Fraser Valley (-14.0%) markets.

S&P/TSX Composite Index
Sector Snapshot

Sector	Month Return	YTD Return	Weight (%)
Energy	2.34	19.35	20.0
Telecoms	-1.99	15.01	5.4
Industrials	2.86	15.55	9.0
Consumer Staples	4.81	12.60	4.4
Utilities	-3.24	14.07	2.8
Financials	1.56	7.60	35.8
Consumer Discretionary	1.59	5.95	6.2
Health Care	13.83	-66.65	0.9
Materials	-9.92	45.11	12.7
Information Technology	1.40	4.02	2.9

S&P/TSX Composite - 1Y Return

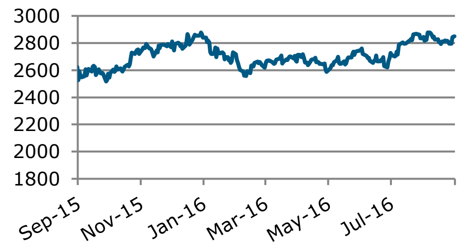


U.S. Markets

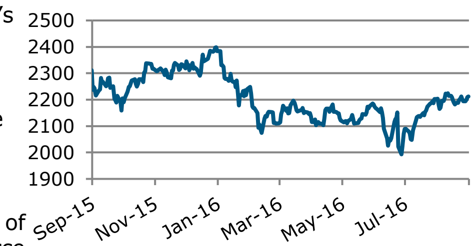
- **U.S. market moves sideways.** The U.S. stock market had a rather quiet August. All three major indices ended the month without major movements. The broad-based S&P 500 moved down 0.1%, ending the month at 2,171. The Dow Jones Industrial Average lost 0.2% for the month, closing at 18,401. Nasdaq was the biggest mover among the three, advancing 1%, wrapping up the month at 5,213.
- **FOMC Minutes Release.** The Federal Reserve kept its benchmark interest rates unchanged in July. In the Federal Open Market Committee (FOMC) meeting minutes released this week, officials were divided over the urgency of a rate hike. Those who wanted to see it soon believed that the economy is strong enough to warrant at least one rate hike this year, especially with a close to maximum employment job market. Those who preferred to defer raising rates suggested that inflation remains tamed and the impact from Brexit on global growth has not surfaced.
- **Yellen speaks at Jackson Hole summit.** Federal Reserve Chair Janet Yellen gave a speech at the annual Jackson Hole Summit. Market participants were looking for cues from her speech on interest rate movement in the near future. Yellen said that the Federal Open Market Committee "continues to anticipate that gradual increases in the federal funds rate will be appropriate over time to achieve and sustain employment and inflation near our statutory objectives." She also added "...I believe the case for an increase in the federal funds rate has strengthened in recent months."
- **Q2 GDP growth revised down.** U.S. second quarter GDP growth was revised down slightly as businesses continued to unload inventories. The Commerce Department revised Q2 GDP growth to 1.1% from the first estimate of 1.2%. The revision was in line with economists' expectations. Business inventories were reported to fall by $12.4 billion in Q2 instead of the $8.1 billion originally reported. However, consumer spending was revised up to a 4.4% growth from the first estimate of a 4.2% growth.
- **Economy adds more jobs than expected.** The Labor Department released the job numbers for July, and the result blew past expectations. The U.S. economy pumped out 255,000 new jobs in July, handily beating economists' estimate for an increase of 180,000. Unemployment held steady at 4.9%. Job creations were broad-based, occurring across a range of industries and different wage groups.

- **Inflation stays tame.** U.S. consumer prices were unchanged in July according to the Labor Department. July's consumer price index (CPI) was reported to be unchanged in July, matching economists' forecast. In the 12 months through July, CPI increased by 0.8%, slightly missing economists estimate of a 0.9% increase. Core CPI, which excludes food and energy prices, edged up 0.1% in July; year-over-year, core CPI increased by 2.2%.
- **PPI falls.** Producer prices in U.S. unexpectedly fell in July. The Labor Department reported that its producer price index (PPI) dropped 0.4% in July, the first drop since March, missing economists' forecast for a gain of 0.1%. In the 12 months through July, PPI declined by 0.2%. A strong US dollar and low oil prices have been keeping price pressures tamed. Core PPI, which excludes food and energy, was flat in July. In the 12 months through July, core PPI increased by 0.8%.
- **Industrial production rises.** As the headwinds of weak oil price and a strong dollar faded, U.S. industrial production posted its largest increase in more than a year. The Federal Reserve reported that industrial production jumped up 0.7% in July, the largest advance since November 2014. Industrial production in U.S. had been affected by a strong US dollar, which affected U.S. exporters' competitiveness abroad, and weak commodity prices, which hit miners' bottom line.
- **U.S. 'flash' PMI weakens.** Despite remaining above the 50-mark, both manufacturing and service sector 'flash' PMI weakened from the previous month in August. Markit's manufacturing 'flash' purchasing managers' index (PMI) fell to 52.1 in August from July's 52.9. Service sector 'flash' PMI was reported to be 50.9 in August, a drop off from July's 51.4 and the lowest level since February.
- **ISM indices drop.** U.S. manufacturing sector grew slower in July. The Institute for Supply Management (ISM) reported that its manufacturing index dropped from June's 53.2 to 52.6 in July, slightly lower than economists' estimated reading of 52.7. Despite the drop, it was the fifth straight month the gauge was above the 50 division line. Its nonmanufacturing index fell to 55.5 from June's 56.5. Economists were expecting the gauge to fall to 56.0.
- **U.S. retail sales unchanged.** Retail sales were flat in July, pointing to moderation of consumer spending that could negatively affect Q3 GDP growth. The Commerce Department reported zero growth for retail sales in July compared to June's rise of 0.8%, missing economists' forecast for a rise of 0.4%. Year-over-year, retail sales rose 2.3%.

