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CANADIAN ETF Watch

canadianetfwatch.com

Low Volatility Strategy
Stratégie de faible volatilité

SPECIAL CONFERENCE EDITION
EXCHANGE TRADED FORUM 2013
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- Canadian ETF Flows
- Building Portfolios with the Efficient Frontier
- TSX: Home to Canada's Exchange Traded Notes
- Seasons Change – Shouldn't Your Investments Change Too?
- Everything You Know About Asset Allocation is Wrong
- The Unbearable Lightness of the Central Bank Put

2013 Marks Our 3rd Annual Exchange Traded Forum Montreal

Looking back, demand for ETFs proved robust in 2012, with fourth quarter sales of $2 billion and full year net creation of $12 billion. Assets expanded over 30% to end the year at $56.4 billion. This growth is significant and is expected to continue.

We have just hit a notable milestone, the 300th ETF has just been listed on the TSX, and we have in excess of $60 billion in assets under management. What's in store for ETFs in 2014? We believe we will see continued growth in this rapidly expanding sector. However, in order to attract new assets the providers will need to launch new cost effective, innovative products. These products will be more sophisticated in both structure and sector allocation.

To this end there will be increased regulatory focus and plenty of media exposure, both good and bad. The need for education and understanding in all types of exchange traded products is now more necessary than ever.

AUGUST HIGHLIGHTS
Source: BlackRock ETP Research

With uncertainty about economic growth and Federal Reserve policy, the Global ETP industry experienced outflows of ($15.0bn) in August, the second month of redemptions this year following very strong asset gathering in July. Similar to June, outflows were driven by Fixed Income with ($5.3bn), including ($8.1bn) from funds with longer/broader maturity profiles vs. inflows for short maturity funds.

This is the largest monthly outflow on record for global ETPs. The previous monthly record for global ETP outflows was in January 2010, when the industry witnessed outflows of ($13.4bn).

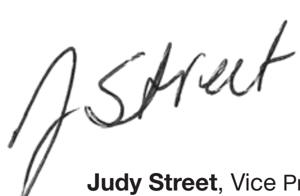
News that the Eurozone posted its first economic expansion in 18 months helped fuel record setting monthly flows of $4.7bn into Pan European Equity ETPs in August.

Overall Equity ETP flows were negative at ($9.4bn) as US exposures lost momentum in August, registering outflows of ($14.5bn). However excluding significant SPY (SPDR S&P 500) redemptions of ($14.0bn), US Equity outflows were modest at ($0.5bn).

Year-to-date Equity ETP flows were $138.5bn, still well ahead of last year's pace.

In the broader mutual fund space, market uncertainty helped fuel $52bn of flows into Money Market funds, the highest monthly total this year and $21bn higher than last month.

Continued uncertainty around the timing of the Fed's tapering, the direction of economic data and potential geopolitical conflict is likely to lead to increased volatility for equity and bond markets in September.



Judy Street, Vice President
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Canadian ETF Flows: August 2013
Bonds for Sale, Developed Markets in Favour

FINANCIAL PRODUCTS RESEARCH

September 3, 2013

- ***Outflows of $318 million or a modest -0.5% end a lacklustre summer for ETF flows in Canada***
- ***Weak Canadian Equity flows and withdrawals from rate sensitive bond ETFs continue to weigh***
- ***Demand in the equity space remains for U.S. and now international developed equity through EAFE funds***
- ***In fixed income, floating rate funds and short-term corporates remain the trade of choice***

Flows by Category

Fixed Income ETFs shrank by $400 million in August, leading the selling as the key driver of the net $318 million in outflows. Most of the outflows were from rate-sensitive segments of the bond fund market. Despite positive flows of $100 million in equity, investors continue to sell Canada and continue to favour U.S. and more recently international developed equity through EAFE funds.

ETF Flows by Category - August 2013

Asset Class	AUM ($M)	Flow ($M)	% AUM
Equity	$33,860	$99.6	0%
Commodity	$715	$3.0	0%
Multi-Asset	$1,489	-$19.2	-1%
Fixed Income	$22,125	-$402.0	-2%
Levered Long	$628	$0.0	0%
Inverse	$529	$0.0	0%
Total	**$59,345**	**-$318.6**	**-0.5%**

Source: National Bank Financial, Bloomberg

Flows by Provider

For the second month in a row, Vanguard's Canadian lineup of ETFs tops the list of inflows, accumulating $70 million for 6% growth. This includes Vanguard's timely launch of five new equity ETFs in Canada, which include Canada All Cap (**VCN**), U.S. dividends hedged and unhedged (**VGH** and **VGG**), developed equity (**VDU**) and broad U.S. equity unhedged (**VUN**). First Trust's inflow came from seeding its actively managed Senior Loan ETF (**FSL**). BlackRock was the only provider with a net outflow, with $527 million in assets leaving its ETFs again focused on Canadian equity.

ETF Flows by Provider - August 2013

Asset Class	AUM ($M)	Flow ($M)	% AUM
Vanguard	$1,195	$70.0	6%
BMO	$11,803	$51.0	0%
PowerShares	$1,701	$42.7	3%
Horizons	$4,104	$26.7	1%
First Asset	$214	$8.0	4%
First Trust	$22	$8.0	56%
RBC	$186	$2.0	1%
BlackRock	$40,121	-$527.1	-1%
Total	**$59,345**	**-$318.6**	**-0.5%**

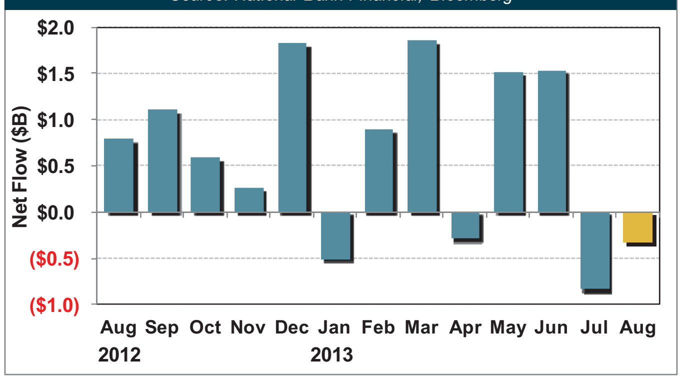
Source: National Bank Financial, Bloomberg

Flows by Product: August 2013

XIU and XIC were key drivers in the month, drawing down a combined $337 million in assets. After that, almost all outflows were confined to rate sensitive fixed income funds, including corps (**ZCS**, **XCB**), prefs (**CPD**) and aggregate bonds, (**XBB**, **ZAG**). Inflows reflected the continued demands into U.S. equities (**ZSP**) and now developed international markets (**ZDM**, **XIN**). In keeping with rising rate concerns, floating rate bond ETFs saw high percentage inflows with **HFR** growing by 12% and **XFR** by 14%. In contrast with the widespread selling of broad Canadian equities, mainstay Canadian sector ETFs in banks (**XFN**, **XEB**) and Energy (**XEG**) saw some inflows.

Chart 1: Canadian ETF Flows by Month

Source: National Bank Financial, Bloomberg



Flows by Product: Year-To-Date 2013 (table on page 2)

With $840 million in inflows, ZPR (BMO Rate-Reset Prefs) remains the ETF with the highest inflows year-to-date, although interest in this asset class has subsided in the last month. Horizons Floating Rate Bond ETF (**HFR**) has picked up enough inflows to make the top 10. Outflows remain concentrated in Canadian equities and bonds, with **XIU**, the largest and most liquid ETF in Canada, down $1.8 billion year to date.

AUGUST 2013 FLOWS

INFLOWS

Top Single Long ETF Inflows

	Ticker	Name	Flow ($M)	% AUM
1	ZSP	BMO S&P 500 ETF	$91.3	15%
2	ZDM	BMO MSCI EAFE Hedged to CAD Index ETF	$86.5	22%
3	XFN	iShares S&P/TSX Capped Financial Index Fund	$67.1	9%
4	XEG	iShares S&P/TSX Capped Energy Fund	$58.0	9%
5	HFR	Horizons Floating Rate Bond ETF	$33.7	12%
6	PSB	PowerShares 1-5 Year Laddered Inv. Gr. Corp	$31.4	13%
7	ZEB	BMO S&P/TSX Equal Weight Banks Index	$30.1	6%
8	PFH	PowerShares Fundamental Hi-Yield Corp CAD	$25.0	20%
9	XIN	iShares MSCI EAFE Index Fund CAD-Hedged	$20.1	2%
10	XFR	iShares DEX Floating Rate Note Index Fund	$16.1	14%

OUTFLOWS

Top Single Long ETF Outflows

	Ticker	Name	Flow ($M)	% AUM
1	XIU	iShares S&P/TSX 60 Index Fund	-$216.4	-2%
2	XIC	iShares S&P/TSX Capped Composite	-$121.4	-9%
3	XCB	iShares DEX All Corp Bond Index Fund	-$83.2	-4%
4	XBB	iShares DEX Universe Bond Index Fund	-$63.0	-4%
5	CPD	iShares S&P/TSX Canadian Pref	-$60.1	-4%
6	ZAG	BMO Aggregate Bond Index ETF	-$41.0	-5%
7	PGL	PowerShares Ultra DLUX Long Term Govt Bond	-$39.4	-6%
8	ZCS	BMO Short Corp Bond Index ETF	-$35.4	-4%
9	XTR	iShares Diversified Monthly Income Fund Unit	-$17.7	-2%
10	COW	iShares Global Agriculture Index Fund	-$16.5	-7%

