

THE VANCOUVER SUN

Higher gold prices, flat Canadian stocks seen In 2012, portfolio managers also forecast higher interest rates, lower real estate prices, loonie between 90 cents and par and flat food costs

BY MARK JASAYKO AND NEIL MCIVER, VANCOUVER SUN JANUARY 3, 2012

A year ago, Vancouver portfolio managers Mark Jasayko and Neil McIver made forecasts about the direction of world currencies, stock markets, gold prices, oil, natural gas, commodities, interest rates, Canadian real estate and carbon credits. They were on the money on every front except interest rates. Here are their fearless forecasts for 2012:

Last year was characterized by volatility as Europe's debt crisis created dramatic up-and-down days in global stock markets. Greece was at the centre of the storm, causing anxiety for investors throughout the year. Greece will continue to be a source of worry as it stumbles toward a technical default of its debt obligations in 2012. We still believe that inflation resulting from printing money is the only way for modern economies to escape from the black hole of debt and that early signs of this eventual outcome will become more evident this year.

CANADIAN STOCK MARKET

We correctly anticipated that Canada's exposure to natural resources would provide headwinds for the Canadian stock market. Even though we are approaching fair valuations, these headwinds should continue into 2012 as resource demand from China slows down. In addition, Canada's large financial-sector weighting in stock markets will cap the potential for gains as Canadian financial institutions face challenges from a rising interest rate environment. We predict a flat performance for the Canadian stock market by the end of 2012.

AMERICAN STOCK MARKET

As we predicted, the one bright spot in 2011 among the global stock markets was the U.S. Decent valuations in many sectors, close-to-zero short term interest rates, the promise of more central bank liquidity, and being the least ugly of all the world's miserable markets benefited U.S. stocks. We

continue to foresee single-digit gains for 2012 as all of these factors are still in place. As well, the fourth year of the presidential cycle is typically a good one for U.S. stocks.

U.S. DOLLAR

We expected the U.S. dollar to benefit from its safe-haven status in times of financial panic in 2011 and expect this to continue through 2012. The U.S. dollar should see gains against the euro, the yen, and the Canadian dollar. The trade flows between Canada and the U.S. will keep the exchange rate in a tight range. If global economic crisis persists during 2012, the Canadian dollar will fall to the 90 cent range as foreign investors rush to the U.S. dollar. If not, expect a Canadian dollar trading between 95 cents and par for most of the year.

CANADIAN DOLLAR

As discussed above, the Canadian dollar should remain between 90 cents and par relative to the U.S. dollar. The low end of the range is five cents lower than last year, because of slightly lower international demand for our resources in 2012.

INTEREST RATES

This was the only item last year that moved in the opposite direction of what we forecast. We had expected an increase of about half a percentage point for longer-term rates in the U.S. and Canada. The rush into U.S. Treasury bonds, with their miserly yields in the face of the eurozone crisis, surprised us. This put a lid on rates. However, history tells us that excessive money-printing, like we have seen over the last number of years, will result in inflation and higher interest rates. The European Central Bank also appears to be on the cusp of falling prey to the seduction of printing money, adding to inflationary potential.

GOLD

Our 2010 forecast was \$1,500 per ounce. Our 2011 forecast was \$1,700. Our forecast for 2012 is \$1,900. We don't have faith that politicians and policy-makers have the skill to find a clean solution for the overhang of burdensome global debt. As this faith declines generally, it would not be a stretch for gold to recapture and hold onto its highs from the past year. Gold is now up for 11 years in a row. But, it is not in a bubble. The real and present bubble is the exponential growth in government debt over the last decade. Gold, which should keep pace with the growth in government debt, is still lagging considerably.

CRUDE OIL

Last year we predicted oil would trade in a range from \$90 to \$100. We think 2012 will also be characterized by this trend. Forces keeping the price of oil from breaking out include an expected recession in Europe and a general global economic slowdown. Sabre-rattling from rogue nations like Iran, and other possible supply and logistical problems, are probably worth an unsustainable \$5 to \$10 spike, but that is about it.

NATURAL GAS

Excess supply and the common practice of flaring off natural gas during the oil refinement process suggest that the upside in price is extremely limited. Seasonal effects, such as a higher price during the higher demand winter months, can still impact the market. However, the average price through the year will be lower than in the past couple of years.

GRAIN/COMMODITIES

Food security will continue to be a theme because of its importance in maintaining social and economic order in emerging economies. Governments will be willing to pay a premium to secure access to grains, fertilizers, and other food commodities. However, natural resource commodities are vulnerable to a global economic slowdown, which should keep prices flat on average for the year.

CANADIAN REAL ESTATE

In Toronto and Vancouver, real estate prices have broken through the affordability ceiling. Prices elsewhere in Canada have eased off as we predicted last year. We also wrote last year that the record levels of debt carried by Canadians was concerning and that was later acknowledged by Bank of Canada governor, Mark Carney, as well as the Organization for Economic Co-operation and Development (OECD). Average personal Canadian debt loads grew even more during 2011 and now surpass levels in the United States. This is the No. 1 threat to real estate prices in general, and to prices in Toronto and Vancouver, in particular. A five-to-10 per cent decline nationally is likely, especially if our forecast of a half per-cent-point increase in interest rates comes to fruition.

CARBON CREDITS/CAP & TRADE

The political crusades focused on engineering green economies have lost momentum. With unemployment remaining at unacceptably high levels, the risk of increasing unemployment further by raising the cost of doing business would be political suicide for incumbents during an election

year. Expect U.S. President Barack Obama to relegate these policies far from implementation for the foreseeable future.

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