

# Travel with Caution, Not Fear

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Chief Investment Strategist



# Roadmap For Today

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What happened in 2018?

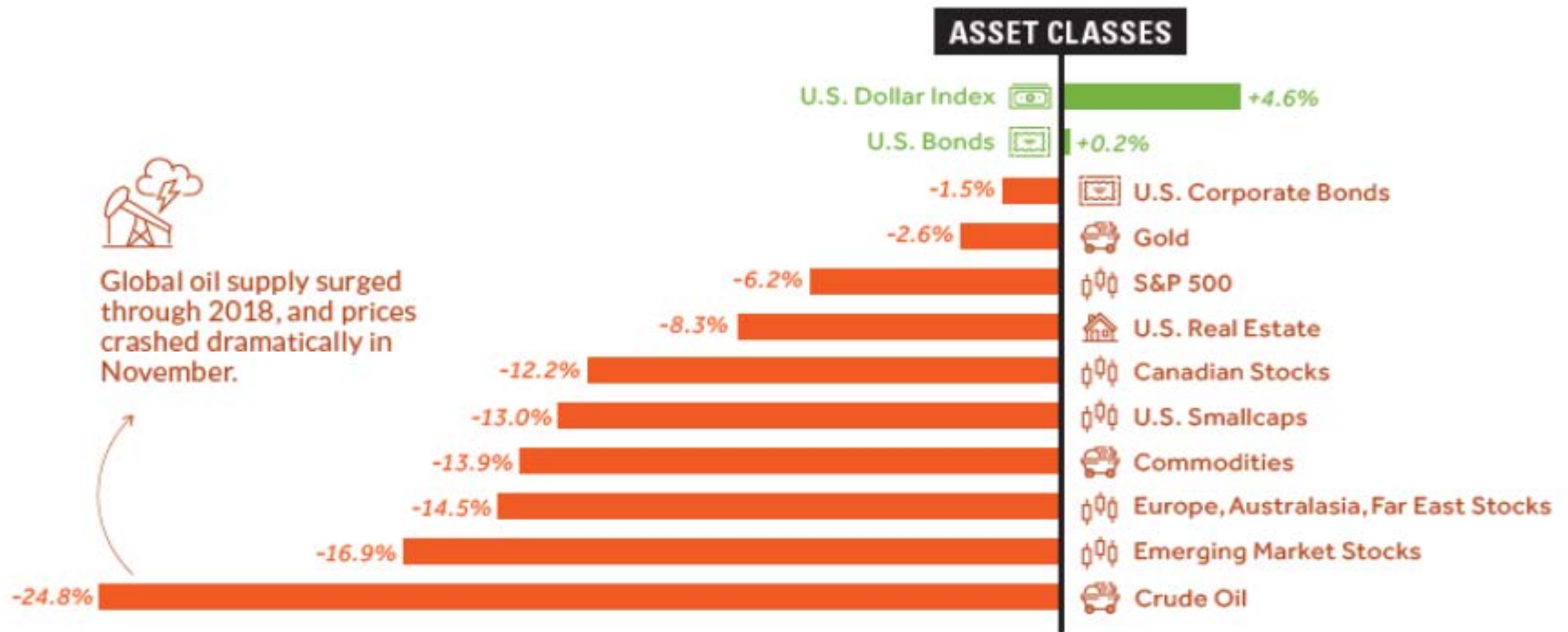
Why it happened?

What do we do about it?