Source: National Bank Financial, Bloomberg

NATIONAL BANK FINANCIAL

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2013 YTD FLOWS

INFLOWS

Top ETF Inflows - 2013 YTD

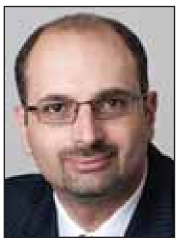
	Ticker	Name	Flow ($M)	% AUM
1	ZPR	BMO S&P/TSX Laddered Pref	$840	2149%
2	ZSP	BMO S&P 500 ETF	$660	3501%
3	HXT	Horizon S&P/TSX 60 Index ETF	$460	96%
4	ZIC	BMO Mid-Term US IG Corp Bond Index ETF	$390	N.A
5	ZDM	BMO MSCI EAFE Hedged to CAD Index ETF	$290	180%
6	ZMU	BMO Mid-Term US IG Corp Bond CAD	$240	N.A
7	CBO	iShares 1-5 Year Laddered Corp Bond Index	$214	13%
8	PGL	PowerShares Ultra DLUX Long Term Govt	$213	44%
9	HFR	Horizons Floating Rate Bond ETF	$172	130%
10	HND	Horizons BetaPro NYMEX NatGas Bear Plus	$170	276%

OUTFLOWS

Top ETF Outflows - 2013 YTD

	Ticker	Name	Flow ($M)	% AUM
1	XIU	iShares S&P/TSX 60 Index Fund	-$1,766	-14%
2	ZCN	BMO S&P/TSX Capped Composite Index ETF	-$506	-35%
3	XBB	iShares DEX Universe Bond Index Fund	-$242	-12%
4	XCB	iShares DEX All Corp Bond Index Fund	-$190	-10%
5	XEG	iShares S&P/TSX Capped Energy Fund	-$189	-22%
6	ZFS	BMO Short Federal Bond Index ETF	-$182	-44%
7	XRB	iShares DEX Real Return Bond Index Fund	-$141	-20%
8	XIC	iShares S&P/TSX Capped Composite	-$109	-8%
9	HNU	Horizons BetaPro NYMEX Natural Gas Bull Plus	-$95	-53%
10	HOU	Horizons BetaPro NYMEX Crude Oil Bull Plus	-$86	-35%

Source: National Bank Financial, Bloomberg



Pat Chiefalo
Director, ETF Research and Strategy, National Bank Financial

ETF Research & Strategy Team Overview

NBF ETF Research & Strategy team offers the most comprehensive and street leading research on ETFs.

Team lead is Pat Chiefalo with 14 years of industry experience in the investment dealer industry on both the sell-side and buy-side as a research analyst and in derivatives.

Mr. Chiefalo spent 6 years in research at both Scotia Capital and Merrill Lynch as lead analyst as well as several years on the derivatives desk for Merrill Lynch - Bank of America.

Pat has a Mechanical Engineering degree from the University of Toronto, an MBA from the Schulich School of Business and is a CFA charter holder.

Low Volatility Strategy

BMO Low Volatility Canadian Equity ETF (ZLB)
BMO Low Volatility U.S. Equity ETF (ZLU, ZLU.U)

Mark Raes
Vice President &
Head of Product,
BMO ETFs

Target Low Risk Broad Market Exposure

The trade-off between risk and return remains at the heart of portfolio construction and investing. Particularly following the market downturn of 2008, investors have become more aware of portfolio risk levels in addition to returns. They are questioning how much risk is in their portfolio and how it will affect their returns. Our low volatility strategy allows investors to target a specific portfolio risk level that is lower than the broad market, and potentially shelter their investments from market uncertainty.

Studies have shown that less volatile or defensive stocks have outperformed the broad market over the long term, as less volatile stocks may benefit from a smaller decline during market corrections while still increasing during advancing markets. Additionally, low volatility stocks tend to be more mature and have a higher dividend yield, and as a result both ZLB and ZLU have a higher dividend yield than their broad markets. The larger dividend yield helps to minimize swings in portfolio value.

BMO | Exchange Traded Funds

Studies have also noted that higher volatility stocks underperform over time, as investors are willing to pay a premium for "lottery tickets", high risk - high reward stocks that often do not meet expectations. Investors have been attracted to these glamour stocks, preferring short term big winners over long term steady performers.

To develop the low volatility strategy, we focus on the beta of a security. Beta is defined as the stock's sensitivity to broad market movements, where the broad market is assigned a value of 1.00. A lower beta, where the beta is less than 1.00, is viewed as less risky than the broad market.

Beta: The Stock's Sensitivity to Broad Market Movements

Implementation of the Low Volatility Strategy

The initial portfolio screen ensures only larger, more mature companies are considered for inclusion. For ZLB, the selection universe consists of the 100 largest and most liquid securities in Canada. Stocks are ranked by their beta, and the lowest 40 betas are selected. For ZLU, the lowest 100 betas from a universe of U.S. large cap stocks are included in the portfolio. ZLU and ZLU.U offer unhedged exposure in Canadian and U.S. dollar units respectively.

The portfolios are also rebalanced semi-annually, where the security weights of the existing holdings are adjusted to reflect changes in their beta or market sensitivity.

Performance Profile

As the following charts illustrate, the low volatility strategy has outperformed the broad market over longer time periods. The strategy had much less of a decline than the broad market during the major correction of 2008. An additional benefit is the reduced risk level of the portfolio, which lessens the swings in performance.

Over the same period, we have observed the added benefit of an even better risk adjusted return, as the returns are less volatile. So not only does the lower volatility strategy have a higher return over the period, the risk adjusted return further favours the strategy.

Reduce your portfolio's risk profile and diminish the impact of market corrections

The strategy has strong portfolio construction benefits due to both the superior long term returns and the reduced risk profile. As investors look to diversify to mitigate portfolio risks, ZLB and ZLU can be used as a core portfolio holding as it has a lower risk target than the broad market. ZLB and ZLU can also be used as tactical trading vehicles, where in periods of greater market uncertainty, a more defensive portfolio may be appropriate.

Visit **bmo.com/etfs** or contact **Client Services** at **1-800-361-1392.** For market views that lead to a variety of BMO ETF solutions subscribe to the Monthly Strategy Report at **bmo.com/etfs**.

Mark Raes, Vice President & Head of Product, BMO ETFs
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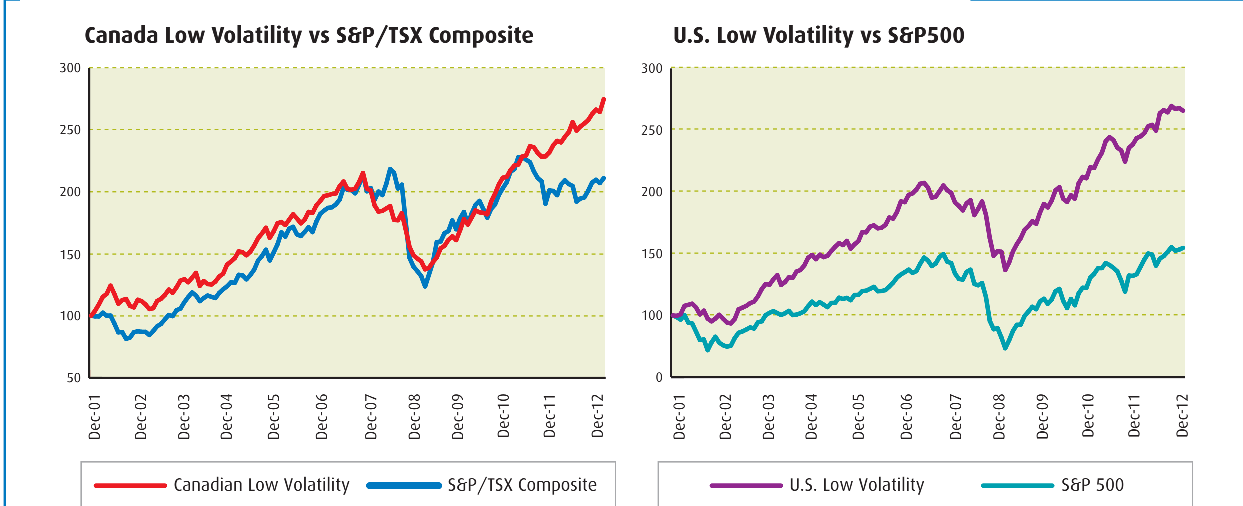
Low Volatility vs Broad Market Indices Dec. 2001 - Dec. 2012



Source: Bloomberg & Factset

Stratégie de faible volatilité

FNB BMO d'actions canadiennes à faible volatilité (ZLB)
FNB BMO d'actions américaines à faible volatilité (ZLU, ZLU.U)

Mark Raes
Vice President &
Head of Product,
BMO ETFs

Miser sur des titres à faible volatilité provenant de l'ensemble du marché

Le lien entre le risque et le rendement demeure au coeur des stratégies d'élaboration des portefeuilles et d'investissement. Les investisseurs sont, notamment depuis le repli des marchés de 2008, de plus en plus à l'affût du niveau de risque auquel est assujetti leur portefeuille. Ils ne recherchent plus uniquement le rendement. Ils remettent en question le profil de risque de leur portefeuille et se demandent de quelle manière le rendement sera touché par ce risque. Nous avons donc mis au point la stratégie de faible volatilité pour permettre aux investisseurs de viser un degré de risque précis moins élevé que celui associé à l'ensemble du marché et pour leur offrir un abri potentiel pendant les périodes d'incertitude.

