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Market Bulletin

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Commentary – Nasdaq at 4,000: Some takeaways

Technology bellwether is on much firmer ground that it was 13 years ago

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In March 2010, on the 10th anniversary of the Nasdaq Composite's record high of 5,132.52 posted on March 10, 2000, we had speculated on when the index could possibly reach that level again. We had three conclusions in that March 12, 2010 Bulletin (which can be accessed at http://www.globalsec.com/market_news/market_research.aspx) – the Nasdaq had an outside chance of getting to 5,000 over the next 10 years; Microsoft was quite unlikely to be the largest Nasdaq-100 stock; and healthcare-related companies, which numbered 19 on the Nasdaq-100 at that time, may account for a greater proportion of the index in future.

Those predictions have been more or less on the ball. The Nasdaq could get to 5,000 much sooner than our initial estimated timeline of 2020, and Microsoft has long ceded its No.1 position (it now ranks behind Apple and Google in terms of market cap). And while the number of healthcare-related companies on the Nasdaq has declined to 14, the number of pharma / biotechs in the Top 15 on the Nasdaq-100 has increased to four (from three).

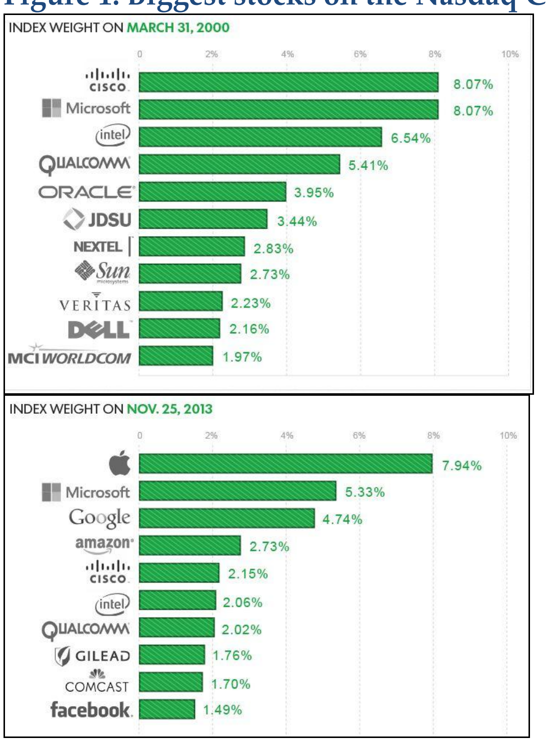
The Nasdaq Composite last week broke through the 4,000 barrier on the upside, a level it first breached in the heady days of December 1999, and then on the downside during the selloff of September 2000. Although concerns have resurfaced about a repeat of the technology-fuelled boom-and-bust of that period, the Nasdaq is fundamentally on much firmer ground at present than it was 13 years ago. Here are some key takeaways –

- **The Nasdaq Composite has outperformed during this bull run**: Since this bull phase commenced on March 9, 2009, the Nasdaq has advanced 219% (total returns 237%), outperforming the S&P 500 (+167%, TR 195%), and the DJIA (+146%, TR 179%). However, although the S&P 500 and DJIA have surged to new records, the Nasdaq remains 20% below its all-time peak.
- **The Nasdaq's advance has been broad**: The breadth of the move can be gauged by the fact that the Nasdaq-100 companies, with a combined market cap of $3.89 trillion, now account for about 64% of the total $6.09-trillion market cap of the Nasdaq Composite. In March 2010, the Nasdaq-100 accounted for 92.7% of the Nasdaq Composite. The 70% advance in the Nasdaq Comp. since March 2010 has seen broad participation.

- **Valuations are much better**: The Nasdaq Comp currently trades at a P/E of 24.75, compared with 59.60 at end-2002, and a stratospherically higher multiple at its March 2000 peak. The dividend yield is also substantially higher at 1.4% currently, compared with 0.4% at end-2002.
- **Fewer members**: The index presently has 2,471 members, a 40% decrease from the 4,077 constituents it had in December 2001. Many of the speculative stocks that contributed to the dot-com boom have vanished for good.
- **Higher average market cap**: The average market cap of a company on the Nasdaq Composite – excluding the Nasdaq-100 companies – is presently about $925 million, up sharply from about $100 million in March 2010. For the Nasdaq-100, average market cap has increased to about $39 billion compared with $33.2 billion in March 2010.
- **New entrants in the ranks of the biggest**: Only four of the top ten Nasdaq stocks from March 2000 are among the biggest presently (Figure 1). The survivors are MSFT, INTC, CSCO, and QCOM. AAPL tops the list, while newer entrants like GOOG, AMZN and FB have surged up the ranks. This level of "churn" indicates that innovation continues to drive the US tech giants.
- **Largely a US story:** The Nasdaq-100 remains dominated by the US giants, with only a handful of foreign companies. There is zero Canadian representation – Blackberry ranked No.14 on the Nasdaq-100 in March 2010, but has since been booted out.

Conclusion: The Nasdaq does not seem to be in a bubble presently. Not yet at least.

