Weekly Trends

PRIVATE CLIENT SOLUTIONS

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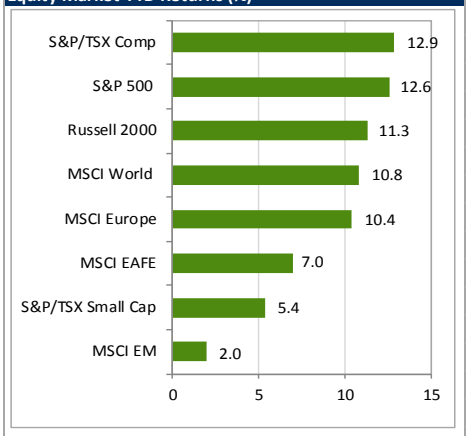
That's a Wrap

US earnings season has essentially wrapped up with ~90% of S&P 500 companies having reported first quarter results as of the end of last week. The quarter did not offer many surprises as we saw the typical earnings and sales upside surprises.

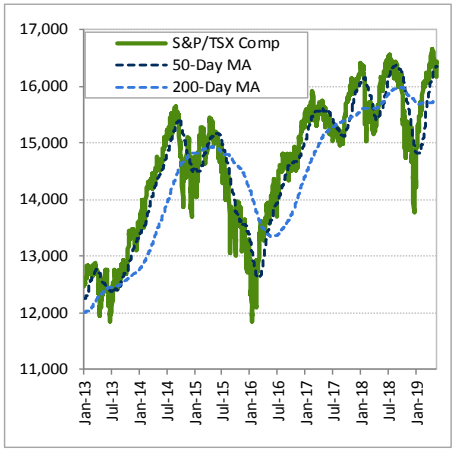
- The blended (combines actual results for companies that have reported and estimated results for companies that have yet to report) earnings growth rate of Q1/19 stands at -0.5% today. It is likely the S&P 500 could avoid a negative quarter once the dust has settled, but if the actual decline for the quarter stands it will mark the first time the index has reported a yoy decline in earnings since Q2/16 (-3.2%).
- We believe corporate share buyback activity has played a significant role in this quarter's earnings results. US corporations bought a near-record US$194 bln in their own stock in the first quarter, up 8% yoy.
- Looking at the next quarter, analysts have lowered Q2/19 EPS expectations by 5.4% since the beginning of the year and are now expecting growth of -0.3% yoy. More recently, a higher percentage of S&P 500 companies have issued negative EPS guidance for Q2/19 (80%) compared to the 5-year average (70%), but analyst revisions since the start of the quarter have been smaller compared to the historical average.
- US defensive sectors, such as utilities, have moved into a market leadership position while the majority of cyclicals are struggling. Consumer discretionary and information technology are the only two areas showing leadership among the broader group; however, in recent weeks the ratio has weakened and both have crossed below their respective 50-day moving averages.

Equity Market YTD Returns (%)



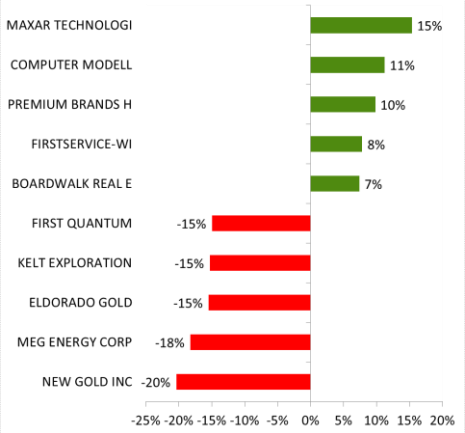
Canadian Sectors	Weight	Recommendation
Consumer Discretionary	4.1	Underweight
Consumer Staples	4.1	Overweight
Energy	17.8	Underweight
Financials	32.2	Market weight
Health Care	2.1	Underweight
Industrials	11.5	Market weight
Technology	5.0	Market weight
Materials	9.5	Market weight
Communications	5.8	Overweight
Utilities	4.3	Market weight
Real Estate	3.5	Overweight

