



## American Recovery?

*"There are two fools in this world. One is the millionaire who thinks that by hoarding money he can somehow accumulate real power, and the other is the penniless reformer who thinks that only he can take money from one class, and give it to another, and all the world's ills will be cured."*

Henry Ford

The first quarter of 2012 represented the strongest start for the US stock market since 1998. Japan had its best quarter in 24 years. Canada no so much, it was a laggard, as fear of a China slowdown hurt the commodities and materials sectors. There was a reduction in fears about an extremely negative outcome in Europe, combined with stronger US economic data, which were the catalysts for the upside.

In the face of challenges for developed economies, there is a persistent view of America as an "empire in decline." This was reinforced by last year's downgrade of US debt and by the stalemate in congress over dealing with America's deficit and debt challenges. If you read any of our writings, you will know I don't subscribe to that view. Without dismissing its issues, America's biggest competitive advantage is its vitality and capacity for change and innovation. It continues to dominate high tech and remains a magnet for the best and brightest talent from around the world.

I'm not alone in that view. Here is an excerpt from Warren Buffet's annual letter to investors released in February:

*"In 2011, we will set a new record for capital spending, \$8 billion and spend all of the \$2 billion increase in the United States. Money will always flow toward opportunity, and there is an abundance of that in America. Commentators today often talk of "great uncertainty." But think back, for example, to December 6, 1941, October 18, 1987 and September 10, 2001. No matter how serene today may be, tomorrow is always uncertain."*

*"The prophets of doom have overlooked the all-important factor that is certain: Human potential is far from exhausted, and the American system for unleashing that potential, a system that has worked wonders for over two centuries, despite frequent interruptions for recessions and even Civil War, remains alive and effective. We are not natively smarter than we were when our country was founded; nor do we work harder. But look around you and see a world beyond the dreams of any colonial citizen. Now, as in 1776, 1861, 1932 and 1941, America's best days lie ahead."*

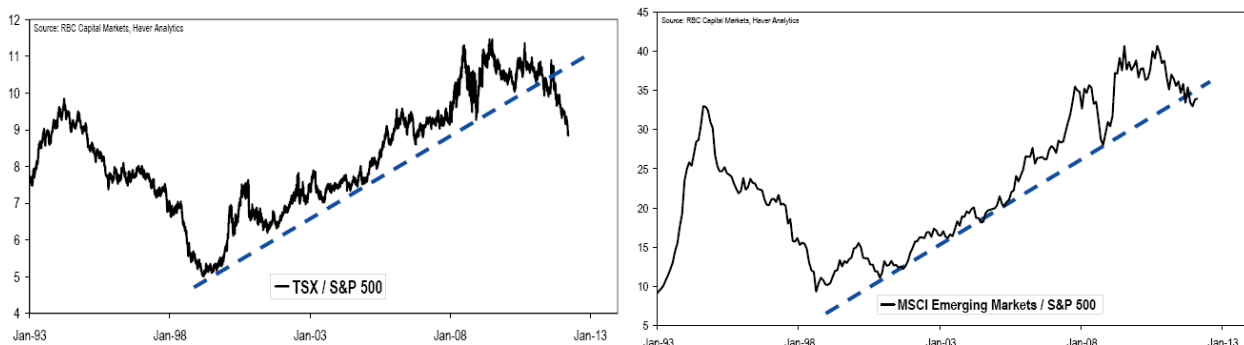
That doesn't mean there are some speed bumps in the period ahead. But when I even dare mention the US market, it is usually met with disdain, because the S&P 500 has barely moved in 12 years, and the rising Canadian currency made it a double whammy. After a

decade of poor performance, however, it would be a poor choice not to explore the attractiveness of the US markets.

As for Canada vs. the US, while there is no denying a better fiscal situation in Canada and generally a saner political situation, the USA still accounts for 70% of Canadian exports. As much as we would like to think we are not joined at the hip, it would take major surgery to separate the two; thus why US elections should matter to Canadians.

Canadian markets have begun to show some worrisome signs. Valuations in certain sectors, especially those that pay big dividends, have begun to reach higher levels of acceptable values ranges. This is probably not due to growing business, but more likely a lack of viable alternatives for Canadian investors seeking income. Other segments are going through regulatory issues (banks), cost headwinds (gold and oil) or are highly sensitive to interest rates.

As you can see on the following chart, the TSX has outperformed the S&P 500 since 1998. That relationship recently changed, as the commodity heavy TSX of Canada and MSCI Emerging Markets have reversed trends against the S&P 500:



The United States has gone through an arduous period of intervention and rehabilitation since the Great Recession of 2008-2009. It was the economic equivalent of the emergency room. Then it went to intensive care, to the recovery room, and just recently was discharged from the hospital. The US is up and walking, but perhaps not ready to run or sprint just yet. The US recovery has helped to set a calming and constructive tone to the rest of the world, even as Europe still struggles with a debt crisis on the periphery, and while emerging markets experience a cyclical slow down.

Politics is also in play as this November's presidential and congressional elections will decide who will lead the world's superpower. The economic improvements have already helped President Obama's re-election prospects, as has the continuing drama of a drawn out, divisive, expensive Republican primary.

While heading in the right direction, there is no guarantee the process continues. The recovery is fragile. We need caution, discipline, good management and a bit of good luck right now.

Once we get running, then it will be time to look at getting into a position to repay the massive hospital bill.

Stay Tuned,

Vito Finucci  
Vice President & Director  
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