Investment Notes

September 28, 2018

GLOBEINVEST
CAPITAL MANAGEMENT INC.

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Overview

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The US economy continues on its growth path, as evidenced by the low unemployment rate, wage growth and corporate earnings growth. While there may be some short-term slowdowns in some sectors of the economy, e.g. housing, and there will likely be some slowdown in 2019 corporate profit growth once the impact of the tax cuts wear off, we do not see any imminent and severe negatives for the economy.

In fact, given the current economic momentum and projected forward earnings, it is quite conceivable that growth could continue into 2020. We have opined for some time that given the depth of the Great Recession, any recovery would be slower than past ones and would go on for longer than many expect.

Nonetheless, we remain cognizant of the risks to our current view. The continuing U.S./China trade war is potentially a major destabilizing event. We think that in due course, the likelihood of US and China reaching a mutually beneficial agreement is high.

Another risk, to the extent of which we don't know, is the outcome of the U.S. mid-term elections and subsequent impact. Once the results are in we will review them and make whatever adjustments we think is appropriate.

Lastly, the inherent risks associated with higher interest rates, such as how will they impact the economy, corporate earnings, the stock market (the S&P 500), and its forward price to earnings ratio.

Regarding interest rates, let's review (1) where nominal and real interest rates were a year ago and today (2) the slope of the yield curve a year ago and today, in Canada and more importantly, in the U.S.

Canadian & US Government Bonds Rates

	09/30/17		09/30/18	
	Nominal	Real	Nominal	Real
2 year maturity:				
Canada	1.53%	0.13%	2.19%	-0.6%
US	1.48%	-0.42%	2.81%	0.11%
5 year maturity:				
Canada	1.75%	0.35%	2.32%	-0.48%
US	1.94%	0.04%	2.94%	0.24%
10 year maturity:				
Canada	2.11%	0.71%	2.41%	-0.38%
US	2.33%	0.43%	3.05%	0.35%
30 year maturity:				
Canada	2.47%	1.07%	2.41%	-0.38%
US	2.86%	0.96%	3.19%	0.49%

Slope of Yield Curves (basis points "bp")

	09/30/17	09/30/18
5 YR less 2 YR:		
Canada	22 bp	13 bp
US	46 bp	13 bp
10 YR less 2 YR:		
Canada	58 bp	22 bp
US	85 bp	24 bp
30 YR less 2 YR:		
Canada	94 bp	22 bp
US	138 bp	38 bp

Observations:

- While nominal interest rates have risen during the past year, real rates in most cases are lower, indicating inflation has risen at a faster pace.

- Each country's yield curves has flattened, but they remain positively sloped with 10YR rate greater than the 2YR rate, e.g. in Canada the spread is 22bp and in the U.S. 24bp. Historically, the U.S. Treasury inverted yield curve has been a good predicator of economic recessions. In each of the last seven U.S. recessions, the yield

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curve inverted prior to the onset, with an average lead time of 15 months.

- To date, rising rates have not impacted stock prices other than to be a partial cause of the January pullback. Nor have they impacted corporate earnings growth, particularly in the U.S. They may have impacted forward price earnings ratios (PER). For example, a year ago the consensus forward PER for the S&P 500 was 17.8x. In January of 2018 it had increased to 18.8x and is currently 16.7x. Arguably, higher corporate growth expectations has also contributed to a lower PER. An increase in U.S. Treasury 10 year rate to the 3.50% - 4.00% may cause the PER to contract modestly, but in our opinion, not in a significant way given the current inflation environment. So long as corporate profit growth continues, stock prices should have further upside.

Summary

While we remain aware of the potential risks and concerns, we are staying with our constructive view on equities. Based on the economic data and indicators we follow, the likelihood of an economic recession in the foreseeable future is low. Recessions are what ultimately ends a bull market.

The risks we have identified as well as any other unexpected events that may unfold, will be closely monitored. Adjustments to our investment outlook will be made if warranted.

Peter Brieger, HBA, CFA
Christine Poole, MBA, CFA
Wendy Sanita, CFP®, CIM®
Chris Blumas, MBA, CFA

2018 BNN Dates

October 10 @ 6:00 pm C. Poole
October 25 @ 7:00 am C. Poole
November 13 @ 12:00 pm C. Poole
November 22 @ 7:00 am C. Blumas
December 11 @ 12:00 pm C. Poole

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September 30, 2018 Statistical Summary

STOCK MARKETS	**YTD**	**1 Year**
S&P TSX Composite Total Return (CAD)	1.4%	5.9%
S&P 500 Total Return (CAD)	13.4%	22.0%
S&P 500 Total Return (USD)	10.6%	17.9%
DJIA Total Return (USD)	8.8%	20.8%
NASDAQ Composite Price Return (USD)	16.6%	23.9%
MSCI World Index Price Return (USD)	3.8%	9.2%
COMMODITIES		
GOLD	-8.7%	-7.9%
SILVER	-13.7%	-12.4%
COPPER	-13.1%	-3.2%
NATURAL GAS	1.9%	-0.3%
WTI	21.2%	42.1%
BRENT	22.8%	41.1%
CANADIAN UNIVERSE BOND INDEX	-0.3%	1.7%

TREASURY BONDS	**09/30/18**	**12/29/17**
2 Year Maturity (CAD)	2.19%	1.69%
(US)	2.81%	1.89%
5 Year Maturity (CAD)	2.32%	1.86%
(US)	2.94%	2.20%
10 Year Maturity (CAD)	2.41%	2.03%
(US)	3.05%	2.40%
30 Year Maturity (CAD)	2.41%	2.24%
(US)	3.19%	2.74%
Inflation		
CPI (CAD)	2.8%	1.9%
(US)	2.7%	2.1%

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