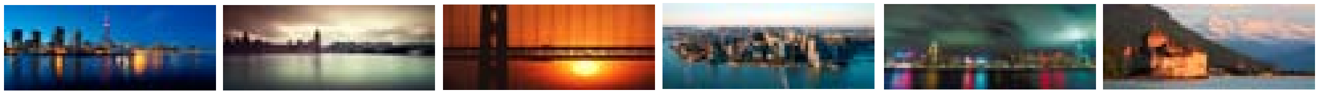
RBC Wealth Management

Global Insight Weekly



» Solid trade data boosted U.S. and Canadian stocks on Friday. Safe-haven sovereign bonds rallied across regions for the week.

» M&A activity is showing signs of life. An important North American industry is dominating the deal flow. (page 2)

» Global Roundup: An overview of Canada's weak employment report, and highlights from the U.S., Europe, and Asia Pacific. (pages 3-4)

Global Insight Monthly Now Available

The February edition includes RBC's latest thoughts about the economy, equities, fixed income, commodities, and currencies. The article titled, *Think Globally, Act Regionally*, discusses why strategies that capture regional trends should reap rewards this year. The monthly also includes two changes to our equity recommendations:

U.K. downgraded to "underweight." With its high proportion of defensive companies, it tends to lag when leading indicators rise. The economy faces a painful grind, and equity valuations are no longer cheap.

Canada upgraded to "neutral with a positive bias." As Chinese GDP growth improves further in the coming year, Canadian commodity stocks are likely to offer investors additional upside.

Equity Scorecard – February 8, 2013

Index (local currency)	Level	1 week	MTD	YTD
S&P 500	1,517.93	0.3%	1.3%	6.4%
S&P/TSX Comp	12,801.23	0.3%	0.9%	3.0%
FTSE All Share	3,294.27	-1.0%	0.2%	6.5%
Hang Seng	23,215.16	-2.1%	-2.2%	2.5%
Dow (DJIA)	13,992.97	-0.1%	1.0%	6.8%
NASDAQ	3,193.87	0.5%	1.6%	5.8%
Russell 2000	913.67	0.3%	1.3%	7.6%
STOXX Europe 600	287.34	-0.3%	0.0%	2.7%
German DAX	7,652.14	-2.3%	-1.6%	0.5%
Nikkei 225	11,153.16	-0.3%	0.1%	7.3%
Straits Times	3,270.30	-0.6%	-0.4%	3.3%
Shanghai Comp	2,432.40	0.6%	2.0%	7.2%
Brazil Bovespa	58,497.83	-3.1%	-2.1%	-4.0%

Note: Equity returns do not include dividends.

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All values in U.S. dollars unless otherwise noted.

Markets & the Economy

Market Scorecard – February 8, 2013

Govt Bonds (bps chg)	Yield	1 week	MTD	YTD
US 2-Yr Tsy	0.250%	-1.2	-1.2	0.3
US 10-Yr Tsy	1.950%	-6.5	-3.5	19.3
Canada 2-Yr	1.111%	-7.6	-4.6	-3.0
Canada 10-Yr	1.962%	-7.7	-2.8	16.4
UK 2-Yr	0.317%	-3.4	-6.0	-0.6
UK 10-Yr	2.095%	-0.2	-0.2	26.7
Germany 2-Yr	0.181%	-6.6	-8.8	19.6
Germany 10-Yr	1.609%	-6.3	-7.1	29.3
Commodities (USD)	**Price**	**1 week**	**MTD**	**YTD**
Gold (spot $/oz)	1,667.95	0.0%	0.3%	-0.4%
Silver (spot $/oz)	31.43	-1.2%	-0.1%	3.6%
Copper ($/ton)	8,164.50	-1.1%	0.4%	3.3%
Oil (WTI spot/bbl)	95.72	-2.1%	-1.8%	4.2%
Oil (Brent spot/bbl)	119.27	1.5%	1.4%	5.7%
Natural Gas ($/mlnBtu)	3.26	-2.3%	-2.1%	-5.2%
Agriculture Index	453.54	-2.0%	-2.5%	0.5%
Currencies	**Rate**	**1 week**	**MTD**	**YTD**
US Dollar Index	80.23	1.4%	1.3%	0.6%
CAD/USD	1.00	-0.7%	-0.6%	-1.1%
USD/CAD	1.00	0.7%	0.6%	1.1%
EUR/USD	1.34	-2.0%	-1.6%	1.3%
GBP/USD	1.58	0.7%	-0.4%	-2.8%
AUD/USD	1.03	-0.8%	-1.0%	-0.7%
USD/CHF	0.92	1.0%	0.8%	0.2%
USD/JPY	92.70	-0.1%	1.1%	6.9%
EUR/JPY	123.91	-2.2%	-0.5%	8.3%
EUR/GBP	0.85	-2.7%	-1.2%	4.2%
EUR/CHF	1.23	-1.0%	-0.8%	1.5%
USD/SGD	1.24	-0.3%	0.0%	1.3%
USD/CNY	6.24	0.1%	0.3%	0.1%
USD/BRL	1.97	-0.8%	-0.9%	-3.8%

