April Market Comments

General Comments

Economies are expanding and stock markets in the world are rising.

Perhaps the question is whether the significant stall in growth in 2011 was simply a pause in a greater economic recovery cycle that began in 2009, or if a new economic cycle is in its infancy.

Challenges exist for the remainder of the year, and markets have often peaked in the early spring season. Weakness in financial markets over the next few months may present opportunity to increase exposure to early business cycle growth securities.

Reasons to be excited about the current stage investors are in the economic cycle include:

- The consensus forecast of U.S. real GDP growth for 2012 has been revised up to 2.2%. 4th-quarter 2011 GDP estimates were revised upward to 3.0% annualized growth.
- U.S. Personal income grew faster at 3.8% rather than the previously estimated 3.4%, overall a healthy rate.
- The US labour market showed job gains averaging 245,000 from December 2011 to February 2012. Initial claims for unemployment insurance declined with the four-week trend level now standing near its point lowest since early 2008. Purchasing managers' surveys showed a growing number of employers intend to hire.
- Bank of Canada left the overnight policy rate at 1.0%. The statement showed the Bank downplayed level of concern about global developments The Bank is comfortable keeping "considerable monetary policy stimulus" in place.
- The Federal Reserve has promised not to raise interest rates for almost two years, maintaining a significant driver for growth.

Year to Date Returns in C$

S&P/TSX Composite	3.7%
S&P 500 Index	9.7%
MCSI World Index	8.7%
Euro Stoxx 50 Index	7.5%
MSCI Emerging Markets	11.4%
DEX Bond Universe	-0.2%

Investors who owned Canadian equities and safety-oriented fixed income performed poorly, while investors in global equities participated most in the first-quarter rally.

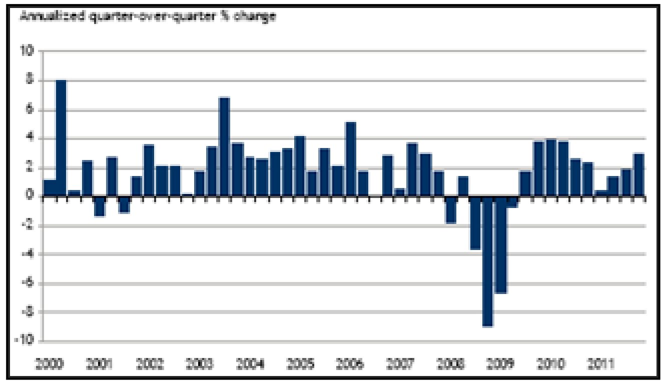
Negotiations about the conditions under which Greece is expected to get bailout funding and the ability of its government to enact the new fiscal arrangements continue to unsettle investors. The restructuring of other weak countries in the European Union also remains an uncertainty.

Markets were shaken by China's announcement that its economy is likely to grow at a 7.5% pace in 2012, which is slower than the previous estimate of 8.0%. The direction of negative change is more relevant than the seemingly large growth rate.

Finally, negative U.S. election rhetoric threatens to further undermine confidence and highlight weaknesses in the American recovery.