# Like A Kick To The Stomach – Multiple Times

## HOW MARKETS DID IN 2018

We'll start with broad asset classes, including stocks, bonds, commodities, and cash:

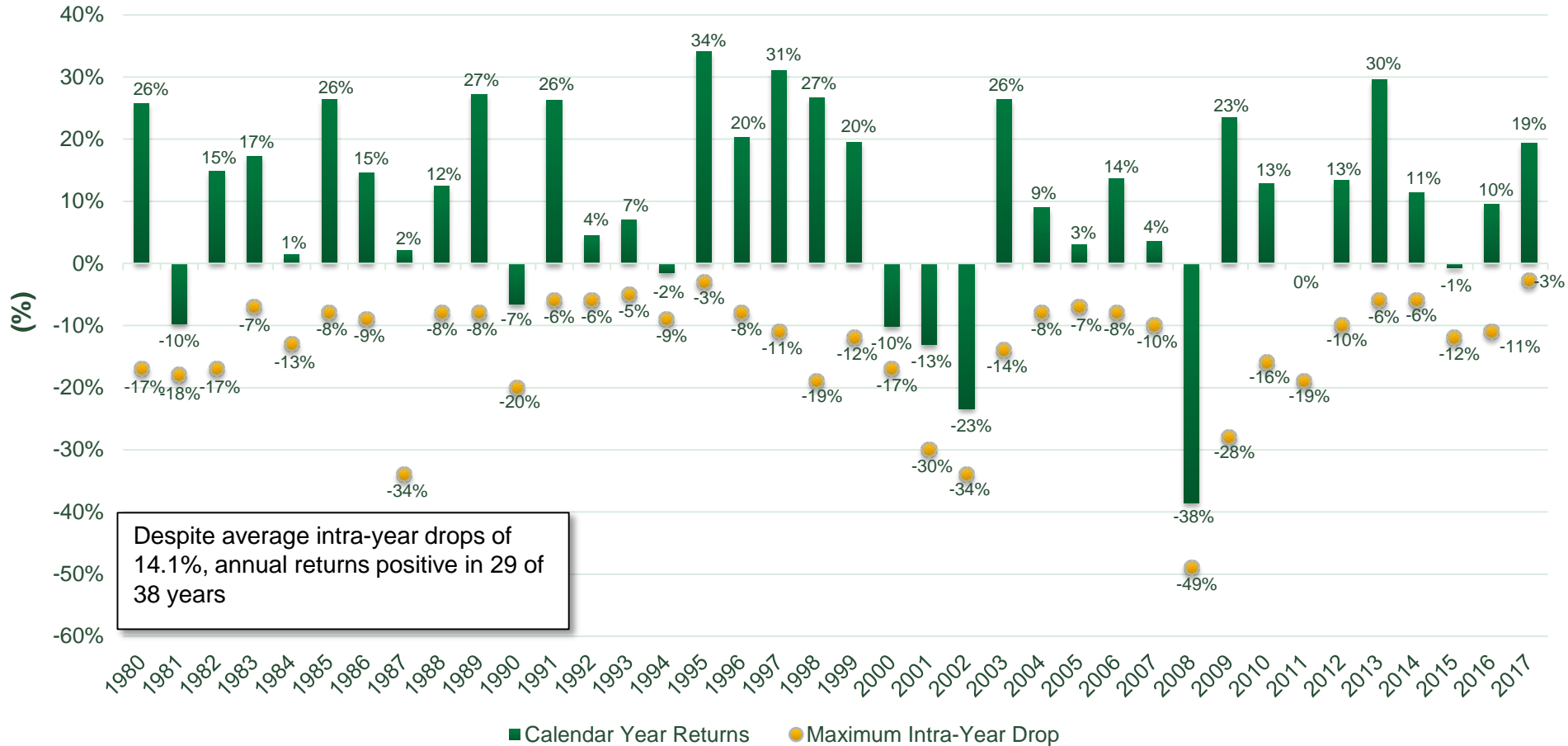


*Note: Figures for equity markets are not including dividends*

Source: Visual Capitalist. As of December 31, 2018

