2019 – A Brighter Year for Stocks & Bonds?

Runtime 3:11

Benjamin Tal
Deputy Chief Economist,
CIBC World Markets

When it comes to 2019, we all know that the current expansion is going to be the longest expansion ever, by May or June of 2019. So the question is to what extent we should start talking about a recession. This is a very old cycle. Now I know that the yield curve, namely the difference between a short-term and long-term interest rates is now close to inversion, basically a situation which short-term rates are higher than long term rates, and this is always a signal of a recession. However we believe that 2019 will not be a recessionary year. We are going to slow down, but we're not going to see a recession.

GFX
Recession unlikely in 2019

The main reason is that central bankers will not repeat past mistakes. Every economic recession over the past 50 years was helped, if not caused, by monetary policy error in which central bankers raise interest rates way too quickly. The signals that we are getting from the Fed in the U.S. and from the Bank of Canada – we are not going to rush it, we are not going to raise interest rates very quickly. And that's exactly what we are seeing. We're seeing a situation, which the Fed will be moving very, very slowly in 2019 if at all. And even the Bank of Canada maybe once, maximum twice, and that will be the end of it. So we see a very muted interest rate cycle this time around. This has major implications for the bond market and of course the stock market.

GFX
Rising interest rates?

We believe that the bond market will actually outperform expectations because rates will not be rising as quickly as expected. As well, I see some pockets as far as the stock market is concerned that actually will surprise on the upside. I do believe that the energy sector in Canada might surprise on the upside. Valuations are extremely, extremely attractive and those spreads are narrowing and we see actually some improvement in oil prices globally. But overall the energy sector is actually cheap.

GFX
Positives for 2019

One of the reasons why we are not totally depressed when it comes to 2019 is the fact that we reached some sort of agreement with the U.S. on NAFTA 2. This is a positive for business investment. We also see the consumer actually showing some life in 2019. So we have the

consumer and we have business investment actually leading to a situation in which overall economic growth would be 1.8, 1.9. This actually can improve profitability down the road. And one of the reasons why we expect 2019 to be an okay year, as far as the stock market is concerned, is the fact that corporate earnings will actually surprise on the upside.

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Equity market expectations

Overall, I think that the stock market in Canada will not outperform what we're seeing in the U.S. We see a situation in which the market is trying to figure out and find a price. We are not there yet, and I believe that the fact that interest rates will not be rising as quickly as the market is expecting will be a net positive for the market. It will not be a great year for the stock market, but it will not be a disaster year.