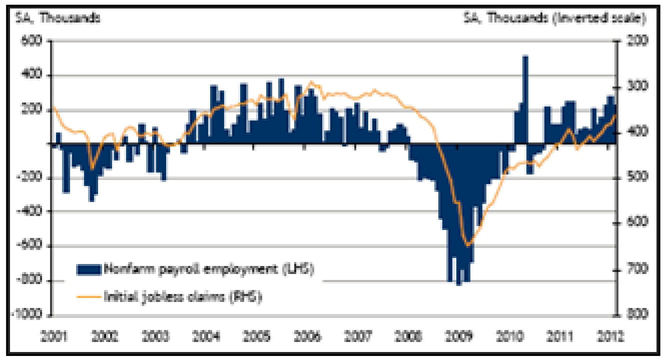
Economic Snapshot

US Real GDP



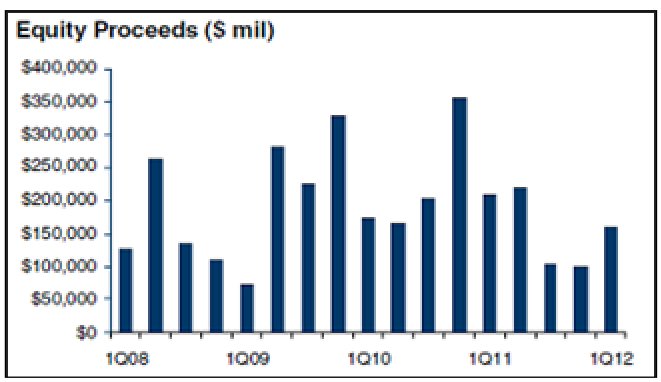
Source: Statistics Canada

US Employment Change, Initial Jobless Claims



Source: Bureau of Labor Statistics, Department of Labor

Global Equity New Issues



Source: Dealogic, Credit Suisse First Boston

Current Strategy

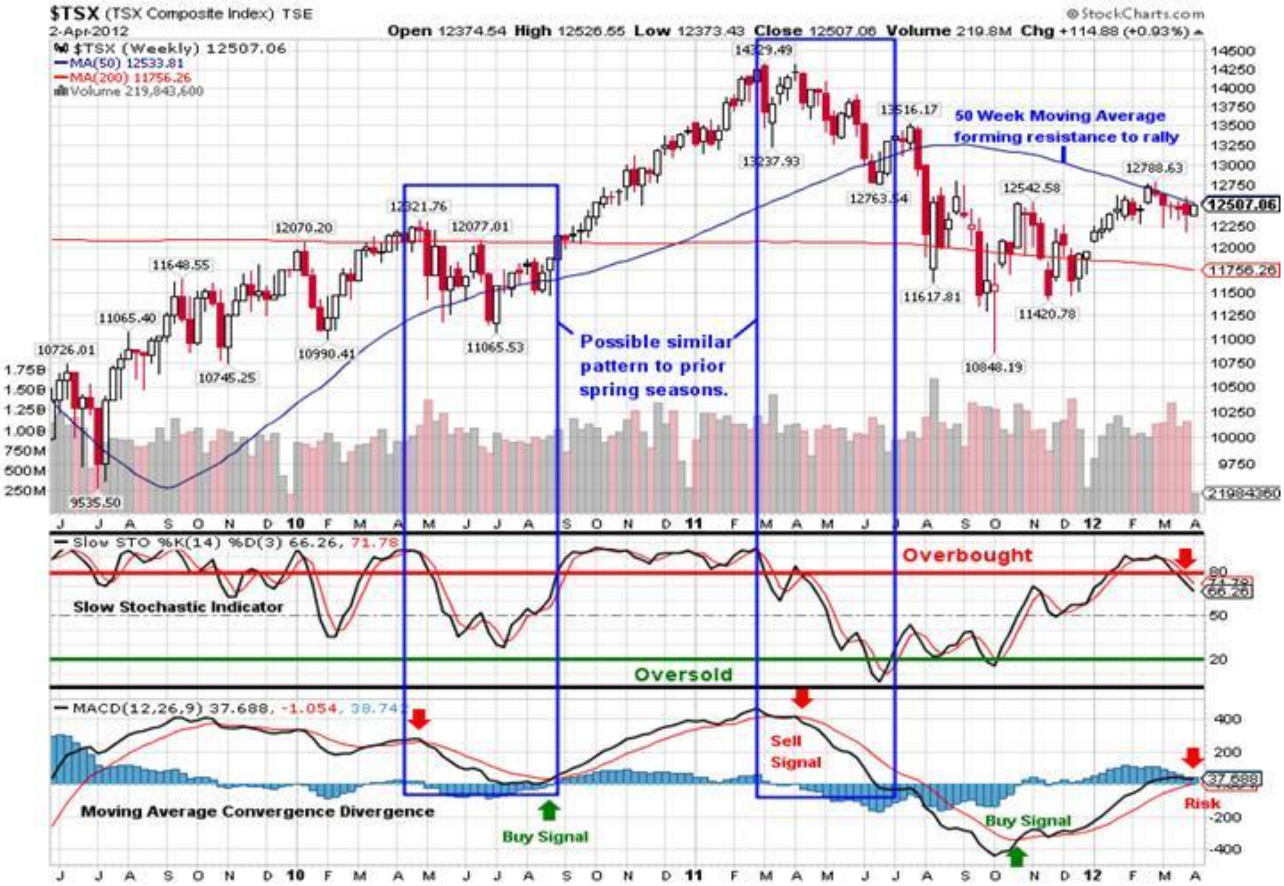
Earnings season in April often marks the peak in stock markets. Underlying economic indicators are generally much stronger than anticipated. Continued stimulative, low interest rates are likely to have their intended effect over the next few years.