Les études démontrent qu'à long terme, les titres moins volatils, ou plus défensifs, obtiennent un meilleur rendement que l'ensemble du marché puisque leur valeur baisse souvent moins pendant les périodes de correction et qu'elle augmente tout de même pendant les périodes haussières. De plus, les titres à faible volatilité proviennent de sociétés arrivées à maturité et présentent un meilleur rendement. C'est pour cette raison que les fonds ZLB et ZLU obtiennent un meilleur rendement que leurs marchés respectifs. Par la suite, ce rendement supérieur contribue à réduire à son tour les variations de la valeur du portefeuille.

Les études font également ressortir que les titres à volatilité élevée obtiennent un rendement inférieur à long terme puisque les investisseurs sont disposés à les acheter à un prix supérieur à leur valeur réelle dans l'espoir qu'ils rapportent davantage, alors que souvent, ce n'est pas le cas. Ces titres vedettes sont attrayants pour les investisseurs, qui préfèrent se laisser tenter par l'idée d'obtenir des résultats élevés à court terme qu'un rendement stable à long terme.

Pour élaborer la stratégie de faible volatilité, nous nous appuyons sur le coefficient bêta des titres. Le bêta représente le degré de sensibilité d'un titre aux mouvements du marché, la valeur attribuée par défaut au marché étant 1,00. Un faible bêta, de moins de 1,00, est associé à un risque moins élevé que celui du marché.

Le coefficient bêta mesure la sensibilité d'un titre aux fluctuations du marché

La mise en application de la stratégie de faible volatilité

Le processus de sélection initial permet de faire en sorte que seules les grandes sociétés bien établies soient retenues. Ainsi, les titres du fonds ZLB sont sélectionnés parmi les 100 titres les plus liquides des plus grandes sociétés aux Canada. Par la suite, les 40 titres dont le bêta est le plus faible sont choisis. Les titres du fonds ZLU sont sélectionnés parmi une grande variété d'actions américaines à grande capitalisation, et les 100 titres dont le bêta est le plus faible sont choisis. Les portefeuilles de ZLU et ZLU.U offrent une exposition non couverte en parts en dollars canadiens et en dollars américaines respectivement.

Les portefeuilles sont également rééquilibrés une fois par semestre pour permettre le rajustement de la pondération des titres en portefeuille en fonction des variations de leur bêta ou de leur sensibilité aux fluctuations du marché.

Profil de rendement

Comme l'illustrent les graphiques qui suivent, la stratégie de faible volatilité a obtenu un meilleur rendement que le marché en général à long terme. Les titres à faible volatilité ont connu une bien moins forte baisse que l'ensemble du marché pendant l'importante période de correction de 2008. Un autre avantage du degré de risque peu élevé du portefeuille est la diminution des variations dans le rendement. Sur une même période, nous avons observé l'avantage d'un rendement mieux rajusté en fonction du risque, à savoir la diminution de la volatililité. Donc, non seulement la stratégie de faible volatilité se traduit par un rendement plus élevé à long terme, mais le rendement rajusté en fonction du risque vient appuyer en retour la stratégie.

Adoptez un profil de risque plus prudent et diminuez l'incidence des corrections du marché sur votre portefeuille

Les avantages de la stratégie de faible volatilité dans l'élaboration d'un portefeuille sont les rendements supérieurs à long terme et le profil de risque peu élevé. Les fonds ZLB et ZLU peuvent être utilisés à titre de placements de base dans le cadre d'une stratégie de diversification visant à réduire le risque puisque le risque cible de leur portefeuille est plus faible que celui du marché dans son ensemble. Ils peuvent également être utilisés comme des placements tactiques pendant les périodes de grande incertitude, où un portefeuille prudent peut constituer un choix judicieux.

Visitez le **bmo.com/fnb** ou communiquez avec le Service à la clientèle au **1-800-361-1392**. Pour connaître des points de vue sur les marchés qui mènent à des solutions de FNB BMO, abonnez-vous à la publication Stratégie boursière trimestrielle, sur **bmo.com/fnb.**

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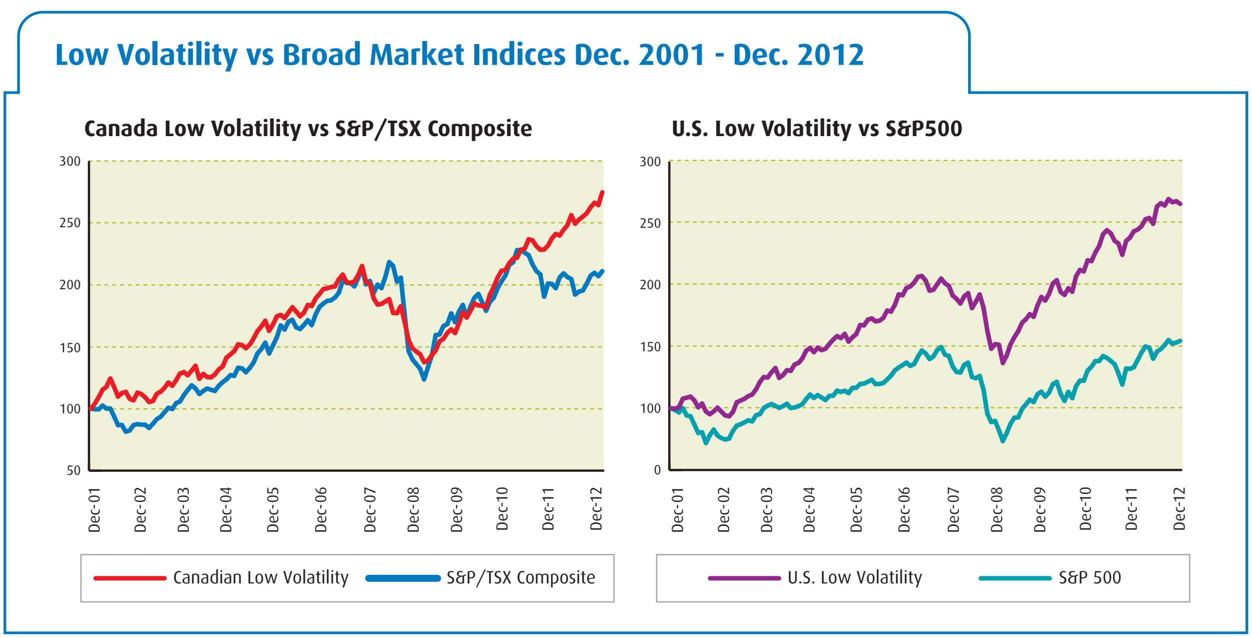


Source: Bloomberg & Factset

Building Portfolios with the Efficient Frontier

Harry Markowitz, who many consider to be the father of modern portfolio theory, postulated that for any particular collection of assets, there is an optimal combination that will maximize the level of return earned for a particular level of risk (risk being defined as standard deviation of returns).

Barry H. Gordon
President & Chief Executive Officer
First Asset

This concept is commonly referred to as the "efficient frontier". The efficient frontier will generate optimal portfolios for an investor. It's often easiest to think of it this way:

For any given level of volatility, consider all the portfolio combinations of your chosen assets which result in that volatility. The one that has the highest expected return will rest on the efficient frontier.

