Q3 2019 MARKET COMMENTARY

GP WEALTH MANAGEMENT

GDP growth in the United States recorded a historic milestone at the beginning of last quarter, chugging past the 10-year mark and becoming the longest business-cycle expansion in the post-war era. That's a notable statistic, to be sure, and unsurprisingly, it generated loads of coverage in the business press.

But as a tool for predicting the direction of the market, GDP performance has dubious value. By its nature, this type of data is backwards looking, whereas stocks are oriented towards the future.

A more relevant statistic for investors attempting to anticipate stock prices is the number 67. That's how many times central banks around the world cut interest rates in Q3 in a coordinated effort to counter flagging global-growth momentum.

In addition to rate cuts, central banks have unleashed other tools, including lower reserve requirements, low-cost loans and asset purchases, to stimulate credit and economic activity.

Looser global monetary policy stokes the overall economy — thereby creating the conditions for higher stock prices — so investors have reason to cheer.

KEY TAKEAWAYS

- Most big economies are in the late phase of the business cycle
- Central banks are using monetary policy in an attempt to stimulate global economic expansion
- Uncertainties surrounding the U.S.-China trade talks are creating a strong headwind to growth
- Globally, stocks largely moved sideways in Q3
- The S&P/TSX Composite Index soared to an all-time high in the quarter, but global risk puts the durability of the rally in question
- U.S. consumer spending remains solid against a backdrop of low unemployment — a typical late-cycle pattern

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The question is, will it be enough to overcome the uncertainties surrounding the U.S.-China trade war, policy unpredictability under President Trump and contracting global manufacturing, not to mention geopolitical concerns ranging from Syria to Brexit to the attacks on Saudi Arabia's oil infrastructure?

Global outlook

Globally, stocks moved sideways in the quarter, and there is a risk that escalating market uncertainties could create a self-fulfilling cycle in which rising pessimism results in lower private-sector spending and higher unemployment. In turn, this could lead to lower profits and falling equity prices — which would create even greater pessimism.

Further, despite the willingness of central banks to encourage growth by expanding the money supply, they have limited room to maneuver. In Japan and Europe, interest rates are already at zero or negative. The U.S. has more scope with the Fed funds rate in a target range of 1.75% to 2%, but prior recessions have seen the Fed cut rates by more than 5 percentage points on average.

Perhaps the biggest risk to the outlook for global markets is the ongoing trade war between the world's two largest economies. Last month, the U.S. upped the ante by applying tariffs on more than $125 billion of Chinese products. China retaliated by imposing additional tariffs on $75 billion of U.S. goods. The prolonged trade dispute has shown signs of weakening the U.S. economy, most notably within manufacturing. In the month of September, the ISM Manufacturing PMI in the U.S. — a widely-watched indicator of recent U.S. economic activity — dropped to 47.8 from 49.1 in the previous month. This represented the steepest contraction in the manufacturing sector since June 2009.

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Canada performance review

Canadian equities, as represented by the S&P/TSX Composite Index, soared to an all-time high in Q3. The index returned +1.7% for the quarter, led by defensive sectors such as utilities, real estate and consumer staples, and is up a total of +16.3% year to date.

In its most recent decision on interest rates, announced September 4, 2019, the Bank of Canada (BoC) held its overnight rate at 1.75%. The BoC's assessment of economic conditions was relatively balanced. On the positive side, it noted stronger than expected second-quarter GDP growth and housing activities, as well as rising wages. However, weakness in business investment, soft consumer figures and increased concerns about global growth were detracting factors.

When making rate decisions, the BoC also has to consider keeping its key lending rate reasonably in line with the U.S. rate (currently set in a range of 1.75% to 2%), given Canada's close trade relationship with its much larger southern neighbour.

U.S. consumers confident

Judging by its tight labor markets, weakening corporate profit margins and flat/inverted yield curve (a hallmark of the late business cycle), the U.S. appears to be firmly in the late-cycle phase of this extended bull run.

Also, consumer spending remains solid in a supportive environment of low unemployment—a typical late-cycle pattern. Q3 consumption growth appears likely to come in at an inflation-adjusted rate of 3%, and housing has been lifted significantly by lower mortgage rates.

However, U.S. consumers are not impervious to the many challenges facing the global economy, and consumer confidence — as distinct from consumer spending — has turned down sharply. Considering interest rates are falling, fuel costs are low and jobs are easy to find, this lack of confidence is likely attributable to mounting uncertainty over the trade war and other market risks, both domestic and global.

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What's next?

The global business cycle continues to mature, with the U.S. and most major economies in the late-cycle phase.

China's economy has steadied but growth reacceleration has not materialized. Overall, a global recession in industry and trade remains a possibility. It's yet to be seen whether the central banks have enough monetary policy ammunition to bring about a sustained global upswing, benefitting both the economy and the markets.

Getting Advice

Are you looking for additional perspective on the financial markets and how they might affect your portfolio? We encourage you to talk to us. Speak to your Financial Advisor or contact investor services at **1 800 608 7707**.

*As of Sept 30, 2019	MARKET MONITOR (Returns in CAD)			
MARKET INDICATORS	MARKET CLOSE*	2018 RETURN	2019 Q3	2019 YTD
S&P/TSX Composite	16449.35	-11.64%	+1.69%	+14.85%
DJIA	26573.72	+2.63%	+2.34%	+11.38%
MSCI World	2153.82	-2.59%	+1.21%	+11.79%

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