

Another 'Irrational Exuberance' Moment?

Equity markets pushed higher this week, despite a brief scare from geopolitical tensions in the Middle East and a downed Malaysian passenger jet. The S&P 500 rose 0.5%, with technology and banks leading the pack, while the TSX jumped 0.9% as oil prices moved higher. Encouraging North economic data provided some support, if one can look past the rain-soaked U.S. housing starts report.

With stocks pushing steadily higher, the Fed's Monetary Policy Report continued to dabble in the equity valuation debate. In it, the Fed largely reiterated the recent messaging that *"valuation measures for the overall market in early July were generally at levels not far above their historical averages"*. But more

interesting was the pointed remark that *"valuation metrics in some sectors do appear substantially stretched—particularly those for smaller firms in the social media and biotechnology industries"*, and many likened this to Alan Greenspan's *"irrational exuberance"* moment. For the record, note that the forward p/e on the S&P 500 in recent days sat close to that seen at the time of that famous speech in December 1996 (15.6 versus 16.2), while the cyclically-adjusted p/e is within 1.5 points after rising briskly over the past year. Of course, Greenspan's

Market Performance as of July 18, 2014

	Current Price	Performance (percent)					2013
		1 Week	1 Month	3 Months	1 Year	YTD	
S&P/TSX	15,267	0.9	1.0	5.3	20.9	12.1	9.6
Dow Jones	17,100	0.9	1.1	4.2	10.0	3.2	26.5
FTSE 100	6,749	0.9	-0.4	1.9	1.7	0.0	14.4
China CSI 300	2,164	0.8	0.2	-2.7	-3.6	-7.1	-7.6
DAX	9,720	0.6	-2.1	3.3	16.6	1.8	25.5
S&P 500	1,978	0.5	1.1	6.1	17.1	7.0	29.6
CAC 40	4,335	0.4	-4.3	-2.2	10.4	0.9	18.0
NASDAQ	4,432	0.4	1.6	8.2	22.7	6.1	38.3
NIKKEI 225	15,216	0.3	0.7	4.8	2.7	-6.6	56.7

Source: Bloomberg.

comment did a better job of marking the start of the technology bubble than the end, drilling home the point that stocks, when expensive, often get even more expensive before they get cheaper—especially if monetary policy allows it.

While the Fed Chair was musing about valuations, earnings reports were rolling in better than expected, especially in the financial sector. While trading revenues were down across most banks, the declines were not as sharp as many had warned. And, while mortgage originations are down from year-ago levels, stronger investment banking results and improving consumer and business lending are helping. Here are some encouraging comments from the front lines:

