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## Canadian Equity Strategy (Bi-weekly)

### A Closer Look at TSX Seasonality

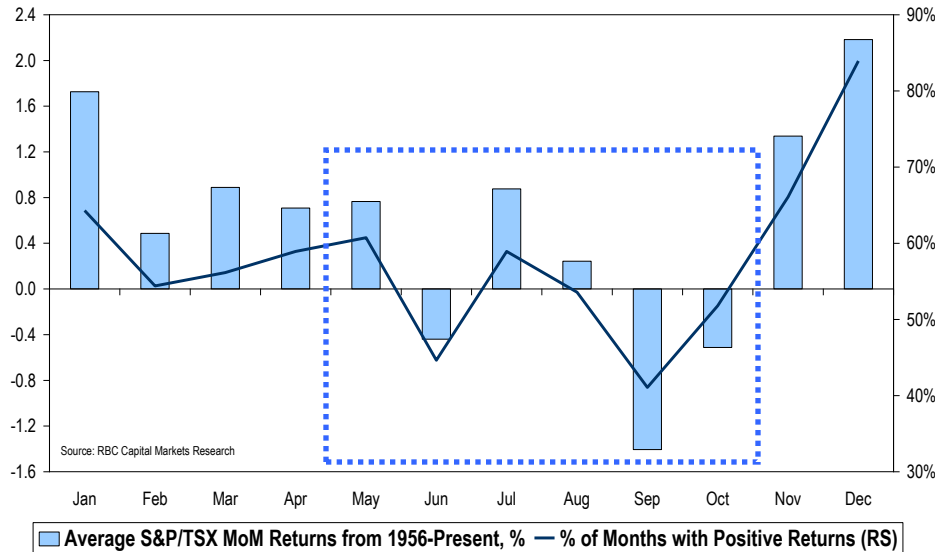
The age-old adage of “sell in May and go away” is fast approaching. Does the Canadian market comply with this seasonality phenomenon?

#### **Our analysis of the TSX finds merit behind this widely known, yet poorly explained, seasonal anomaly:**

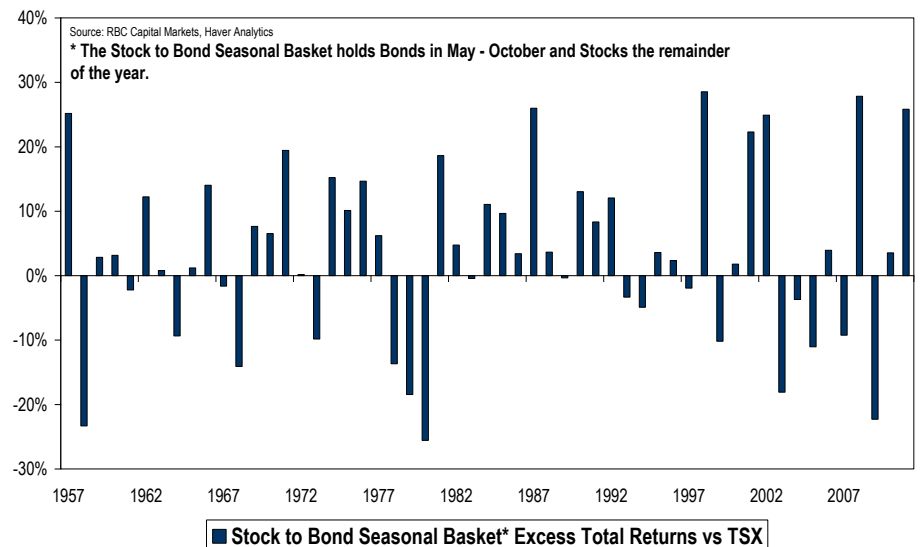
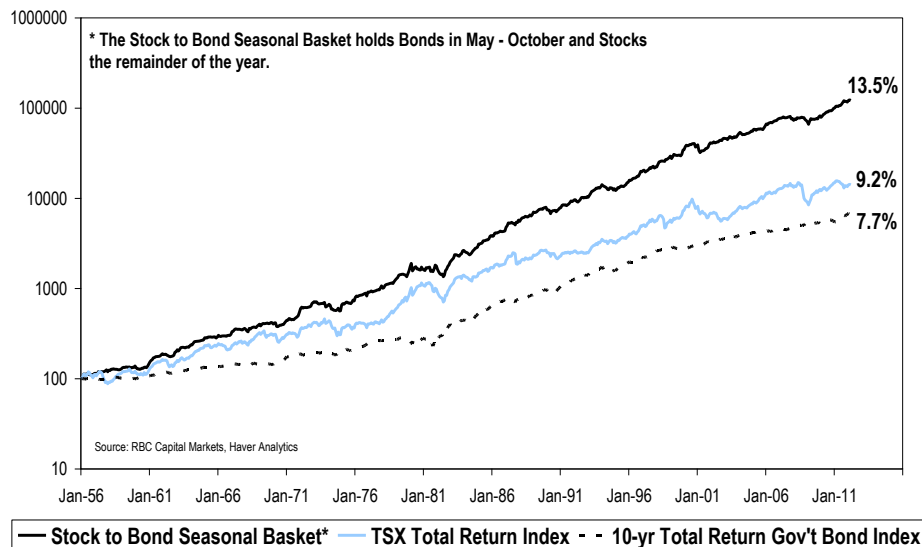
- Using data back to 1956, we find that a simple trading rule to own stocks in the November through April period and switching into bonds in the remaining months yielded an annual return of 13.5%. This compares with a return of 9.2% for a buy-and-hold strategy for stocks and 7.7% for bonds. Furthermore, the beat rate of this switching strategy outperforms a long-only TSX strategy in 35 of the 55 years under study.
- For investors constrained to equities, we also found a simple and effective trading rule at the sector level. Holding cyclicals in the November through April period and defensives in the remaining months generated annual excess returns of over 300 basis points with a success rate of 65% over the past 32 years.
- A deeper look at the sector data reveals that in the May to October period, Consumer Staples, Utilities, and Telecom have been consistent outperformers while leadership among the major groups can be found within TSX Banks.