Technical Considerations	Level	YE Target
S&P/TSX Composite	16,165	15,600



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	140	56%
Weekly Decline	102	41%
Advance-Decline	38	
New 52 wk high	14	6%
New 52 wk low	19	8%
No. Stocks Above 50-d	94	37%
No. Stocks Above 200-d	127	51%
Arms Weekly Index	1.21	Neutral
RSI (14-day)	38.6	Neutral
50-DMA	16,353	Downtrend
200-DMA	15,715	Uptrend

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

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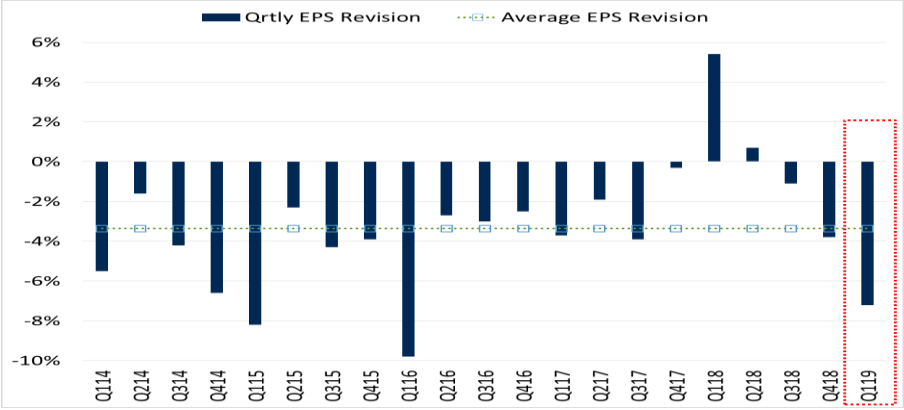
US Earnings Wrap Up

US earnings season has essentially wrapped up with ~90% of S&P 500 companies having reported first quarter results as of the end of last week. The quarter did not offer many surprises as we saw the typical earnings and sales upside surprises. In aggregate, companies reported earnings that were 5.4% above analysts' estimates, which is slightly above the 5-year average beat rate of 4.8%. Recall, analysts aggressively cut their Q1/19 earnings expectations ahead of the reporting season; the median EPS estimates dropped by 7.5% during the quarter, which placed the negative earnings revision well above historical averages (5-year revision at -3.2% and 10-year of -3.7%). In fact, the first quarter marked the largest percentage decline in the bottom-up EPS estimate during a quarter since Q1/16 (-9.8%).

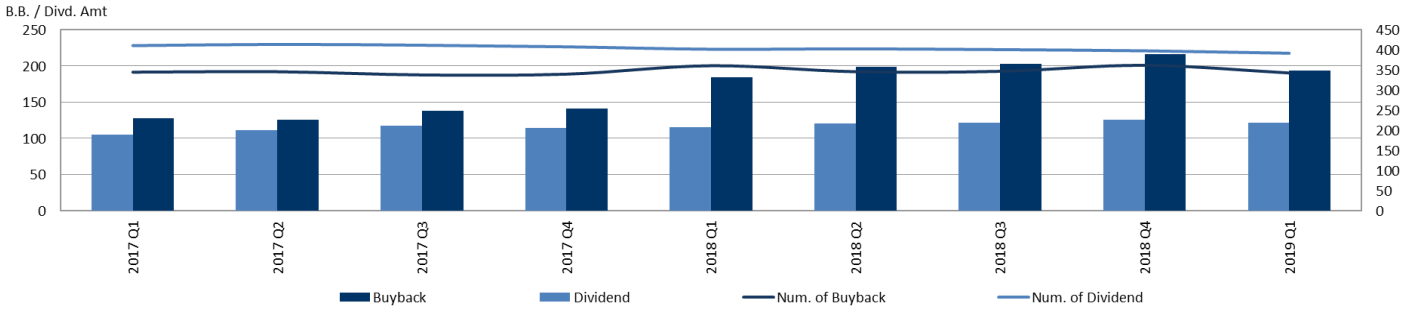
S&P 500 Q1/19 EPS Revisions



Source: Bloomberg, Raymond James Ltd.

We believe corporate share buyback activity has played a significant role in this quarter's earnings results. US corporations bought a near-record US$194 bln in their own stock in the first quarter, up 8% yoy. Considering net fund flow data, corporate America was the largest contributor to equity purchases as asset flows YTD have overwhelmingly favoured bond over equity funds. If we assume a similar level of buyback activity for the rest of the year, S&P 500 share repurchases is on pace to smash last year's record high!