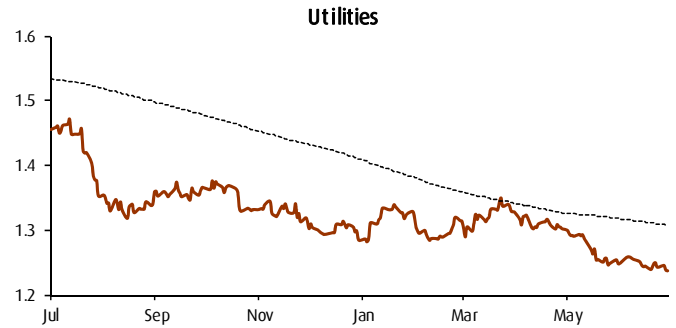
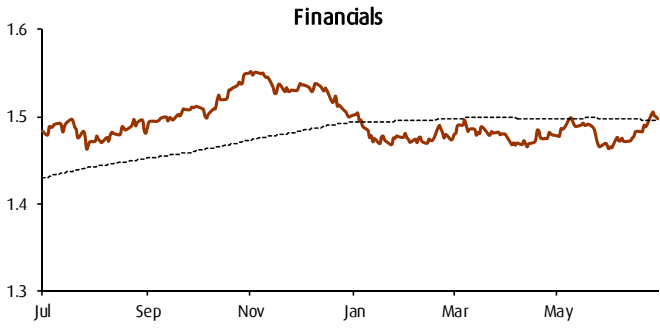
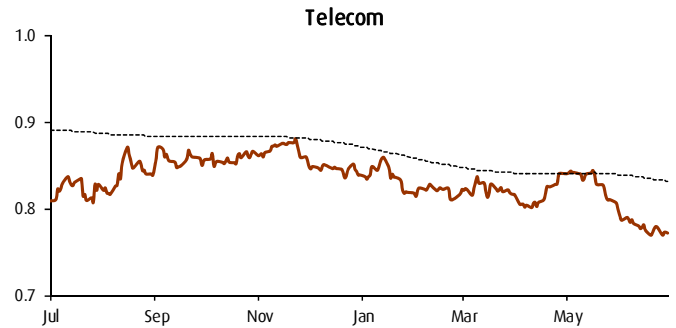
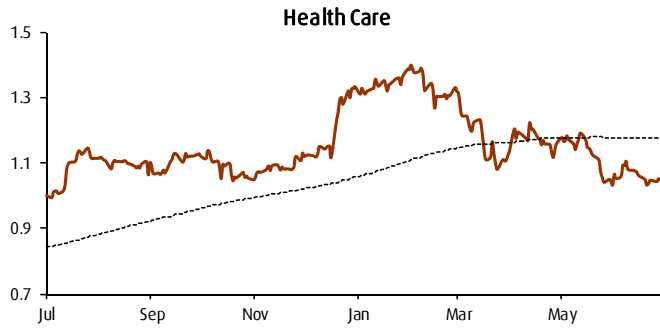
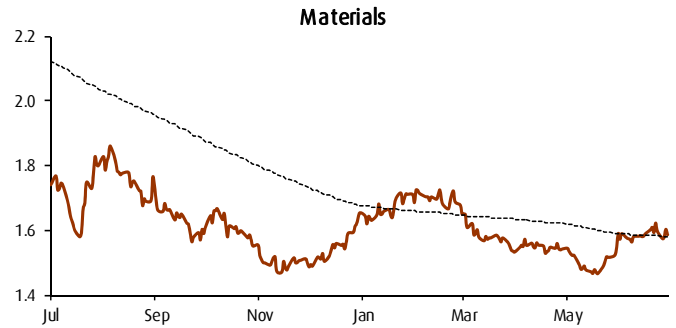
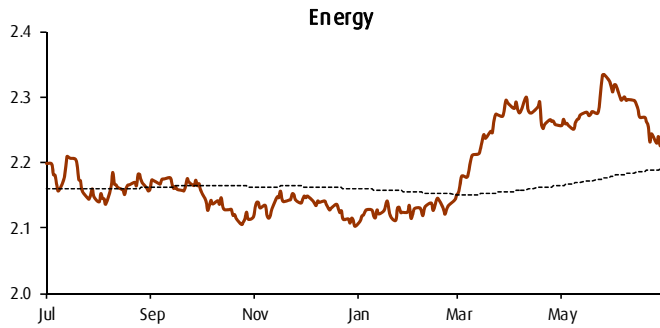
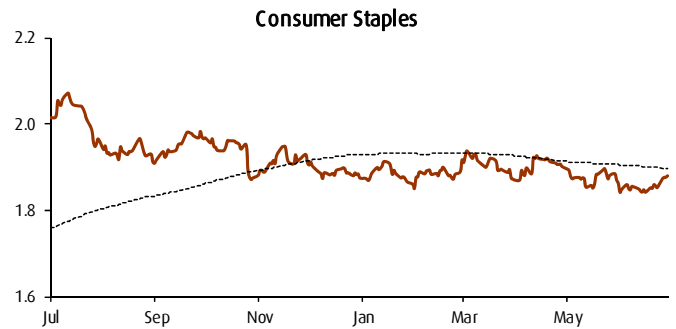
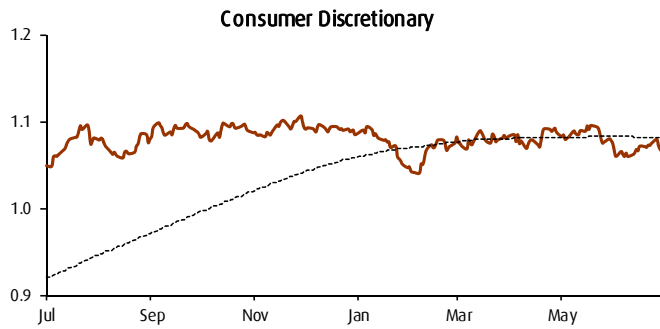
JPMorgan: *"Across the board, consumers are spending healthily in all categories"*.

Bank of America: *"The economy continues to strengthen... Consumers are spending more, brokerage assets are up by double digits and our corporate clients are increasingly turning to us to help finance business expansion and merger activity"*.

