DM Monthly Report

APRIL 2016

PORTFOLIO ACTIVITY

In March, we used accumulated cash in the DM Canadian Equity Portfolio to open a new position in Methanex Corp. No trades were executed in DM Foreign Equity.

FEATURE STOCK

Saputo Inc. (SAP)

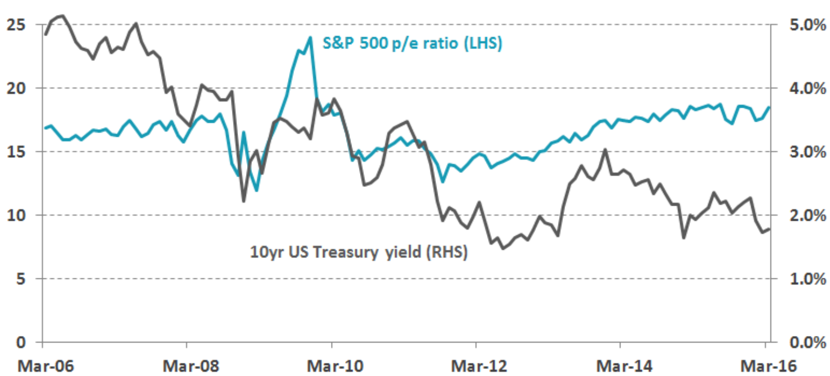
In its most recent quarterly release, SAP reported per share earnings of $0.44, handily beating consensus expectations of $0.39. Gains were driven by the company's US operations, which saw a 13% jump in sales based on strong volume growth in both its retail and food-service components, as well as by the company's ongoing commitment to cost management. While global pricing pressure has challenged the industry in recent quarters, and is expected to last through the fiscal year, SAP remains well positioned to weather the storm, as the company's diversified platform and focus on productivity should support earnings growth until conditions improve. This breadth of operations and geographic diversification, with significant processing capacity in both the US and Australia, should also help SAP to cope with any pressures stemming from the pending Trans Pacific Partnership trade agreement. So far this year, SAP shares have gained roughly 20%.

WHAT ABOUT VALUATIONS?

The plunge in stocks at the beginning of the year gave pessimists just what they were looking for: initial confirmation that markets are dangerously overpriced and in need of a big reset to bring prices back in line with earnings. Since that time, however, the S&P 500 and TSX have recovered lost ground and, by the end of March, both were already positive for the year. While it's true that the economic backdrop remains tepid and the odds of market wide earnings surge in the months ahead are low, the price that investors are paying for underlying fundamentals doesn't seem extraordinary; this is especially true when the prevailing level of interest rates is taken into consideration. The chart below plots the trailing price/earnings ratio for the S&P 500 for the past decade, alongside the yield of the 10yr US Treasury Bond (we've used the S&P instead of the TSX because its data are less skewed by the volatile energy and materials sectors). As you can see, the current p/e of the US market is not much different than it was a decade ago—in other words, investors are paying no more for a dollar of earnings today than they did back then. At the same time, however, one of the chief competitors for equity capital—government bonds—has seen promised returns fall by more than half. This begs the question: *is the "right" earnings multiple for stocks at any given time a fixed number, or is it more nuanced, weighing a wider array of inputs?* If it's the latter, we can probably say that, while market valuations don't necessarily deserve much of a premium for imminent profit growth, the stingy interest rate structure probably makes current earnings worth relatively more than they were in past periods. Regardless, with multiples sitting about where they were a decade ago and bond yields down significantly, it doesn't feel like equity valuations are meaningfully stretched. With this backdrop, it is likely that stock picking (i.e. finding companies that can break from the earnings pack, but whose stocks are nonetheless reasonably priced) will be well rewarded.

S&P 500 P/E Ratio vs. 10yr US Govt. Treasury Yield

Mar-2006 to Mar-2016



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