GLC ASSET MANAGEMENT GROUP

Market Matters

FEBRUARY HIGHLIGHTS

- Global equity markets were strong across the board in February as investors continued to gain confidence in a U.S. economic recovery, and progress was afoot over the latest Greek debt crisis.
- Bond markets weakened modestly as investors regained interest in equity markets.
- Oil prices rose strongly as tensions in the Middle East threatened to magnify into a significant supply disruption.
- The Canadian dollar rose above par with the U.S. dollar, boosted by the rising price of oil.

Table 1
Summary of major market developments

Market returns*	February	YTD
S&P/TSX Composite	1.5%	5.8%
S&P500	4.1%	8.6%
- in Canadian dollars	*2.2%*	*5.4%*
MSCI EAFE	5.3%	9.3%
- in Canadian dollars	*4.1%*	*7.5%*
MSCI Emerging Markets	4.4%	12.1%
DEX Bond Universe**	-0.4%	0.1%
BBB Corporate Index**	0.5%	1.8%

*local currency (unless specified); price only
**total return, Canadian bonds

Table 2
Other price levels/change

	Level	February	YTD
U.S. dollar per Canadian dollar	$1.0135	1.8%	3.0%
Oil (West Texas)*	$107.14	8.8%	8.2%
Gold*	$1,735	0.2%	10.2%
Reuters/Jefferies CRB Index*	$322.43	3.2%	5.6%

*U.S. dollars

Table 3
Sector level results for the Canadian market

S&P/TSX Composite sector returns*	February	YTD
S&P/TSX Composite	1.5%	5.8%
Energy	2.5%	6.1%
Materials	-1.8%	8.4%
Industrials	-0.9%	1.7%
Consumer discretionary	5.5%	9.0%
Consumer staples	-1.3%	-1.5%
Health care	8.2%	12.6%
Financials	3.4%	6.1%
Information technology	-2.1%	4.1%
Telecom services	-0.2%	-2.7%
Utilities	3.1%	1.9%

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

ONE HURDLE AT A TIME

Investor confidence continued to strengthen in February, driving a broad advance in global stock markets (see Table 1). U.S. economic indicators showed strength and revealed an economic recovery that is finally gaining traction. Likewise, investors were pleased that progress was made toward helping Greece clear its latest debt-hurdle.

In time to mark the third anniversary of the bear market low (on March 9, 2009), investors felt confident enough to return to equity markets. Most notably, the American S&P500 managed back-to-back monthly gains of more than four per cent (USD). According to statistics gathered by Standard and Poor’s, in the two short months of 2012, stocks regained all their 2011 losses - a tidy sum of over $3 trillion (USD).

RESULTS CLOSER TO HOME

The Canadian S&P/TSX Composite joined global peers with a decent monthly advance, although sector results were mixed. Strong earnings results from Canadian banks helped the Financial sector, while a sharply rising oil price bumped the Energy sector higher. Rounding out the big three sectors on the Canadian stock market, the Materials sector did not fare as well. This was in part due to gold companies continuing to find themselves under pressure from rising production and operation costs.

Better economic news is starting to be reflected in modestly rising bond yields (albeit still very low), and the loss of demand from less risk-averse investors resulted in the Canadian bond market down slightly for the month of February.

BEING NEIGHBOURLY

There has been a string of positive economic surprises in the U.S. recently (e.g. an improving job market, which is making an important contribution towards the U.S. housing market recovery), all amounting to confidence in the U.S. recovery continuing. Given that the U.S. is Canada’s biggest trading partner, improved economic performance in the U.S. will have a spill-over effect, and could signal a growing appetite for Canadian manufactured goods and commodities such as oil and metals. Cross border manufacturing linkages are especially important for Ontario. With, finally, some decent job creation occurring in the U.S., this will give the consumer recovery momentum, and will play an important stabilizing role for U.S. housing.

PUMP PAIN

Prices at the gas pumps rose alongside rapidly increasing oil prices in February, up a substantial 8.8% per barrel (WTI). The primary driver of the higher oil prices has been geopolitical concerns within the Middle East, specifically, the risk that tensions with Iran that could spill over into a significant conflict causing disruptions in oil supplies. While Iran's oil production is significant, it is not massive. However, the likelihood of the Strait of Hormuz being cut off (where 17 million barrels a day flow through) poses a significant supply disruption concern, and has put upward pressure on oil prices.

For recovering economies (i.e. the U.S.), higher fuel costs are likely to weigh on consumers and dampen discretionary spending. Higher oil and fuel prices are among the important risks facing both markets and the world economy in 2012. Furthermore, for Canadians, higher oil prices tend to translate into a higher Canadian dollar value - creating a double whammy for industries dealing with rising fuel costs and less competitively- priced goods for export. At this point, the current risks remain relatively contained, but are likely to cause volatility in oil prices (and markets) in the short term.

STILL MAKING HEADLINES

European debt issues are still dominating global headlines and significant risks remain. However, recently policy makers (albeit when their feet are held to the fire) have shown themselves capable of dealing with the immediate financing troubles within the weaker eurozone nations. Additionally, the European Central Bank's (ECB) Long-Term Refinancing Option (LTRO) program has gone a long way to lessen concerns about their banking system liquidity. These two factors have been key contributors to improving investors' outlook on Europe. While substantial progress has been made, the real test (and therefore the risk) is still to come in terms of actually implementing the plans being made by policy makers. Short-term resolutions aside, debt control will be the pre-occupation of governments for years to come.

Finally, after a long tightening campaign by China that has slowed expectations of global growth, there are indications that China will start to ease monetary policy. This could result in a renewed confidence among global investors that China will manage to orchestrate a soft economic landing.

EBB AND FLOW

We anticipate an increase in market volatility over the next several months as situations in Europe and the Middle East ebb and flow, as geopolitical concerns and global financial problems often do. Likewise, after such a fast run up in equity markets, a pull-back (otherwise known as 'taking a breather') would not be unexpected. We caution against making any wholesale change based on short-term market movements. Rather we recommend building a long-term plan within your personal risk tolerance, so that each ebb and flow of the market doesn't rock your financial boat.