The Bull Market in Everything:

Investment positioning for times that can’t last forever.

EXECUTIVE SUMMARY

glc asset management

2019 Mid-Year Capital Market Outlook

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Data as of June 21, 2019 unless otherwise stated.

The Bull Market in Everything

Investment positioning for times that can't last forever

The global economy has been slowing for a year (see exhibit 1.1 – Global GDP Growth) marking the third global slowdown of the past 10 years. Trade frictions have exacerbated the slowdown and remain an unpredictable cloud dimming future growth expectations. This makes the question of whether we're closer to the end or the beginning of the current slowdown particularly challenging. **We believe the global economy has enough positive momentum to exit the current global slowdown within the next two to four quarters.** When we dig deep and weigh out the evidence, we find ourselves tilting in favour of growth re-emerging late in 2019 or early in 2020. Our view is aided by economic metrics that signal future demand expectations, such as the Chinese credit cycle and U.S. inventory cycle turning positive, along with our expectation for a synchronized easing of financial conditions globally. The old adage, "Don't fight the Fed" has expanded to become "Don't fight the Fed, PBoC, ECB, BoE, BoJ, RBA, BoC, RBI…"[1] Each of these central banks has already loosened monetary policy (or are poised to), greenlighted by slowing economic growth, and despite historically low unemployment in most regions, a persistent lack of inflation.

Even if economic data continues to weaken in the near term, that does not preclude stocks from beginning a march higher in anticipation of better days ahead – a scenario we've seen repeat itself many times. However, at this juncture, equities are pricing in some of the more positive outcomes, despite great uncertainty remaining with the outcome of the U.S. trade agenda and the magnitude and timing of central bank easing interventions. **What's causing us concern are the sharp advances in equities, commodities and bonds. The 'bull market in everything' scenario is not one that can last forever.**

Our base-case is one of simmering China-U.S. tensions that spurs action from U.S. and Chinese monetary and fiscal authorities to support growth and equity valuations. Any escalation that results in actual implementation of trade barriers will need to be negatively factored in to an already tepid earnings growth outlook. This presents enough risk to warrant some defensive protection and diversification within investment portfolios.

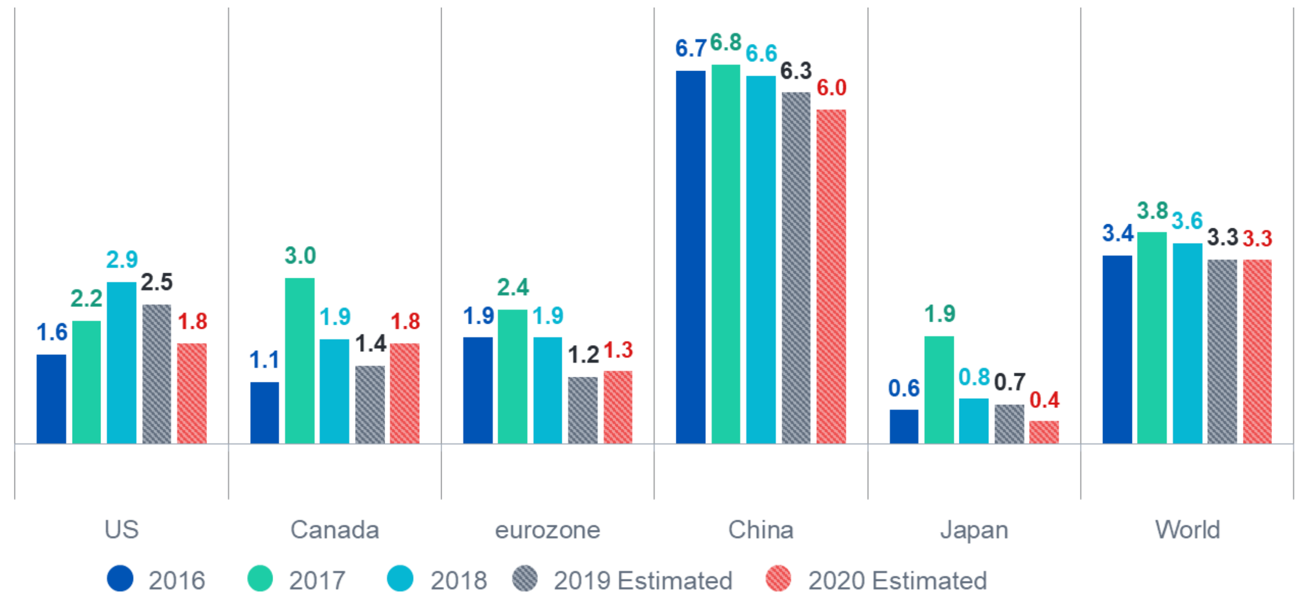
We think a lot of the fear around the economy is already reflected in the substantial decline in bond yields witnessed thus far in 2019. Should stocks correct, fixed income is able to offer further gains. However, over our forecast horizon, we don't think bonds offer much further upside, unless a slowdown or recession scenario unfolds (not our base-case scenario).