# Corrections Are Normal

S&P 500 intra-year declines vs. calendar year returns  
1980 - 2017



Source: Manulife Investments, Bloomberg. As of December 31, 2017

# Why it Happened?

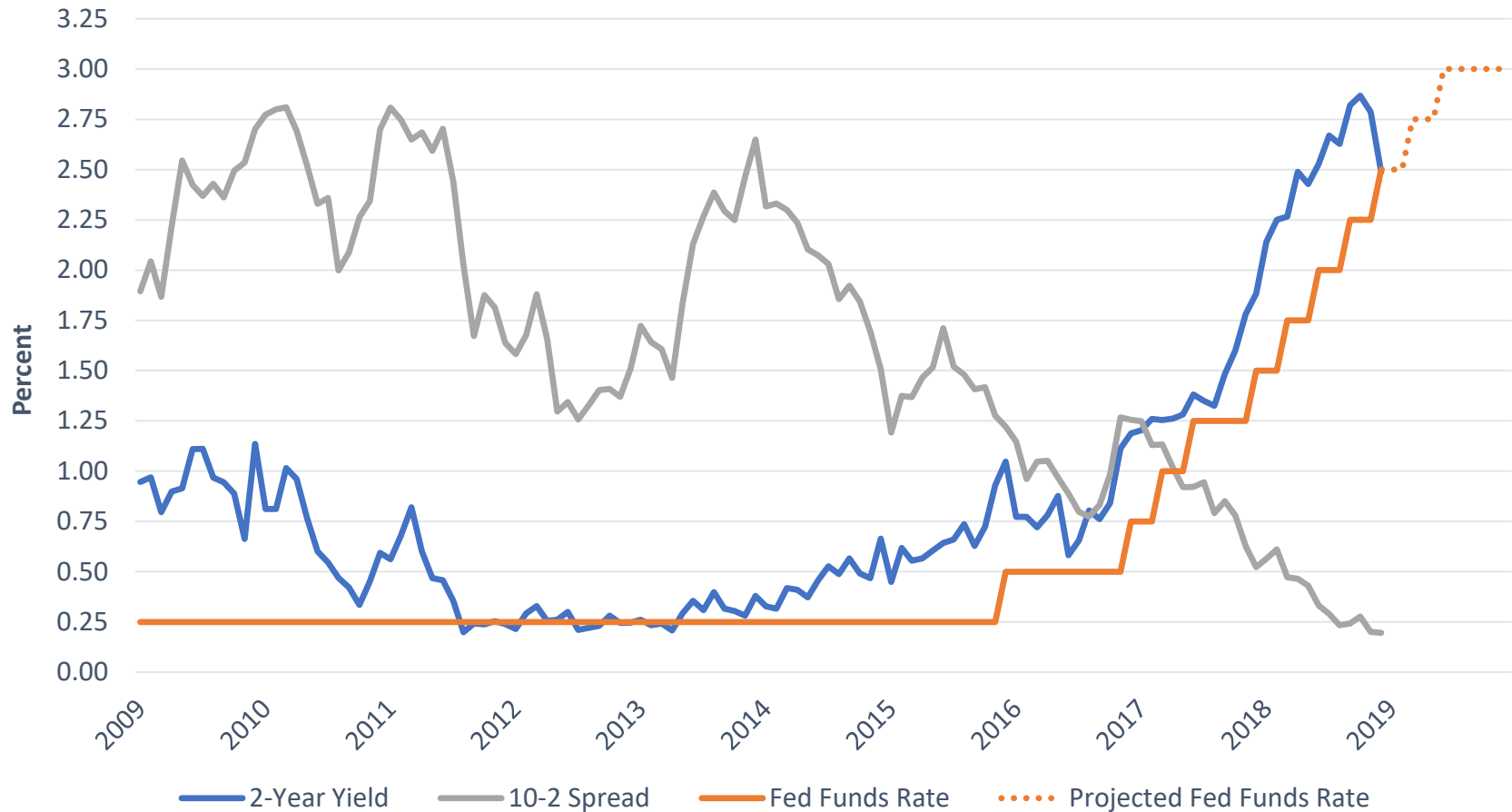
## Conditions Leading to the Equity Market Volatility