However, technical analysis of market index charts reveals some short-term warning signs coming this spring. Even though a longer-term recovery seems to be unraveling, it may be slower and weaker than in the past due to the higher levels of existing sovereign and personal indebtedness. Investors should view short-term weakness as opportunity to build a more growth-oriented portfolio.

Technical Analysis

Stock prices move based on the media's news, supply and demand for the underlying stock, and simply emotion. "Fair value" is something that stocks seldom trade at, and something investors with a substantial financial background seldom agree on. A branch of economic study focusing on behaviour (sometimes called neuroeconomics or behaviour economics), tries to find patterns in the way market participants behave. Their behaviour is not always rational – in fact authors like Dan Ariely might say it is "Predictably Irrational", the name of the book he published.

Technical Analysis of charts has been developed for decades. During the last fourteen years, where buy and hold strategies have netted equity investors close to nothing, strategies that involve some trading have received more attention. Technical analysis is still somewhat of an art, but does have some commonly-used practices that are quite useful in buying and selling securities.



Seasonal investors "buy when it snows and sell when it goes". The chart above shows how the last two (actually three) spring seasons have all had negative performance. (But no statistic is perfect, the spring quarter in 2009 was one of the most positive quarterly return periods in history). Simply entering April is a reason to begin being cautious with stocks.

Stochastics and the moving average convergence divergence (MACD) are tools that determines momentum of a stock relative to itself. Stochastics are primarily used as short-term trading tools but can help confirm patterns identified by other disciplines. Stochastics often stay in overbought and oversold territory for long periods of time. In fact, once an index becomes overbought, it often stays that way during the entire subsequent growth phase (while many value-oriented contrarians complain and wait for a bargain, they miss the entire move in the market). Being overbought should not prevent one from buying, but moving from an extended period of a security or index being overbought back below being overbought can be a sign that the current rally has ended. The current period is one such time when the market was overbought, but is already starting to weaken. One current positive, is that the TSX Index did not become overbought for very long, which means that any subsequent correction may also be relatively short.

MACD is a smoother indicator. It provided a buy signal in the TSX composite starting somewhere in October or November of 2011, and has been in a positive position ever since. Recently, there is risk that the MACD line (black) crosses its signal line (red) which would be a sell signal. If the MACD also crossed the "zero-line" of its axis, it would be an extremely strong sell signal. Current trading activity is dangerously close to triggering both these negative signals, although this has not yet occurred.

On the price chart itself, the 50-week moving average represents the average price an investor has bought the index over the last trailing year. This price tends to be resistance when the market is trying to recover and support when it breaks down. In this case, I make three negative observations: the moving average is going downwards; the index level is below the moving average, and the market has unsuccessfully broken through this moving average for six weeks now. One positive observation is that the market has set higher lows each time it has corrected subsequent to mid-October, 2011. It would need to set a higher low again moving forward to continue to be optimistic about a longer-term recovery.

Despite all of the positive headlines about employment and economic growth, the chart above shows that investors in Canada are starting to take profits. Short-term caution is warranted. Note that my analysis of the U.S. indexes are similar but show a slightly more optimistic outlook. You'll have to come to my seminar next month to learn more.

