

A Volatile Start to 2019 – 01/07/2019

By Peter Goodall, CFA, FRM

We started 2019 with a rollercoaster in the stock market. The S&P ended the week up 1.90% while the MSCI World Index gained 1.81% in the shortened trading week. Emerging markets were up 1.15%.

Apple Cuts Guidance

Apple cut its revenues forecast for the first time in 16 years as the Chinese market slowed and demand for the iPhone dropped off. There may be a bit more going on here. Apple products have been a status symbol over the past decade. Part of this was well deserved. Apple was one of the first companies to implement a touch screen display and helped innovate the \$0.99 song (compared to buying a collection on a CD). Their innovation had allowed them to charge a premium for their phones. At this phase in development, the company has innovated less. The Apple Watch and various minor changes to the phone and tablet space are not providing the same levels of growth for the company.

Apples decision to push off 5G integration makes sense for the US markets. The infrastructure is still being developed state side. Internationally, this strategy places Apple at a disadvantage. For those looking to replace their phones, a 5G ready device should be more desirable as it can operate at 10x the speed of a 4G network. The average life of a cell phone is a little over 2 years. Why would someone buy a phone that costs more and is 1/10th the speed of a generic brand? Apple is aiming to transition into a more services driven brand though it is unclear what that will look like.

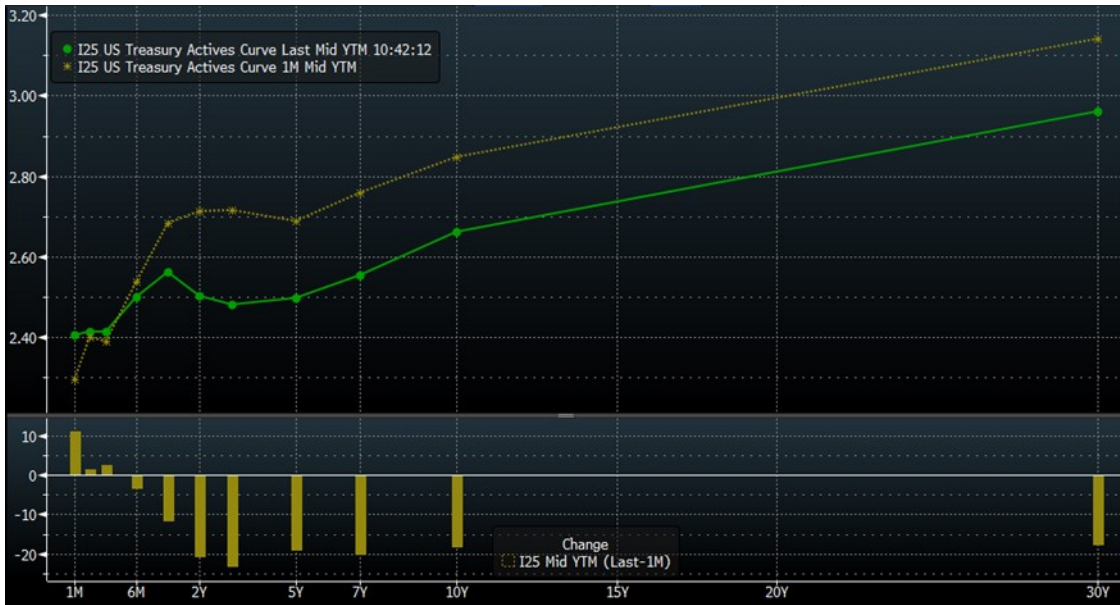
Broader Economic Indicators

Most economic indicators missed their estimates last week. Canada was a bright spot, showing better than expected employment/unemployment figures. The UK, missed 3 out of 4. The US missed on 4 out of 6 indicators. The exception for the US was a really strong beat on change in Nonfarm payrolls (312k vs a rather rosy 184k expectations). This drove the Friday rally that brought the index back into the green for the week.

The tight jobs market is squeezing some employers who are struggling to find US workers willing to take on temporary, low paying, labor intensive work. NPR reported the visa application system needed to be taken down due to the high volume of applications from US employers.

The US Treasury Curve

Credit markets appear to be less enthusiastic about the long-term US prospects as the 7-year rate has joined the 2-, 3- and 5-year rates in inversion. Historically, when the 10-year drops below the 2-year rate, we have seen a recession occur within the next 2 years.



Conclusion

We are in the longest recovery in US economic history so we are in somewhat uncharted territory. The rally this year is probably just a correction from the overly pessimistic last 3 months of 2018. However, I would caution our readers to remember that we are still in the late cycle. Economists are expecting a recession in 2020. We are still facing the same challenges (e.g., rising interest rates squeezing profitability as debt is rolled over the next 2 years, a potential hard Brexit, slowing Chinese consumption). Long term investors should be cognizant of the risks.

On the plus side, an overly pessimistic 4Q18 and strong retail earnings over the holidays should provide a bit of a boost to the markets in the new year. If we can get past some of the bigger short-term risks (e.g., Brexit), we have the potential to end the year in the green.

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Stock Market Performance

	1/7/19	W-o-W	M-o-M	Y-o-Y
DJIA	23,587	1.1%	-3.3%	-6.8%
S&P 500	2,547	1.6%	-3.3%	-7.1%
MSCI World	1,904	1.1%	-3.1%	-11.7%
S&P/TSX	14,440	0.8%	-2.4%	-11.7%
BSX	1,980	1.1%	-7.8%	-9.0%
FTSE100	6,809	1.2%	0.5%	-11.9%
DAX	10,737	1.7%	-0.5%	-19.4%
CAC	4,713	-0.4%	-2.1%	-13.9%
Nikkei	20,039	0.1%	-7.6%	-15.5%
Hang Seng	25,836	0.0%	-0.9%	-16.2%
Shanghai	2,533	1.6%	-2.8%	-25.3%

Key Rates and Prices

Currencies	1/7/19	Month ago	Year ago
EUR	\$1.15	\$1.14	\$1.20
GBP	\$1.28	\$1.27	\$1.36
JPY	¥108.54	¥112.69	¥113.05
CAD	\$0.75	\$0.75	\$0.81
CHF	\$1.02	\$1.01	\$1.03
AUD	\$0.71	\$0.72	\$0.79

Fixed Income

3M LIBOR	2.80	2.77	1.70
3M Treasury Bill	2.42	2.39	1.40
2Yr Treasury Note	2.52	2.71	1.96
10Yr Treasury Note	2.68	2.85	2.48
Fed Funds Rate	2.50	2.25	1.50

Commodities

Gold/oz.	1,287.30	1,248.35	1,319.35
Silver/oz.	15.67	14.62	17.13
Copper/lb.	2.68	2.79	3.23
Oil	49.24	52.61	61.44

Global Economic Calendar (January 7th — January 11th)

- Mon:** Factory Orders MoM (GE)
- Tues:** Industrial Production YoY (BZ)
- Wed:** Bank of Canada Rate Decision (CA); MBA Mortgage Applications (US)
- Thurs:** Jobless Claims (US); BoP Current Account Balance (JN)
- Fri:** CPI MoM (US); IBGE Inflation IPCA YoY (BZ); Industrial Productions (UK)

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