S&P 500 Quarterly Buyback and Dividends



Source: Bloomberg, Raymond James Ltd.

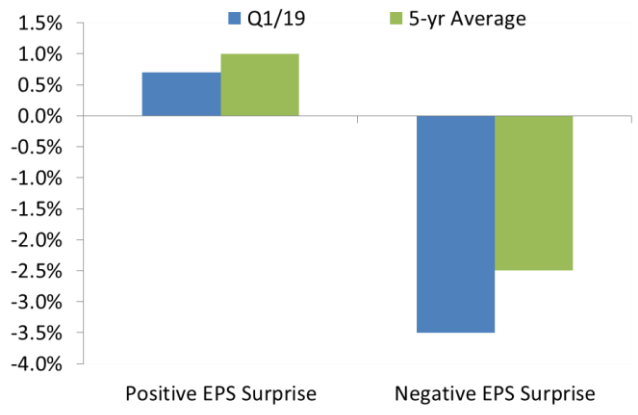
The blended (combines actual results for companies that have reported and estimated results for companies that have yet to report) earnings growth rate of Q1/19 stands at -0.5% today. It is likely the S&P 500 could avoid a negative quarter once the dust has settled, but if the actual decline for the quarter stands it will mark the first time the index has reported a yoy decline in earnings since Q2/16 (-3.2%).

In terms of sales, S&P 500 companies have reported revenue above estimates. In aggregate, companies have reported sales that were +0.4% above estimates, which is below the 5-year average of +0.8%. The blended revenue growth rate for Q1/19 thus far is 5.3%.

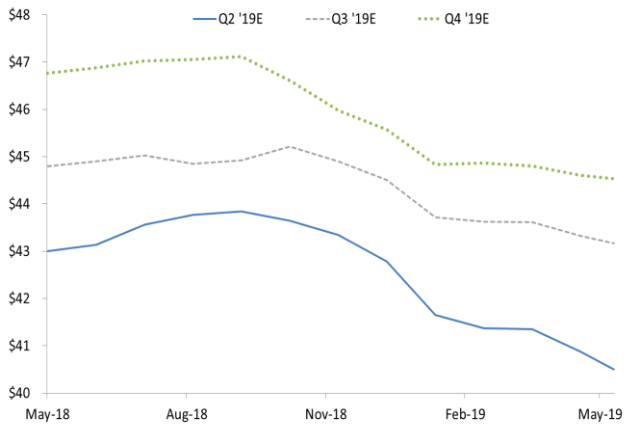
With companies handily beating earnings estimates, surely the market would reward these companies with higher stock prices. However, this has not been the case. Companies reporting positive earnings surprises saw an average percentage change of just +0.7% from two days before the company reported actual results through two days after the company reported actual results. This is below the 5-year average of +1.0% during the 4-day window. On the other hand, companies posting negative earnings surprises experienced a -3.5% change during the 4-day window compared to the 5-year average of -2.5%.

Looking at the next quarter, analysts have lowered Q2/19 EPS expectations by 5.4% since the beginning of the year and are now expecting growth of -0.3% yoy. More recently, a higher percentage of S&P 500 companies have issued negative EPS guidance for Q2/19 (80%) compared to the 5-year average (70%), but analyst revisions since the start of the quarter have been smaller compared to the historical average.

