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Gestion de portefeuilles / Portfolio management

La voie des Alizés

Navigating the Trade Winds

October 2017

Dear friends,

The summer lull was not as typical as you might expect. The overcast clouds finally dissipated in September on equities as well, the crisp autumn light shed hope on returns. In fact, the S&P/TSX clocked in at a 3% gain for the quarter. We can thank the swift rebound in the oil patch and the rate hikes that favoured the Financials. Down south, the S&P 500 basically was flat in our currency and held on to a 4.5% yearly gain. Canadian investors, were essentially stymied by the strong gains of the loonie, thus leading to foreign returns being constrained. The Canadian dollar had a stellar performance with the strongest quarterly rise since 2004 (average Q3 vs. Q2), for a 7.7% gain against the USD in 2017. In the short term, the CAD's run will hit a wall as it gets closer to its purchasing power parity and its 200-week average, both being at around US 81¢.

	Closing	Change**	
	30-Sep-17	Quarter	2017
Stock Indices *(% in C$)*			
S&P/TSX	15,635	3.0%	2.3%
S&P 500	2,519	0.0%	4.5%
MSCI EAFE*	1,974	0.8%	8.8%
Currencies			
CAN$ (US$/C$)	0.8020	4.0%	7.7%
Euro (US$/EUR)	1.1814	3.4%	12.3%
Commodities (US$)			
Oil (WTI)	$ 51.67	12.3%	-3.9%
Gold	$ 1,284	3.2%	10.9%
Volatility Index			
VIX	9.51	-14.9%	-32.3%

** MSCI Europe, Australasia and Far East (US$)*

*** Changes are expressed in C$ for Stock Indices.*

The forward thrust of international equity markets validated our call, albeit, we would have preferred for the CAD not to slice some of the gains. Despite that, the year-to-date return in Canadian dollars for the MSCI EAFE of developed countries is a healthy 8.8%, while it is a whopping 16.5% for the MSCI Emerging Markets. Overseas was the place to be and it is the place to remain as both developed and emerging indices are cheaper than North American ones. We are optimistic for the possibility of further outperformance abroad. Furthermore, as we see the Canadian dollar stabilizing within a US 3-to-4¢ range in the next 12 to 18 months, Canadian investors should take full advantage of overseas returns.

At this stage of the cycle, we believe that if equity markets are still rising, it is the result of the solid worldwide economic expansion and sustained liquidity availability. But, we must also emphasize the growth in corporate earnings. In fact, earnings remain crucial for the bull market to continue. For Q2, results were in line with expectations. As a result, the consensus remains on track for an 11% earnings growth in 2017 for the S&P 500 and a close to 20% figure for the S&P/TSX. We would not be shocked if the markets were to correct slightly eventually. The present 11-month stretch without a 5% pull back for the S&P 500 is the fourth longest since 1960. But as long as the economy remains solid and the VIX does not sag convincingly under the 9-point threshold, we could get away without a major correction. Unseen factors, like a sudden rise in inflation triggering more rate hikes than expected, could spell trouble. For now, this scenario seems unlikely. Therefore, the winds are still favourable and we maintain course. We still concentrate our efforts on quality stocks and sectors that trade at affordable prices. This has been a proven strategy that enabled us to add value in Q3. It bodes well for the coming months.