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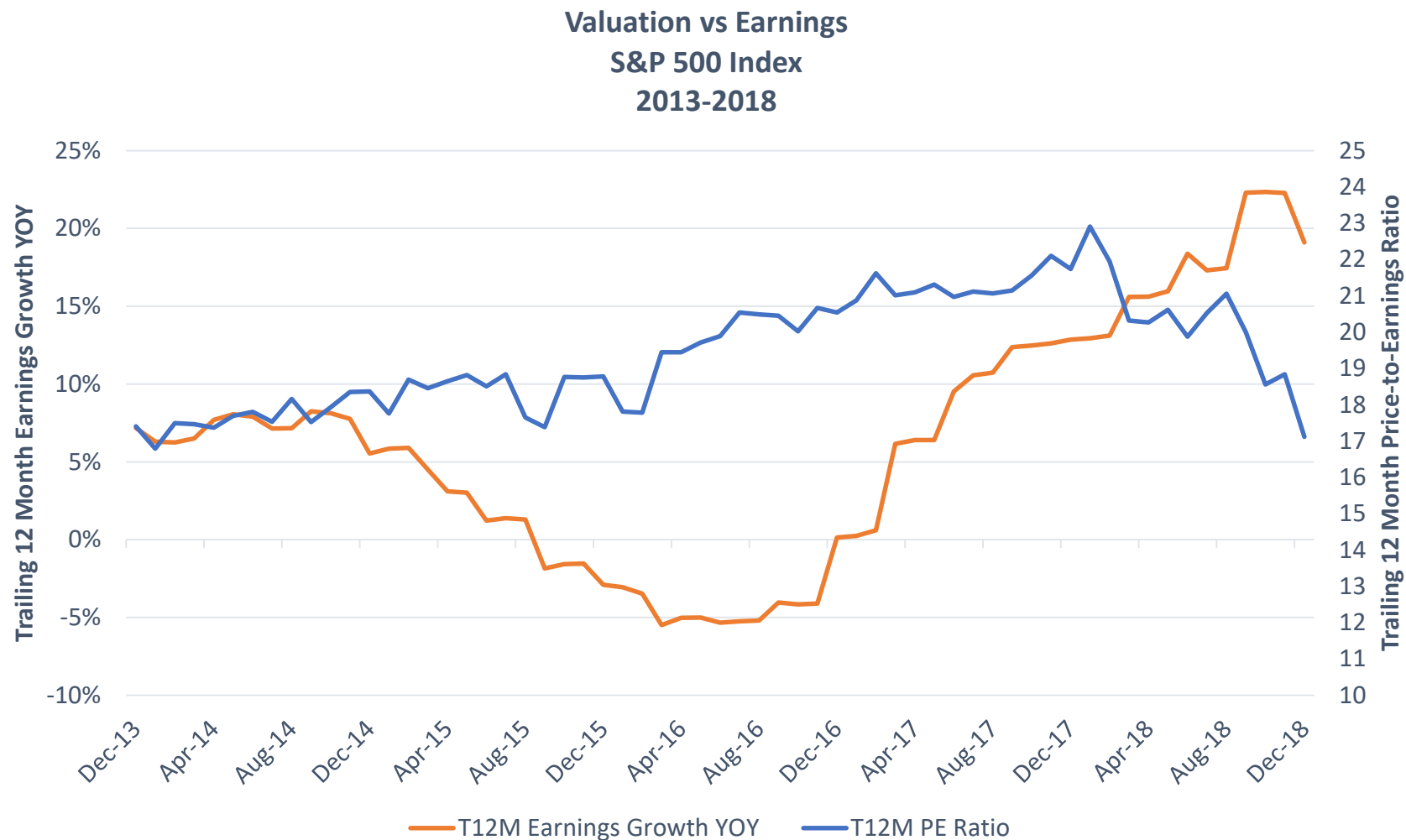
# Interest Rates Headed Higher

