

Market Review

October 10, 2018

Market Outlook

Equity markets are re-calibrating to the prospect of sustainable higher U.S. interest rates, driven by a buoyant U.S. economy and Central Bank commentary alluding to a continuation of rate increases. Neither was that surprising, so the ensuing market pullback could partly be attributed to a much needed pause after the strong run in the last quarter for U.S. stocks.

More recently, the U.S. Treasury Yield Curve has shifted up and steepened, albeit moderately, with the spread between the 10 Year and 2 Year now at 32 basis points. The steepening is encouraging given that with inflation expectations in check, the Fed intends to continue gradually raising interest rates.

Low unemployment combined with higher wages are supportive of continued U.S. consumer spending, which accounts for two-thirds of U.S. GDP. Both consumer and small business sentiment remain at elevated levels, boding well for future economic activity.

Consensus expectations is for third quarter earnings per share (EPS) for the S&P 500 companies to be up over 20% year-over-year. Excluding the beneficial impact of lower corporate taxes, underlying EPS growth is estimated to be 12%. Tariffs, elevated input costs, a stronger USD and softening economic growth in regions outside of the U.S. are potential headwinds. Commentary to the extent these factors may dampen future profit growth will be closely monitored.