

Market Watch

Big Picture

Harper wins majority; U.S. jobless recovery

Prime Minister Stephen Harper won his first-ever majority government on May 2nd, promising Canadians stability and a focus on jobs and the economy. In the U.S., a “jobless recovery” has seen top U.S. firms post massive profit gains while barely one-fifth of job losses have been recouped. Fortune 500 companies’ combined earnings jumped 81% to US\$318-billion in 2010, according to *Fortune Magazine*. Yet the number of Americans filing for jobless benefits rose to an eight-month high last week and millions are running out of extended jobless benefits. Nonetheless, consumers remain resilient, with retail sales rising 8.9% in April, tying March 2010 for the largest monthly gain on record over the past 11 years.

U.S. productivity rose at a slower rate in the first quarter, while workers’ wages adjusted for inflation fell by the largest amount in almost three years, due to higher gasoline and food prices. Quebec leads Canada’s research and development spending, according to the OECD, which measured spending by businesses as a percentage of gross domestic product. But Quebec’s 1.5% score was low by international standards, with Massachusetts leading the way at 5.5% and Northern Finland at 4.3%. Portugal agreed to a three-year, €78-billion (US\$116-billion) bailout loan from the European Union and IMF. Canada will have nearly 668,000 new millionaire households by 2020, for a total of 2.4 million, the eighth-largest concentration of millionaires among 25 countries surveyed.

Markets

Commodities peak, trigger global sell-off

Soaring commodity prices and weak economic data in Europe and the U.S. triggered a four-day sell-off as investors worried high costs would derail global growth. Sentiment ensnared everything from natural gas to wheat to copper to cotton, with silver prices plummeting 20% and oil falling 10% on Thursday. World stocks declined as the 19-commodity Reuters/Jefferies CRB Index shed nearly 5%, headed for its biggest weekly decline since December 2008. Suncor reported first-quarter profit of \$1.028-billion compared with \$779-million a year ago, benefiting from high oil prices. Intel unveiled a revolutionary 3-D chip that uses very little power, which could allow the firm to finally break into the mobile market.

Beijing-based social networking website Renren – dubbed the Chinese Facebook – launched a successful IPO, raising over US\$700-million. Loblaw’s quarterly earnings rose 23% as profits at the pumps offset flat grocery sales. Upscale grocer Whole Foods Markets reported its strongest results in five years, as profits rose 33% from a year ago. Kellogg plans to raise prices by 4% this year to offset higher costs and lift revenue. European Union agricultural exports jumped 21% in value to a record €1-billion (US\$135-billion) in 2010, due to emerging economies demand and higher prices. GM tripled its quarterly profit to a whopping US\$3.2-billion, compared with a year ago, driven by a U.S. market recovery and strong sales in Asia.

Our Recommendation

Earnings season positive for equities

- **Equities.** Steve Uzielli, Portfolio Manager, Portfolio Advisory Group, says: “We still believe equities are vulnerable to a pullback but are biased toward buying any market weakness.”
- **Fixed income.** Anthony Mentor, Associate, Portfolio Advisory Group, highlights the following recommendations: “Term Call – given the recent decline in yields, we no longer see value in the mid-to-long end of the curve and recommend investors stay short at this time. Sector Call – overweight Canada, overweight Municipals, Provincials and Corporates. Currency Call – we recommend Canadian investors remain in Canadian dollars for their fixed income holdings. Alternative Strategies – overweight high yield, marketweight Emerging Markets Debt, overweight inflation protected debt.”
- **Portfolio strategy.** Scotia Capital Portfolio Strategist Vincent Delisle anticipates eventual monetary tightening means we are passing the midway point of the cycle. It doesn’t imply outright equity weakness, but it portends lower expected equity returns.



The Month in Review

April: Growth spurs inflation

Canada started the year on a strong note, with gross domestic product growing at a 4% annualized pace in the first quarter, following 3.3% and 1.8% in the two previous quarters. Factories expanded production in January at the fastest rate since 2003, boosting the overall economy by 0.5%.

But by March, Canada's annual inflation rate had surged to 3.3% – the fastest pace since September 2008 – driven up sharply by energy and food prices. The cost of gasoline as well as fresh vegetables rose 19% in the past year. As a result, Canadian businesses are expecting sales to slow over the next 12 months, according to a Bank of Canada quarterly business outlook.

Canada exports more to China and the U.K.

Canadian exporters shipped a greater share of goods to China and the U.K., and relied less on U.S. markets last year. While the U.S. still commanded a 75% share of Canada's exports, the figure is down from 87% in 2001. Global exports jumped 14.5% overall last year – the biggest rise since 1950.

Increased border security adds huge cost

A university study showed that increased border security in the wake of the September 11th attack is costing Canada up to \$30-billion a year, or 2% of GDP, a figure large enough to offset the economic gains produced by the North American free-trade agreement.

Japan downgraded as earthquake costs mount

Standard & Poor's downgraded Japan's debt outlook to "negative" from "stable," warning the huge cost of last month's earthquake – now estimated at 50-trillion yen (US\$613-billion) – will hurt already-weak public finances. With public debt sitting at US\$10-trillion, the highest of any advanced country, Japan now faces a recession as industrial output plunged 15.3% in March from February, and consumer spending fell 8.5% versus a year ago.

Portugal seeks aid

Portugal became the third eurozone member to seek a bailout from the European Union and IMF, amid soaring borrowing costs and deepening political instability.

PC sales decline, but tech sector flourishes

Worldwide shipments of personal computers fell by 3.2% versus a year ago, according to research firm IDC, as consumers flocked to the iPad and other electronic devices or simply held back from buying PCs. The tech sector showed surprising strength in April – Apple revenue was up 83% year-over-year, Intel profit gained 29% and IBM logged the fastest revenue growth in a decade.

RIM PlayBook faces scrutiny

Research In Motion Ltd. (RIM) retreated 1.7% on the Nasdaq after its new PlayBook tablet received tough reviews from influential technology critics at the *Wall Street Journal* and *New York Times*.

Infrastructure and clean energy

Siemens said it will add a new division to target city infrastructure such as urban trains, building technologies and water treatment. Global investment in clean energy jumped 30%, reaching a record US\$243-billion in 2010, with China and Germany leading the way. GE will invest US\$600-million to build the largest solar panel plant in the U.S., with manufacturing starting in 2013.

For more information or a copy of our in-depth ScotiaMcLeod Weekly Strategy report, please call:

Jolene Laing, CIM, FCSI
Associate Portfolio Manager

(604) 535-4733 | jolene_laing@scotiamcleod.com

