REVIEW AND COMMENTARY
3rd QUARTER - 2016

As discussed last quarter, the firming of oil prices and the unsettling U.S. political landscape should make investing in Canadian capital markets attractive. Canadian equity prices continued to improve over the quarter but were unable to continue the relative outperformance it had enjoyed in the previous quarter. Canada's broadest equity measure, the SP/TSX Composite Total Return Index increased by 5.5% with Industrials and Information Technology leading the way. These returns continued to outshine Canada Government bond returns of all durations. The upcoming election in the United States gives us some pause given that policy is often overshadowed by sensationalism and rhetoric. It gets very difficult to properly understand what the alternatives are given the more personal tone of the coverage. It is hard to believe that Republicans, who have embraced their candidate as a 'political outsider', won't be equally disappointed in their candidate given he has made so many promises which appear close to impossible to deliver; something he has accused the incumbents of doing for years. Democrats are finding it even more difficult to keep on topic as they attempt to not only deflect the accusations of impropriety that appear to be, at least to some measure, true. Sadly, it appears that current political debate focuses more on candidates' past foibles rather than the viability of their vision of the future. Regardless, it would appear that many factors point to continued support for investing in Canada.

While it may be too early to confirm, it would appear that the Saudi's have blinked when it comes to oil prices. They have offered to lower crude production and want to encourage other OPEC members, as well as Russia, to cooperate. There are many skeptics who are quick to point out that many members of OPEC cheated on their productions levels in the past and will probably do so in the future. Whether a firm agreement can be reached, it is important to note that the Saudi's are obviously, at least at some level, starting to feel the strain of being a price taker rather than a price setter. Estimates are that the Saudi's, due to their elaborate social programs and subsidies, lose over $100 billion (USD) dollars a year with crude at present levels. Saudi has thousands of unpaid foreign workers that remain in the country too poor to return home given they haven't been paid. Certainly, there are deep pocketed producers around the world that will not be required to honor any agreement the Saudi's might be able to forge however, the damage done to the oil industry is significant. Financing will be scarce for all those except the well-established senior producers. It will take a while for the industry to repair. However, if there is any serious collaboration oil prices will be higher, possibly much higher.

Firming oil prices will be good for Canada's economy, our loonie and our stock market. After many years of relative underperformance, the recent trend of outperformance could continue. With our relative political stability Canadian markets may be the recipient of international cash flows looking for an attractive and relatively stable environment to invest.

There are many other concerns for equity investors; there always are. Beyond the U.S. election, interest rates appear to remain low for longer. While the US economy appears to be improving slowly there are few other bright spots throughout the globe and most Central banks continue to ease in terms of their monetary policy. While the US Federal Reserve appears to be coming to terms of eventually increasing interest rates, it would appear that any increase would be marginal at best. The US dollar is already relatively strong and any increase in rates would make the U.S. even more attractive (and expensive) which would make US exports increasingly unattractive- something the US presently would like to avoid given it would have a knock on effect and potentially weaken the US economy. Our belief is that the U.S. Federal Reserve would prefer to make sure the US economy is trending strongly before it undertakes to normalize interest rates. So while U.S. rates may move up marginally in the next few quarters, there will not be a significant move until the U.S. economy is significantly stronger.

With the background of lower interest rates throughout most global economies, firming oil prices and political uncertainty to the south of us, Canada should continue to benefit from the international flows of money looking for a place to invest.