BNN BLOOMBERG MARKET CALL

***e*Research Corporation** is pleased to provide two excerpts from Friday's BNN Bloomberg Market Call Newsletter.

Set out below are the respective Market Outlook commentaries from two leading investment analysts, plus Links to their respective 45-minute video interviews.

MARKET OUTLOOK

Mike Philbrick, President at ReSolve Asset Management
Focus: Exchange Traded Funds

October marked the second major trend reversal this year for risk assets, exacerbated by a profound surge in volatility. Virtually all global stock indexes plummeted in concert alongside oil-related names. The effect was a cascade down that offered little time for adjustment for all but the shortest trend signals.

A continuation of currency trends offered some ballast, with a persistent surge in the U.S. dollar across most major crosses. Results for longs and shorts in softs, grains, and metals were mixed.

Perhaps the most interesting dynamic that played out in October was that rate instruments failed to play any role in risk management. Despite cascading losses in equity markets, government bond futures whistled past the graveyard, with nearly flat returns on the month.

Of course, we don't expect bonds to come to the rescue every time that stocks dump. But their muted behaviour reflects the potential for a major shift in correlation dynamics between stocks and bonds. From a macroeconomic perspective, this should play out when markets become concerned about the potential for an inflation shock.

In the context of these dynamics, it is likely that the current tumult is related to market microstructure rather than to any true shift in economic expectations along the axes of growth or inflation. Had there been a genuine shift in inflation expectations, we would have expected out-performance in inflation-linked assets. Instead, inflation-sensitive commodities dropped precipitously and Treasure inflation protected securities (TIPs) barely registered a pulse.

This has caused a meaningful increase in exposure to safe assets like bonds and safe-haven currencies like the U.S. dollar accompanied by a steep reduction in risk assets like stocks in our portfolios.

This is risk management at its best. Rather than holding static allocations of asset classes and allowing risk to run you over, we suggest that it is better to target your risk level and let asset classes fluctuate.

It is interesting that bonds have not acted as a solid source of returns in the current draw-down in equities. This could be because of the massive amount of issuance that must be completed over the next year; this draws money away from risk assets likes stocks and drives yields higher, further attracting capital away from risk assets. This is a more negative self-reinforcing cycle.

VIDEO: Mike Philbrick's 45-Minute Video Interview **<CTRL-CLICK>** **HERE**

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MARKET OUTLOOK

Jon Vialoux, Research Analyst at CastleMoore Inc., Focus: Market Technicals

Storm clouds are moving in. Following the volatile month of October, it is becoming increasingly apparent that the market is reacting to the threats building in the economy. Of course the tariff war, the impact of rising interest rates, and a strong U.S. dollar are well telegraphed, but the market was resilient to these headlines through the summer when key benchmarks in the U.S.A. achieved their best summer return in years. Now the economic data is reflecting the headwinds and deteriorating as future growth prospects become doubtful without some resolution to these headline risks.

Weakening home sales was an area of concern highlighted during my last appearance here and for good reason: the weakness in this area of the economy has preceded every major equity and economic downturn since the 1950s. The inventory of existing homes in the USA is higher by 29 per cent year-to-date, more than two times the growth that is average by this point in the year. The inventory overhang threatens to weigh on the value of the largest asset of most Americans, which would thereby weigh on consumer sentiment.

This inventory overhang is not isolated to housing. Manufacturing activity has been booming in both Canada and the USA for the past couple of years, but inventory levels that are growing well above average threaten to weigh on future activity. Total inventories of manufactured goods in Canada have climbed 10.8 per cent through the end of September, well ahead of the 3.4 per cent average increase by this point in the year. In the USA, it is far less pronounced, but still elevated, with a year-to-date increase of 5.9 per cent versus a 4.3 per cent average rise through the end of September. Should demand fail to catch up to supply, future manufacturing activity is at risk.

Other factors that are presenting a warning pertaining to the health of the global economy include the over 30 per cent plunge in the Baltic Dry Index in November, the bear market decline in the price of oil, a rare October decline in small truck sales in the USA, and evidence of below-average employee confidence in the United States. Altogether, caution in equity markets would be expected.

Between now and the end of the year, tendencies for stocks are overwhelmingly positive; a tradeable low to retrace some of the October's loss remains a good possibility. Over the past 50 years, the S&P 500 Index has gained an average of 1.5 per cent in the month of December, with 72 per cent of periods showing a positive result. This is the best return and frequency of success out of any month on the calendar. But beyond this near-term reprieve in selling pressures, the strength of the broader market is questionable.

VIDEO: Jon Vialoux's 45-Minute Video Interview **<CTRL-CLICK>** **HERE**

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Bob Weir, CFA, Director of Research

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