Weekly Commentary – February 6, 2017

Alfred Lam, MBA, CFA
Senior Vice President & Portfolio Manager

Richard J. Wylie, MA, CFA
Vice President, Investment Strategy

Economic Calendar

Date	Release	Period	Consensus	Previous
U.S.				
February 6	3-Month Bill Auction		0.540%	0.515%
February 7	Balance of Trade	December 16	$16.40 B	$24.53 B
February 9	Wholesale Inventories	December 16	1.0%	1.0%
Canada				
February 7	Balance of Trade	December 16	-$1.40 B	$0.53 B
February 10	Participation Rate	January 17	65.63%	65.80%
February 10	Unemployment Rate	January 17	6.8%	6.9%

Key Earnings:
February 6: Arrowhead Pharmaceuticals Inc., Everest Re Group Ltd., Tesoro Corp., Patient Home Monitoring Corp.
February 7: Highwoods Properties Inc., Emerson Electric Co., Penske Automotive Group Inc., Spirit Airlines Inc.
February 8: Time Warner Inc., Equifax Inc., CenturyLink Inc., Allergan PLC, Caesarstone Ltd., HTC Corp.
February 9: CVS Health Corp., Newpark Resources Inc., Travelzoo Inc., Iteris Inc., Ideal Power Inc., Apptio Inc.
February 10: American Axle & Manufacturing Holdings Inc., Salon Media Group Inc., India Globalization Capital Inc.

Source: Trading Economics, Yahoo Finance

Market Focus

Canadian economy shows resilience

Updated data from Statistics Canada revealed a 0.4% gain (month-over-month) in GDP by industry during November. In addition, the contraction reported for October was revised from 0.3% to 0.2%. Goods-producing industries rose by 0.9% in November, almost offsetting a 1.0% decline in October. The much larger services industries (representing 70% of total industry) grew at a more modest 0.2% rate in November. The combined figures suggest that the slowdown widely expected in the data for the fourth quarter as a whole may not have been as dramatic as previously anticipated. The most recent forecast from the Bank of Canada pegs Q4 2016 growth at 1.5% annualized, while even a very modest gain in December will like result in a gain of 1.7% or more. However, even if this stronger result materializes, concerns over the uncertainty surrounding the future of international trade will continue to dampen near-term growth expectations for Canada.

Fed reflects market uncertainty

Following the U.S. Federal Reserve Board's 25 basis point (a basis point is 1/100th of one per cent) interest rate hike in December, the central bank shifted to a "wait and see" stance at its latest policy meeting. After the two-day meeting, the target range for the federal funds rate was left unchanged at 0.50% to 0.75%. In the press release that accompanied the statement, the Fed acknowledged that "measures of consumer and business sentiment have improved of late" but the generally optimistic tone was hedged, as it also stated that "near-term risks to the economic outlook appear roughly balanced." By the Fed's next meeting on March 14 and 15, more information on the new administration's actual plans for taxes and infrastructure spending should be known. Whether or not a policy change emerges here, at this juncture, market participants continue to anticipate two or three 25 basis point rate hikes over the balance of 2017.

Employment, GDP and inflation gain ground in Europe

Eurostat handed out some good news for 2016 as the year appears to have come to a close on a strong note. The 19-nation Eurozone experienced a GDP expansion of 0.5% (quarter-over-quarter) in the final quarter of 2016. This was stronger than the

0.4% advance in the previous period, but was only sufficient for 2016 to record full-year growth of 1.7%. This was down from a 2.0% expansion in 2015, but the momentum appears to have remained intact heading into 2017. Similarly, the 9.6% unemployment rate posted for December is now the lowest jobless rate since May of 2009. Good news came in threes as the flash inflation estimate came in at 1.8% for January 2017 (year-over-year), well above the 1.1% figure in December 2016 and the highest since February 2013. The inflation figure now appears to align well with the ECB's target of "just below 2%." While no immediate change is anticipated, more data like this may be sufficient for the European Central Bank to contemplate a shift in policy.

Longer View

Following several years of a general expansion in the price-earnings ratio of equities, we believe returns from this asset class will moderate somewhat and become more closely tied to the rate of growth in company earnings. With equity market volatility increasing to at least the normal range, it's important to keep in mind that equities are best suited for long-term investing, and that the allocation in your portfolio should reflect your investment horizon and risk tolerance. Fixed-income investments, while generally providing limited income in today's low interest rate world, are an effective diversifier in a portfolio. When there is extreme pessimism in the equity market, fixed-income tends to outperform. There is no one asset class that looks better than others, in our view, as their current valuations accurately reflect their potential and risk. Talk to your professional advisor to ensure your portfolio is optimized and continues to meet your needs.

Weekly Summary

January 30

▲ Germany's consumer prices continued to rise, as CPI revealed a 1.9% year-over-year pace in January. This follows a 1.7% increase in December. The preliminary data showed that the key drivers behind the overall increase in January were rising energy prices and higher food costs. While the result came in slightly weaker than consensus estimates of a 2.0% increase, it was still the highest inflation rate since July 2013. The result matches the European Central Bank's "price stability" target of just under 2%.

▲ According to the U.S. Bureau of Economic Analysis, personal income increased 0.3% in December while personal consumption expenditures (PCE) increased 0.5%. Based on revised figures, personal income increased 0.1% and PCE increased 0.2% in November. Given the revisions, these results are broadly in line with expectations. Income and spending patterns of consumers are critical factors in the health of the broader economy.

