Weekly Trends

PRIVATE CLIENT SOLUTIONS

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September 22, 2017

Q3/17 Earnings Preview

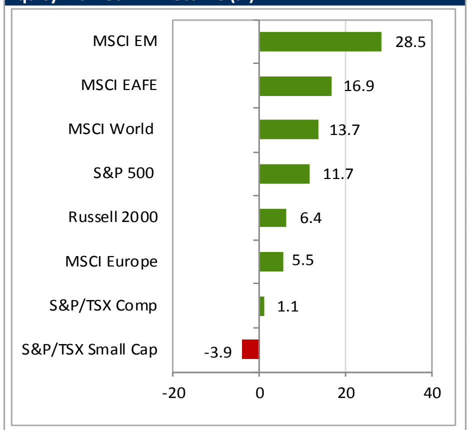
All eyes were on the Fed this week. Ahead of the meeting there were many questions: will the Fed raise rates, will they signal that more rate hikes are in the cards, will they change their median interest rate forecast, will Yellen discuss the future of her role (her term expires in February 2018), and potentially the most impactful, will they announce the beginning of balance sheet normalization?

Well, the Fed didn't disappoint as they did indeed announce they will begin to normalize their balance sheet. This was a historic event as the Fed will be the first central bank to begin unwinding quantitative easing. The initial reaction saw equity markets slump, bond yields rise and safe haven gold slip. Yield sensitive sectors, such as utilities, also came under pressure with the backup in yields. The US dollar index rallied ~0.8% on the news; the USDCAD pair moved a full cent. The Canadian dollar, however, began to weaken earlier in the week on comments from deputy governor Timothy Lane that the Bank of Canada (BoC) "will be paying close attention to how the economy responds to both higher interest rates and the stronger Canadian dollar." These comments were interpreted as a dovish signal and are not too surprising, as historically the BoC often attempts to talk down the loonie when it has moved too far too fast. However, with Fed now lending a helping hand, the BoC will not have to do all the heavy lifting themselves.

As for the particular details of the Fed meeting, officials signaled one more rate hike remains on the table for 2017 and three potential hikes in 2018. Balance sheet normalization will begin in October with the Fed reducing its holdings by US$10 bln per month. The run-off will step up by a gradual and predictable manner to eventually reach US$50 per month. The Fed's long-term normal fed funds rate inched down marginally to 2.75%, but the path to higher rates remained unchanged.

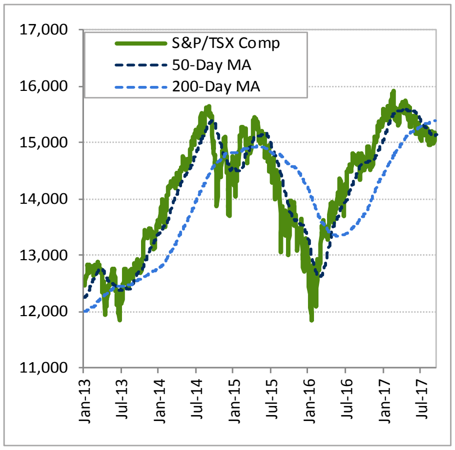
Trimming the long-term fed funds forecast appears to be a routine exercise,

Equity Market YTD Returns (%)



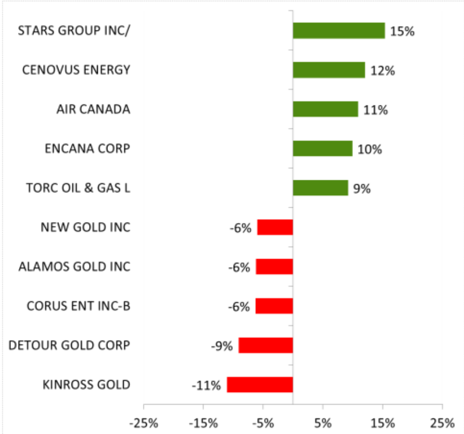
Canadian Sectors	Weight	Recommendation
Consumer Discretionary	5.5	Market weight
Consumer Staples	3.6	Market weight
Energy	20.4	Overweight
Financials	34.1	Overweight
Health Care	0.6	Underweight
Industrials	9.5	Overweight
Technology	3.2	Market weight
Materials	11.6	Market weight
Communications	4.8	Underweight
Utilities	3.8	Market weight
Real Estate	2.9	Market weight

Technical Considerations	Level	Target
S&P/TSX Composite	15,455	16,500



Source: Bloomberg, Raymond James Ltd.
Sectors are based on Bloomberg classifications

S&P/TSX Top 5 Gainers/Laggards*



S&P/TSX Market Internals

Weekly Advance	155	62%
Weekly Decline	93	37%
Advance-Decline	62	
New 52 wk high	9	4%
New 52 wk low	2	1%
No. Stocks Above 50-d	144	57%
No. Stocks Above 200-d	121	48%
Arms Weekly Index	0.63	Neutral
RSI (14-day)	71.4	Overbought
50-DMA	15,144	Uptrend
200-DMA	15,384	Uptrend

Source: Bloomberg, Raymond James Ltd; * 5-day price return

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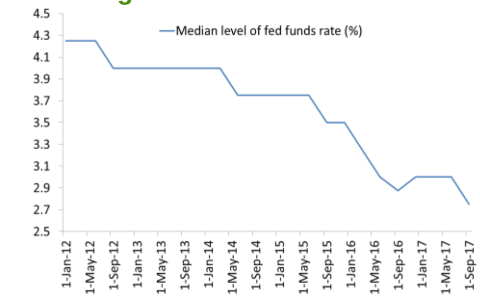
however. Over the last 5 years, the Fed has lowered the forecast by a full 150 bps, an indication that the growth potential of the economy has permanently shifted lower and that rates will be lower for longer.

