

SEPTEMBER NEWSLETTER



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Published for the friends and clients of
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Market Review

The third quarter of 2014 has seen many markets stumble, and some sectors have experienced long anticipated corrections. Commodities have been very weak and the Canadian resource sector is down sharply. Fortunately we have been underweight in the oil and gas sector and have almost no equity positions in the mining sector.

	<u>Sept</u> <u>30/13</u> <u>Close</u>	<u>June</u> <u>30/14</u> <u>Close</u>	<u>Sept</u> <u>30/14</u> <u>Close</u>	<u>90-Day %</u> <u>Change</u>	<u>1-Year</u> <u>% Change</u>
S&P 500	1,682	1,960	1,974	0.7%	17.4%
S&P/TSX Composite	12,787	15,146	14,960	-1.2%	17.0%

While it is always difficult to determine what exactly causes a market correction, my own feeling is that the markets are concerned about falling demand in China. To a lesser extent the sanctions on Russia, while hurting Russia more, have reduced the growth rates of European economies.

<u>World Indices</u>	<u>YTD*</u>
S&P/TSX Composite	9.83%
S&P 500	6.70%
DJ Stoxx 50	4.66%
MSCI Emerging Markets	0.26%
MSCI Japan	-1.28%
MSCI Hong Kong	-1.60%

*YTD: Year to date figures as of September 30, 2014

Fixed Income

Due to the economic slowdown in Europe and the emerging markets, rates have become lower for 10 and 20 year bonds, while rising for 2 and 5 year bonds. If this flattening trend continues we can expect a recession. If short term rates become the same or higher than longer term rates, I will be recommending reducing equity exposure.

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Canadian T-Bills and Bonds

	<u>Mar. 31,</u> <u>2014</u>	<u>June 30,</u> <u>2014</u>	<u>Sept. 30,</u> <u>2014</u>
90 day	0.89%	0.93%	0.91%
180 day	0.91%	0.96%	0.93%
1 year	0.95%	1.00%	1.00%
2 year	1.07%	1.10%	1.13%
5 year	1.73%	1.53%	1.63%
10 year	2.47%	2.24%	2.15%
30 year	2.96%	2.78%	2.67%

U.S. T-Bills and Bonds

	<u>Mar. 31,</u> <u>2014</u>	<u>June 30,</u> <u>2014</u>	<u>Sept. 30,</u> <u>2014</u>
90 Day	0.04%	0.03%	0.02%
180 Day	0.05%	0.07%	0.04%
1 year	0.11%	0.11%	0.10%
2 year	0.45%	0.47%	0.59%
5 year	1.76%	1.63%	1.78%
10 year	2.74%	2.52%	2.51%
30 year	3.57%	3.35%	3.21%

International 10 Year Bond Yields

	<u>Mar. 31,</u> <u>2014</u>	<u>June 30,</u> <u>2014</u>	<u>Sept. 30,</u> <u>2014</u>
Japan	0.63%	0.56%	0.52%
U.S.	2.74%	2.52%	2.51%
Germany	1.56%	1.24%	0.95%
Canada	2.47%	2.24%	2.15%
U.K.	2.73%	2.67%	2.42%
France	2.08%	1.70%	1.28%
Spain	3.22%	2.65%	2.13%
Italy	3.29%	2.84%	2.33%
Portugal	4.04%	3.62%	3.14%
India	8.80%	8.72%	8.51%

The Resource Sector



Oil

CME Group WTI FINANCIAL

Copper

CME Group COPPER HIGH GRADE (GLOBEX)



Iron Ore

CME Group IRON ORE 62% FE, CFR CHINA

Lumber

CME Group RANDOM LENGTH LUMBER

As the above charts indicate, the prices of most commodities have behaved poorly over the last year. This has been felt in resource companies, as indicated below.

	<u>Sept.</u> <u>30/13</u> <u>Close</u>	<u>June</u> <u>30/14</u> <u>Close</u>	<u>Sept.</u> <u>30/14</u> <u>Close</u>	<u>% Change</u> <u>in 1 Year</u>	<u>% Change</u> <u>in 90 Days</u>
Teck Resources	\$26.84	\$22.83	\$18.89	-29.6%	-17.3%
Suncor	\$36.83	\$45.50	\$40.53	10.0%	-10.9%
iShares S&P/TSX Capped Materials	\$12.65	\$14.26	\$12.77	0.95%	-10.4%
iShares S&P/TSX Capped Energy	\$16.57	\$20.96	\$18.45	11.3%	-12.0%

European Markets

	<u>Sept.</u> <u>30/13</u> <u>Close</u>	<u>June</u> <u>30/14</u> <u>Close</u>	<u>Sept.</u> <u>30/14</u> <u>Close</u>	<u>% Change</u> <u>in 1 Year</u>	<u>% Change</u> <u>in 90 Days</u>
iShares MSCI Austria (EWO)	\$19.32	\$19.58	\$16.12	-16.6%	-17.7%
iShares MSCI Russia (ERUS)	\$21.62	\$20.23	\$17.27	-20.1%	-14.6%
iShares MSCI Eastern Europe (ESR)	\$25.96	\$24.94	\$21.85	-15.8%	-12.4%
iShares Germany (EWG)	\$27.81	\$31.28	\$27.70	-0.40%	-11.4%
iShares France (EWQ)	\$26.88	\$29.15	\$26.55	-1.23%	-8.92%

While the Russian Index is performing poorly, the Eastern European index is down almost as much, and France and Germany are down significantly. Fortunately we do not have European exposure, except indirectly through Canadian or U.S. multinational companies.