**Bottom Line:** For those willing to get involved, we find empirical evidence supporting the “sell in May” seasonal phenomenon. At the sector level, cyclicals tend to outperform in the November to April period and underperform in the summer months.

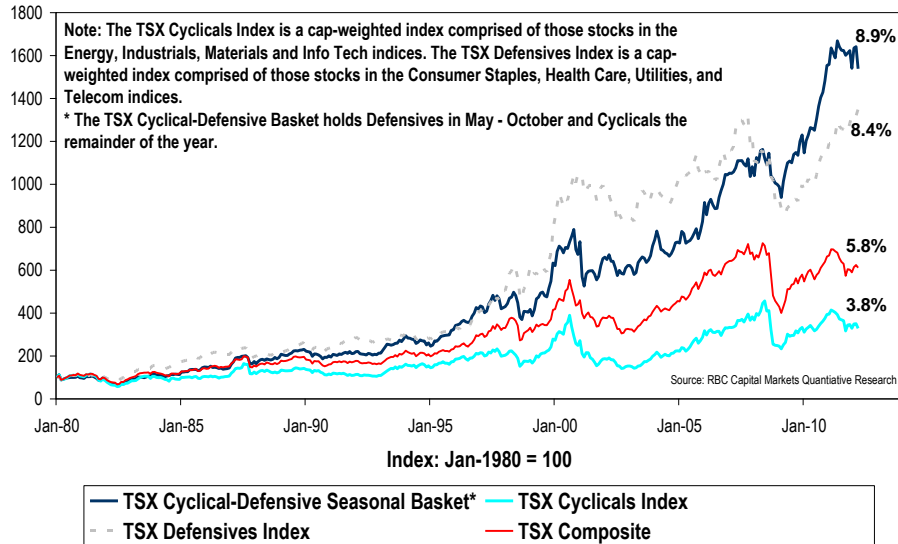
# Bracing for Seasonal Effects



- The months from May through to October appear to provide the most challenging environment for Canadian equities. Average monthly returns during this period not only look light, but the proportion of positive returns seen within each of these months is depressed relative to the rest of the calendar.
- For broader asset allocation purposes we tested a trading rule of holding stocks in the November through April months and switching into bonds for the remainder of the year. Based on data back to 1956, we find that this simple trading rule yielded annual portfolio returns of 13.5% compared with a return of 9.2% for a buy-and-hold strategy for stocks and 7.7% for bonds.
- Furthermore, the beat rate of this switching strategy outperforms a long-only TSX strategy in 35 of the 55 years under study.

