glc asset management

Market Matters

Summary for July 2018

Highlights

Equity markets rose as strong corporate earnings results overshadowed trade concerns.

U.S. and Canadian GDP results were stronger than expected.

A slow, ratcheting uptrend in longer-term yields continues to unfold, putting pressure on bond returns. .

Trade concerns hit commodity values (and weakened currencies versus the US dollar).

The economy, corporate earnings and trade moved capital markets in July 2018

Three ongoing narratives dominated the headlines and moved capital markets:

- Economic data: Better than expected North American employment figures, retail sales and GDP growth.
- Corporate earnings: With a few notorious exceptions, North American companies pleased investors with strong earnings results.
- Trade tensions: Rhetoric worsened between nations (primarily in relation to the U.S.) with some threats becoming reality in July. Commodity and currency values were negatively affected.

Strong economic results and corporate earnings buoyed equity markets and gave the needed encouragement to the Bank of Canada to raise interest rates, putting downward pressure on Canadian bond returns as yields rose. Meanwhile, trade tensions and the ensuing currency volatility added a degree of uncertainty to the investing landscape, but did not derail the upward momentum of stock prices or bond yields.

Economic data with a nice summer glow

Recent economic data releases turned out to be brighter than expected. U.S. GDP (Q2) grew 4.1% q/q annualized (the strongest pace in nearly four years), helped by strong consumer spending. In Canada, GDP results from May were also strong– a rebound from weather-affected weakness in April and higher oil prices leading into the summer months. Canadian GDP is on track for ~3% annualized growth in Q2. Both Canadian and U.S. labour market reports were cheered by stock and bond investors alike. The job gains were substantially higher than forecast. The US labour market attracted 601,000 new workers (the second largest gain in over 15 years) and the Canadian labor force expanded by 75,600 (the biggest increase in six years). In a further sign of late-cycle economic expansion, Canada's headline inflation rate hit a six-year high of 2.5% in July, juiced by the rising fuel prices (as anyone taking a summer road trip can tell you).

Market Summary

Canadian Fixed Income[1]	Month	YTD
FTSE TMX Canada Universe Bond Index	-0.7%	-0.1%
FTSE TMX Canada All Corporate Bond Index	-0.5%	0.2%

Canadian Equities[2]	Month	YTD
S&P/TSX Composite	1.0%	1.4%

	Month		YTD	
Global Equities[2]	Local	CAD	Local	CAD
S&P 500	3.6%	2.5%	5.3%	9.4%
MSCI EAFE	2.6%	1.4%	-0.2%	1.6%
MSCI Emerging Markets	1.2%	0.6%	-2.8%	-2.5%

Currencies and Commodities (in USD)	Level	Month	YTD
CDN $	0.769	1.0%	-3.4%
Oil (West Texas)	68.76	-7.3%	13.8%
Gold	1,226.11	-2.3%	-5.9%
Reuters/Jeffries CRB Index	194.53	-2.9%	0.3%

Canadian Sector Performance[2]	Month	YTD
Energy	1.0%	3.8%
Materials	-4.0%	-1.5%
Industrials	4.8%	10.8%
Cons. Disc.	-0.4%	2.0%
Info Tech	-2.1%	19.5%
Health Care	-8.9%	-10.3%
Financials	2.2%	-1.2%
Cons. Staples	0.8%	-2.5%
Telecom	3.8%	-3.6%
Utilities	0.6%	-7.9%
Real Estate	1.6%	4.4%

Local currency unless otherwise stated.
[1]Total return [2]Price only return
Source: Bloomberg

The Bank of Canada (BoC) noted that the composition of Canadian economic growth is shifting: exports and business investment are picking up, while housing and consumption decelerate. This is a welcome and healthy development, and something the Canadian economy has been waiting many years to see. The BoC raised interest rates by 25 bps to 1.5% on July 11th, as expected. The slow, ratcheting uptrend of interest rates and bond yields continued to unfold and pose a headwind for fixed income returns.

Corporate earnings: most soar, some Faceplant.

Despite a few high-profile misses, Canadian and US corporate earnings results were very solid, fueled in part by reduced U.S. tax rates. The strong earnings season overshadowed trade concerns. Even as the trade rhetoric amplified, equity markets focused on company results, liked what they saw, and rewarded stock values with a steady rise.

> *"The bigger they are, the harder they fall."*
> Joe Walcott, welterweight champion of the world from 1901-1904.

Facebook's earnings report disappointed, and the stock set a new U.S. traded company record for value lost in a single day (nearly $120 billion). High valuations made Facebook particularly susceptible to disappointment, but before you feel too bad for the poster-child of tech-related superstars, it's worthwhile to note that Facebook's stock saw an epic rise from late March 2018 to late July of 43%. July's month-end record loss only brings investors back to stock values last reached in April of this year. Facebook still remains the fifth largest company on earth based on market capitalization.

Trade rhetoric turns up the volume.

Markets have been climbing a 'wall of worry' on trade fears, with US and Canadian equities up roughly 9% and 8% since a correction back in March when the trade rhetoric initially ramped up. While political saber-rattling on trade amplified in July, there were small gains that tempered anxiety. Investors cheered the positive outcome of the discussions between European Commission President Junker and US President Trump as the U.S. and European Union moved toward resolving certain trade disputes. Likewise, though NAFTA negotiations had taken a recent negative turn in June, temperaments softened in July. Even so, it was somewhat surprising to see capital markets pay little heed to the political, tit-for-tat spats that have coloured recent trade talks. Either market investors are sanguine on the extent to which the trade wars might escalate, or they have become complacent for now (and complacency is rarely a good long-term, sustainable strategy).

Meanwhile, commodities and currencies didn't escape the trade fall-out. Commodity values weakened in response to the potential negative impact on growth that further trade disputes would have. Oil prices dropped sharply in July. Canadian energy stocks weakened, but managed to buck the downward trend in oil prices overall for the month. The Canadian Materials sector on the other had was not so fortunate and the sector suffered along side falling copper and gold prices.

Currencies have become the latest battleground to be added to the trade war. In July, the Chinese continued to let the yuan depreciate against the U.S. dollar, effectively making Chinese exports that much more affordable when converted back into U.S. dollars.

This bull can run, and that's no bull.

The aging S&P500 bull is set to make history by becoming the longest-running bull market for the index on August 22, 2018, after a little more than a whopping 113 months!

We acknowledge that there is still room for the current bull market to run (e.g. U.S. tax reduction plans have breathed new life into corporate earnings); overall, we consider markets to be in the later stages of the cycle. For investors, that means we caution against becoming overly optimistic and investing beyond your neutral risk tolerances (see [GLC's Mid-Year Capital Market Outlook] for our late market cycle positioning strategies).

In a nutshell: Feel free to reminisce and celebrate the historic milestones of capital markets (we do!). Just don't go crazy (we don't!), because tomorrow is yet another day (we know!).

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VP Marketing and Communications, has more than 15 years of investment industry experience and has been writing the monthly Market Matters for over 10 years.