Managed Accounts – March Transactions

Managed accounts are discretionary accounts in which I can proactively make trades in a client's best interest based on a written Investment Policy Statement and an intimate understanding of their financial goals. Conflicts of interest from commission are eliminated since commissions are not charged on individual trades. Logistical difficulties in contacting clients and obtaining authority for changes they would likely want are eliminated and all parties gain time not spent on discussing small details of individual securities. Instead, time can be focused on wealth planning and discussing what the client feels is important and wants to discuss.

The comments below represent changes I have already made for managed clients, but also represent a good source of ideas for those that manage their own portfolio and rely on me for implementation, ideas, and a source of professional feedback.

Summary: *Cash positions were increased during the later stages of March, as financial markets moved to short-term highs. My quantitative model is showing a rotation in the stocks it is selecting, moving slowly out of defensive sectors into early recovery stage sectors such as financial stocks and consumer discretionary companies. Unfortunately, most of the companies attractive to buy on an earnings and fundamental basis tend to be at very high, short-term overbought levels. Market weakness over the spring will likely be treated as a buying opportunity for securities showing the greatest opportunity. A small position in both fixed income and equity was taken in the early stages of a potentially stronger U.S. real estate market.*

New Positions:

Walton Westphalia Development Corporation: This investment consists of a combination of a seven-year 8% debenture and common shares in a land development in Washington DC (by Baltimore, close to Andrew's Air Force Base). The project specifically is for the immediate development of infrastructure on the land (over three phases), and then sale to multiple developers. Holders of this security are only developing infrastructure, not the final properties – development companies the land is sold to will do that. The vacancy rate in this area is substantially lower than other areas, and the unemployment rate is about half of the country's average.

Existing Positions Added To:

Alamos Gold: Alamos has continued growth and expansion projects that make it an attractive security to hold. Recently they announced a 6% increase in proven and probable reserves including good exploration results at the El Victor North site. The shares recently have traded between a low of almost $16 and high of nearly $21, primarily in response to the underlying changes in gold commodity prices. A covered call strategy provides lucrative premiums and sets a sell target of $20, while additional shares were acquired last month when they approached a $17 level. Gold appears to be in the late stages of a long-term rally and is likely to move to an underweight position in managed portfolios in 2012.

Ishares MSCI Brazil Index: The Bovespa Index in Brazil (up 13.3% in C$ year-to-date), the BSE Sensex 30 Index in India (up 14.4% in C$ year-to-date) and the DAX Index of Germany (up 18.3% in C$ year-to-date) were three of the best performing markets in the world during the first quarter of 2012. Exposure to the Brazilian market was increased last month. Exchange traded funds (ETFs) are traded in managed accounts in countries that exhibit relative strength to Canada and have the advantages of a low expense ratio and the ability to write covered calls on them for income and a sell discipline.

Completely Sold Positions:

Canadian Real Estate Investment Trust: This company is a personal favourite of mine because it was the first new issue I ever purchased for clients in 1994. At this point, the shares are trading close to an all time high, and the company has started to hit some real challenges in continuing to grow. My models are revealing far too many companies with much greater potential, while the relative valuation of these shares is remarkably high.

Keyera Corp: Keyera was originally acquired in 2009. In January the position held was cut in half, as the outlook for the natural gas business, service companies, and facilities Keyera owns, deteriorated. Last month, fundamentals continued to weaken, and the price of the shares also began to decline to levels that decisively broke the prior three-year uptrend. Estimate revisions have become very negative, causing the position to be entirely exited.

Reduced Positions:

Canadian Energy Services & Technology: Half of the position owned in this high-growth business is intended to be traded. On their chart, the shares appear to be trading between a low of close to $10 and peak close to $13. The underlying strength of the company's earnings growth combined with its attractive 5.0% dividend have earned it a longer-term position that compliments the trading one in the managed portfolio. As the position neared $13, half was sold in March.

Covered Calls Written:

Rogers Communications Jul $41
Valeant Pharmaceuticals Intl Jul $56

May Seminar

On Thursday, May 3rd, 2012, I will host a market summary seminar in our boardroom. I hope to discuss current developments in the financial market and the instruments and strategies best used to take advantage of current opportunities. It will be over the noon hour with lunch and refreshments provided. I will send you an invitation by email closer to the event date to confirm your attendance.

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