The Market in Review

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October 12th, 2018

This week's articles and insights

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"The big money is not in the buying or the selling, but in the waiting."

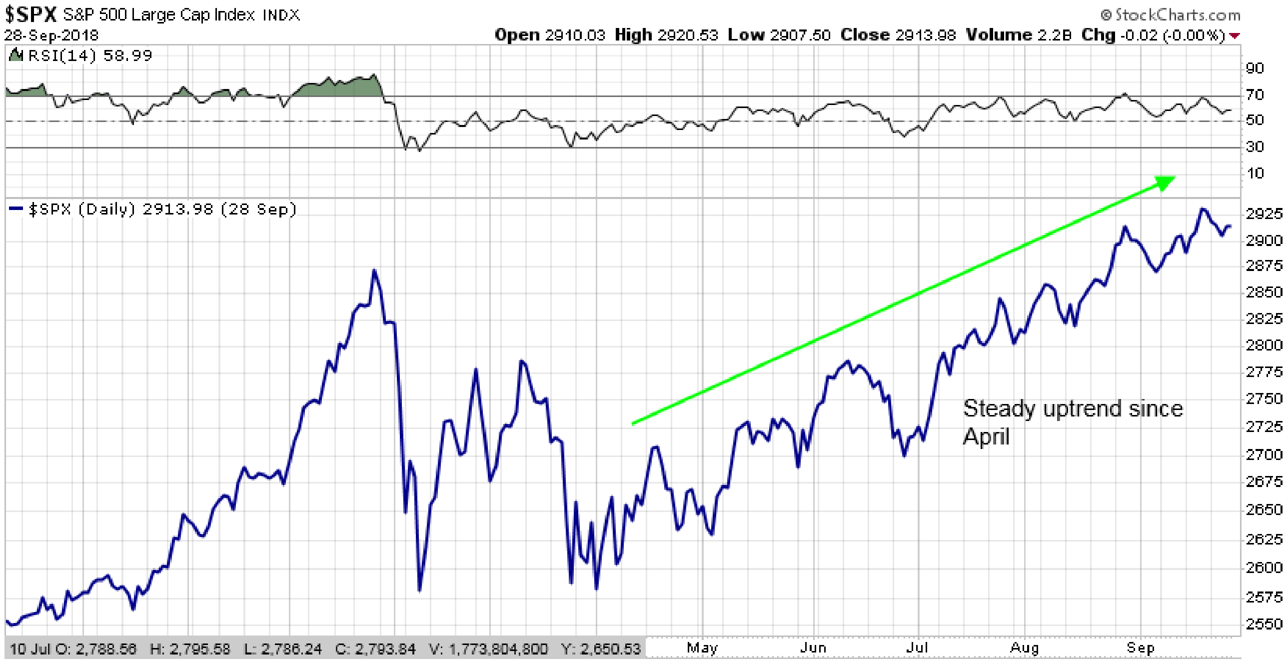
- ***Charlie Munger***

Your Index Report

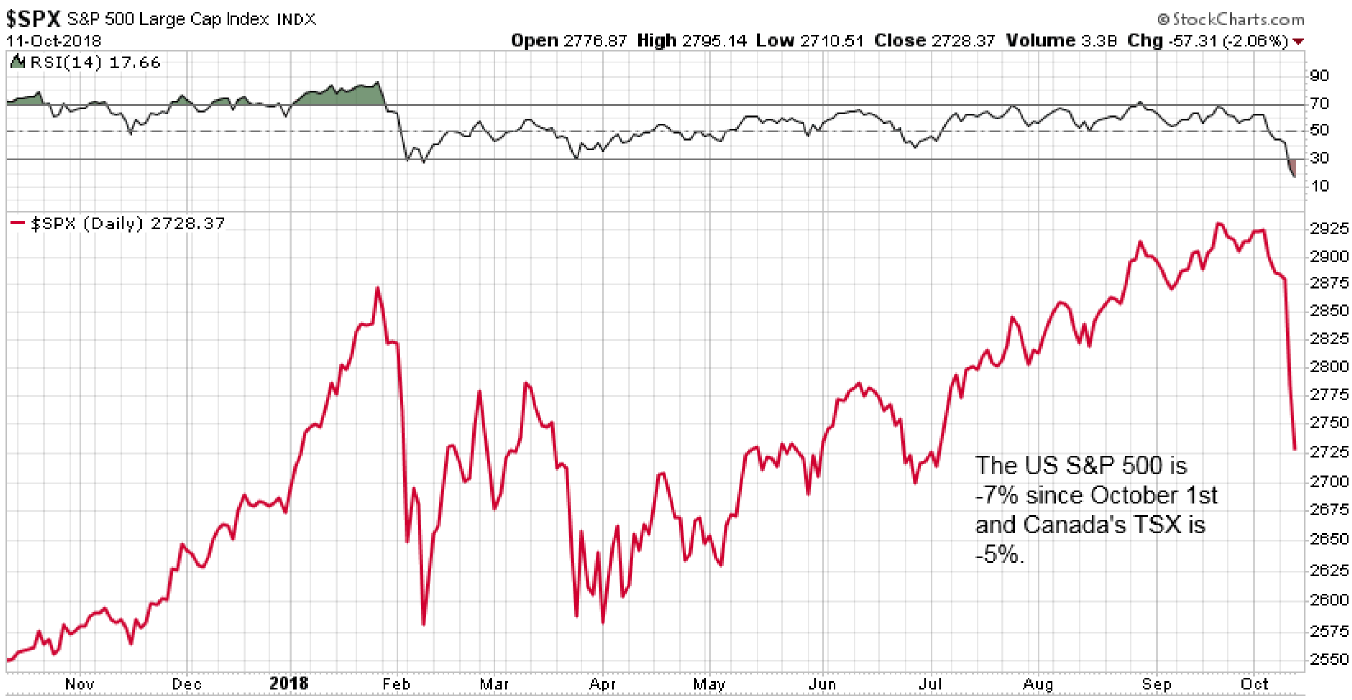
	Current	Last Week	Year-to-Date
Dow Jones Ind. Avg.	25,052	- 5.91%	+ 1.35%
S&P 500	2,728	- 5.97%	+ 2.05% (+5.69% in $CDN)
TSX	15,317	- 4.31%	- 5.50%

