

Weekly Markets Commentary

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David Joy

Chief Market Strategist,
Ameriprise Financial

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Stocks Search for Direction Amid Mixed Economic News

The search for direction in U.S. stocks remains elusive. For more than three months, the S&P 500 has drifted, unable to see enough progress on trade to mount a rally, but finding enough support from easing monetary policy and the strong consumer to prevent a serious downturn. The index closed last week at 2,986, up 0.5 percent, only slightly more than one percent below its all-time high. But as far back as July 3, it was trading at 2,996. Since then, it has traded in a range between 3,225, its all-time high, and a low of 2,840 on August 5, hardly dramatic stuff.

But that headline price action belies the underlying volatility that was better captured by the VIX. At the beginning of the period on July 3, the VIX traded at 12.6. But on August 5, it doubled to a high of 24.6, the same day the S&P hit 2,840. Throughout the period, the VIX averaged 16.2, close to its long-term average, but with a noticeably wide range around that average.

Trade hopes fall through

Investors have had a lot to digest in the past three months. The Federal Reserve has lowered rates twice, and the European Central Bank has restarted its own stimulus program. All the while, the global economy has slowed. And there has been a lot of talk, but little progress, on trade. But that has been enough to keep investors at the table, afraid of missing out on what could be a powerful rally if a meaningful deal is struck. Unfortunately, at least so far, they have been repeatedly left at the altar.

For a while last week, it looked like we were witnessing simultaneous breakthroughs on both U.S.-China trade and Brexit. But once again, at least so far, it has proven to be a triumph of hope over experience. As it turns out, the Chinese had very different ideas from President Trump about the details of the so-called phase one agreement. And Prime Minister Johnson has run into the political realities of getting the newly agreed deal with the European Union through Parliament. In the meantime, the tariffs remain in place, along with the debilitating uncertainty for business.

A mixed bag for third quarter earnings

While all this was happening, third quarter earnings season was in full swing. According to FactSet, about 15 percent of the S&P 500 has reported so far, with the blended earning growth rate for the quarter projected to be -4.7 percent, the same projection as last week.¹ Some better-than-anticipated results in the healthcare and financials sectors were offset by worse-than-expected results in

energy. This week will see up to 25 percent of the index report. Among the notables are Amazon, Microsoft, McDonald's, and Caterpillar.

Weak economic news out of China, the U.S.

Last week's economic data provided more evidence of the headwind created by trade uncertainty. China reported year-over-year growth of just 6.0 percent, its slowest pace in 27 years. It is widely expected to report a rate below 6.0 percent in the fourth quarter. In the U.S., manufacturing production and retail sales were decidedly soft, and leading indicators fell for the second straight month. That weakness was offset to some extent by a strong home builders report. This week will see durable goods orders and new and existing home sales.

But the slowing outlook for the global economy was highlighted by the International Monetary Fund's (IMF) lowered forecast for global gross domestic product (GDP), for both 2019 and 2020, now projected to total 3.0 and 3.4 percent respectively. The IMF estimated the drag from trade will trim growth by 0.8 percent by 2020, partially offset by a 0.5 percent boost from monetary stimulus.

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S&P 500 Index is an unmanaged capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Chicago Board Options Exchange (CBOE) Volatility Index (VIX) is a widely used measure of market risk. It shows the market's expectation of 30-day volatility. The VIX is constructed using the implied volatilities of a wide range of S&P 500 index options.

Past performance is not a guarantee of future results.

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¹ FactSet, Earnings Insight, October 18, 2019

https://www.factset.com/hubfs/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_101819.pdf