Market Not Rewarding Beats & Punishing Misses



S&P 500 2019 Quarterly EPS Estimates



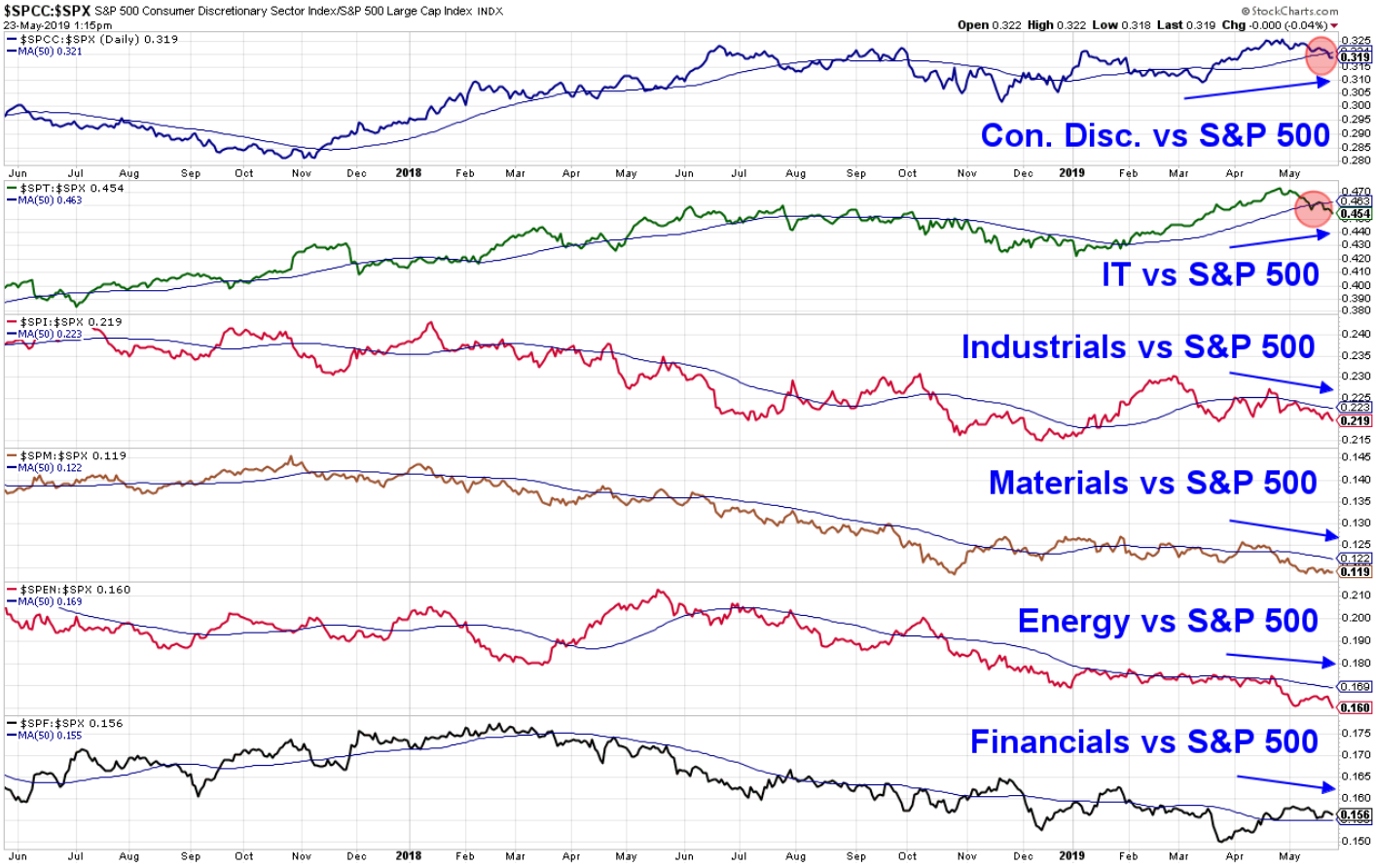
Source: Factset, Raymond James Ltd.

Market Behaving Defensively

US defensive sectors, such as utilities, have moved into a market leadership position while the majority of cyclicals are struggling. In the chart below, we show US cyclical sector market-relative performance. Consumer discretionary and information technology are the only two areas showing leadership among the broader group; however, in recent weeks the ratio has weakened and both have crossed below their respective 50-day moving averages. Over the past month, utilities are the market's

third strongest sector; right behind healthcare and REITs. Consumer staples are in fourth place. That certainly suggests that investors have turned more defensive during the month of May. Other indicators also point to a defensive rotation, such as the bond market which continues to signal a deceleration in economic activity. The US 10-year treasury yield has slipped to 2.30%, a full 100 bps from just 7 months ago. Over the same period, investment grade bonds have outperformed high yield. Further, the bond market is increasingly pointing to a Fed rate cut this year as the implied fed funds rate by the end of the year currently sits at 2.04%.

Cyclicals Misbehaving: Sectors Relative to S&P 500



Source: stockcharts.com, Raymond James Ltd.

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