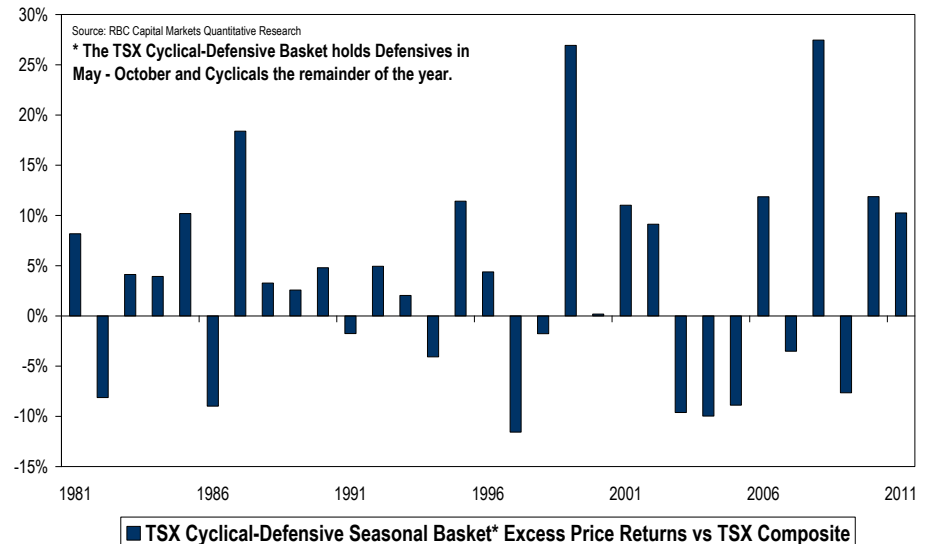


# Sector Seasonality - Cyclical versus Defensives

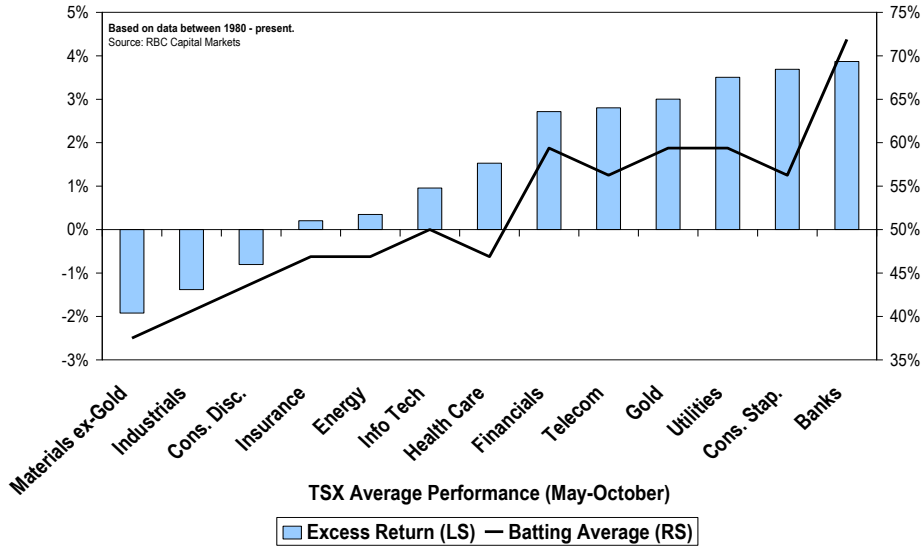


- Furthermore, the batting average for this strategy suggests that it has some merit. Rotating from cyclicals to defensives in the May to October months outperformed the long-only equity portfolio in 65% of the years under examination.

- For those investors constrained to equities, we note a simple and effective trading rule at the sector level. By grouping the TSX sectors into cyclicals and defensives, we found that by holding cyclicals from November through April and defensives in the remaining months, excess annual returns can be generated based on 32 years worth of data.
- The sector switching strategy yields excess returns of more than 300 basis points over the TSX composite.



