

**July 1, 2011 Edition - Ottawa**

The year got off to a good start, the markets were focused on improving earnings, stronger economic data, and all indicators seemed to point to a global economic recovery. In early April of this year all that changed. Since the market peaked in mid-April, we have seen a 10% decline in the TSX and a 23% decline in the Venture exchange. Our neighbours south of the border have fared a little better with the S&P 500 down about 8% while NASDAQ fell 9%. There are strong parallels between investor's sentiments today and where they were at this time last year. The bottom line is that, just like last year, I believe that confidence will return to the equity markets in the second half of this year and the performance should improve dramatically.



**Jim Armiento**

### **Instruments like Gold or Commodities**

In the December update, I spoke of several investment themes and positioning for 2011. Reducing the holdings in commodity based assets, as well as small cap holdings and looking for investment opportunities south of the border was one of them. Although I am still a long term bull on commodity prices, particularly energy, there are some short term issues. The monetary tightening that is currently underway in China has been a drag on commodity prices for the first six months of 2011. Emerging markets, led by China, have been the main driver in the demand for our commodities, and Canadian equity markets are closely tied to the growth in these economies. In an attempt to fight inflation and orchestrate a soft landing we have seen the Chinese implement policies that would slow down the demand for our commodities. It is difficult to say just when the monetary tightening will subside but I believe that the markets could anticipate this occurrence as early as this summer and the commodity rally will get its next leg up in the second half of this year.

### **The World Economy**

The U.S and China are the main growth drivers for the world economy and the contrast in the current economic policies reflects the broader stark contrast between the emerging markets and the developed nations (North America, Europe). The emerging markets are concerned about

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inflation and the rapid level of growth while the developed world is worried about deflation and the lack of growth. While China has been doing everything it can to slow down its economy, the U.S has taken unprecedented steps in an attempt to get its economy off life support. What we need to see in the U.S is better employment numbers and strength in the U.S real estate market. Recent economic data in the States seems to be indicating that the worst is behind them. With plenty of excess capacity there is no reason to expect an increase in U.S interest rates any time soon. This should all be positive for the equity markets in the second half of this year.

## **What's Next**

We started the year gradually transitioning the portfolios by reducing exposure to small cap holdings as well as commodities and building positions in cash or high yield bonds. While the big picture is not completely clear, I do believe that the correction has run its course. Stocks are still relatively cheap and earnings have been robust. Earnings reports will commence in early July and I believe this will be the catalyst that begins our summer rally. However, this leg up in the market will not be as easy as 2009-2010. The market will be moving up but it will remain range bound. Large cap equities will be the leaders and dividends will become more important. Recently both BMO and Horizons have come out with ETF's (Exchange Traded Funds) that employ a "covered call" strategy. These strategies tend to outperform in sideways and declining markets and are well suited for this stage of the recovery. I will be looking to reduce cash and become more active in the second half of the year.

**"If you have a temperament to be afraid when everyone else is, you will not do well in the equity markets." Warren Buffet 2010**