CIBC
CIBC Asset Management

Market Spotlight

February 2015

Global Markets

Global equity markets fell -1.81% in U.S. dollar terms in January but gained 7.49% in Canadian dollar terms, as the Canadian dollar tumbled almost 10% against the U.S. currency.

European equity markets were higher in local currency terms, but almost unchanged in U.S. dollar terms as the euro declined. The European Central Bank (ECB) initiated its much-anticipated economic stimulus package, which attempts to weaken the euro by expanding the ECB's balance sheet more aggressively than most other major central banks. In a surprise move, the Swiss National Bank discarded its long-held peg of the Swiss franc to the euro, causing the franc to soar.

Emerging markets edged higher as India, Turkey and Russia cut key interest rates. The cut in Russia came after a huge rate increase in December, which was designed to support its declining currency.

The U.S. market was slightly lower as corporate earnings have been mostly underwhelming. The U.S. Federal Reserve (Fed) reassured investors that it is in no rush to raise interest rates. Lower energy prices and loose global monetary policy give the Fed reasons to delay tightening U.S. monetary policy.

Canadian equities were close to unchanged, although sector returns varied considerably. The surprise interest rate cut from the Bank of Canada (BoC) produced a sharp drop in the Canadian dollar, which should have a positive effect on exports.

Current Asset Allocation*

Asset Class	Weighting
Canadian Bonds	Underweight
International Bonds	Underweight
Canadian Equities	Market Weight
U.S. Equities	Market Weight
International Equities	Overweight
Emerging Market Equities	Overweight

**For balanced portfolios, as at January 31, 2015.*

"Sound Bites"

Luc de la Durantaye

"Similar to many other developed economies, Canada's monetary policy outlook relative to the U.S. is not supportive for its currency. While the Fed now seems more determined to hike rates in 2015, the BoC shows no intention of following suit, cutting rates by 25 basis points in January.

The drop in oil prices has been substantial and its impact on the Canadian energy surplus could be significant. If oil prices stay depressed and foreign demand remains unchanged, Canada's overall trade balance will potentially reach negative record proportions. Given the recent changing conditions in the energy sector, the USD/CAD bilateral exchange rate could decline further, assuming oil prices remain depressed. "

Fixed Income

Following the longest period of stable monetary policy since the 1950s, the BoC surprised the markets by lowering interest rates at the January 21 policy meeting. The cut in the overnight rate was a warning shot to the market that the BoC was sufficiently worried about weakening economic growth and a move towards uncomfortably low inflation. Many other central banks, including Switzerland, Denmark, Singapore and Russia, cut their administered rates, while the ECB announced its long-awaited quantitative easing program. The ECB stated that it plans to buy 1.1 trillion euros in an effort to improve the economy and stave off deflation.

Canadian Equity

The S&P/TSX Composite Index was up 0.6% in January, with the market impacted by concerns of weaker global economic growth. U.S. economic data, while slightly disappointing in some areas, still pointed towards modest economic growth. The U.S. dollar strengthened over the period with the onset of competitive currency devaluations by other countries. These various developments led to a higher gold price, lower energy and copper prices and a weaker economic and equity market outlook for Canada by the end of January.

"Sound Bites" *Lower Canadian dollar - what does it mean?*

Fixed Income Insight

Steven Dubrovsky

"The BoC's rate cut helped nudge the dollar lower, which may lead to an improvement in non-energy exports. A decline of just over 15% since July of last year should help the automobile and aerospace industry in Ontario and Quebec. The Canadian dollar is sensitive to movements in commodity prices and, more specifically, the price of oil. An energy shock of this magnitude will have a negative impact on oil-based provincial economies such as Alberta, Saskatchewan and Newfoundland."

Equity Insight

Vincent Lépine, *Global Asset Allocation*

"The drop in oil prices is significantly impacting our fair value estimates for the Canadian dollar. Given the magnitude of the current oil shock, the valuation reading for the Canadian dollar is changing and we can no longer argue that the Canadian dollar is significantly undervalued. Adjusting for the oil shock, the fair value for the Canadian dollar, previously around 0.88 USD, has dropped below 0.86 USD."

Scott Vali, *Global Resources*

"In the crude oil market, the bulk of the recent increase in supply is from U.S. producers, who have U.S. dollar production costs. All else being equal, the decline in the Canadian dollar does help offset some of the decline in crude prices for Canadian producers, because their costs are in Canadian dollars. However, Canadian producers will not all be beneficiaries, as many produce heavy oil which has deteriorated in value more than the largely light oils produced by the American-based producers."

Colum McKinley, *Canadian Equities*

"The businesses that are most positively affected by the weakness in the Canadian dollar are those that derive their revenue in U.S. dollars and have operating expenses predominately in Canadian dollars. Businesses such as Sun Life Financial and Manulife Financial could potentially benefit because of their geographic diversification. These companies have significant foreign operations in the U.S. and Asia while their head offices, of course, are located here in Canada."