2-Year Yield, Federal Funds Rate and 10-2 Spread  
2009 - 2018



Source: Bloomberg, Manulife Investments as of December 31, 2018

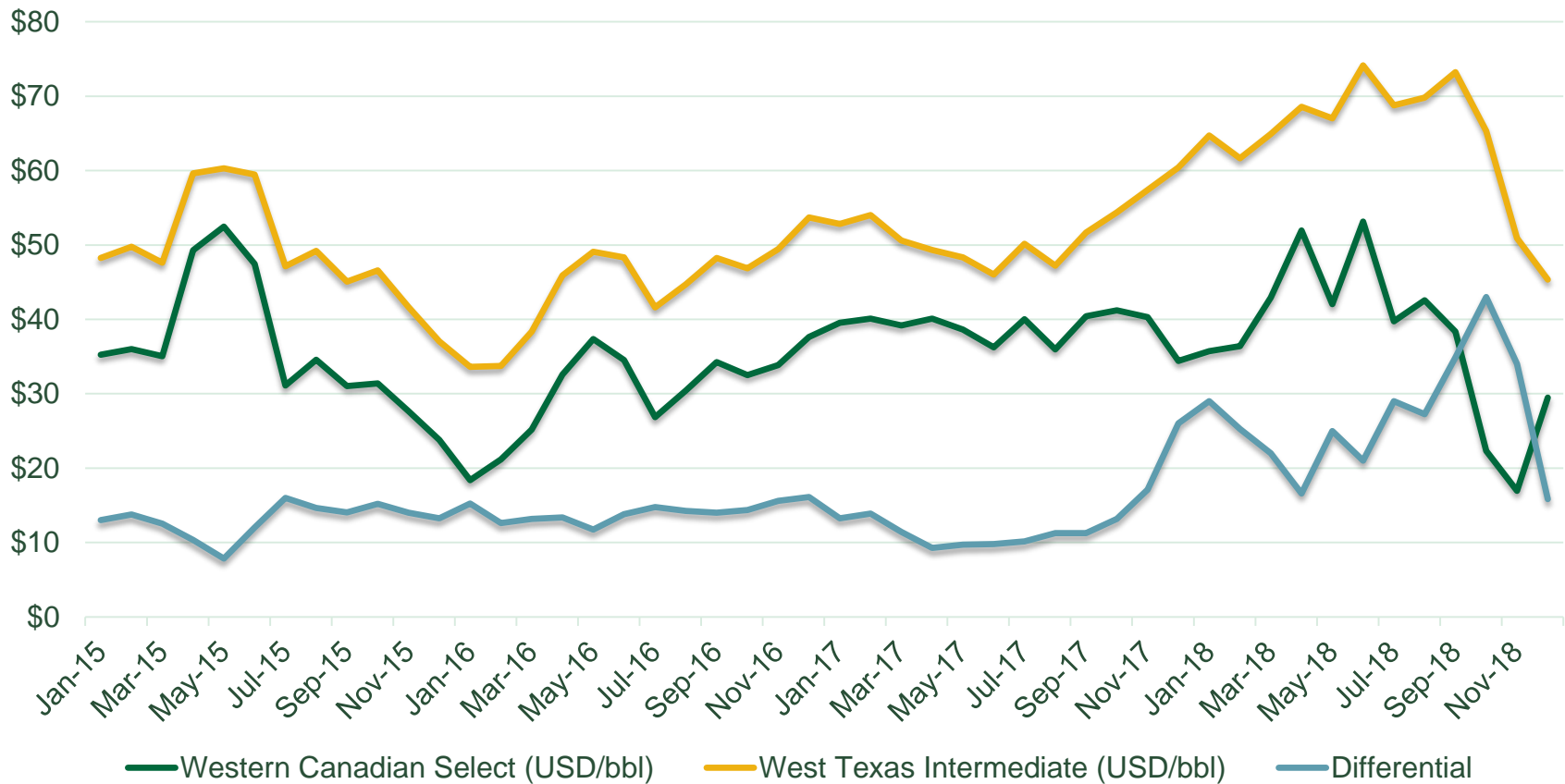
# P/E Multiples Contracted and Earnings Growth Accelerated