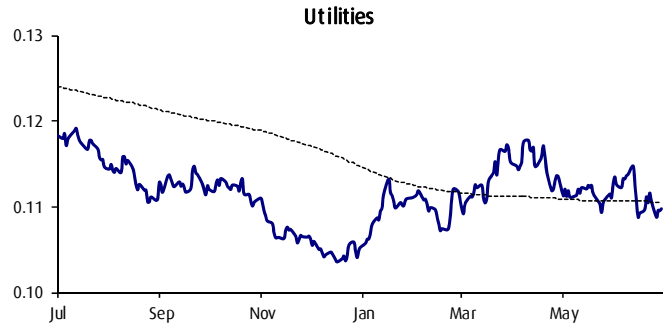
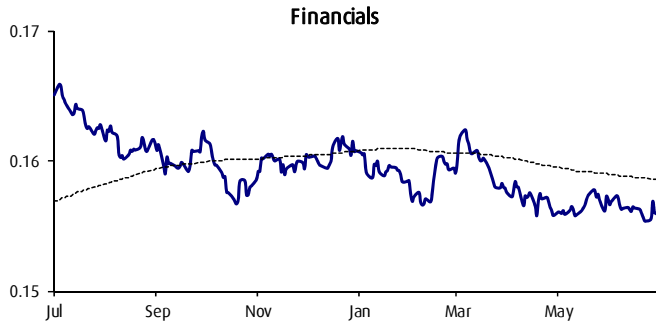
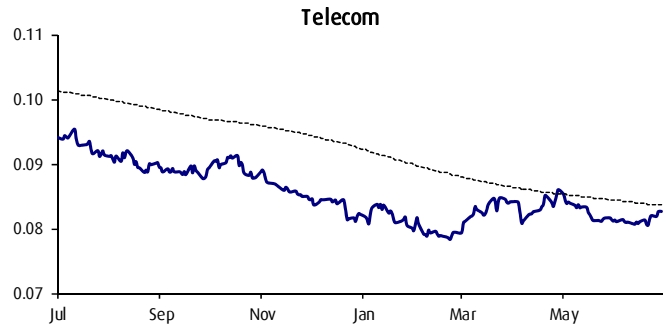
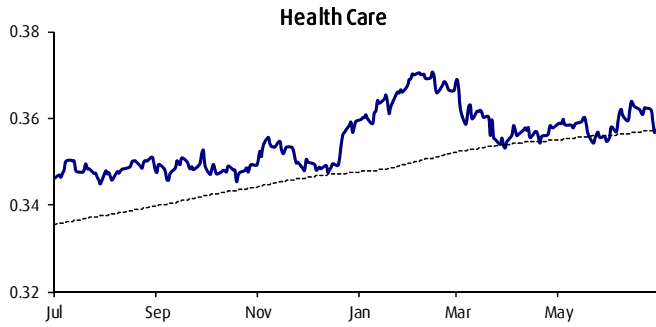
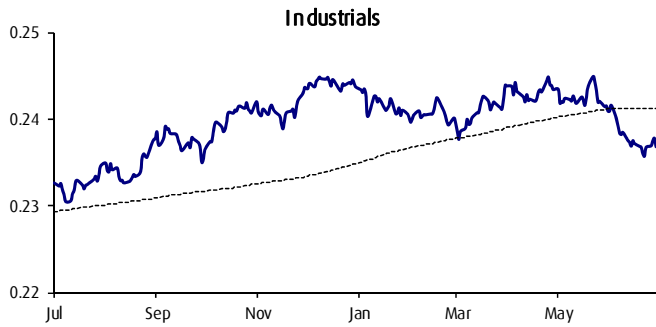
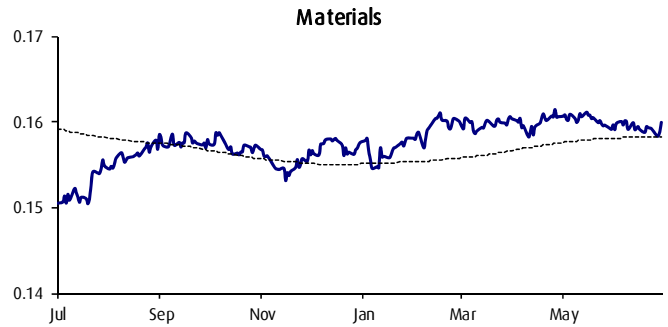
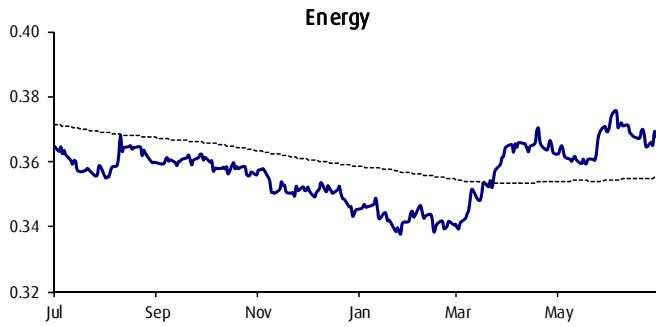
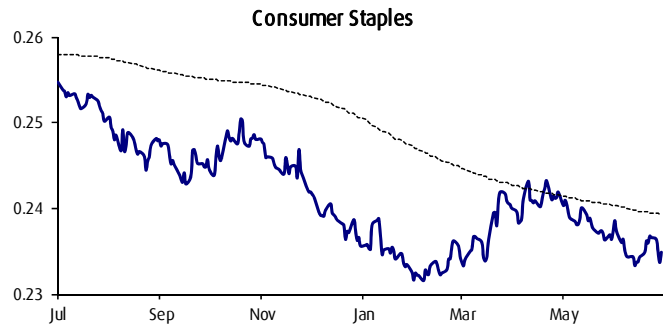
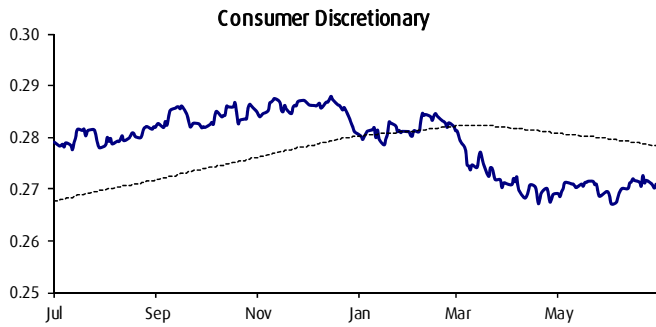
Citigroup: *Corporate loan growth has been "pretty widespread"*.