S&P 500 - 1Y Return (CAD)



MSCI EAFE – 1Y Return (CAD)



- **Consumer spending increases.** Consumer spending continued to climb in July. The Commerce Department reported that consumer spending rose 0.3% in July after increasing 0.5% in June. July's rise was on par with Economists' expectations. It was the fourth straight month consumer spending was moving upward. On a year-over-year basis, consumer spending grew at 4.4%, the fastest pace in nearly two years.
- **Consumer sentiment falls.** Consumers were feeling slightly less optimistic in August, according to the University of Michigan's Index of Consumer Sentiment. The index final reading dropped to 89.8 from July's final reading of 90.0; economists were expecting a final reading of 90.6 for August. It was also a drop off from the preliminary reading of 90.4.

- **U.S. housing news**
  - **Building permits fall.** The Commerce Department reported that building permits for July dipped 0.1% to a seasonally adjusted annual pace of 1.15M units; economists were expecting a gain of 0.6% to a 1.16m unit pace.
  - **Housing starts rises.** Housing starts in U.S. unexpectedly rose in July. The Commerce Department reported that groundbreaking climbed 2.1% to a seasonally adjusted annual pace of 1.2M units, the highest level since February. Economists forecast housing starts to drop slightly to a 1.18M unit pace.
  - **Home prices climbs.** Home prices continued to climb but at a slower pace. The S&P's CoreLogic Cash-Shiller 20-city home price index for June was reported to rise 5.1% year-over-year, a slowdown from June's 5.3% pace and was the slowest year-over-year pace since last August. Home prices in Portland, Seattle, and Denver continued to lead the pack, rising 12.6%, 11%, and 9.2% respectively.
  - **Pending home sales rise.** Low mortgage rates and steady demand continued to propel the housing market in U.S. The National Association of Relators' pending home sales index rose 1.3% to 111.3 in July, higher than economists' expected increase of 0.7%. Year-over-year, pending home sales rose 1.4% in July.

European Markets

- **Bank of England cuts interest rates.** In an effort to cushion the impact of Brexit on the U.K. economy, Bank of England (BOE) acted proactively by cutting interest rates and expanding its stimulus package. The BOE reduced its benchmark interest rates for the first time since March 2009 from 0.5% to 0.25%. It also announced plans to pump 65 billion pounds to buy government bonds and 10 billion pounds to buy corporate bonds. As much as 100 billion pounds will be injected into the banking system to help banks pass on the base rate cut to borrowers.
- **Euro-zone GDP growth slows.** GDP growth within the 19-member economic zone slowed in Q2. Eurostat reported GDP growth within the bloc expanded by 0.3% in the second quarter; that matched economists' expectations and was only half of Q1 growth. When compared with the same quarter last year, GDP was up 1.6%. France and Italy contributed to the slowdown as both countries reported no growth in the quarter. The economic locomotive within the zone, Germany, reported a Q2 growth of 0.4%, better than economists' estimated 0.2%.
- **Euro-zone 'flash' PMI rises.** Euro-zone 'flash' composite purchasing managers' index (PMI) moved up to 53.3 from July's 53.2, a seven-month high. Economists were expecting a slight fall to 53.1. France's composite PMI unexpectedly grew to 51.6 from July's 50.1, which helped pushing up the aggregate figure. Composite PMI of Germany, the region's economic locomotive, dropped from July's reading of 55.3 to a two-month low of 54.4 in August.

