Murray Wealth Group

Third Quarter 2018 Market Commentary

On October 11th, we sent out the following bulletin to our clients. We reiterate our remarks here as they continue to represent our sense of what is going on in the markets and our expectations during these volatile times. In early November, we will provide our usual monthly update, which will contain performance numbers to the end of October. As of final edit of this report at 2 pm Friday Oct 26 the S&P 500 was down 8.7% month to date and the S&P/TSX had lost 7.2%.

"In the wake of this week's market sell-off, we would like to highlight the following excerpts from a Reuters article.

"Worries about the impact of a tightening job market on the prospects for inflation and a surge in bond yields sent investors fleeing equities"

"It was the biggest daily point fall in the Dow since December 2008 during the financial crisis."

"People are starting to really get increasingly uncomfortable with the rapid rise in interest rates that we have seen and the uncertainty of how that is actually going to start to play out relative to competition for stocks,"

Although these excerpts are directly applicable to this week's stock market trade, the Reuters article was published on February 2, 2018.

We like to say we are students of history at Murray Wealth Group. We have seen this price action (rising bond yields cause stocks/bonds to fall) as recently as July and, as noted above, in February 2018. After both of these events, markets recovered to their highs.

Going a bit further back, we witnessed a similar move in yields in 1993/1994, which also caused short-term drops in the market as stocks fell 8% in the first half of 1994. Subsequently, they rebounded as well and were 200% higher in 4 years time.

And finally, history lies in data. Credit Suisse published a Q3 preview slide deck highlighting several strong points.

- *Equity valuations typically strengthen until U.S. 10-year interest rates reach 5%. Currently, they are sitting at 3.15% (up from 2.43% at the start of the year).*
- *Technology and consumer discretionary stocks perform well in periods when interest rates start to move higher. Utilities and consumer staples tend to underperform. This past week's price action has been the opposite.*
- *The 10-year yield is generally seen as a barometer for the economy. If it rises, it is because investors think the economy is strong. Typical recession indicators include falling interest rates, flattening yield curve, consumer credit deterioration, housing market angst, and weakening manufacturing. None of these indicators suggest a recession is imminent.*

Market expectations are strong going into third-quarter earnings with earnings growth forecast to be 20% higher than Q3 2017. As they are revealed over the next two to three weeks and corporate outlooks are formalized we expect more stability. However, several economically sensitive companies have reported underwhelming Q3 results to date, which is leading to a lowering of expectations. China remains a headwind *and we are hearing that business conditions in China are becoming tougher. Italy and its fiscal situation is also a worry.*

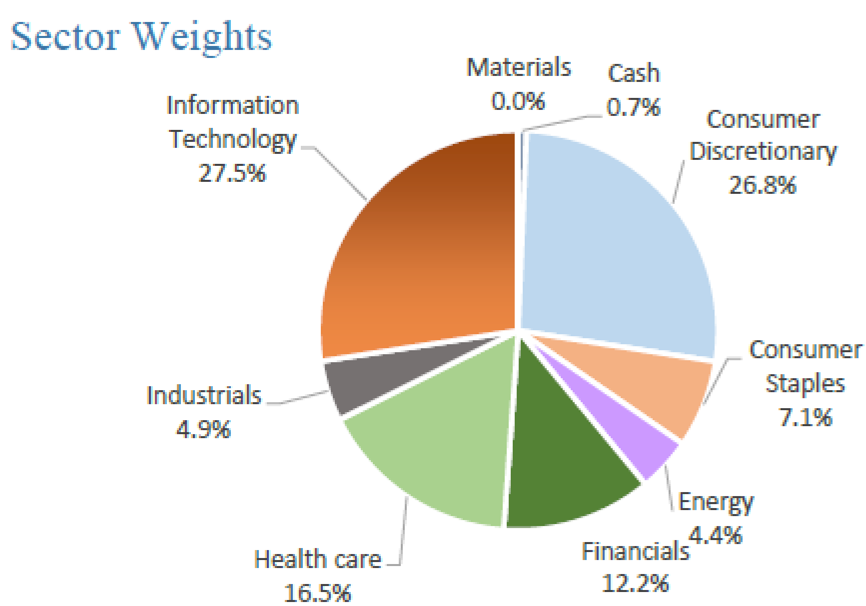
Sometimes when markets are climbing the wall of worry, they have a stumble. While we have indicated we do not expect outsized market gains after a very strong 8-year bull market, we do believe U.S. stocks can continue to trend higher and thus we remain positive on the market. In this very volatile environment, we are actively looking for opportunities to upgrade our portfolios looking for great companies at good prices."

Portfolio Positioning

Global Equity Growth Fund

To date, the Global Equity Growth Portfolio has returned 4.8%, 12.3% and 13.0%, respectively, in the quarter, year-to-day, and since inception (annualized).

Our portfolio remains overweight the technology and consumer discretionary sectors, with health care and financials also representing significant weights.



During the quarter, we made several tactical switches within the portfolio. Below we highlight our rationale for new purchases and sales.