Indeed, financials have been a major factor behind the solid start to the Q2 earnings season. Just over 76% of S&P 500 companies have topped earnings expectations so far, according to Bloomberg's tally, and nearly 70% have beaten the mark on revenues. The technology sector has been no slouch either, and broad forward-year S&P 500 earnings expectations are again moving higher. We'll get a broader sector picture of earnings performance in the coming weeks, but so far, generally upbeat results are consistent with our outlook for stronger economic growth in Q2 and beyond, and exactly what equity investors need to see in light of recent valuation expansion.

TSX Sector Performance (Relative to the index, dashed line = 200-day m.a.)



S&P 500 Sector Performance (Relative to the index, dashed line = 200-day m.a.)



North American Sector Performances as of July 18, 2014

S&P 500 Sectors	1 Week	1 Month	3 Months	1 Year	YTD	2013
Information Technology	1.5	3.2	10.5	26.6	11.0	26.2
Banks	1.1	-0.6	2.5	9.2	4.8	32.3
Financials	1.0	0.4	4.8	10.5	4.7	33.2
Telecom Services	1.0	2.5	3.8	2.5	4.7	6.5
Energy	0.7	-0.1	6.3	18.5	10.8	22.3
Materials	0.6	0.9	5.2	24.4	8.1	22.7
Industrials	0.3	-0.9	2.7	20.2	3.3	37.6
Cons Discretionary	0.1	1.5	5.9	13.3	1.0	41.0
Utilities	-0.2	-1.5	1.0	8.5	12.4	8.8
Cons Staples	-0.2	0.0	3.6	8.3	4.9	22.7
Health Care	-0.3	2.3	7.9	23.0	10.6	38.7
S&P 100 Large Cap	0.9	1.7	6.5	16.2	6.8	27.4
S&P 400 Mid Cap	0.1	-0.6	4.5	14.6	5.2	31.6
S&P 600 Small Cap	-1.9	-3.3	-0.5	10.9	-1.6	39.7
S&P 500	0.5	1.1	6.1	17.1	7.0	29.6

TSX Sectors

Industrials	3.0	4.1	13.2	33.2	15.2	34.9
Cons Staples	1.8	1.2	5.2	11.0	11.5	21.4
Financials	1.5	3.0	6.5	21.4	9.3	19.1
Banks	1.4	3.3	7.8	25.3	11.1	17.7
Energy	1.1	-2.6	2.5	22.8	16.9	9.9
Health Care	1.0	1.3	-0.4	24.5	2.6	71.7
Cons Discretionary	0.3	-0.1	3.9	21.7	9.3	39.5
Telecom Services	0.0	-3.2	-0.5	11.3	2.1	8.1
Utilities	-0.2	-0.5	-2.2	1.4	6.9	-8.6
Materials	-1.2	3.9	8.7	15.6	17.0	-30.6
Gold	-1.8	6.1	13.8	18.5	25.5	-45.0
Information Technology	-2.1	3.0	6.1	30.7	11.1	36.2
REITs	0.4	0.7	0.0	3.8	6.7	-10.6
Income Trusts	0.3	0.3	0.1	6.1	6.3	-7.6
S&P/TSX 60 Large Cap	1.3	1.9	6.3	21.0	12.2	9.8
S&P/TSX Mid Cap	0.0	-1.3	2.6	20.6	11.8	8.8
S&P/TSX Small Cap	-0.6	-1.7	4.0	25.9	14.6	4.4
TSX	0.9	1.0	5.3	20.9	12.1	9.6

Source: Bloomberg.

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