Economic Commentary

Third Quarter 2019

U.S Fed Cuts Twice During Q2

The U.S. Federal Reserve cut interest rates at both of its meetings during the quarter. However, prospects for future moves were left unclear following the September rate cut. Economic growth has surprised on the upside and continues to be led by the consumer sector. Household spending has been rising steadily and the housing market has also exhibited strength as declining interest rates have boosted demand. The manufacturing and business investment sectors are still being held back due to on-going uncertainty surrounding the U.S./China trade talks, along with weakening global demand. The Institute for Supply Management (ISM) manufacturing index declined to its lowest level in a decade in September. The larger services component, however, had maintained solid growth levels throughout the year, before retreating in September to the lowest level in three years.

Bank of Canada Remains on Hold

Canadian economic growth surged during the second quarter, led by a strong export sector. This allowed the Bank of Canada to remain on the sidelines with regard to interest rate moves. However, weak demand from the consumer sector, in addition to a decline in investment, are areas of concern going forward. Despite a solid labour market, expectations are for growth levels to slow in the second half of the year. July GDP was flat, bringing down the year-over-year GDP rate to 1.3% from 1.5% in June. As is the case in the U.S., lower interest rates are providing a boost to the housing sector, however, trade concerns and weaker global growth will dampen near-term growth prospects.

Bond Buying Resumes at ECB

The European Central Bank introduced a new stimulus package at its September meeting as a result of protracted weakness in the eurozone economy. The risks surrounding the growth outlook remain tilted to the downside, due primarily to the slowdown in global trade. Inflation is also below targeted levels at around 1% and may decline further over the near-term before potentially rising into the New Year.
As a result, the ECB announced its biggest package of interest rate cuts and economic stimulus in three years. The ECB cut interest rates further into negative territory and re-launched its bond-buying program. They committed to buying 20 billion euros a month in bonds and other financial assets starting in November and will continue to do so for as long as necessary.

Equity and Bond Market Divergence Continues

North American equity markets remain at lofty levels, generating minimal returns on the quarter. The on-going trade war between the U.S. and China remains the wild card for financial markets. The further that talks are pushed down the road the greater the negative impact that it will have on the already depressed manufacturing, investment and export sectors.
Bond yields continued to decline , fueled by the actions taken by the Fed and the ECB. Despite the fact that bond yields in Canada and the U.S. are near historic lows, the massive amount of negative yielding sovereign debt in Europe has made North American bond yields look relatively attractive.

Key Metrics

Indicator	Value	Chg Q3	Chg 1Y
S&P/TSX Composite	16,658.63	2.5%	7.0%
S&P 500 (USD)	2,976.74	1.7%	4.2%
MSCI EAFE (USD)	1,889.36	-1.0%	-0.8%
USD/CAD	$ 0.76	-1.1%	-2.5%
WTI Crude ($/bl))	$ 54.07	-7.5%	-26.2%
GoC 10Y Bond	1.36%	-11 bps	-107 bps
GoC Deposit Rate	1.75%	0 bps	25 bps
Cdn CPI YoY	1.9%	-0.1%	-0.3%
US 10Y Treasury	1.67%	-34 bps	-140 bps
Fed Funds Rate	2.00%	-50 bps	-25 bps
USD CPI YoY	1.7%	0.1%	-0.6%

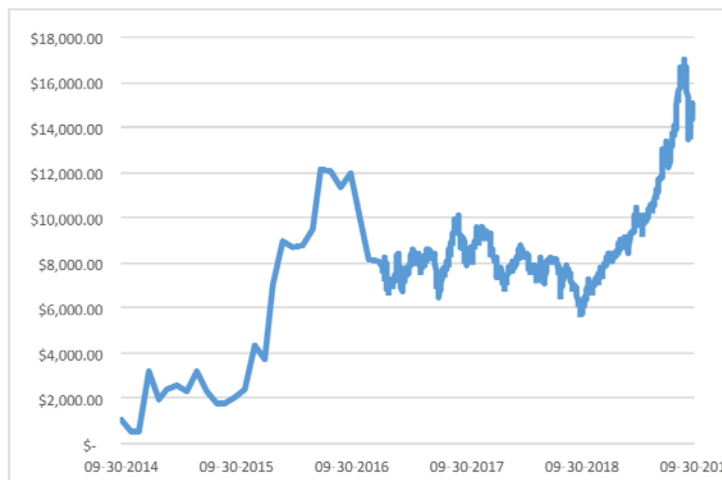
Top Themes

U.S. Fed cuts interest rates twice

ECB cuts rates + re-launches bond buying program

Bank of Canada holds the line

Top Chart: Bloomberg Barclays Global Agg Negative Yielding Debt Market Value USD (billions)



Source: Bloomberg, Lincluden