Source: Bloomberg. Note: Bond yields in local currencies. Copper and Agriculture Index data as of Thursday's close. Dollar Index measures USD vs. six major currencies. Currency rates reflect market convention (CAD/USD is the exception). Currency returns quoted in terms of the first currency in each pairing. Data as of 9:30 pm GMT 2/8/13.

Examples of how to interpret currency data: CAD/USD 1.00 means 1 Canadian dollar will buy 1.00 U.S. dollar. CAD/USD -1.1% return means the Canadian dollar fell -1.1% vs. the U.S. dollar year to date. USD/JPY 92.70 means 1 U.S. dollar will buy 92.70 yen. USD/JPY 6.9% return means the U.S. dollar rose 6.9% vs. the yen year to date.

Most equity markets languished in negative territory for much of the week as large mutual funds and pension funds stepped to the sidelines and fast-money hedge funds took profits following strong gains since late last year. However, a number of markets pared their losses or flipped into positive territory on Friday with the help of solid Chinese and U.S. economic data.

Chinese exports rose by a swift 25% pace in December versus the year-ago period, and consumer inflation declined to 2% in January from 2.5% (see page 4 for details).

The U.S. trade deficit narrowed in December to its lowest level in almost three years, courtesy of a jump in industrial supply shipments and record energy exports. Shale oil production has helped vault the U.S. to the top position among fuel-exporting nations. Because trade plays an important economic role, the preliminary fourth-quarter GDP reading of -0.1% should be revised higher due to the lower-than-expected trade deficit, barring negative shifts from other sectors.

Solid U.S. earnings reports have also provided support for equities. The fourth-quarter S&P 500 earnings growth rate climbed to 5.2% year over year from 4.4% the previous week, according to Thomson Reuters I/B/E/S. That compares quite favorably to the 2.9% rate analysts expected when the quarter ended.

Comments by European Central Bank (ECB) President Mario Draghi have sparked a debate among market participants about whether or not he has officially entered the so-called global "currency war."

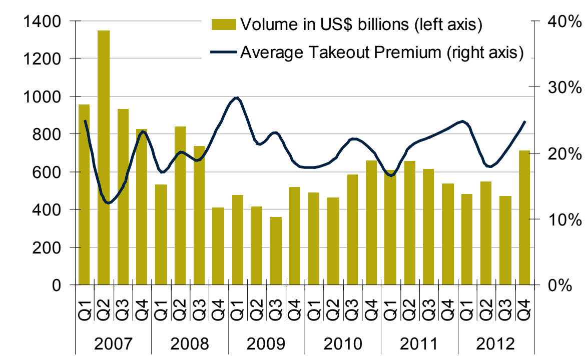
Draghi signaled the euro is too high and risks weighing on economic activity, reducing European competitiveness, and pulling inflation down to a sub-optimal level. However, he and the ECB Governing Council have yet to adopt formal policies aimed at weakening the currency such as lowering interest rates. For now, they seem satisfied with mild verbal intervention. So far, it's working. Since Thursday's ECB meeting, the euro dropped 1.7% against five major currencies.

A number of central bankers and policymakers, including in Japan, have been talking down their currencies in order to give their exporters an advantage. When talk turns to aggressive actions by major trade powers, it can devolve into a "race to the bottom" for currencies, which can create economic dislocations and earnings disruptions for multinational companies. From our perspective, the recent currency chatter among officials has yet to reach "war" status, but does warrant attention and is unlikely to go away anytime soon.

M&A Showing Signs of Life

Corporate deal making finally may be coming back in vogue. In fourth quarter 2012, merger and acquisition (M&A) activity rose to the highest level in four years (see chart). Executives dipped their toes in the water after acute European policy risks receded.

Global M&A Volume Bounced During Q4 2012 and Reached its Highest Level Since the Financial Crisis



Source - RBC Wealth Management, Bloomberg; data as of 2/6/13

During the past 12 months, acquirers spent the bulk of their funds buying companies headquartered in the U.S., followed by the U.K, China, and Canada.

Only five acquisitions topped $20 billion in the past year, four of which occurred in the fourth quarter. While some market participants are wringing their hands about this, we actually prefer when large transactions represent a relatively modest proportion of total volume.