Source: Bloomberg, Manulife Investments as of December 31, 2018

# Oil Prices Didn't Help Confidence

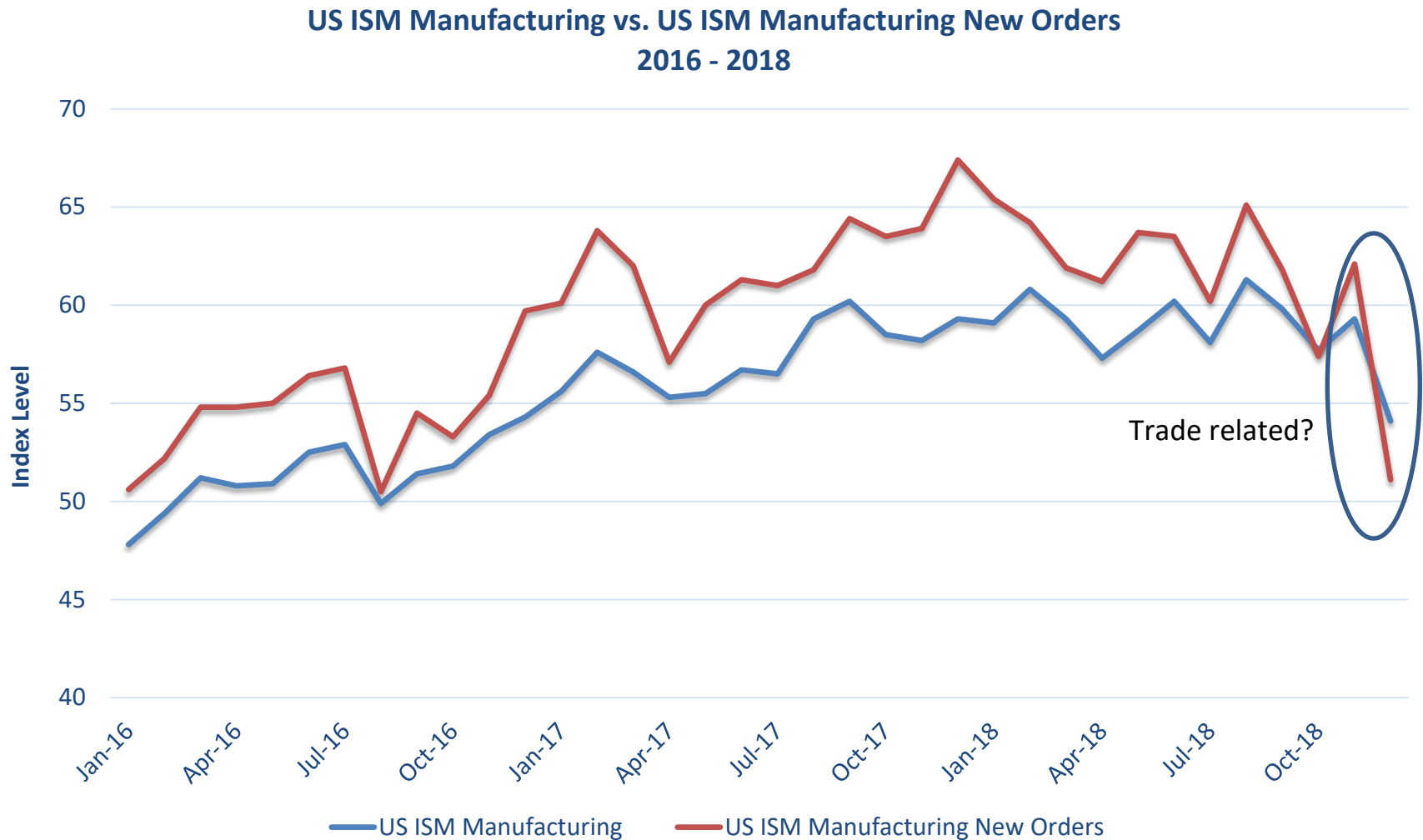
**Oil Benchmark Prices  
Western Canadian Select vs West Texas Intermediate  
2015-2018**



