Market Review | June 2018

Please find below our monthly market review. Please don't hesitate to contact us if you have any questions.

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Economic Highlights

Bank of Canada hints at July hike

The Central Bank left the overnight rate unchanged at 1.25%, but hinted at a July hike. While acknowledging uncertainties about trade policy and housing (amidst the ongoing adjustment to new mortgage guidelines), the BoC said that "developments since April further reinforce Governing Council's view that higher interest rates will be warranted to keep inflation near target". The central bank sounded more upbeat about the labour market by emphasizing its expectations that solid labour income growth will support housing activity and consumption going forward.

Tariffs will hurt Canadian exports

In the 12 months to March 2018, Canadian exports of steel products to the U.S. amounted to C$7.4 bn and those of aluminium products totalled C$11 bn. Taken together, those represent less than 5% of Canadian goods exports to the U.S. and less than 1% of Canadian GDP. While the impacts are small, those measures open the door for a broadening of tariffs to include more goods, something that cannot be entirely ruled out as U.S. politicians seek to boost their approval ahead of mid-term elections.

OPEC are targeting slow price increases

On May 25, Saudi Arabia and Russia announced their plan to ease production cuts in the next quarters and, unsurprisingly, oil prices reacted negatively to the news. Despite some short-term pain, OPEC's decision should only have a very limited impact on the long-term horizon, as an exit strategy from the supply reduction agreement was already in the cards for 2019. In a way, OPEC took on the mantle of an energy central banker whose mandate is to reduce crude's volatility. The primary goal was to put a floor on prices until the overproduction situation resolved itself and, on that front, they were wildly successful. Now they are managing an orderly appreciation in value and as long as the cartel has some spare capacity, they should be able to reign in runaway moves. Consequently, we expect they will achieve their objective and help prices to slowly increase by year-end.

Asset Class Review

Fixed Income

U.S. 10-year Treasury yields initially received a boost from strong economic data, reaching a fresh 7-year high of 3.12% on May 18, but completely reversed course in the second half of the month, following dovish FED minutes and Italy's political jitters. Canadian 10-year rates also backed off late in May, as the Bank of Canada left its policy rate unchanged at 1.25% and opened the door for a July rate hike in the face of robust economic activity and accelerating inflation.

Canadian Equities

The S&P/TSX delivered its best monthly performance in nearly two years (July 2016), supported by rising commodity prices and outpacing all major foreign equity indices. Gains were particularly strong in the Healthcare, Technology, Industrials, Materials, and Consumer Discretionary sectors, while Utilities and Telecom lagged.

U.S. Equities

U.S. equities closed the month in positive territory and volatility remained well contained for the most part, supported by a stellar Q1-2018 earnings season and robust economic indicators.

Commodities

Crude oil prices have been stirred up in both directions through the month, initially pushed higher by President Trump's decision to pull the U.S. out of the Iran nuclear deal, and latter dragged down by rumours surrounding OPEC's intention to increase supply.

Foreign Exchange

This is the second consecutive strong month for the greenback, having gained more than 7% against the euro since its February trough, as growth differentials started turning in the U.S.'s favour and Italy's political crisis escalated.

For its part, the loonie closed the period marginally weaker after the confirmation that the U.S. would follow through with its threat to impose tariffs on Canadian steel and aluminum. This announcement cancelled the positive effects of the BoC's upbeat comments on inflation and growth.

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