January 31

▲ Eurostat announced that the Eurozone economy grew 0.5% in the fourth quarter of 2016 (quarter-over-quarter), a modest improvement from the 0.4% figure (upwardly revised) recorded in the previous three-month period. For the full year of 2016, GDP in Eurozone expanded at a 1.7% rate, after increasing by 2.0% in 2015. These results are somewhat stronger than expectations.

▲ Eurostat also reported that its flash estimate for consumer prices in the Eurozone revealed a 1.8% increase in January 2017 (year-over-year). This is up from a 1.1% increase in December of 2016. The sharp inflation surge was boosted by rising fuel prices (8.1% in January compared to 2.6% in December). This is the fastest pace of inflation since February of 2013. These inflation figures are stronger than expectations.

▲ Statistics Canada announced that, on a monthly basis, real GDP by industry grew 0.4% in November, the fifth increase in six months. The increase in November came mainly from higher output in manufacturing, mining, quarrying, and oil and gas extraction, finance and insurance and construction. On a year-over-year basis, GDP growth stands at 1.6%. These results are somewhat stronger than market expectations. GDP is the broadest measure of aggregate economic activity and encompasses every sector of the economy.

▲ Statistics Canada reported that its Industrial Product Price Index rose 0.4% in December while its Raw Materials Price Index jumped 6.5% during the month. On a year-over-year basis, the indices are up 2.2% and 17.2%, respectively. Higher prices for energy products during the month were the primary driver for both indices. These figures are broadly in line with expectations. The IPPI and RMPI data are closely watched as they indicate relative inflationary pressures at the industry and raw materials levels.

February 1

▲ The U.S. Institute for Supply Management reported that its Purchasing Managers Index moved higher to a 56.0 reading in January. This is a 1.5 point gain from December's 54.5 figure and moves the index further above the key 50.0 (generally expanding) level, where it has now been for five consecutive months. The reading is above expectations and indicates an acceleration in manufacturing activity.

▼ The U.S. Census Bureau announced that construction spending fell 0.2% in December, following a 0.9% gain in November. On a year-over-year basis, construction was up 4.2%. The monthly growth figure is below consensus estimates. This result indicates a slowing of the late-year momentum in the construction sector.

■ The U.S. Federal Reserve held interest rates steady following its latest two-day policy meeting, with the target range for the federal funds rate remaining at 0.50% to 0.75%. In its statement, the Fed struck a generally optimistic tone, as economic data continues to point toward improving fundamentals in both employment and inflation. The "no change" announcement was widely anticipated, with most analysts looking for another 50 to 75 basis points of increase spread out over the balance of 2017. Monetary policy, as decided by the Fed, has significant influence on both the U.S. and global economy. Its lead is often followed by policymakers in other countries.

February 2

■ The Bank of England's Monetary Policy Committee decided to leave interest rates unchanged at the record low of 0.25% at their latest policy announcement window. Meanwhile, the central bank upgraded its GDP growth forecasts for 2017 to 2.0% from November's estimate of 1.4%. The growth forecasts for 2018 and 2019 were also raised to 1.6% and 1.7%, respectively. Although the rate decision was no surprise to the market, some policymakers remain concerned about inflationary risks and there may be a case for the bank to raise rates over the balance of the year.

▼ The U.S. Department of Labor announced that initial jobless claims totalled 246,000 (seasonally adjusted) in the week ending January 28, a decrease of 14,000 from the previous week's revised level. The previous week's level was revised up by 1,000 to 260,000. The four-week moving average was 248,000, an increase of 2,250 from the previous week's revised average. The previous week's average was revised up by 250 to 245,750. These results are somewhat stronger than consensus estimates.

▲ The U.S. Bureau of Labor Statistics announced that non-farm labour productivity increased at a 1.3% (annualized) rate during the fourth quarter of 2016 while unit labour costs rose 1.7% on the same basis. These figures are in line with market expectations. Productivity growth is important for longer-term economic stability as it allows for higher wages and faster economic growth without inflationary pressures.

February 3

▲ The U.S. Bureau of Labor Statistics reported that the unemployment rate rose by 0.1 percentage points to 4.8% in January, and non-farm payroll employment rose by 227,000. The up-tick in the unemployment rate was driven by a 0.2% increase in the participation rate to 62.9%. Employment continued to trend up in retail trade, construction, and financial activities. The employment figures are stronger than expectations and the mild increase in the unemployment rate does not detract from the strength of the overall report. This is the most closely followed set of U.S. statistics as it indicates the relative health of the various sectors of the economy and is suggestive of consumer spending.

▲ The People's Bank of China, China's central bank, unexpectedly raised the interest rate on open market operation reverse repurchase agreements by 10 basis points (a basis point is 1/100th of one per cent). The surprise came on the first day back form the lunar New Year holiday, indicating a clear sign of a further tightening of monetary policy. The modest increase reinforced the Chinese authorities' intention of containing corporate debt and capital outflows. It was also aimed at the overheating real estate market. The move came against a backdrop of slower economic activity at the close of 2016.

▲ The U.S. Census Bureau reported that factory orders increased 1.3% in December. This followed an upwardly revised 2.3% decline in November (originally reported as -2.4%). Excluding transportation, new orders jumped 2.1% in December. These results are stronger than expectations. The orders data indicate how busy factories will be in coming months as manufacturers work to fill those orders.

▼ The Institute for Supply Management announced that its Non-manufacturing Index recorded a 56.5 reading in January. It was down 0.7 points from the 57.2 level registered in December, but remained above the key 50.0 (generally expanding) level for a 85th consecutive month. This figure is below consensus expectations and indicates continued growth, but at a slightly slower rate in the non-manufacturing sector.