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North American equity and fixed income markets got hurt badly this week, with a similar fate hitting European and Asian indices. The three major US equity markets experienced the worst declines in over two years. Since 1930, the S&P500 has averaged drawdowns of negative 5% or more each calendar year, however the US market has not experienced a pullback of this magnitude (-5%) since June 2016.

We are closing the week with both the S&P 500 and S&P/TSX off 3.9%, with several technical support levels having been breached. Even the on-going "priced for perfection" corporate financial releases out of the US this week could not stem the pullback. Odds were stacked against us that the severe decline we have experienced this week was long overdue.

Managing the downside protection in diversified portfolios requires active management, and this week we have been selective in a number of our sales to raise some cash across our client accounts. Risks on our radar continue to be focussed on rising inflation expectations, ongoing political tensions, interest rate volatility and the potential for a sell off in large cap equities, especially in the tech sector. Since 1990, the average pullback is roughly 6% and takes two to three weeks to work itself through the system.

The stock market's worst enemy this week has been the near rout in the bond market, and rising interest rates coupled with a weaker US Dollar. Although the January 30/31 two-day Federal Reserve Open Market Operation Committee meeting left short-term interest rates unchanged, the tone amongst the governors was decidedly more hawkish than in previous meetings given the accelerating economy and expectations of prices moving higher next year. More on that below.

Through the week, we saw the yield on ten-year US Treasuries, which broke through resistance last week at 2.62%, rise consistently over the five-day period to settle in at 2.845%, a four-year high (May of 2014). The yield curve steepened slightly with the 30-year rate trading up to 3.087%, a level not seen since March of last year. Concerns around faster-than-expected increases in interest rates and core inflation had markets firmly on their back foot as traders and investors alike tried to assess the trade off between stronger economic growth and higher borrowing costs. In the end, rising interest rates may not be all that negative for stocks as it confirms that global reflation is working its way through the world economy. Time will tell.

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On the jobs front this week, we saw two relatively robust releases. Mid-week, we had a red-hot ADP jobs report that hit the tape at 234k versus expectations of 185k. This morning, the US Labor Department reported that the US economy added 200k jobs in January, topping estimates of 180k, with unemployment holding steady at 4.1%. Economists were closely watching for the increase in average hourly earnings that came in at an annualized rate of 2.9%.

Today also marked Fed Chair Janet Yellen's last working day at the Federal Reserve as she makes way for her successor, Jerome Powell. After a fourteen-year career at the Fed, she is passing the torch onto Mr. Powell amid relatively heavy praise for steering the US economy through a tumultuous period. The unemployment rate is at multi-year lows, job creation is broadly disbursed across most sectors, and inflation is inching upwards to the central bank's 2% target and may well be there by year end. "Gradual normalization" has been the overriding theme of her tenure. Ms. Yellen is scheduled to join the Brookings Institution on Monday after leaving the Fed.

Market participants are still divided on whether the Fed will increase rates three or four times through the coming year. Nothing out there is likely to sway them from increasing them by 25 basis points at the upcoming March 21st meeting, with the current "futures" probability just over 90%. Indeed, it seems that all four "live" Fed meetings through 2018 may well see increases as the US and global economies continue their synchronized growth path.

Sincerely,
Dekker Hewett Group

TODAY'S STOCK WATCH

S&P/ TSX Composite	15,606
Dow Jones Indus. Avg.	25,520
S&P 500	2,762
Canadian/US Dollar	$0.8048
US/Canadian Dollar	$1.2421
Euro / Canadian	$1.5475
Gold	$1335.20
Silver	$16.55
Copper	$3.18
Brent Crude Oil	$68.22
WTI Crude Oil	$65.06
Natural Gas	$2.86