

Q3 2017 Commentary

During the third quarter of 2017, news headlines were dominated by geopolitical tensions, social unrest, terrorism and severe hurricanes, but the stock market's ability to keep rallying after these various crises show how little it takes to keep the bull market going!

U.S. stocks started the fourth quarter on a strong note, with all three major indexes hitting record high closes. Underlying this is a combination of positive business fundamentals, strong economic data and corporate earnings. Economic data continued to show this Goldilocks-type situation, which the market tends to like, ie., "It's not too hot, it's not too cold."

While we saw pockets of volatility in the markets, mainly in reaction to the events in North Korea, the markets have figured out that geopolitical events are fairly short-lived.

Stocks are where they are because of recent earnings growth and expected earnings growth. The performance reflects a "risk on" sentiment as investors view positively the prospects for tax reform and improving global economic conditions.

Late summer, the Fed announced its plan to initiate "balance sheet normalization" in October. The process would gradually unwind the Fed's extraordinary accumulation of Treasury and mortgage-backed securities. Leading up to the event, some analysts were concerned about a repeat of the "Taper Tantrum" in 2013, which triggered a brief selloff in stocks. This time, though, markets remained stable; investors widely anticipated the announcement and, perhaps, viewed the decision as confirmation that the economy was sufficiently healthy to withstand the withdrawal of monetary stimulus.

Recent signs of tightening labor markets, though, suggest that inflation may be on the rise. Moreover, strengthening business confidence could deliver wage growth that ultimately drives prices higher. The Fed also noted that recent hurricane activity will impact third quarter economic data, but past experience suggests that the storms are unlikely to materially alter the course of the national economy over the medium term.

It should be an interesting Q4 coming ahead!

Several factors, including low interest rates, low inflation, high employment levels, and moderate economic growth, support the extended bull market. While it is too early to speculate, heightened discussions about the likelihood of tax reform suggest the possibility for a significant economic boost. And, renewed efforts at deregulation are

lowering business operating costs and providing growth opportunities. Several factors, including an improving economic outlook, the disciplined approach shown by many companies in pursuing growth strategies, and investment-friendly monetary policies across the globe, support a more optimistic view of the market.

As an earnings-driven investor, I recognize that an interest rate rise in 2017 could be problematic to maintaining the rate of expansion in stock prices and economic forecasts. Industrial activity might have to work overtime to keep pace with analysts and investor's expectations for this year's figures. As the spigot of "free money" closes, so too will the ability to manufacture profits at any cost.

As always, we will remain focused on long-term!