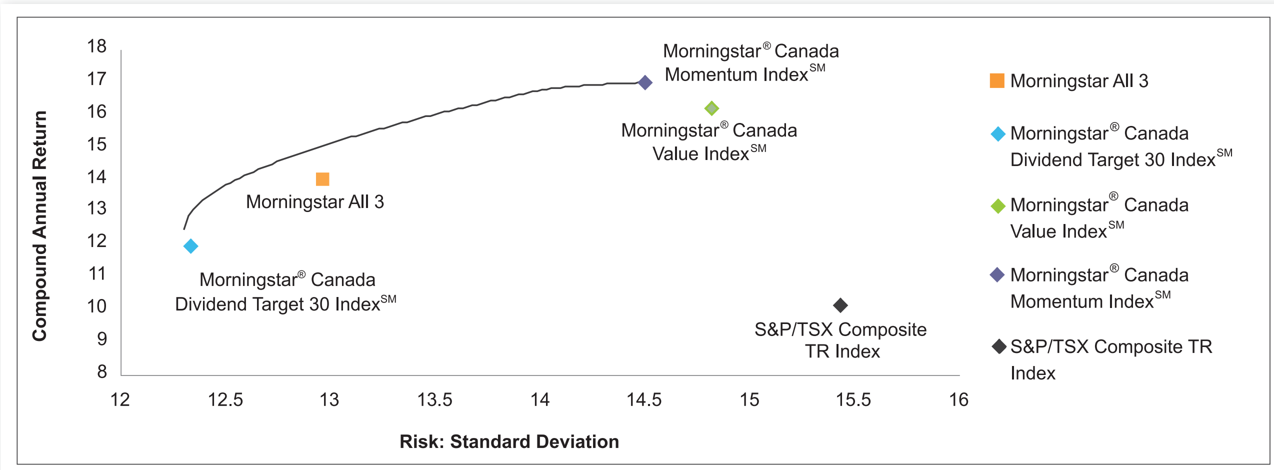
The efficient frontier analysis is commonly employed in determining what an investors' optimal portfolio will look like, given that investor's risk budget and/or return requirements. Consideration has to be given to the fact that the data used in determining an efficient frontier is historic, and thus the predictive strength of the efficient frontier analysis rests in large measure on whether the levels of return and risk for the assets included in such analysis continue in the future. Understanding the foregoing; combining different assets or entire portfolios in an efficient frontier analysis can be very instructive and helpful to investors looking to diversify risk and, more importantly, earn the best risk-adjusted return possible for their portfolio.

FirstAsset™
Exchange Traded Funds

Morningstar® Indexes

The chart below sets out the efficient frontier based on the historical compound rate of return versus standard deviation for three Canadian Morningstar Indexes – Morningstar® Canada Dividend Target 30 Index℠, Morningstar® Canada Value Index℠, and Morningstar® Canada Momentum Index℠ – and the S&P/TSX Composite Total Return Index, over a 10 year time period. All three Morningstar Indexes are powered by Morningstar's factor-based CPMS strategies that are reconstituted and rebalanced quarterly, and equal-weighted on such rebalancings.

The Efficient Frontier – Chart 1



Source: Morningstar® Direct

The three Morningstar Indexes, individually and collectively, outperform the S&P/TSX Composite Total Return Index over the 10 year time period1, both on an absolute basis and a risk-adjusted basis. This helps demonstrate that each factor index has been successful in delivering the premium that each is designed to capture.

The point labeled 'Morningstar All 3' represents an equally weighted portfolio of these three Canadian Morningstar Indexes (at an equal weight of 33% each). The Morningstar All 3 portfolio is a simple portfolio strategy to implement. It falls just below the efficient frontier, demonstrating a good balance of diversification and return for the expected amount of risk.

Optimal Portfolio Choices

As discussed above, the optimal investment portfolio is one that provides maximum potential returns for a specified, chosen level of risk, as measured by standard deviation of returns. Portfolios that land directly on the efficient frontier are defined as being 'optimal'.

We created three 'optimal' portfolios, achieved by weighting different percentages of the 3 Morningstar® Indexes at a chosen level of volatility. The weightings given to each index are broken out in the table below:

Portfolio	Morningstar® Canada Dividend Target 30 Index℠	Morningstar® Canada Value Index℠	Morningstar® Canada Momentum Index℠
Higher Risk/Return Portfolio	0	35	65
Medium Risk/Return Portfolio	35	20	45
Lower Risk/Return Portfolio	65	5	30

Source: Morningstar® Direct *For illustrative purposes and ease of implementation the portfolio mix percentages were rounded.

Each portfolio combination represents the highest possible historical return achieved for the level of risk. These optimal portfolios fall directly on the efficient frontier when they are plotted on the chart:

Continued on page 12

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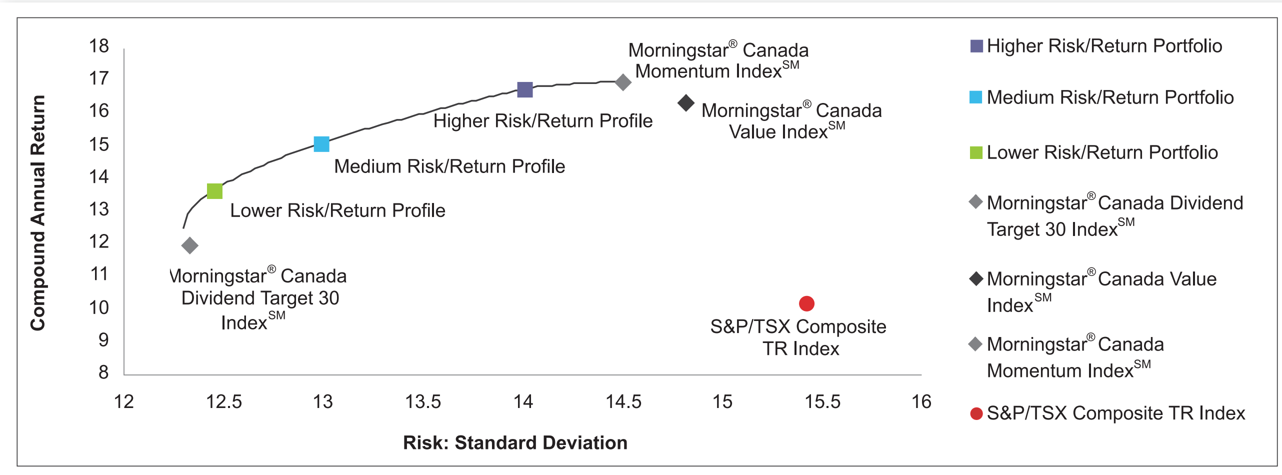
The Efficient Frontier – Chart 2



Source: Morningstar® Direct

All three optimal portfolios provide excellent historical risk-adjusted returns. Working with a financial advisor, an investor can choose a portfolio combination that best suits their needs.

Barry H. Gordon, President and Chief Executive Officer, First Asset

The views and opinions expressed herein are of a general nature and is intended for informational purposes only and is not, and should not be construed as, investment and/or tax advice to any individual. Before making any investment decision, please consult your investment advisor.

1. Performance data for the Morningstar Indexes assume the reinvestment of all distributions. Morningstar Index performance data results prior to 12/31/2011 are hypothetical, but are calculated using the same methodology that has been in use by the index provider since the Index was first published. Information regarding the Index, including the applicable index methodology, is available at http://indexes.morningstar.com. As a result of the risks and limitations inherent in hypothetical performance data, hypothetical results may differ from actual Index performance.

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TSX: Home to Canada's Exchange Traded Notes

More than two decades ago, the world's first index-linked Exchange Traded Product (ETP) was listed on Toronto Stock Exchange (TSX). Since then, the ETP industry has enjoyed phenomenal growth both in the Canadian marketplace and globally.

Gary Knight
Vice President, Trading, TSX Markets

Today, the global ETP industry has grown to reach over $2 trillion in assets under management (AUM). In Canada, a similar growth trend is apparent – the widespread adoption of these products has resulted in about $70 billion in market exposure. Alongside this impressive growth in assets, the industry's scope has evolved to provide investors plenty of choice in accessing both domestic and international markets.*

As the industry has grown, investor awareness has followed closely. There is increasing demand from investors who are turning to ETPs as an efficient means to portfolio diversification. Exchange Traded Funds (ETFs) have commanded much of the attention so far, as they dominate in terms of assets and number of products listed. Yet, there is another product that is capturing the interest of investors seeking bespoke products that deliver enhanced market access.

Exchange Traded Notes (ETNs) give investors asset allocation with targeted sector exposure, as well as competitive expense ratios. However, ETNs and ETFs should not be used interchangeably, as key differences set them apart.

TMX | Toronto Stock Exchange

A Tale of Two Products: ETNs and ETFs

An ETN is a senior, unsecured debt obligation that is typically issued by a major bank. Put simply, a bank issues a note that promises to give investors a return based on the performance of a specific index or other benchmark (less fees).

In some ways, ETNs are similar to ETFs because they both track an underlying index or single reference asset such as commodity futures, foreign currencies and emerging markets. They are convenient, cost-effective, tax efficient and – at the most basic level – both products can be bought and sold on an exchange throughout the trading day, just like conventional stocks.

However, ETNs and ETFs have a fundamentally different structure and other key distinctions. Before investors or advisors decide that ETNs are a good fit for their investment portfolios, an appropriate understanding will help them make an informed decision.

What is an ETN?

ETNs are positioned as a flexible investment vehicle that can utilize customized strategies to enhance exposure to a diversity of asset classes and, in some cases, serve as effective hedging tools. Here's a look at four key characteristics that define ETNs.