- **Euro-zone producer prices rise**. Producer price level within the Eurozone rose more than expected in June. Eurostat reported that its producer price index increased by 0.7% month-over-month in June, the second consecutive month of increase. Year-over-year, producer prices declined by 3.1%. Both figures were higher than economists' forecast of a month-over-month rise of 0.4% and a year-over-year decline of 3.5%.

Asian Markets

- **Disappointing economic data out of China.** China reported disappointing economic data last week. Retail sales of the world's second largest economy rose 10.2% year-over-year in July compared to June's 10.6% increase; economists were expecting a 10.5% rise. Industrial output increased by 6% year-over-year in July, missing expectations for a 6.2% rise. Fixed asset investment rose 8.1% in the first seven months of 2016, also missing economists' estimated 8.9% growth.
- **China's inflation eases.** China's consumer inflation slowed down in July, increasing the likelihood of more monetary easing from the central bank. The consumer price index rose 1.8% in July year-over-year, a drop off from June's 1.9% increase. On the other hand, the producer price index posted its 52nd consecutive month of decline, albeit at a slower pace of 1.7% compared to June's 2.6% decrease
- **China's official manufacturing PMI falls.** In July, China's official manufacturing purchasing managers' index (PMI) dropped from previous month's 50.0 to 49.9, missing economists estimate of 50.0. The gauge for the health of large state-owned companies went below 50.0 for the first time since May, indicating the sector was in contraction mode. In contrast, the Caixin's PMI, which tracks small and medium-sized companies, surprisingly increased to 50.6 from June's 48.6.
- **Japan approves fiscal stimulus.** In an attempt to jump start the sluggish economy, Prime Minister Shinzo Abe announced the approval of a 28 trillion yen fiscal program including 7.5 trillion yen in new spending over the next two years. The government will pump money into infrastructure projects, aiming at helping the export sector and tourism.
- **Japan Q2 GDP growth stalls.** Despite aggressive stimulus measures, Japan's economic growth saw no big improvement. The world's third largest economy posted an annualized growth of 0.2% in the second quarter, a big drop off from Q1 growth of 2% and missing economists expected 0.7% growth. Private consumption, which accounts for roughly 60% of GDP, rose 0.2% in Q2, slowing down from the 0.7% growth reported in Q1.
- **Japan's unemployment rate falls.** Despite a stagnant economy, Japan's unemployment rate dropped to a 21-year low. July's seasonally-adjusted unemployment rate was reported to be 3%, dropping from June's 3.1%. Household spending, which accounts for about 60% of the economy, slipped 0.5% year-over-year in July, better than economists' estimate for a 0.9% drop.
- **Japan's consumer inflation continues to slide.** The core gauge on inflation monitored by the Bank of Japan (BOJ) fell in July, adding more pressure to BOJ Governor Haruhiko Kuroda to announce more stimulus in the central bank's next meeting in September. The consumer price index, which includes fresh food prices, fell 0.5% year-over-year in July. Economists forecast a decline of 0.4%. It was the fifth straight month that consumer prices were reported to be lower.

Key Take-aways:

- **Job data trend:** The employment pictures between Canada and U.S. continued their divergence in July. Canada saw another raise in unemployment rate accompanied by a slash in full-time jobs. Although the unemployment rate in U.S. remains unchanged, the fact that the job openings went up, and of broad-based nature, was encouraging. As the next scheduled FOMC interest rate meeting is not until Sep 21, it remains to be seen how July's data will impact decision for an interest rate hike. The relative weakness in Canada, however, brought downward pressure to the Loonie vs. USD, and offset all the gains during the week.

- **Canada's inflation remains sluggish.** Rising price growth is one sign of a strengthening economy. Tellingly, this remains lacking in the Canadian economy as inflation continues to have difficulty in gaining traction and fell during the month of July to 1.3% annualized. This decline has mainly been attributed to the Alberta wildfires in May, as its effects continue to work its way through the economy, but has also been blamed on the global slowdown that has begun to affect even the robust U.S. economy. Inflation data, targeted at 2%, plays an important role in determining the positioning of the Bank' of Canada's key interest rate (i.e., whether it should be cut or hiked higher).

- **Fed to hike soon?** Held in a holding pattern over the summer, activity is starting to brew at the U.S. central bank. With a quiet week of economic activity, most eyes and ears were pointed towards the annual Economic Symposium in Jackson Hole, Wyoming where the Federal Reserve is a key speaker. With a December hike becoming more of a possibility, in her speech, Chairwoman Janet Yellen stoked the markets with suggestions of a potential increase as early as September - at the next FOMC meeting. This was also iterated by Vice Chairman Stanley Fischer as economic data is becoming aligned to support a rate rise. In response, the U.S. dollar gained strength against all major currencies, including the Canadian dollar. In Canada the effects will be felt in the manufacturing sector, which has been struggling to gain growth traction.

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