Large deals have a dismal track record for shareholders. Since 1996, they have generated share price losses for acquiring companies roughly 66% of the time, according to a Bloomberg study. Of the 78 acquisitions examined, the acquirer's stock fell a median of 21% three years after the large deal was completed and underperformed the MSCI World Index by a median of 13%.

A large deal can fizzle because of an acquirer's inability to extract promised cost synergies (which are often overestimated to begin with), clashes in corporate cultures, poor execution, an initial misread of opportunities, or gross overpayment. Shareholders seem to reap greater rewards with small and mid-size deals—"tuck-ins" in which companies buy smaller rivals or expand product and service lines.

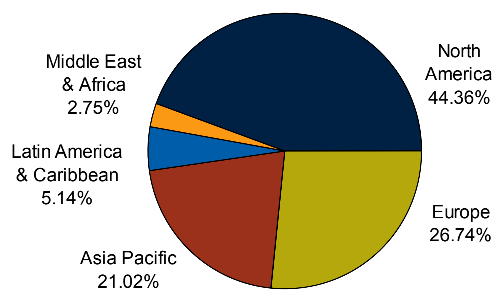
Among industries, oil and gas M&A activity continues to stand out, mainly because of the North American shale boom. After moving into the top position in 2011, the industry led again during the past 12 months thanks to a year-end frenzy (see chart below). Oil and gas deals surged $135 billion in fourth quarter 2012, up from the $38 billion average in previous quarters since 2001.

Acquirer energy firms paid 33% premiums for their targets, on average, during the past 12 months. By country, U.S., Russian, and Canadian oil and gas companies were the top targets. Among sub-industry groups, exploration and production companies were by far and away the most frequently sought-after firms.

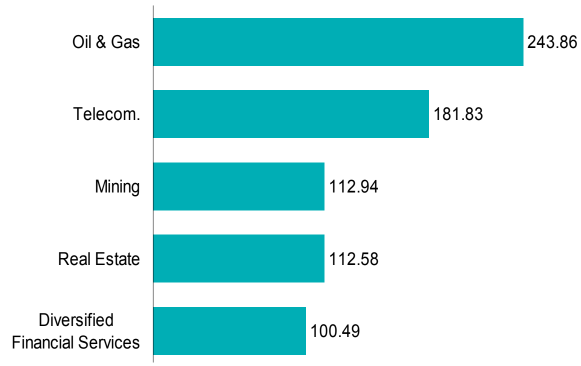
Global M&A activity should accelerate in 2013 if European and U.S. policy risks remain muted. Organic growth may be challenging to deliver due to ongoing global economic constraints, and corporate earnings could rise only modestly. So tuck-in acquisitions may provide attractive opportunities for companies seeking to boost revenue and profits.

Global Merger & Acquisition Activity for the Past 12 Months

Regional Breakdown of Target Companies (% of dollar volume)



Industries Leading in M&A Activity (in US$ billions)



Source - RBC Wealth Management, Bloomberg; 12-month data through 2/6/13

Global Roundup

United States

- **The strong 5% S&P 500 rally in January could bode well for the rest of the year if history is a guide.** Since 1970, there have been 12 other instances when the Index rose 4% or more in January. In 11 of the 12 instances, or 92% of the time, the S&P 500 rose by the end of the year. Better yet, the market rallied by an average of 12.7% from February through December, according to our national research correspondent. The only year it lost ground was in 1987 because of the October crash.
- **The 10-year Treasury yield** backed away from the 2.0% level and recorded its **highest weekly decline in yields so far this year**, although the 6.5 basis-point move was meager compared to weekly declines last year. Jitters about Spanish and Italian politics and concerns about the sluggish European economy drove global investors into safe-haven bonds, including Treasuries.
- **Coming up:** President Obama's State of the Union address (Feb 12); Advance Retail Sales (Feb 13); 55 S&P companies are scheduled to report earnings.

Canada

- The TSX ended the week up, as **BlackBerry** reported strong sales in the U.K and Canada. Several companies in Canada reported earnings results. In Energy, **Suncor** fell ~5% after it wrote off a $1.5 billion investment in its Voyageur upgrader, while **Husky** ended the week nearly flat. In Materials, despite strong copper sales, **Teck** was down just under 10% after it released lower-than-expected guidance, while **New Gold** had solid results. Lifecos trended higher, as **Manulife** and **Great West Life** reported stronger-than-expected earnings. **Just Energy** was a notable mover in Utilities, as its shares plunged after it announced a 32% cut to its annual dividend, coupled with a reduction in 2013 guidance.