- First, ETNs are debt instruments issued by a financial institution, whereas ETFs represent a share of an underlying portfolio of securities. Unlike ETFs that buy or hold assets to replicate the performance of a particular index or strategy, ETNs have an indicative value that reflects the performance of that index or strategy. The ability to redeem ETNs at the indicative value for cash helps to keep the market price close to that value. Therefore, the trading price of an ETN will reflect both the indicative value and the supply and demand in the marketplace.
- Second, by their very nature, ETNs allow investors to access specialized market sectors, niche asset classes and trading strategies that may otherwise be difficult for average investors to buy or replicate. For example, market segments such as commodities may be hard to reach in a cost-effective way using other types of investments. As a result, ETNs have gained popularity as a strategic alternative to broaden the scope and reach of an investment portfolio.
- Third, ETNs are immune to tracking error – an ever-present risk in the ETF space. As debt instruments, ETN investors are guaranteed to receive a fixed rate of return because ETNs are, essentially, prepaid contracts with a bank. While an ETF may fall short of its benchmark, when a bank issues an ETN it promises to pay the investors the total return of their indices (minus fees), either at full maturity or upon early redemption (subject to a one-time redemption charge).
- Finally, as unsecured debt securities, ETNs do not provide principal protection. For that reason, investors could be exposed to credit risk as the repayment of principal and payment of returns hinge on the issuer's ability to pay. Therefore, it is important to consider the issuer's credit rating when making a decision to invest in ETNs. However, if an investor has an appetite for credit risk, an uncollateralized product with minimal tracking error is not necessarily a bad thing. It is also worth noting that ETNs can be redeemed by the holder of the ETN or called for redemption by the ETN issuer before their maturity date. The ability to redeem notes prior to maturity can help investors better manage credit risk.

Types of ETNs

There are currently 12 ETNs listed on TSX, with a market value of over $1.3 billion. These products help investors meet their unique needs and diverse investment strategies. Here is a look at several categories where ETN investors can gain exposure to a variety of asset classes.

Fixed Income

There has been much discussion and debate in the financial services industry and media about the risks that could develop from a potential rise in interest rates. To help mitigate these risks, ETN investors can access a particular fixed income strategy for additional portfolio diversification and flexibility.

Generally speaking, fixed income ETN investors can implement a strategy based on expectations of future economic cycles. For instance, they can execute tactical views regarding expectations of shifts in the U.S. Treasury yield curve or apply a hedging strategy to mitigate their sensitivity to the yield curve or specific yield shifts.

Exposure to Commodities

Commodity ETNs allow investors to further diversify their investment portfolio, while also providing tactical asset allocations that can be fine-tuned and tailored according to their desired exposure to commodities, or allow them to hedge against inflation.

The iPath Pure Beta Crude Oil CAD Hedged ETN (TSX:PBO) is an example of a commodity-linked ETN. It tracks the Barclays WTI Crude Oil Pure Beta Index, hedged to the Canadian dollar. This ETN provides exposure to hard-to-reach markets through an index that offers a more representative exposure to the underlying commodity than traditional front month futures-based indices.

Volatility Exposure

A number of ETNs attempt to either reduce or minimize investor exposure to volatility or capitalize on overall uncertainty in the market by following volatility futures. Most investors have benchmarks that they watch closely to keep tabs on the market, such as the widely followed CBOE Volatility Index, which is an important benchmark to gauge the volatility of the S&P 500®.

Here is a look at two volatility-linked ETNs listed on TSX:

- iPath S&P 500 Dynamic VIX CAD Hedged ETN (TSX:DVX) is linked to the S&P 500® Dynamic VIX FuturesTM Total Return Index, hedged to the Canadian dollar. This ETN offers exposure to a dynamic strategy that aims to reduce the effects of contango during normal or low volatility regimes.
- iPath S&P 500 VIX Short-Term Futures CAD Hedged ETN (TSX:VIX) is linked to the S&P 500® VIX Short-Term Futures™ Index^TR and offers exposure to shorter-term futures on the CBOE Volatility Index.

Exposure to Foreign Currencies

Many investors have also turned to ETNs to gain exposure to foreign currencies, either to hedge against exposure found elsewhere in their investment portfolio or to speculate on movements in global exchange rates.

Currency-linked ETNs can help investors gain exposure to foreign exchange spot rates, which measure the relative value of foreign currency relative to the U.S. dollar. These could include the euro, the Japanese yen or the British pound.

Some ETNs also allow investors to borrow in low yielding currencies in order to establish long positions in higher yielding currencies, thereby exploiting interest rate differentials across different markets. However, there are always risks involved in this strategy, such as rapid appreciation of a specific currency against the U.S. dollar or other unforeseen fluctuations.

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Buy-Write Strategy

Option overlay strategies have been used primarily by day traders, high net-worth individuals or institutions who can skillfully manage this complex approach involving many moving parts. However, the buy-write strategy – commonly referred to as covered call – is gaining popularity as a simple, boiled down approach which achieves a similar objective. At its root, a buy-write is an investment approach where covered call options are written on the underlying securities, and premiums are earned from the option writing.

For those investors who prefer to get their covered call exposure through an ETN, some notes track the CBOE S&P 500 BuyWrite Index℠, which measures the total rate of return of a hypothetical buy-write on the S&P 500®.

Gary Knight, Vice President, Trading, TSX Markets

All figures year-to-date August 31, 2013

*Source: ETFGI LLP, "ETFGI Global Press Release: End of Aug. 2013." Sept. 5, 2013.

ETNs listed on TSX

1. iPath U.S. Treasury Steepener ETN (SST, SST.U)
2. iPath U.S. Treasury Flattener ETN (FFL, FFL.U)
3. iPath Pure Beta Crude Oil CAD Hedged ETN (PBO)
4. iPath S&P 500 VIX Short-Term Futures ETN (VXX, VXX.U)
5. iPath S&P 500 VIX Mid-Term Futures ETN (VXZ, VXZ.U)
6. iPath S&P 500 Dynamic VIX CAD Hedged ETN (DVX)
7. iPath S&P 500 VIX Short-Term Futures CAD Hedged ETN (VIX)
8. iPath EUR/USD Exchange Rate ETN (ERO, ERO.U)
9. iPath GBP/USD Exchange Rate ETN (GBX, GBX.U)
10. iPath JYN/USD Exchange Rate ETN (JYN, JYN.U)
11. iPath Optimized Currency Carry ETN (II, II.U)
12. iPath CBOE S&P 500 BuyWrite Index ETN (BWV, BWV.U)

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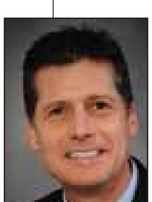
The table represents average management expense ratios for all Canadian-domiciled mutual funds and exchange traded funds as reported by Morningstar and calculated by Vanguard as of December 31, 2012. The Vanguard ETFs are managed by Vanguard Investments Canada Inc. Commissions, management fees, and expenses all may be associated with the Vanguard ETFs. This offering is only made by prospectus. The prospectus contains important detailed information about the securities being offered. Copies are available from Vanguard Investments Canada Inc. at www.vanguardcanada.ca. Please read the prospectus before investing. ETFs are not guaranteed, their values change frequently, and past performance may not be repeated.

Seasons Change – Shouldn't Your Investments Change Too?

Investors have long wondered if there is any empirical evidence to support the old investor adage "Sell in May and go away."



Howard J. Atkinson
President, Horizons ETFs Management (Canada) Inc.

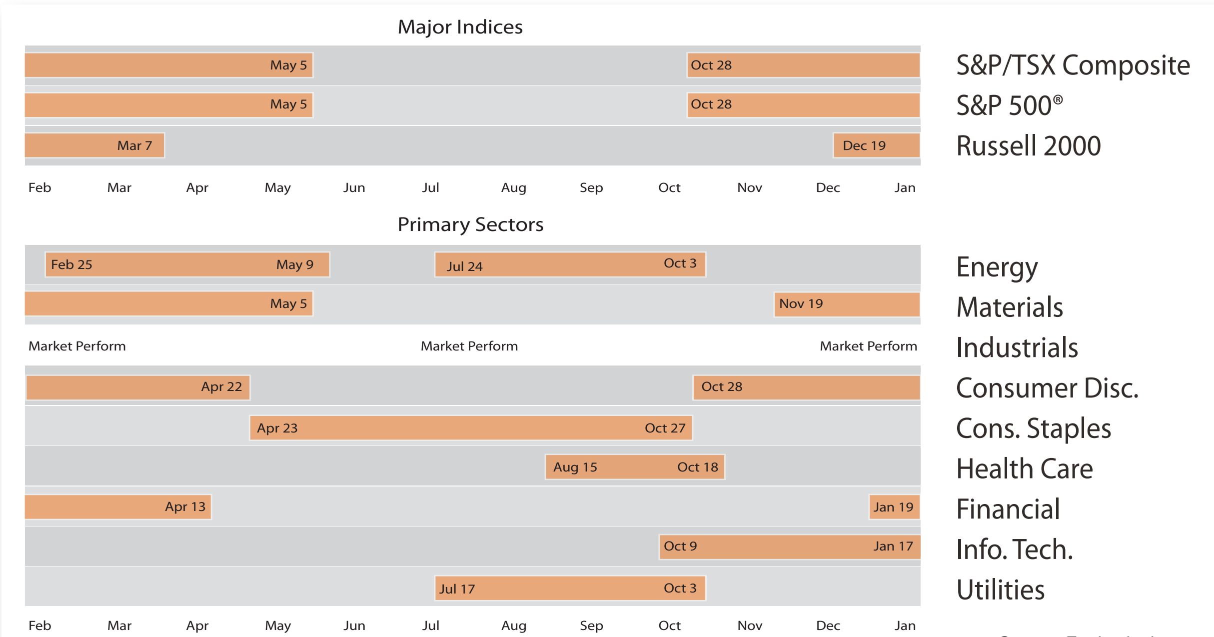
To find out, Ben Jacobsen and Cherry Zhang of Massey University in New Zealand examined more than 300 years of market data in 108 countries. They determined that stock market returns from November through April were on average 4.52% higher than those between May and October. Over the past 50 years, the average difference was 6.25%.