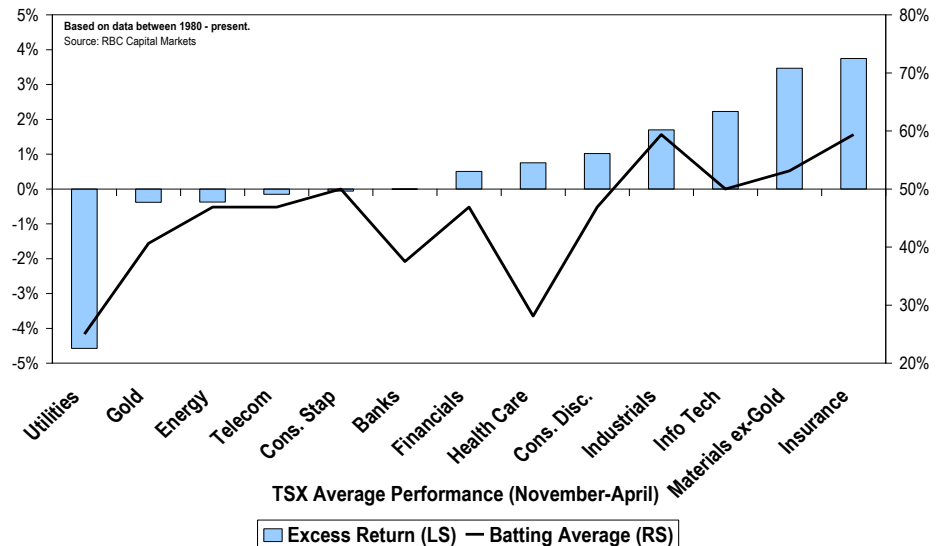
# Sector Seasonality Under Scrutiny



- A deeper dive into the data yields more clarity into seasonal sector and group leadership.
- In the May to October period, the performance of Consumer Staples, Utilities, and Telecom round out the top three among the TSX sectors, all with decent batting averages of ~60%.
- In the November to April period, Info Tech, Materials (ex-gold), and Industrials are the leaders. However, note that Info Tech's success rate is no better than a coin toss.

- As for the major groups, there are some interesting intra-sector rotation possibilities for Financials and Materials, respectively. TSX Banks and Gold tend to outperform in the upcoming months while a rotation into TSX Insurance and non-Gold Materials in November has historically proven to be fruitful.

**Bottom Line:** For those willing to get involved, we find empirical evidence supporting the “sell in May” seasonal phenomenon. At the sector level, cyclicals tend to outperform in the November to April period and underperform in the summer months.

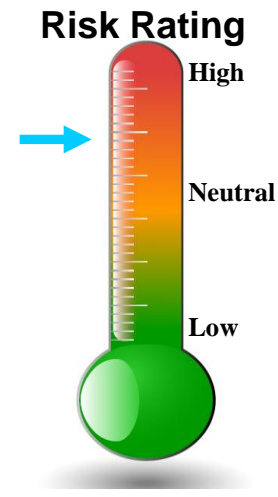


## RBC CM North American Market Views

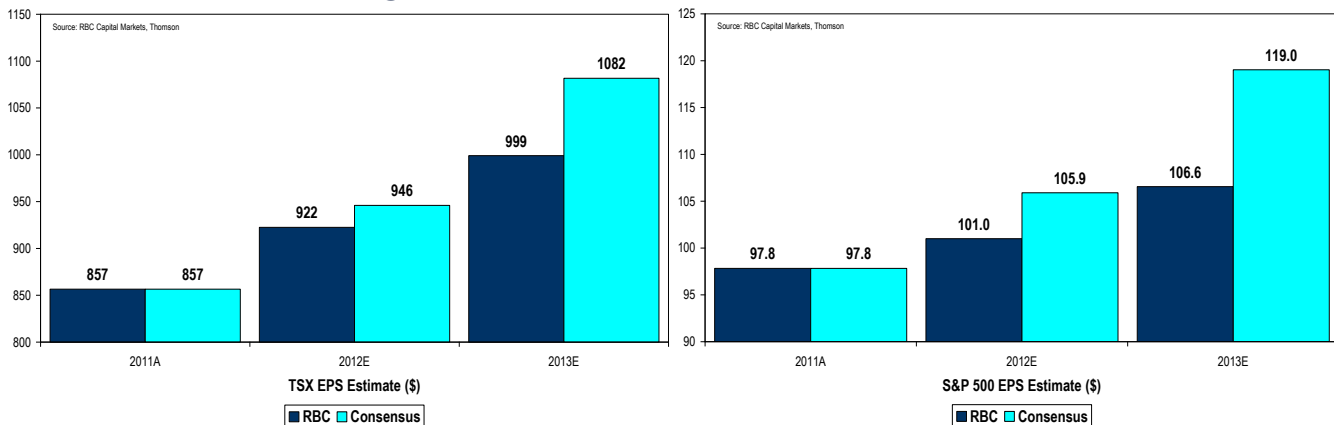
### Market Outlook (Next 6 - 9 months)

