Market Update

12 February 2016

In past weekly updates, I have talked about the Federal Reserve getting it wrong when it comes to the timing of an interest rate hike. Well, did Chairwoman Janet Yellen get it right? No. The EU, Japan, UK and most emerging economies are heading the opposite direction by lowering interest rates. Soon, our own Bank of Canada will jump in and do the same. In a world of negative interest rates and deflation which recently has been only magnified by the price drop in oil leads to price appreciation of hard assets and dividend paying equities.

The main issue with America's economy is not current success which is hitting necessary targets. Wage inflation, job growth and consistent consumer consumption are all present. What is dampening future out look is not oil, not a slowing China but a threat to the American dollar and future manufacturing. Strong currency prices are the kiss of death for manufacturing and export for any country, America included. After the great recession, the American dollar dropped to all time lows with calls for the greenback to collapse. The dollar did not collapse; it did serve to come to the aid of American manufactures and exporters by boosting demand for American goods around the world. As with any economy when it strengthens so does its currency. All was fine until the Federal Reserve chose to raise interest rates pushing gold out of favour as a safe haven for capital reserves and bring back the American dollar as the choice destination to park your money. When large institutions and investors park money in a specific currency it does the domestic economy no good. It only serves as cost burden on corporations and individuals alike. Why? These funds are never invested into the domestic economy which would drive corporate expansion and job growth. The more the demand on the currency the higher treasury prices go. Canada had the same issue only a few years ago, as investors took advantage of higher Canadian short term deposit rates by piling in capital and forcing our Loonie to all time high valuations.

This resulted in our manufacturing sector almost becoming extinct seeing nearly 500,000 jobs leave Canada in a short period of time.

America could see the same if the greenback is allowed to appreciate too much too quickly. Just

as interest rates can be raised by central banks, they also can be decreased. A drop in interest rates would see the dollar retreat. The Federal Reserve must have realized that the desired outcome in cooling the economy was already achieved long before the actual interest rate hike but took action to stem aggressive intervention by Chinese leadership in their currency the Yuan. The mere mention of increasing interest rates nearly two years ago sent markets on a slow cooling off.

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Central banks always make errors by either being too proactive or reacting too late. The most recent attempt by Ms. Janet Yellen was one of too much too soon. Over the last two days of speeches by the chairwoman, another future rate hike looks to be a possibility.

Most developed nations are launching or have launched fiscal stimulus policy spending tools in addition to monetary policy better known as quantitative easing. America has not announced any major fiscal policy measure to better grow the economy and jobs. So Ms. Yellen is in a holding pattern keeping interest rates pat for now. The underlying driver for such behaviour would be the up and coming federal election. Politicians and not central banks approve fiscal spending programs. The right kind of announcements will more than likely carry a victory at the ballot box. So just as in Canada, the Federal election in America will be an intense battle and closely watched by market makers.

American sentiment is also ready and willing to accept major change come election time. The billion dollar question is who wins and what type of change they bring with them and their administration.

The below table illustrates the market indices since the beginning of January 2016. As with all client strategies our objective is with a strong eye to not following market drops. For your individual portfolio performance please login into your personal wealth management page. This is a service available to all clients. You can find the login on our website.

YTD Performance as of Close February 10th, 2016

Major Indices (CAD)	YTD %
S&P 500	**-8.98%**
Russell 2000	**-14.90%**
MSCI EAFE	**-11.63%**
MSCI AC World	**-10.03%**
S&P TSX	**-6.06%**

Lastly considering it is tax time, the following tax changes for 2016 should be kept in mind:

The Liberal government announced that they will make a change to federal income tax brackets

starting in 2016.

There are two parts to this change. The first is cutting the "middle class" income tax bracket from 22% to 20.5%. If your taxable income is between $45,282 and $216,987 you'll pay less tax. The second part of this change is the introduction of a new 33% tax bracket for people who earn more than $200,000 each year.

- The annual TFSA limit will be reduced from $10,000 to $5,500 (indexed to inflation); the 2015 limit will remain at $10,000.
- Starting in July, the UCCB and CCTB will be replaced with one non-taxable Canada Child

Benefit; the formal changes won't be announced until the budget in the spring.

- The family tax cut will be repealed.

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