Testing a trading strategy based on these findings, using 300 years of UK market data, Jacobsen and Zhang found that a "Sell in May" (or "Halloween") approach would have beat the market "over 80% [of the time] for investment horizons over 5 years; and over 90% [of the time] for horizons over 10 years, with returns on average around 3 times higher than the market."

Simply being "in" or "out" of the market at different times of the year, however, is not something that many investors want to – or can – do. Some institutional investors instead try to capitalize on the market's seasonal rhythms using a seasonal rotation strategy.

As its name implies, a seasonal rotation strategy shifts a portfolio's weight in favour of particular asset classes (such as stocks, bonds, commodities or cash) at the times of the year when they typically do well, or that invests more heavily in particular industry sectors when they typically outperform the broader market (such as the S&P 500 or the S&P/TSX). The strategy is usually combined with traditional fundamental analysis and technical analysis.

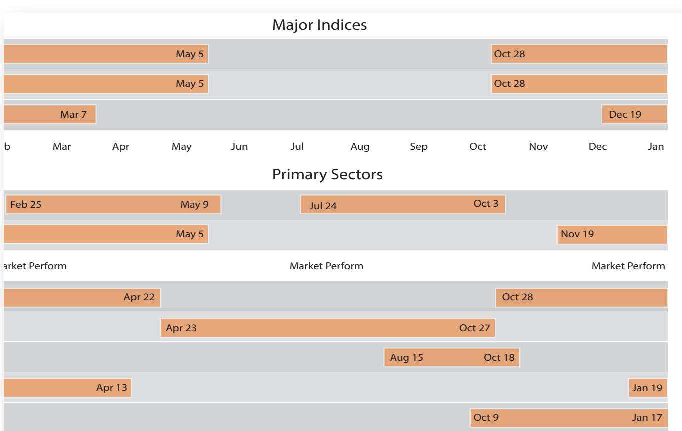
Seasonality in the Markets The observation that particular asset classes or industry sectors tend to move higher at certain times of the year is not a new one. Sidney Watchel, for example, published the first study of the "January Effect" in 1942, noting that stock prices rise in January more frequently than in any other month. The January Effect is often explained, at least partly, by the buying activity that takes place following tax-loss selling in December. Other seasonal trends can be caused by recurring seasonal spikes in demand, inventory lows, weather effects, annual corporate earnings announcements, or investment flows from year-end bonuses. Consumer spending habits, for example, are influenced by annual celebrations such as Christmas or conferences such as the yearly Las Vegas consumer electronics show. There are times when oil refineries switch from producing winter heating oil to gasoline for the summer driving season, reducing inventories and driving up the price of oil and oil stocks. The "Sell in May" adage itself may have originated with the time of year when traders in Britain started their summer holiday.



Source: Equityclock.com

Does a Seasonal Rotation Strategy Always Work?

Like any investment strategy, seasonal rotation does not always work. It can go through periods, sometimes multiple years, when historical seasonal trends are overridden by other factors. The expectation, however, is that it will work more times than not and lead to outperformance over the long term. Average monthly returns of the S&P 500® Index between 1950 and 2013 show that the November to April months have tended to do better in aggregate than the May to October months.



Source: Bloomberg, from January 1, 1950 to August 30, 2013.

Jacobsen and Zhang tested the effectiveness of a straightforward "Halloween" trading strategy relative to a buy-and-hold strategy in 37 countries between 1998 and 2011. From November to April each year, the strategy hypothetically invested in a market portfolio, and from May to October in Treasury bills. The results suggest that the strategy would have generated higher returns over the period than a buy-and-hold strategy in 31 of the 37 markets, with lower standard deviations and higher Sharpe ratios, implying superior risk-adjusted performance.

Seasonal rotational strategies, of course, are not as simple as being "in" or "out" of the market. They dynamically increase a portfolio's weighting in certain asset classes at the times of the year when doing so appears advantageous. And they overweight certain industry sectors to coincide with historically recurring seasonal events.

Timing is an important consideration. It is not simply a matter of, say, buying oil stocks just before the cold weather sets in. Other investors, anticipating the seasonal event, have usually already bought in, fully pricing in the expected benefit. Unless there is a strong positive surprise, the sector's outperformance tends to slowly roll over. A seasonal rotation strategy therefore must determine the optimal time to enter a trade, usually two or three months before the seasonal event historically takes place. In this way, the strategy benefits from both the event and the mainstream investor's tendency to buy in too late.

The strategy's timing discipline itself can also be a major advantage. Trades are entered or exited on or around pre-determined dates, taking emotions out of the decision-making process.

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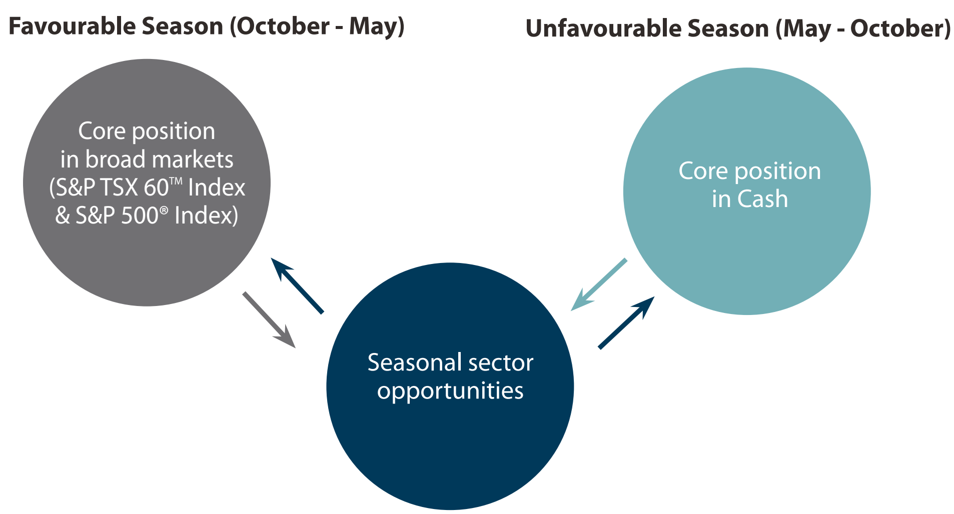
Implementing a Seasonal Rotation Strategy

There are many ways to implement a seasonal rotation strategy, both at the broad market and industry sector levels. Exchange traded funds (ETFs) are a popular choice. ETFs have made it easy for investors to gain transparent, diversified and highly liquid exposure to broad market and sector indices, in both equities and fixed income, as well as to track other asset classes such as commodities. Moreover, ETFs typically have management fees that are much lower than mutual funds.

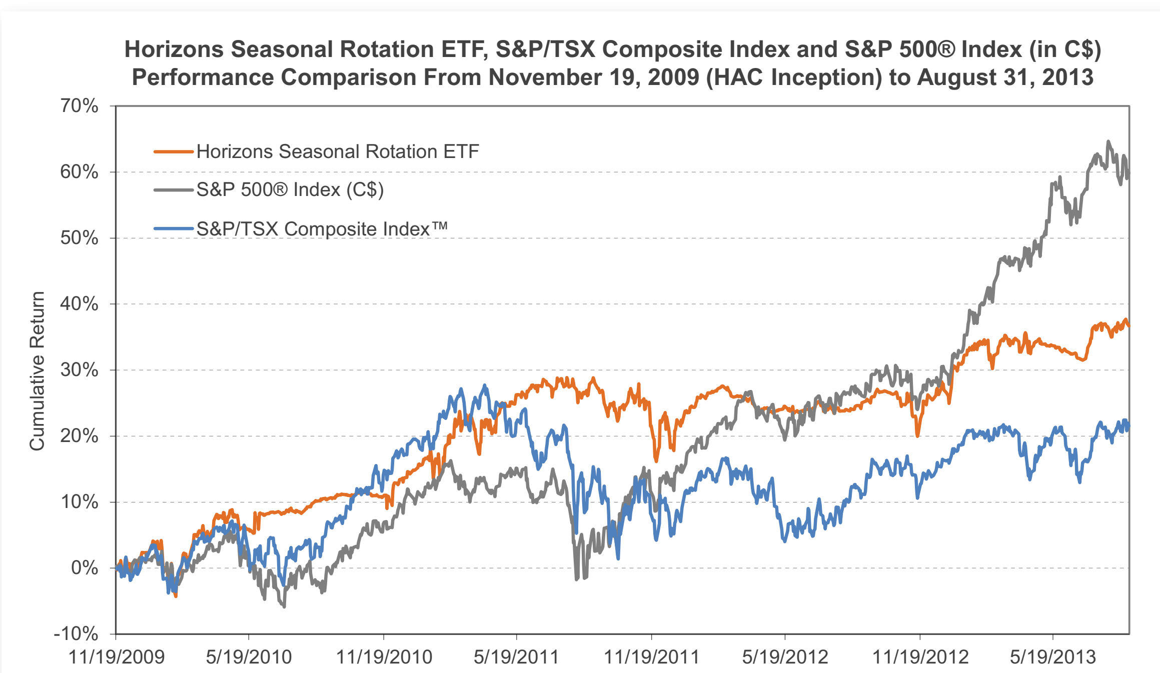
For those who feel more comfortable letting the experts manage their investments, Horizons ETFs offers the Horizons Seasonal Rotation ETF (HAC). HAC uses a proprietary strategy developed by research analysts Don Vialoux and Brooke Thackray, who together have more than 50 years of experience in seasonal investing.

