



August Market Update: Earnings Season Propels Wall Street Forward as TSX Lags Behind

July was another record-breaking month for Wall Street, with the Nasdaq Composite Index setting multiple all-time highs on the strength of surging technology stocks. The S&P 500 Index and Dow Jones Industrial Average also put up firm gains as volatility fell to its lowest level in six months.

Wall Street's tailwind failed to spur commensurate gains in Canada, where the benchmark TSX Index returned less than 1% during the month.

U.S. Stocks Rise on Corporate Earnings

A late-month selloff of technology shares wasn't enough to undermine a stellar July for U.S. equities. The Nasdaq reported five record closes during the month as it crossed 7,900 for the first time in history.

The Dow 30 index was the strongest monthly performer, gaining 4.7% for July.

The broader S&P 500 Index added 3.6% during the month on the back of upbeat corporate earnings. Through the first half of reporting season, S&P 500 companies were on track for their second-best quarter of earnings growth since Q3 2010, according to financial research firm FactSet.^[i] Among companies that have reported so far, four of five (83%) have posted positive earnings surprises and 77% have reported revenue numbers that were higher than expected.

The reaction to earnings was much more subdued in Canada, with the S&P/SX Composite Index putting up minor gains during the month. The Canadian benchmark set a new record high July 12 before giving back 1% over the next three weeks.

Facebook's Historic Decline

Facebook Inc. made the wrong type of history July 26 after posting the biggest loss in U.S. stock market history. The Mark Zuckerberg-led social media giant lost \$119 billion in market cap in a single day of trading after a disastrous earnings call shed light on the company's revenue struggles.

Although Facebook posted solid top and bottom line growth, revenues missed analysts' forecasts for the first time in over three years.^[iii] New privacy laws, struggles to monetize Instagram Stories and declining active users in North America all weighed on investor sentiment.

Bank of Canada Lifts Interest Rates

Canada's central bank raised interest rates in July for the fourth time in 12 months despite underlying risks tied to free trade and global growth.

"Although there will be difficult adjustments for some industries and their workers, the effect of these measures on Canadian growth and inflation is expected to be modest," the Bank of Canada (BOC) said in its official statement.

By the Bank of Canada's own measures, U.S. duties on Canadian commodity exports will shave nearly 0.7 percent point from domestic GDP by the end of 2020. However, those losses are expected to be offset by gains from higher oil prices and a stronger U.S. economy.^[iii]

The central bank's trendsetting interest rate now sits at 1.5%. Three of Canada's largest banks, including RBC, TD and Bank of Montreal, raised their prime rates following the July 11 announcement.^[iv]

The Month Ahead

With earnings season winding down, trade negotiations and geopolitics will attract greater attention over the next four weeks. After reaching a tentative trade deal with the European Union in July, the Trump administration is said to be eyeing a resolution to the North American Free Trade Agreement (NAFTA). A deal with Mexico appears to be gaining traction, which could place more pressure on Canada to negotiate a compromise.^[v]

Sincerely,

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[i] FactSet Earnings Insight (July 27, 2018).

[ii] Sam Bourgi (July 27, 2018). "Week in Review: Bitcoin's Bull Run Tempered by Winklevoss ETF Miss; Facebook Makes Wrong Type of History." Hacked.com

[iii] Erica Alini (July 11, 2018). "Bank of Canada delivers another hike, key interest rate rises to 1.5%." Global News.

[iv] Pete Evans (July 11, 2018). "Bank of Canada raises benchmark interest rate to 1.5%, noting trade tensions." CBC.

[v] Tony Media (July 31, 2018). "Trump Close to NAFTA Deal?" The Weekly Standard.