Figure 1: Biggest stocks on the Nasdaq Composite – then and now (Source: USA Today)



Economic Analysis – Canada's Q3 growth pace was fastest in two years

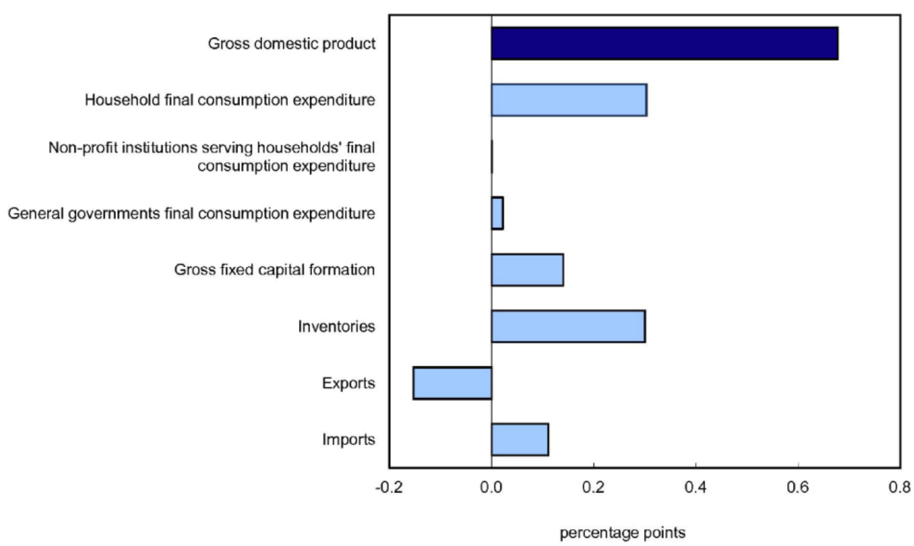
Canadian dollar weakens further ahead of Bank of Canada meeting on December 4
Stronger North American economy, weaker loonie have positive implications for TSX in 2014

The Canadian economy posted its best growth rate in two years in the third quarter, expanding at a 2.7% annualized pace (almost identical to the US economy's 2.8% growth pace in Q3). Canada's Q2 growth rate was revised lower to an annualized 1.6% (from 1.7% earlier). Real GDP expanded 0.7% in Q3, following 0.4% growth in Q2, as household expenditure advanced (Figure 2) and business investment rebounded after declining in Q2. Exports fell 0.5% in Q3 after three quarters of growth, with imports down 0.3% after growing by the same amount in Q2. Higher inventories also contributed to GDP growth – as stockpiles of farm products rose to record levels – which may suggest that the GDP news is not as positive as it seems at first blush.

In any case, while the GDP data exceeded analysts' expectations of 2.5% growth, it did little to change recent bearishness in the loonie, which traded at a two-year low of 1.0618 against the greenback. All eyes are now on the Bank of Canada's December 4 meeting. Recall that BoC Governor Stephen Poloz last month dropped the bank's bias to raise its 1% interest-rate target. A number of trading institutions expect further downside for the Canadian dollar, including Goldman Sachs which forecasts it will trade down to 1.14 vs. the USD in the next 12 months.

Portfolio Implications: **Positive**. The Canadian economy seems to have turned the corner after a sluggish start to the year, and may begin 2014 with greater momentum than 2013. A weaker loonie will help the Canadian export juggernaut and should have a positive impact on corporate earnings. With the North American and global economies on track for stronger growth in 2014, we reiterate our view that this is a good time to accumulate energy and commodity producers.

Figure 2: Contributions to percentage change in Q3 real GDP (Source: Statistics Canada)



M&A – Three Canadian healthcare companies snapped up in November

US sector frenzy spilling over into Canada?

The Canadian healthcare space has seen an unusual number of companies being acquired by overseas buyers. Atrium Innovations (a maker of natural health products, rather than a pharma / biotech) on Friday announced that it would be acquired by European private equity firm Permira Advisers, which will own 75% of Atrium after the deal closes, with existing shareholders Fonds de Solidarite FTQ and Caisse de Depot splitting the remaining 25%.

On November 19, Patheon Inc – a provider of contract development and manufacturing services to the global pharma industry – announced that it would be taken private by New York-based private equity company JLL Partners and Royal DSM NV. Two weeks earlier, Endo Health agreed to buy Paladin Labs for about US$1.6 billion to expand into Canada and emerging markets.

This is a surprising pattern of activity in an often overlooked sector in Canada. The Healthcare sector makes up less than 3% of the TSX Composite, and only has three constituents – Valeant Pharma (VRX, $116.00, +95.6% YTD), Catamaran Corp (CCT, $48.69, +4.1%), and Extendicare (EXE, $6.84, -10.6%). Perhaps the unusual M&A activity could be the result of the frenzy in US pharma / biotech spilling over into Canada. If so, it may not be long before foreign acquirers turn their attention to Canadian bargains in other sectors.

Market Snapshot

At close on Friday, November 29, 2013

S&P TSX	13395.40	+24.57	**Commodities**			**Yields (%)**	**Can.**	**US**
TSX Venture	934.89	+8.22	Canadian $ (US cents)	94.21	-0.30	90 Day T-Bill	0.92	0.06
DJIA	16086.41	-10.92	Gold (Spot)-US$	1253.35	+9.22	2-Year Bond	1.09	0.28
S&P 500	1805.81	-1.42	Oil (WTI-Dec.)	92.78	+0.48	10-Yr.Bond	2.55	2.74
NASDAQ	4059.89	+15.14	CRB Index	274.97	+1.47	30-Yr. Bond	3.14	3.81

Thought for the Day

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