Red October

It was just two weeks ago when we wrote that we were in a ***steady as she goes*** market. And why not? Conditions had been exceptionally steady since April. The economy was humming along, and our new trade deal – USMCA – had just been passed:



Now, just two weeks later, we find ourselves in a very stiff squall. Not a storm, but definitely uncomfortable conditions:



The two poorest months of the year to be investors are September and October. September was relatively benign this year, but October has been anything but benign. Perhaps the market was saving up from September and gave us a double whammy in October.

The first question to be asked is “what happened” and the second is “what do we need to do about it.”

What Happened

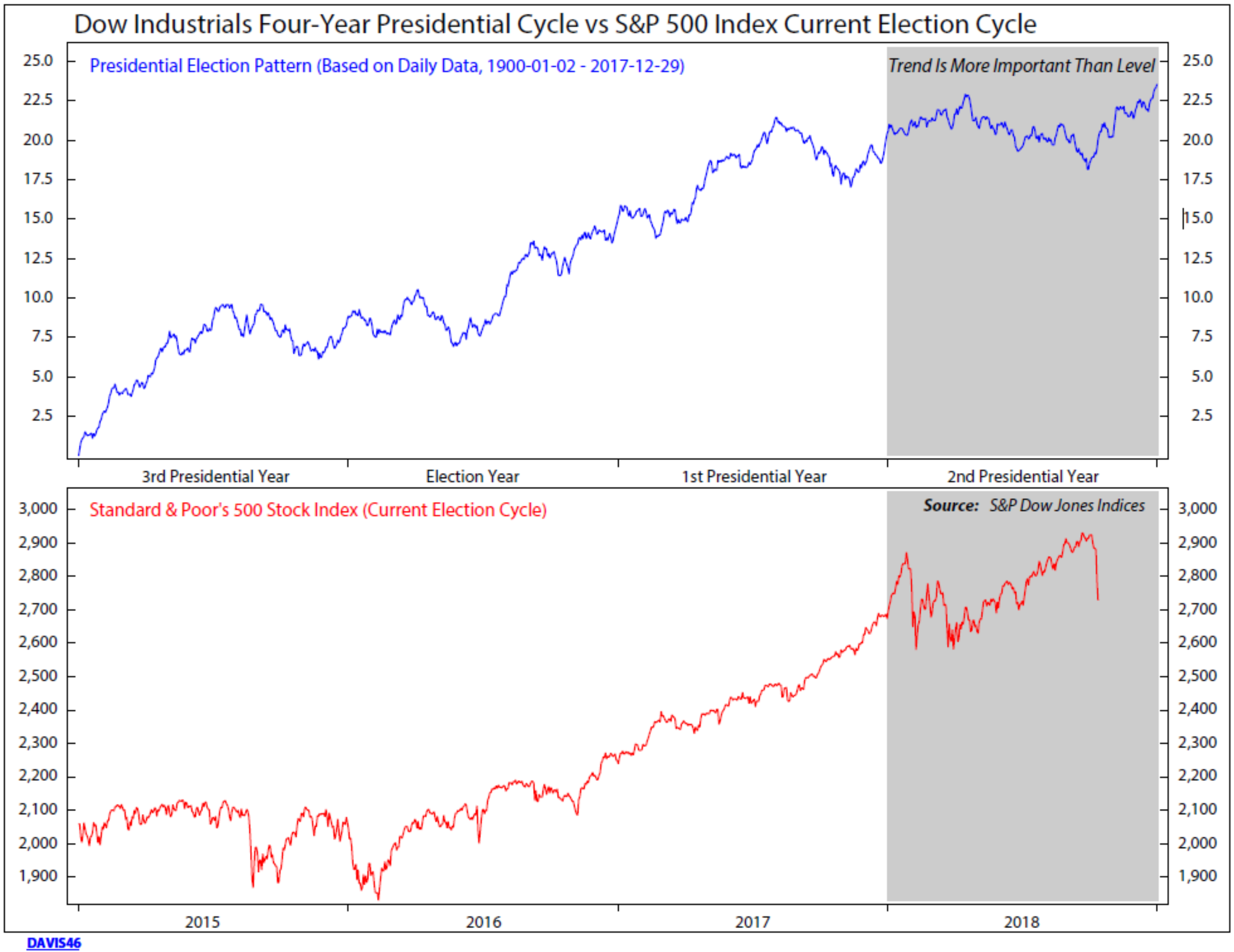
- While stock markets have delivered decent performance in North America, they have been poor just about everywhere else. If you don’t own US stocks this year, you haven’t made any money.