The objective of HAC is long-term capital appreciation in all market cycles by tactically allocating its exposure amongst equities, fixed income, commodities and currencies during periods that have historically demonstrated seasonal trends.

The strategy's core position consists of broad markets at seasonally favourable times of the year and money market securities (cash equivalents) at seasonally unfavourable times of the year. Using additional fundamental and technical analysis, the strategy allocates from the core portfolio to various sectors when those sectors offer attractive opportunities.



Rotating a portfolio in anticipation of seasonal opportunities is designed to deliver returns that are superior on a risk-adjusted basis to a static investment in broad markets.



Source: Bloomberg, between November 19, 2009 (HAC inception date) and August 31, 2013.

Name	Ticker	1 Month	3 Months	6 Months	YTD	1 Year	3 Years	Since Inc.*	Std. Dev.	Sharpe Ratio	HAC Correla-tion	Max Drawdn
Horizons Seasonal Rotation ETF	HAC	0.11%	2.95%	3.38%	7.28%	10.08%	7.32%	8.61%	9.56%	0.80	1.0000	-8.12%
S&P 500® Index (C$)	SPXT	-2.90%	0.67%	8.95%	16.15%	19.31%	18.40%	13.54%	17.27%	0.73	0.4267	-18.64%
S&P/TSX Composite Index™	0000AR	1.55%	0.85%	0.31%	3.86%	9.84%	5.00%	5.29%	13.98%	0.31	0.3992	-20.64%

Source: Bloomberg, between November 19, 2009 (HAC inception date*) and August 31, 2013. Performance greater than one year is annualized.

With a management fee of only 0.75%, HAC offers exposure to a fully managed and diversified portfolio invested in the broader markets (Canadian or U.S. equities, fixed income), sectors, currencies and commodities.

Howard J. Atkinson, CFA, CIMA®, ICD.D President, Horizons ETFs Management (Canada) Inc. info@horizonsetfs.com

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Everything You Know About Asset Allocation is Wrong

The majority of financial industry professionals construct portfolios putting equal weight on a gain of $1,000 or a loss of $1,000 because they have been taught to think of risk as total volatility, and assumes that investors are indifferent between "upside risk" or making money and "downside risk" or losing money.

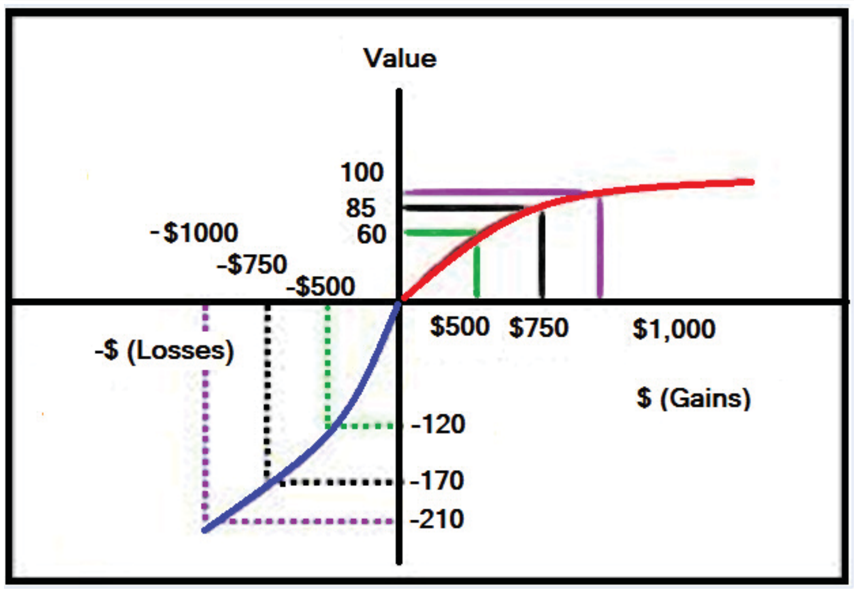
Dr. James Breech
Founder,
Cougar Global Investments

But the research of Daniel Kahneman and Amos Tversky demonstrated that this is not the case (Thinking, Fast and Slow). Most people find that the units of pain (210) they experience from losing $1,000 are more than twice as great as the units of pleasure (fewer than 100) they derive from making $1,000 (see graph on next page).

There is a fundamental mathematical reality that reinforces this: if you start with $1000 and lose 50% you need to double your money to be whole again. All of this takes time, and you will still be in a deficit position regarding your cumulative pain and pleasure.

So the moral of successful investing is that to achieve the desired compound growth, it is important to avoid losing money. This approach was developed at the Pension Fund Research Institute by Dr. Frank Sortino, who recognized that true risk for an investor is the risk of failing to achieve the compound rate of growth required to fund his or her financial objectives.

COUGAR GLOBAL INVESTMENTS



ETFs are ideal vehicles for asset allocators. There are hundreds of ETFs that track the performance of broad asset classes. Sophisticated modelling techniques allow for a unique approach to portfolio construction.

But most importantly, the asset allocation for a downside risk manager results in a much different portfolio than one constructed using traditional methods and is designed to perform in accordance with the investor's specific objectives.

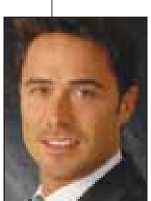
Above all, to achieve the desired compound growth your portfolio must be constructed to avoid bear markets and participate in bull markets. Thereby, not only is downside risk minimized; so is overall volatility!

Dr. James Breech, Founder, Cougar Global Investments ***jbreech@cougarglobal.com***

The Unbearable Lightness of the Central Bank Put

"There is no means of testing which decision is better, because there is no basis for comparison. We live everything as it comes, without warning, like an actor going on cold."

Milan Kundera, The Unbearable Lightness of Being



Tyler Mordy
Director of Research, HAHN Investment Stewards & Company Inc.

Milan Kundera's post-modern masterpiece from 1984, "The Unbearable Lightness of Being", perfectly captures the human paradox of lightness and weight. At times, we sense the transient nature of life, recognizing ourselves as mere participants in a vast unfolding universe. The world feels weightless. Other times, a heavier hand reminds us of a greater significance. We tighten our belts, reluctantly conceding an important role in the grand cosmos. Suddenly, our existence is heavy again.

Today, many investors are experiencing their own existential struggle. On the one hand, global central banks have created a fertile environment for speculation of all stripes. Quantitative easing and its monetary offshoots have the effect of tethering interest rates to zero, coaxing savers and investors further out on the risk curve.

For the most part, the gig has worked. Financial markets have soared on government wings. Aside from minor corrections, most worldwide stock markets have doubled from their 2008 lows (others reaching more vertiginous heights), credit spreads of all types have narrowed dramatically, and Keynes' animal spirits have experienced a Lazarus-like revival.

HAHN INVESTMENT STEWARDS

Looking ahead, the monetary indicators are still flashing green. Global central bankers – despite talk of "tapering" – continue to signal broad support for higher asset prices. Indeed, the "don't fight the Fed" mantra remains in full force.

Meanwhile, the real economy – hobbling along at sub-par growth rates – serves as a sobering reminder that we have yet to arrive. To date, monetary and fiscal largesse has only prompted a modest business expansion in the developed world. Employment levels, capital spending and other measures of economic activity are far below what they normally would be at this stage of an average post-war expansion.

This is the global paradox at hand. Despite the lightness of central bank sponsored risk-taking, underlying economies remain firmly tethered to a weightier slow-growth outlook. Of course, at some point, these divergent paths must be reconciled. Either risk markets adjust for new realities or the global economy confirms today's more robust forecasts.

Where to next?

Below, we highlight some general guidelines for navigating this new environment:

Financial Engineering – A Double-Edged Sword

In an environment of slow top-line revenue growth, corporations will remain focused on cost control and productivity gains. As part of that equation, financial engineering remains critical. Consider that companies have a number of options when utilizing their capital. They can reinvest back in the underlying business, retire debt, buy back shares, or pay out dividends.