We see a balanced and diversified asset mix that includes both equities and fixed income as most appropriate to navigate through our forecast horizon. **Our 2019 Mid-Year Capital Market Outlook highlights adjusted weightings within equities and fixed income to reflect our view of relative opportunities.**

Publish date: June 21, 2019.

1.1 | Global GDP Growth

Global GDP growth remains solid, but peaking, reminiscent of 2016



Source: Bloomberg | June 21, 2019

Bottom line: We're maintaining our asset allocation at neutral, aligned with one's own risk tolerance – a balance between exposure to participate in equity market growth without over-reaching for risk.

- Our 2019 Mid-Year Capital Market Outlook generally calls for single-digit equity price gains between now and the end of the year. Bouts of trade-, political- and geopolitical-related volatility may be severe enough to present buying opportunities for those comfortable with a more pro-risk stance.
- Within equities, we recommend broad, diversified geographic and sector allocations – with a slight equity overweight toward Canada. We recommend neutral exposure to U.S. and EAFE equities and recommend a slight-underweight in Emerging Markets.
- For fixed-income investors, we recommend a neutral weight to sovereign bonds, offset by an overweight to investment-grade corporate bonds and an underweight in high-yield bonds. Overall, we forecast a 0.5% total fixed-income return for the back half of 2019. The main attraction in fixed income is, once again, as a risk-mitigation tool (a role it has repeatedly played well, most recently in Q4-2018 and May of 2019).

[1]Selected Global Central Banks: Fed = U.S. Federal Reserve, PBoC = People's Bank of China, ECB = European Central Bank, BoE = Bank of England, BoJ = Bank of Japan, RBA = Reserve Bank of Australia, BoC = Bank of Canada and RBI = Reserve Bank of India.

GLC Outlook Summary, Mid-Year 2019

Change in view[1] | Under | Neutral | Over

Fixed income =

Bond yields have declined to such an extent that incremental returns moving forward will be modest. Fixed income remains attractive as a risk-mitigation tool. We recommend a neutral weight. Our base-case scenario calls for small enough increases in bond yields that we forecast a further total bond market return of 0.5% for the remainder of 2019.

Government bonds ▼

Government bonds are attractive for their superior risk-mitigation qualities. However, sovereign bond yields have seen a precipitous decline in 2019. Barring a recession (not our base-case scenario), we don't see room for yields to move materially lower from current levels and therefore see minimal return potential.

Investment grade corporate bonds ▲

We see investment-grade corporate bonds as most attractive given their mix of yield pickup and modest safety. We expect them to outperform government bonds. On an absolute basis, investment-grade corporate bond spreads remain narrow, moderating any significant price appreciation from here. We anticipate periods of volatility in spreads, but don't expect the length or the severity of these to be significant enough to negate the benefits of the higher running yield.

High-yield corporate bonds =

High-yield spreads remain low and narrow. When coupled with a lack of risk-mitigation characteristics, we see the risk/reward trade-off in high-yield bonds as unattractive.

Equity =

We believe the global economy has enough momentum to exit the current global slowdown within the next six to 12 months. Trade frictions have weakened the outlook, but globally synchronized stimulative central bank policies are supportive of risk assets keeping our outlook constructive. On a risk-adjusted basis, a neutral stance is appropriate.

Canada =

Canada is a favoured market due to its leverage to global growth and attractive valuations. Sentiment is improving. Steady or improving global economic growth, coupled with a reasonable Canadian economic backdrop, supports mid-single digit earnings growth. Add in the solid dividend yield and we consider Canadian equities to offer the best risk/reward outlook.

U.S. ▼

U.S. equities are home to some of the best secular growth opportunities. However, given current earnings expectations, we see the S&P 500 as fully valued at the 3,000 level, leading us to pull back our positioning to neutral. U.S. equities sit at the epicenter of trade and policy uncertainty, so brace for volatility in the near term.

International =

We hold a neutral view toward EAFE equities. The group offers reasonable valuations and decent earnings growth potential, along with a high dividend yield. However, Europe and Japan have longer-term structural issues, and heavily export-oriented EAFE corporations may face near-term trade challenges.

Emerging markets (EM) ▲

EM equities are most sensitive to trade and policy uncertainty, making their risk/reward trade-off stark. With steady or improving global economic growth, we expect EM equities to outperform. EM equities remain a riskier, high-beta asset class most appropriate for those with higher risk tolerance and longer time horizons.

As at June 2019. [1]From December 2018.

Publish date: June 21, 2019.

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