- The US Federal Reserve is intent on hiking interest rates, something that serves to choke off growth. They raised rates to 2.25% in September and are very likely to move to 2.5% in December.

- A new round of American tariffs on Chinese goods, Argentina and Pakistan begging for International Monetary Fund bailouts, and rising oil prices sent emerging markets into a tailspin.

- More companies are guiding analysts to lower profits in the quarter ahead. Companies in the automotive and housing sectors are saying materials, such as wood and steel, have forced costs up even as they struggle with rising wages. This means the stock market has to adjust to lower profits. This generally means lower stock prices.

- The US mid-term elections are also a cause for concern. Any time there is the potential for a change in power – and possibly gridlock if the Democrats control the House while the Republicans control the Senate – there is uncertainty. As we have shown in previous letters, we are in the 2nd year of the US presidential cycle. This is typically the worst year for stocks of the four year term, with the lows usually hitting right about now, before the vote:



What To Do

The International Monetary Fund in July said they expected world growth to average 3.9% in the year ahead. They lowered that to 3.7% the other day.

While the direction may be worrying, 3.7% is still very healthy growth for the world at large. Our expectation is that this decline in the markets is an adjustment to this slightly lower growth, as well as to higher interest rates. As long as the economy is growing at the same rate as interest rates (it is), then stocks can do fine.

Back to September and October again for a moment. If these are typically the worst months to be an investor, could they also be the best two months to begin as an investor? As it turns out, the two best months of the year to initiate new purchases are…September and October. Why? These weak months are followed by November, December, and January - three of the strongest months of the year for stocks.

Since 1950, there have been 26 years when October was a down month. In 19 of those years, you would have finished the year higher if you had bought. In 23 of those years, you were back in the black if you held for a full year (source: Stock Trader's Almanac).

Also, as the graph above shows, US markets typically pick up after the elections are decided, one way or another. The rally into year-end can be very powerful.

The Bottom Line

Stocks are oversold and fear is high. These are generally good conditions to invest in quality companies and fund managers. Bull markets don't end when the economy is strong with the news full of fear. They end when investors are cheerful enough to ignore weaker data. Stocks can swing wildly with little reason, but markets rarely crash when they hit all-time highs like they did just weeks ago.

While we are not happy with the performance of stocks this year, we know that more fortunes have been lost trying to avoid market declines than fortunes preserved. We are picking through stocks we like and adding judiciously.

Groups we are watching include:

Technology – Just about every technology company has done well this year. Now, they are being winnowed out. Technology remains one of the fastest-growing parts of the economy, and money will return to the leaders.

Oil – As discussed in previous weeks, oil supplies are tight worldwide. Canadian companies are suffering terribly from too much supply and no way to get it to market, but this should start easing by year-end through more rail capacity and the re-opening of US refineries.

The largest project in Canadian history – an LNG export terminal in Kitimat - was just approved. A number of Canadian producers and pipeline companies will benefit once this is built. Most jumped on the news, then fell back. We will be watching all of them.

Gold – Beaten down all year, gold jumped sharply during the downturn. Inflation is simmering, something gold likes.

Utilities – This group has not done well this year. If this recent correction is a harbinger of a recession 12 months out, then utilities should begin outperforming.

Thank you for your referrals this month! They are always handled with great care and discretion.

http://www.dividendvaluepartners.com

We thank you for your business and your referrals and we hope you find our site user friendly and informative. We would welcome your comments.

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Prices shown are as of close October 11th, 2018.