Portfolio Management
Monthly update

October 2019

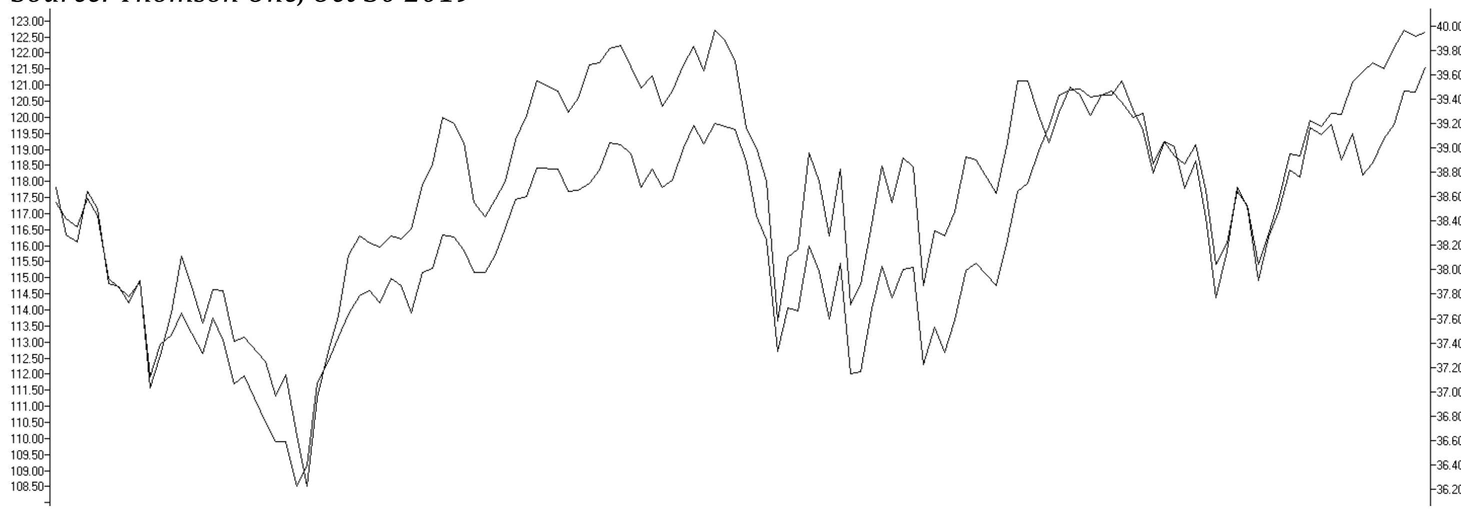
Highlights

- Seasonality favours economically sensitive stocks over defensives & stocks over bonds. Value may finally beat growth.
- The yield curve is no longer inverted.
- The odds of recession are low unless the trade war heats up again.
- Q3 Earnings estimates are down 3.7% year over year results somewhat better so far.
- Globally exposed companies doing worse than US domestic firms.

The extreme outperformance of growth stocks (top line) vs value over the last 3 years may have peaked

Growth & Value 6-month chart

Source: Thomson One, Oct 30 2019



Value is outperforming lately due to expectations that the 40 rate cuts around the world in the last 3 months should start to help economic growth. (Barrons, Oct 28). Value stocks are largely cyclicals & financials which have been hurt by persistent worries over global growth & falling interest rate. If this trend continues the TSX with its heavy cyclical exposure could finally outperform the S&P 500.
Industrial stocks, which also fall in the value-cyclical group have started to improve as well.

High yield stocks are the opposite of value & cyclicals. REITS & utilities have become expensive and are dropping lately. We still like these areas on a pullback though.

Value funds such as Pender & Edgepoint have lagged, but may improve, especially with the positive stock market seasonality going into the New Year.

The usual seasonal rally is likely into the New Year, with Bullish Sentiment at 42%, nearer the lows of 36% associated with market bottoms vs the 60%+ level associated with tops.

Earnings are down but the usual Guide down & surprise up: with 40% of the S&P 500 companies reporting Q3, 80% reported a positive earnings surprise & 64% reported a positive revenue surprise. Earnings estimates for Q3 are down -3.7%. Actual earnings will like be better but ***Q3 will mark the first time S&P 500 companies reported 3 straight quarters of year-over-year earnings declines since Q4 2015 through Q2 2016***. (Fact Set Earnings report Oct 25)

S&P 500 Companies with More Global Exposure Reporting Near 10% Earnings Decline in Q3
Concerns about the stronger U.S. dollar, slower global economic growth, and trade tensions are coming true. With 40% of the companies in the index reporting, those with over 50% of sales inside the U.S. experienced an earnings decline of -0.8% & revenue growth of 4.6%. For companies with under 50% of sales inside the U.S the decline was -9.1% & a revenue decline of 2%. (Fact Set Earnings report Oct 25).

For companies with more global exposure Energy & Information Technology sectors were the largest contributors to the earnings decline, while the Materials and Energy sectors are the largest contributors to the revenue decline.

No More Inverted Yield Curve

Canada did not match the 0.25% US rate cut, which, along with stabilizing energy prices, has helped the Canadian dollar rally from a low of 73.6 cents US to 76.6 lately.US 10 year bond yields have risen from 1.514% early in October to 1.846% lately. This is a good sign, since it moves us away from the inverted yield curve & recession worries.

We expect the China bashing from Trump to simmer down, since no US president has ever been re-electing a slow economy. Emerging markets, which have lagged for many years should rally with an improving global economy and a flat to lower US dollar.

Regards,

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