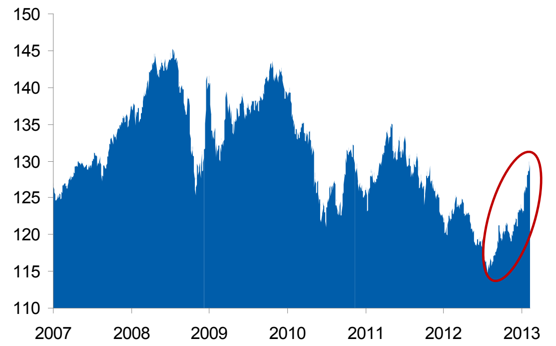
- **Canadian government bond yields moved lower** across the yield curve with the most-pronounced decline experienced in the 5- to 10-year component of the curve. **Weaker-than-expected economic data** increased the allure of federal bonds.
- Canada's January employment report was much weaker than expected, declining by 21.9K versus the expected 5K increase. This marks the **first decline in employment in six months**, as the Canadian labour market had managed to generate net new jobs at a robust pace of ~36.8K per month since July, including a 31.2K gain in December. The internals of the report were also weak, as the **majority of the decrease stemmed from full-time employment**, which dropped by 20.6K. However, the **unemployment rate declined to 7.0%** from 7.1%, given a contraction in the labour force.
- The week also saw a string of soft Canadian housing-related reports. January **Canadian housing starts declined to 160.6K** from 198K in December, while **building permits declined by 11.2%** for December, following a 14.5% drop in November.
- **Coming up:** Manufacturing Sales (Feb 15); Existing Home Sales (Feb 15).

Europe

- After a good run since mid-November, **profit taking took place in U.K. and European equity markets**. For Europe, the pretext was initially an investigation into Spanish Prime Minister Mariano **Rajoy** early in the week and suggestion Silvio **Berlusconi**, the former prime minister of Italy, was making advances in election polls. **A lacklustre earnings release season did nothing to change sentiment**. Europe and U.K. markets closed the week in negative territory.

Euro Trade-Weighted Index

The euro's sizeable move recently (in red) is attracting attention. However, big moves are par for the course during the past six years.



Source - RBC Wealth Management, Bloomberg; spot data of Deutsche Bank Index through 2/7/13

- The week was also dominated by central banks' actions, or lack of actions. **The ECB left interest rates unchanged**. RBC Capital Markets economists believe the ECB will leave policy rates on hold this year unless there is a further tightening in financial conditions or the euro continues to strengthen.
- In the U.K., the Monetary Policy Committee kept the bank rate and the asset purchase target unchanged. In addition, in his address to the Treasury Select Committee, **incoming Bank of England (BoE) Governor Mark Carney played down suggestions that he would rapidly press for changes in the monetary policy framework** and stated he was strongly in favour of the current flexible inflation-targeting framework. He signalled the use of commitment and threshold policies at the expense of gilt purchases, and he hinted at potential changes in the BoE's communication policy to something more akin to that of the Fed.
- **Coming up**: Eurogroup meeting (Feb 11); Ecofin meeting, U.K. CPI and PPI (Feb 12); Eurozone Industrial Production (Feb 13); Eurozone Q4 GDP (Feb 14).

Asia Pacific

- After 12 consecutive weeks of rallying, **Japan's Nikkei** index finally lost ground. Of more significance, though, was the **volatility of daily performance**. On one day the index rallied nearly 4%, and on two other days losses were close to 2% each.
- **China's consumer price inflation rose by 2%** year over year in January, down from 2.5% in December and in line with economists' expectations. **January exports rose by 25%** year over year, and imports rose by 28%. However, Chinese economic data at this time of year is significantly impacted by the timing of the Chinese New Year holiday. Consequently, February's trade data will likely be significantly weaker. Even so, the January data was well above forecasts. Accounting for seasonality, **China's export growth is probably in the high single digits at present**.
- **The People's Bank of China (PBoC) pumped a record amount of liquidity into the market** during the week, over US$100 billion. While the PBoC has been steadily improving liquidity in the banking systems via these kinds of short-term operations since last summer, this most-recent activity was primarily done to enable banks to meet demand for cash during the holiday.
- **Australia** left its benchmark rate unchanged at 3%, as forecast. The statement from the Reserve Bank of Australia balanced a modestly better outlook for the global economy against a modestly weaker domestic outlook. **RBC Capital Markets forecasts a final 25bps rate cut this cycle** in the second quarter.
- **Sinopec** (0386.HK), the largest oil refiner in Asia, raised US$3.1 billion in an **equity private placement.** The shares were placed at a 9.5% discount to the previous closing price. Sinopec's stock fell by 8.1% during the week.

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			Investment Banking Services Provided During Past 12 Months	
Rating	Count	%	Count	%
Buy (TP/O)	787	50.32	280	35.58
Hold (SP)	705	45.08	180	25.53
Sell (U)	72	4.60	9	12.50

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