New positions – Boston Scientific (3.0% weighting), Airbus (2.5% weighting), Alliance Data Systems (2.0% weighting)

Stocks with significant weighting increases – Constellation Brands (+1%), Broadcom (+1.0%), Teleflex (+0.5%)

Boston Scientific – We like Boston Scientific's position in several high growth medical devices technologies in fields such as neuroscience, cardiovascular health and urology. We wrote about our purchase in our August mid-month research report.

Airbus – Airbus is well positioned in the narrow-body airplane market and should generate significant free cash flow as its production ramps up. We wrote more about Airbus in our October mid-month research report.

Alliance Data Systems – Alliance data systems is a financial payments and marketing services provider. The company operates 3 businesses: credit card services for retailers such as Pottery Barn and Victoria's Secret; marketing services focused on using data to optimize marketing campaigns, and loyalty program management, including the Air Miles program in Canada. The company is actively looking at repositioning its business portfolio through the sale of one or more of its businesses, which would simplify its organizational structure and could provide for multiple expansion.

Stocks Sold – Medtronic (-3.5%), Diageo (-2.0%) Costco (-2.0%)

Stocks with significant weighting decreases - Pfizer (-1.5%), Facebook (-1.0%)

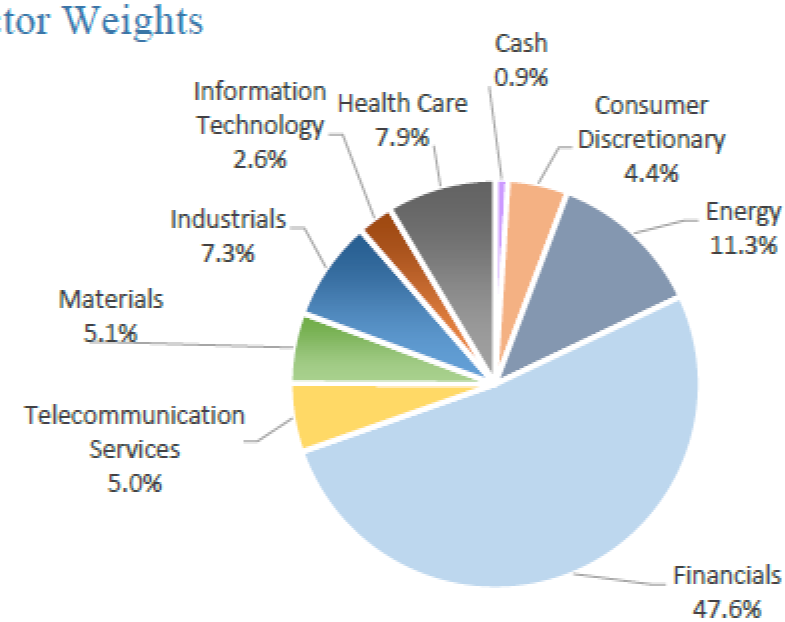
Medtronic – Medtronic is a global leader in medical device technology. We sold the shares, as the price was approaching our target, and redeployed the funds into Boston Scientific, a company in a similar field but, in our view, with more growth opportunity.

Diageo – Diageo is a global alcohol & spirits company. Like Medtronic, we sold the shares as they were approaching our target price and we did not feel a higher target could be justified. We redeployed the funds into Constellation Brands, a North American beer & wine maker that recently made waves by making the largest cannabis investment to date with the purchase of a controlling stake in Canadian cannabis leader Canopy Growth.

Income Growth Fund

To date, the Income Growth Portfolio has returned 5.0%, 1.6% and 12.6%, respectively, in the quarter, year-to-day, and since inception (annualized). Our Income Growth Portfolio is positioned 80% in Canada due to the preferential tax treatment of domestic dividends. We continue to be positioned in stable dividend companies with a focus on total portfolio yield. Shares of financial services companies continue to make up almost half of the portfolio, with a diverse collection of income generating companies filling out the remainder.

Sector Weights



During the quarter, we made several tactical switches within the portfolio. Following is our rationale for new purchases and sales.

New positions – Newell Rubbermaid (3.0% weighting), Intertape Polymer (2.0% weighting)

Newell Rubbermaid – We own Newell in both our Income Fund and our Global Growth portfolio. We believe Newell has the brand management skills to work through a difficult retail market and emerge stronger following the transition. The company is exploring strategic options with respect to its portfolio of brands and should benefit from any divestitures that may occur.

Intertape Polymer – Intertape Polymer is a large provider of industrial tapes. With E-commerce continuing to grow, demand for packaging tape is increasing. Moreover, large players like Intertape are benefitting as the industry consolidates to better serve larger customers. Intertape is finishing up a multi-year investment program that should start to pay off through higher growth in cash flow through 2021.

Stocks Sold – CI Financial (-2.0%), Qualcomm (-3.0%)

CI Financial - We believed CI Financial would benefit from rising equity markets, which historically translates into higher AUM and revenue. However, the mutual fund business in Canada has become much tougher and CI's poor performance within its core funds led to higher than expected redemptions. We believe the company will need to restructure and, thus, sold the shares after the company announced a reduction in its dividend.

Qualcomm - We sold our Qualcomm position as the shares approached our target price as we did not feel justified in increasing it. The yield had also fallen as the share price recovered. We believe other companies in our portfolio offer more attractive returns.

As always, we appreciate your referrals so if you know someone that can benefit from our services, please do not hesitate to give us a call.