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Looking back and moving forward



Craig Maddock, Assistant Vice President of the investment management group at MD Financial, recently sat down to discuss the economic events of the past year and what investors can expect for the year ahead.

WHAT WERE SOME OF THE HIGH POINTS OF 2009?

Last year, a lot of the negatives from 2008 became positives. Energy and materials certainly came roaring back, and these sectors total almost 50% of the Canadian market, compared with just 16% of the U.S. market and 18% of international markets. So that made a very positive impact on Canadian equities.

Much of the financial crisis was centred on the financial services industry, but Canadian banks continued to move along and did quite well last year. That's arguably due to their very conservative nature. The banks make up another significant piece of the Canadian equity market, and they really paid off for investors in 2009.

DO YOU EXPECT THESE TRENDS TO CONTINUE?

I'm not sure we'll see the same kind of market strength as last year. Stock prices dropped out in 2008 because investors no longer had any idea what companies were going to be able to earn. Now, we're in an environment where earnings are firmer, but prices have already come up dramatically. There's less upside potential because valuations are now, in a lot of cases, normalized.

DO OPPORTUNITIES STILL EXIST IN THE MARKET?

Of course, yes, there is always the ability to find opportunities. The goal of good investment managers is to find those opportunities. A year ago, you could throw money at just about anything and get a decent return. The challenge for 2010 is that managers will have to look at individual companies, sectors and countries, and figure out which ones are in the best position to perform. Factors such as earnings growth and competitive advantages are going to be much more important in 2010 than they were in 2009.

HOW HAVE CURRENCY TRENDS AFFECTED INVESTMENT PERFORMANCE?

There was a pretty strong reversal of currency trends in 2009. The Canadian dollar climbed sharply again. So you could look at a U.S. or international investment that had good returns in the local currency, but once you convert that to Canadian dollar terms, it was a bit of a painful year. Canadian investors saw U.S. and international investment performance take a hit of 10%-15% or more.

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WHAT TRENDS HAVE YOU OBSERVED REGARDING INVESTMENT STYLE?

MD funds are generally split between growth and value styles in order to capitalize on the strengths of each. Historically, these styles can have very different results in particular years. Last year was odd because individual industry sectors dominated the market—such as the damage to the U.S. financial services sector, the extremely strong performance of the U.S. information technology sector, and the rally in Canadian energy and material stocks. This sector-based phenomenon largely overshadowed the more typical divide between growth stock and value stock performance.

WHAT NEW TRENDS OR ISSUES DO YOU SEE EMERGING NOW?

I would say the thing that is likely to have the most dramatic influence in the near future is inflation and, ultimately, its impact on interest rates. These issues will affect all portfolio returns going forward, including equities and fixed income. Other economic themes remain important—such as increasing global consumption of natural resources—but in the shorter term, we are all watching closely to see what happens with inflation and interest rates, and how that will affect economies and markets.

HOW SHOULD INVESTORS FEEL AS THEY LOOK BACK ON THEIR PORTFOLIO PERFORMANCE?

I think they can look back at 2009 and feel that it was a pretty good year. As I reflect on the overall performance of MD funds, I see average equity fund returns in the neighbourhood of 20%, and most fixed income funds somewhere in the 3%–7% range. So, in a combined portfolio, I'd expect returns to be somewhere in the low double digits. To me, that looks like a pretty good year, following a very tough year in 2008.

OUTLOOK FOR MD FUNDS

Here are Craig's comments about some of the most popular MD funds.

MD GROWTH

MD Growth is an important fund that's held by a lot of our clients. Unfortunately, the market hasn't been favourable for global value funds lately. Having said that, if you need global equity exposure in your portfolio, I think you'd be challenged to find a better-managed fund in Canada.

MD INCOME FUNDS

Last year was remarkably good for fixed income due to extraordinary circumstances in credit markets. Some funds had double-digit returns. But now that markets have stabilized, and assuming inflation is controlled, I would expect returns back in the low 3% range.

MD SELECT FUND AND MD INTERNATIONAL GROWTH FUND

Our goal is to produce very strong performance relative to our benchmarks and peers, and we've made changes to these funds to achieve that goal. MD Select Fund is now better positioned to take advantage of long-term strength in commodities and materials. MD International Growth Fund had great performance in the past year, and I expect to see more good results.

To put our best thinking to work in your portfolio, please speak with your MD advisor.

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I think, if I went back and reviewed two or three years of returns, I might still have a negative return overall in my portfolio. But that's a reflection not so much of how the funds were invested, but just the markets in general. I think we're going to see the markets continue to slowly work their way back to more typical performance going forward.

WHAT ADVICE WOULD YOU OFFER INVESTORS FOR 2010?

I would say the best advice—and it doesn't change very often—is to adhere to a really good long-term strategic mix. That may sound repetitive to some of our clients, but it's really the best advice.

It's very difficult to try to time what will happen in the market, and to make big, broad-based decisions. For instance, 2008 triggered record stock market losses and, in many respects, valuations suggested that you could expect a dramatic bounce-back like we saw in 2009. But to figure out the timing, and to step in with a strong overweight in equities last year, was a really tough—and risky—decision.

Again, the best thing to do is to take a long-term approach, build a good strategic mix, and then invest in funds that you know are well managed. We believe we are managing the MD funds to a very high standard, so investors don't need to try to figure out which fund to buy, why to buy it, and what the best time to buy it is. So, a good mix of quality funds—that's my best advice for 2010.

QUESTIONS?

CONTACT YOUR MD ADVISOR.

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