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November 2019 Commentary & Outlook

Some Bright Spots Emerging

North American equity markets were mixed for the month of October. The S&P/TSX was down for the month whereas the S&P 500 was up, continuing the longest U.S. economic expansion in history.

Some bright spots have opened for the global economy as well. Trade volumes reportedly grew in Q3 for the first time in four quarters. Both emerging markets and the German economy showed signs of manufacturing and export stabilization. The sustainability of a positive global trend will depend a lot on U.S. policy makers.

Trade negotiations between the U.S and China have been showing some positive signals, with hints of a truce starting to emerge. However, the situation remains uncertain and we believe investors should remain cautious. Similarly, emerging markets may continue to lag until there is some confirmation of a trade truce between the two largest global economies.

That contrasts with the U.S. economy where the expansion shows no signs of ending. U.S. households are benefiting from lower interest rates, rising disposable income and a positive household balance sheet courtesy of the housing market.

This growing 'wealth effect' supports consumption spending which, according to the Bureau of economic analysis, accounts for approximately 70% of U.S. GDP.

And with the U.S. equity markets breaking out to all time highs, investors continue to bet on accommodative fiscal and monetary policies to support further growth at least into the 2020 elections.

While the Canadian stock market has yet to break out to all time highs, we have seen a positive uptick in November based on October's strong economic data, as Canadian economic growth is also exceeding expectations. GDP numbers look good, the job market is strong, driven by the services sector, and Canadians are benefiting from positive household balance sheets in line with their U.S. counterparts.

Based on the recent economic data, the Bank of Canada decided to leave interest rates unchanged, with the expectation that the economy should be able to stand on its own for now.

However, the Canadian market still seems to be hampered by low energy prices, fallout from the U.S. – China trade wars, and recent federal elections that resulted in a minority government, which left investors feeling uncertain about future policy direction. This concern may be overblown as much of Liberal policy aligns with other parties, and a Liberal minority government will likely be able to hammer out 'ad hoc' agreements on issues that will keep the country moving forward.

November 2019 Commentary & Outlook

Conservative Portfolios

Our core Income pool was down 0.85% for the month of October but sits positive 10.47% year to date.

Over the last month we increased the exposure to Fixed Income by 7% for a total allocation of 67.7%. The pool also maintained its exposure to preferred shares at 15.7%.

Early in November, we eliminated the portfolio's exposure to split-corp preferred shares and have deployed the funds into a far out-of-the-money short put on QQQ. This strategy employs a similar level of risk but should generate a higher return.

The current Covered Call allocation is being transitioned to a Collar strategy that limits the downside risks by adding a protective put to the combination.

With the unwinding of the Covered Call positions the Pool reduced its exposure to the Healthcare and Materials sectors.

We had been applying a calendar-spread option strategy across several securities (TSLA, BYND, QQQ) to enhance cash flow in the pool. We have now limited that strategy to just the QQQ index ETF given its outperformance over the strategy as it was applied to the other individual companies.

Growth Portfolios

Over the month of October, our core Equity Pool added 0.34% and sits positive at 14.31% for the year.

During the month, we deployed cash that was sitting on the sidelines into several put writes on three Technology stocks (V, CRM, SQ). Two of these positions were executed pre-earnings to take advantage of high implied volatility and capture greater premium. Given the strength of the U.S. consumer, we also initiated a position in a consumer discretionary sector stock (AMZN) as a new long-term hold position in the core portfolio.

We sold one of our health care sector stocks (JNJ) on news of a litigation settlement that was favorable to the stock price, selling the stock outright as opposed to trimming because of ongoing legal risk and ESG considerations. That stock has since fallen on new negative headlines, in line with the company's current challenges.

Has Our Overall Outlook Changed?

Whispers of a recession continue to get quieter as new global economic data points towards modest, albeit slower, growth over the next couple of years.

Although we may be back to that 'fear of missing out' mentality that has been driving the markets higher all year, more and more data is now suggesting that stocks may have further room to run.

And, as mentioned last month…we mustn't underestimate the impact accommodative

November 2019 Commentary & Outlook

central banks and low interest rates can have on offsetting macro-economic concerns and supporting stock prices.

That said, with the markets at, or close to, all-time highs and investors becoming more complacent, the probability of a pullback is high, especially as we get closer to the end of the year.

We continue to re-analyze companies on our watch list daily as the macroeconomic conditions change, as these changes can influence the underlying corporate fundamentals significantly. Overall, we are looking at selectively putting more cash to work on market pull backs and as we uncover new opportunities, while remaining defensive at these market highs.

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