Overweight	
Market Weight +	X
Market Weight	
Market Weight -	
Underweight	

▲/▼ Directional Bias. Source: RBC Capital Markets



### TSX & S&P 500 Earnings Outlook



### TSX Sector Recommendations

#### RBC CM Recommended TSX Exposure

Canadian Equity Sectors	Current Recommendation	Recent Change (March 9, 2012)
Industrials	Overweight	None
Financials	Overweight	None
Telecom Services	Overweight	None
Information Technology	Market Weight	Upgraded from Underweight
Consumer Staples	Market Weight	Downgraded from Overweight
Consumer Discretionary	Market Weight	None
Materials	Market Weight	None
Health Care	Market Weight	None
Utilities	Underweight	None
Energy	Underweight	None

Source: RBC Capital Markets

## Market Update

Benchmark Performance Review (% chg)						
	1wk	1mo	3mo	12mo	QTD	YTD
<b>CAPITALIZATION</b>						
TSX	1.7	(2.9)	(0.8)	(12.0)	(2.1)	1.5
TSX 60	1.9	(2.5)	(0.8)	(12.1)	(2.0)	1.8
TSX Completion	1.1	(4.0)	(0.8)	(11.9)	(2.4)	0.7
TSX Small Cap	0.6	(6.6)	(3.7)	(20.6)	(4.5)	0.6
<b>TSX SECTOR BENCHMARKS</b>						
Energy	2.6	(6.4)	(4.9)	(19.1)	(3.3)	(4.4)
Materials	(0.1)	(4.9)	(9.8)	(23.7)	(4.6)	(4.6)
Industrials	3.2	(1.2)	0.7	(0.4)	(0.5)	2.2
Info Tech	2.0	(2.2)	(3.5)	(49.7)	(4.6)	2.7
Consumer Disc	1.8	0.5	9.4	(3.1)	(0.1)	13.0
Financials	1.9	(1.0)	6.5	(3.8)	(0.8)	9.0
Consumer Staples	0.8	3.4	9.2	9.9	0.8	7.7
Health Care	2.8	4.0	9.2	12.6	2.5	18.4
Utilities	(0.3)	(2.5)	(0.7)	3.0	(1.4)	(1.5)
Telecom	1.6	1.7	(0.2)	14.5	0.5	(1.6)
<b>US Benchmarks</b>						
S&P 500	2.4	(1.0)	7.5	5.4	(1.3)	10.6
DJIA	3.1	(0.9)	5.1	6.3	(0.7)	7.3
NASDAQ	1.7	(0.4)	11.5	10.1	(1.6)	16.8
Russell 2000	3.4	(2.4)	5.9	(2.9)	(2.4)	9.4

As of April 17, 2012. Source: RBC Capital Markets, Bloomberg

## Recent Publications

- [TSX Entering a New Frontier? From Leader to Laggard](#) – A potential cyclical and secular shift away from the TSX – Apr 4, 2012
- [Implications of Rising Bond Yields](#) – We identify TSX buy and sell candidates for a rising bond yield environment – Mar 21, 2012
- [North American Equity Strategy Outlook - Spring 2012](#) – Macro, market, sector, and style outlook for Q2 2012 – Mar 9, 2012
- [Dividends: The Best of Both Worlds](#) – TSX 60 Dividend Growers offer significant outperformance – Feb 22, 2012
- [Switch Idea: Precious for Industrial Commodities](#) – A window of outperformance has opened for industrial commodities – Feb 8, 2012
- [The Dividend Growth Strategy](#) – TSX 60 Dividend Growers offer significant outperformance – Jan 25, 2012
- [Enhancing the High Income Portfolio](#) – TSX 60 High Yielders offer outperformance and downside protection – Jan 11, 2012
- [Upgrading the TSX, Raising Industrials, and Downgrading Utilities](#) – Better economy and lower market and political risks – Jan 4, 2012
- [TSX vs. S&P 500: Another Tough Year Ahead for Canada?](#) – TSX more leveraged to lagging global economy – Dec 21, 2011
- [North American Equity Strategy Outlook - New Year 2012](#) – Macro, market, sector, and style outlook for Q1 2012 – Dec 9, 2011

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Distribution of Ratings RBC Capital Markets, Equity Research				
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			Count	Percent
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<b>HOLD[SP]</b>	<b>644</b>	<b>43.22</b>	<b>150</b>	<b>23.29</b>
<b>SELL[U]</b>	<b>62</b>	<b>4.16</b>	<b>3</b>	<b>4.84</b>

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