As we discussed in our September *Insights & Strategies*, we anticipate balance sheet normalization will increase market volatility and the corresponding rise in bond yields suggests equity investors should favour cyclical sectors over defensive sectors. We feel comfortable recommending cyclicals at this point given that the global growth backdrop remains supportive and financial conditions outside of the US remain accommodative. The synchronized upswing in global growth has been a key component underpinning equity returns this year and has helped cushion the risks created by geopolitical tensions. In the latest OECD economic outlook, the organization anticipates the global economy to grow at its fastest pace since 2011. The OECD projects global growth of 3.5% this year and 3.7% in 2018.

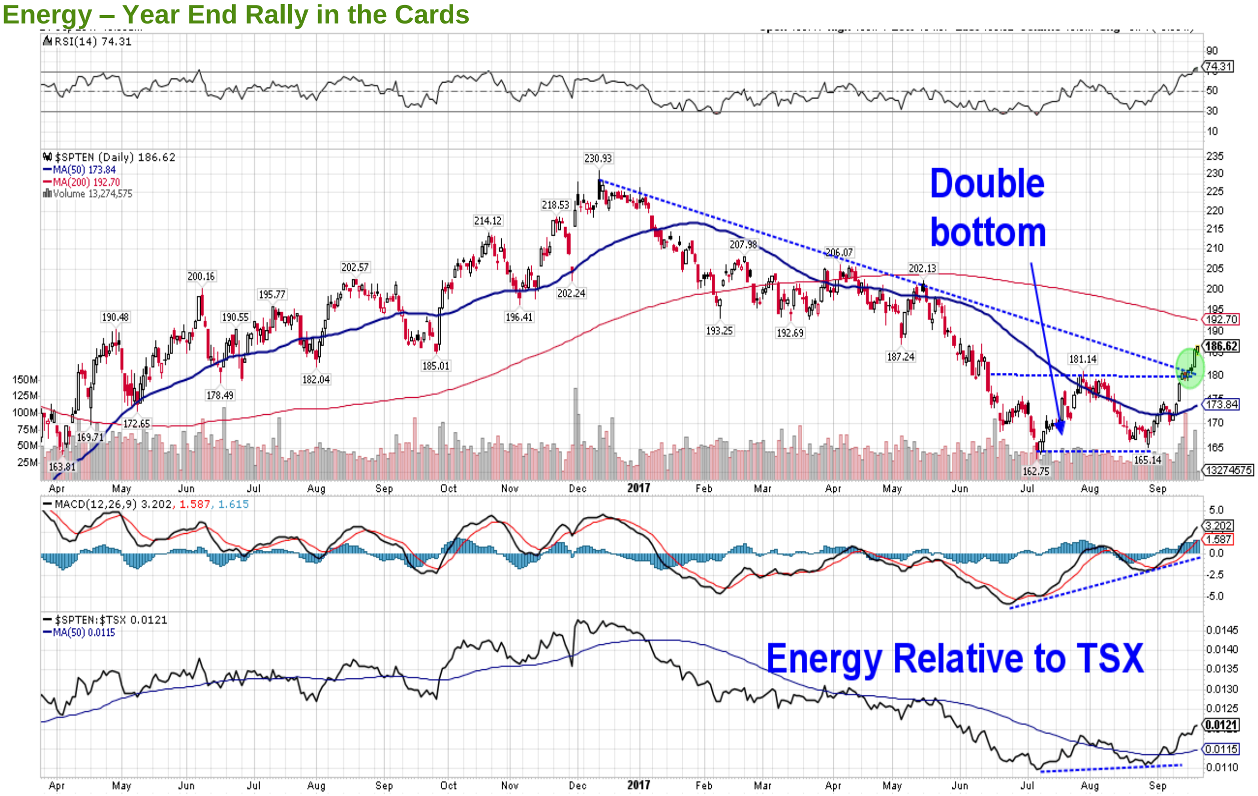
As we highlighted last week, one cyclical sector that we believe looks attractive is the S&P/TSX energy sector given the improved price action in the sector and supportive fundamentals. This week, the sector's price action confirmed a double-bottom pattern with a break above trend line resistance on volume. In addition, the sector is exhibiting strong relative performance compared to the broader S&P/TSX. While the sector is currently overbought, we'd use pullbacks to build on positions with the sector heading into year end.

Fed Long-Term Fed Funds Forecast



Source: Bloomberg, Raymond James Ltd.

Energy – Year End Rally in the Cards



Source: Stockchart.com

US Earnings Preview

US earnings season will unofficially kick off in the third week of October. For Q3 2017, the estimated earnings growth rate for the S&P 500 is 4.5%; however, as per usual the estimated earnings for the quarter has slipped ahead of reporting season. Since June 30, S&P 500 earnings estimates have been revised 2.6% lower. The good news is the percentage decline is smaller than the 5-year average of -3.5% and the 10-year average of -4.3%. The majority of the negative revisions can also be largely blamed on one-time events. Hurricanes Harvey and Irma have had the most negative impact on P&C insurers, chemical makers and airlines. Combined, these three industries account for ~65% of the negative revision to Q3/17 earnings.

As of September 15th, 116 companies in the S&P 500 index have issued EPS guidance for Q3/17 – 73 have issued negative EPS guidance and 43 have issued positive EPS guidance. The percentage of companies issuing negative EPS guidance is 63%, which is below the 5-year average of 75%.

This suggests, excluding the negative impact due to the hurricanes, the underlying earnings trend of the S&P 500 is quite supportive.

The estimated year-over-year sales growth rate for the quarter is 5.2%,unchanged since June 30th.

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