Power Financial Corp \$34.26 (close September 30th)

We highlighted this company in our June 30th newsletter, and it is up 3.16%, better than the overall market. I continue to feel that it represents good value for investors seeking attractive income and longer term growth.

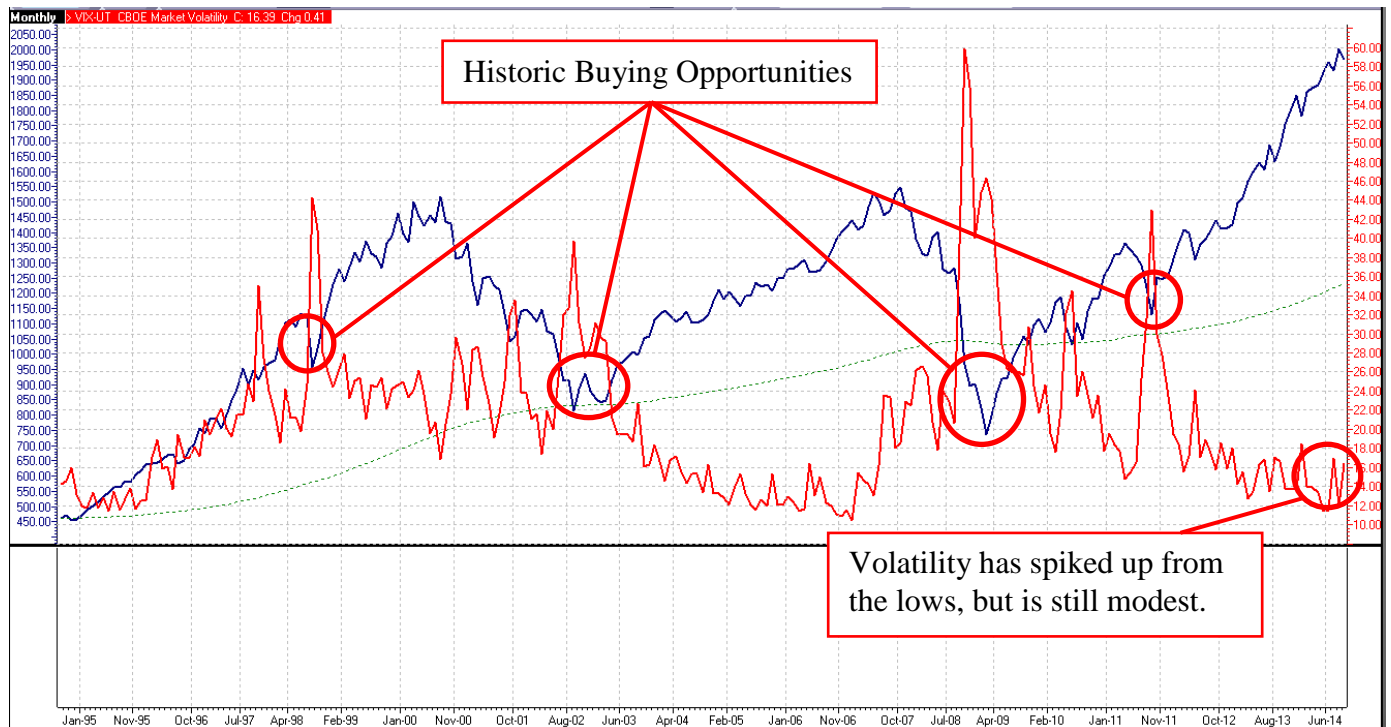
Johnson & Johnson \$106.59 (close September 30th)

This morning you likely flossed your teeth with J&J dental floss and washed your hair with J&J Aveeno shampoo. Highlighted in our March 31st newsletter at \$98.23 and in the June 30th newsletter at \$104.62, Johnson & Johnson closed this quarter at \$106.59. I continue to feel that companies who are industry leaders with strong balance sheets in low volatility businesses have the best risk/reward characteristics for investors.



We like Johnson & Johnson because its success is the result of making excellent products rather than relying on financial engineering.

Volatility Index and S&P 500 Index



There has been a sharp increase in volatility since June 30th, the VIX Volatility Index (in red) rising from \$11.57 to \$16.31. This measure of investor fear is still relatively low.

Outlook and Strategy

While there may be opportunities in beaten down Canadian oil and gas companies, for now our strategy is to reduce or eliminate positions that look vulnerable in the current environment. We will continue to search for high-quality income producing investments that become good value as the markets fluctuate.

If you have any questions about your portfolio, please call.



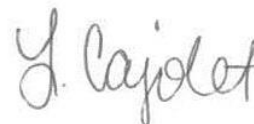
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