Why would corporate executives pursue the first two options when aggregate demand is weak and interest rates are at historic lows? A more rational approach, even if not beneficial to labor, attempts to boost stock prices by reducing share count or increasing dividends. As expected, that has been the observable case, accelerating since 2008. ***The obvious interpretation is that equity sectors with these dynamics should remain well-supported. However, investors must stay vigilant to executive option issuance which effectively cancels out buybacks (e.g. the gold mining sector in recent years).***

"Money Manager Capitalism"

The late economist, Hyman Minsky (who also wrote an excellent book in the 1980s – a non best-seller on financial instability), theorized that institutional investors – i.e. pension funds, mutual funds, etc. – would come to dominate capital flows during advanced stages of capitalism. It was a prescient forecast. International markets are now more interconnected than ever and capital mobility is high.

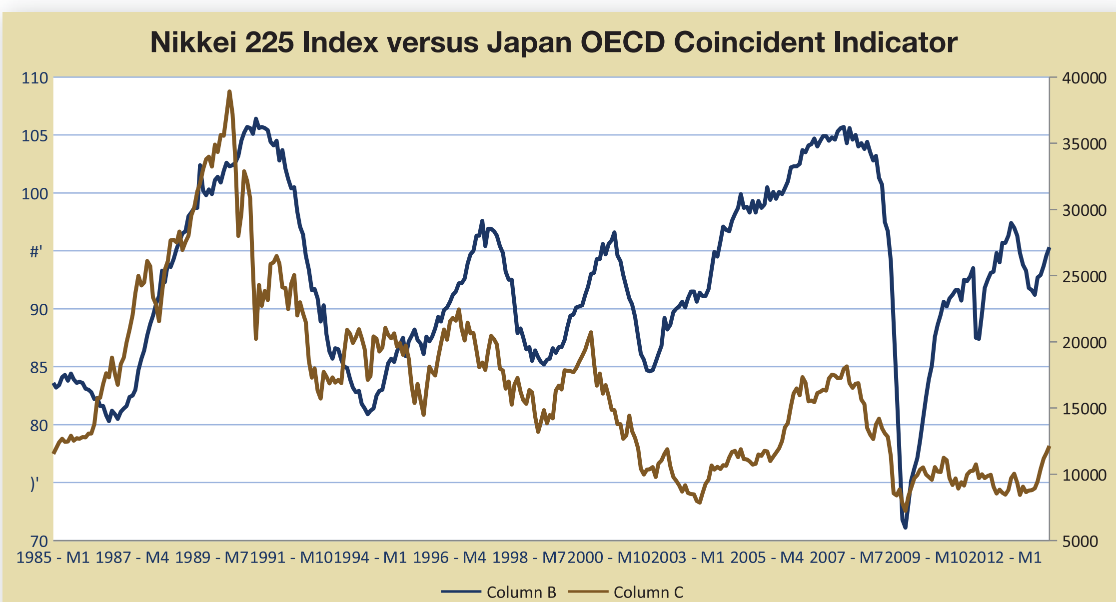
Really, this is symptomatic of an advanced, globalized financial system. After a post-war boom in the developed world, a "global glut of managed money" seeking returns now exists and provides a ready pool of capital to chase investment returns. Underfunded pensions in the West are prime examples of institutional money desperately seeking returns. The lower the interest rate levels, the more dire the situation becomes versus expected liabilities ***Under these conditions, where a surplus of capital is not tied to national boundaries and attractive returns are desperately required, we should follow this money and even anticipate what they may do.***

Currency Wars Continue

Capturing external demand is critical when domestic spending is constrained by weak income growth. One of the key features since 2008 has been the emergence of far more aggressive currency management by governments, classically referred to as "competitive devaluation." Understanding the implications of these new debasement policies will be paramount. ***In this ongoing competition, it will be key to own equities in economies that have already successfully devalued their currency (like the US) or currency-hedged equities of countries that are on an aggressive currency devaluation path (like Japan and the UK).***

(Mis)leading Economic Indicators

In an environment where traditional monetary policy has lost its potency, forward-looking indicators like stock markets have also seen their predictive abilities reduced. Financial markets have become much more reactive than predictive since 2008 (witness the almost perfect correlation between the S&P 500 and US payroll data). In fact, equity and bond markets no longer seem to lead economic events; they have become coincident, or even lagging, indicators.



Source: Macrobond, OECD

If the Japanese experience is a guide, then leading economic indicators will provide useful signals for tactical asset allocation strategies.

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Continued from : The Unbearable Lightness ... page 27

The Japanese de-leveraging case of the 1990s is instructive here. According to a January 2009 research report from Société Générale, the Nikkei's performance has been characterized by strong bull and bear rallies that were more closely synchronized with the economic cycle.

The "Bondification" of Equities

Given the widespread income crisis caused by ultra-low rates, investors are eagerly searching for higher investment yields. A rare condition is that equity markets now have higher dividend yields than mid-term government bond yields (this generally holding true for all countries that have not fallen into a debt trap). ***One result is that stocks – particularly those with high and rising dividends – are gradually becoming re-rated as income assets.***

Global Income Convergence

The living standards of select developing nations are converging with that of the developed nations. On a GDP per-capita basis, the average American was 22 times richer than the average Chinese citizen in 1978. Today, that ratio is down to only 5 times.

Investors should own shares in companies that are exposed to the ongoing transformation in the developing world and that can leverage the rising demand for consumer goods and services. That isn't limited to Western multinationals, but should also focus on select emerging market sectors. ***However, generally, the same stock market sectors that should be underweighted in the West should be overweighted in most emerging markets (i.e positioned to benefit from a rising middle class). Beware broad-based emerging market equity ETFs, as much of their indexes are geared towards the exporting component of their economies.***

Macro Volatility Increases

It is no secret that government activism has surged since the onset of the global financial crisis. But, less known, is that deficit-driven economies will experience more frequent bursts and lapses in growth, speeding up the cyclical rhythms compared to "normal" cycles. Why? Because private sector driven expansions typically produce organic, sustainable, and long-lasting recoveries. Government-fueled expansions do not.

The above observation is closely correlated with recent trends in volatility. Currently, world economies have trouble returning to "normal" growth, despite ongoing stimulus measures. The years 2010, 2011, 2012 and, now 2013, witnessed a similar pattern. The year begins with hopeful expectations (driven largely by renewed stimulus initiatives) and, by mid-year as growth fades, pessimistic outlooks and attendant volatility resume. This merely reflects the tug-of-war between economic realities and increasingly frantic policy responses. ***Expect continuing episodic surges in volatility. Those with ongoing expectations of an imminent private sector-led recovery will be disappointed. For the next few years, a key strategy will be to reduce risk once the consensus becomes convinced of a self-sustaining recovery.***

Experimental Economics and Confessions from the Fed

The tentacles of the Fed's monetary easing are reaching far beyond American borders. Richard Fisher, president of the Federal Reserve Bank of Dallas, in a refreshingly candid speech in 2010, admitted that in his "darkest moments" he questioned if monetary stimulus was already working in the wrong places. Crucially, he noted that the Fed's easy money has created risks of "competitive quantitative easing", a beggar-thy-neighbour phenomenon among central banks trying to sterilize or outdo the effects of each other. Fisher cites the Bank of Japan's governor at the time, Masaaki Shirakawa, quoting his reasons for another bond-buying program in anticipation of the Fed's second round of QE: "If a central bank tries to seek greater impact from its monetary policy, there is no choice but to jump into such a world."

Experimental monetary policy is now widely accepted as standard operating procedure in today's post-crisis era. Yet, the law of diminishing returns applies. As regular ice cream-eaters progressively experience less pleasure with additional indulgence, so does the market demand ever-increasing portions to produce the same wealth effect (i.e. witness the declining effects of QE). ***Be skeptical of any announcements of major policy exits. Opportunities will emerge due to monetary dysfunctions. Out-of-the-box thinking is required here.***

Conclusion

Kundera's novel courted controversy, challenging the Nietzschean "heaviness" of eternal recurrence. This was a prominent philosophic debate in the 1980s. Many believed that Nietzsche's philosophy was anti-humanist and, thus, inherently totalitarian. It didn't allow the possibility of human autonomy, because everything in life was structured in repetition.

Today's financial debates are similarly polarized by the hopeful "lightness" of plentiful liquidity supplied by central banks and the weightier slow-growth environment. However, a more balanced perspective here is important. Economies will not remain eternally hostage to recurrent sub-par growth. As in both life and markets, nothing lasts forever.

Likewise, continuing central bank liquidity does not mean downside risks have been completely eliminated. For the last five years – arguably since the early 1980s – investors have been privilege to the central bank put. Yet we have still seen continuing rolling crises and corresponding policy responses.

Looking ahead, the fall in real household income levels in the developed world means that deficient aggregate demand and slow domestic growth will likely be a longer-running issue. Under that view, policymaking will move further into the realm of the unorthodox during this next stage. Indeed, we may only be in the foothills of a longer journey.

Investors cannot become complacent in this environment. Rather than seeing the current climate as an unbearable crisis, they will need to stay tactically nimble, seek global opportunities and only cautiously swallow the pills prescribed by central bankers.

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