Source: Bloomberg, Manulife Investments as of December 31, 2018



# Is this “Normal” or Trade Related?



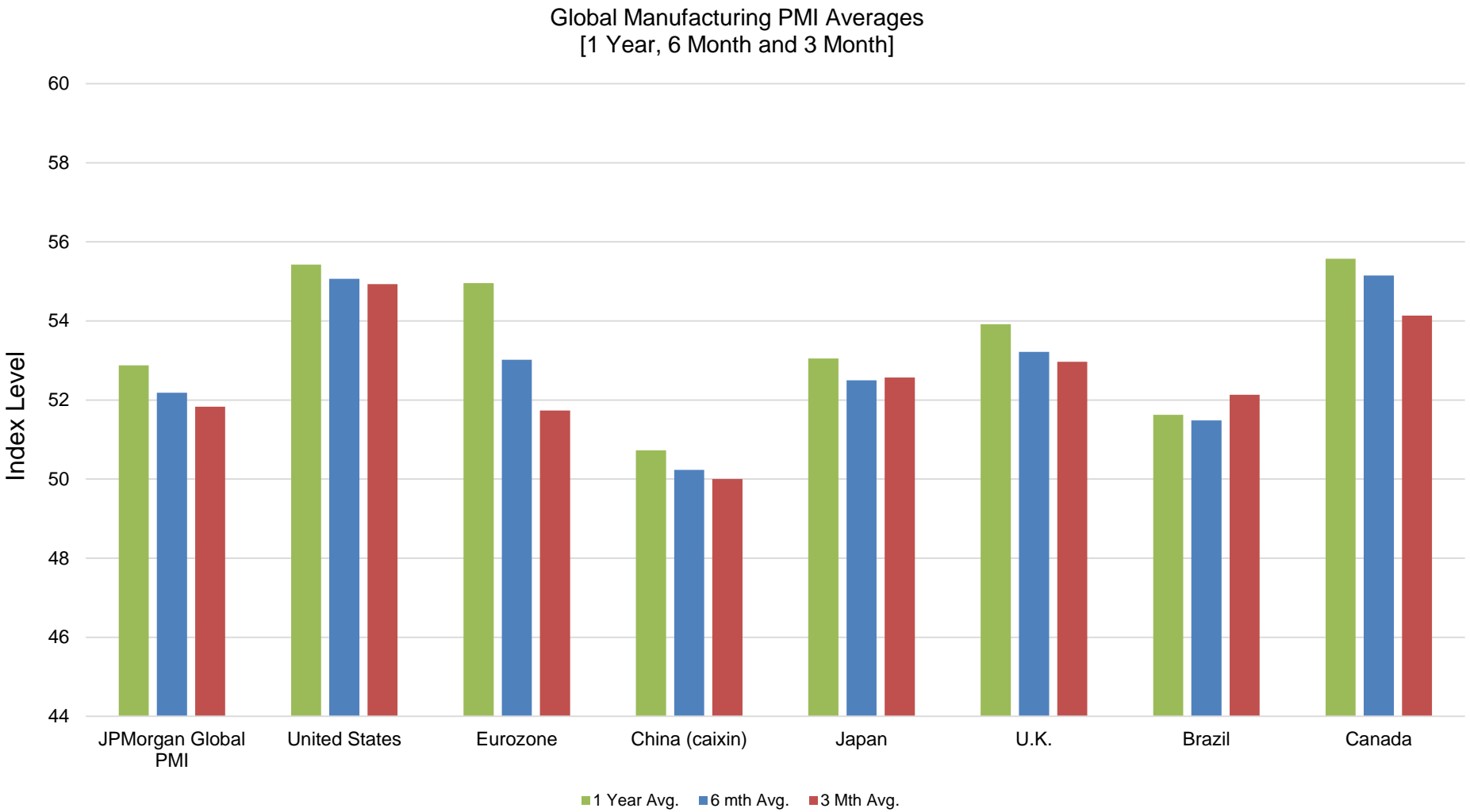
Source: Bloomberg, Manulife Investments as of December 31, 2018

# Global Manufacturing PMI Heat Map

	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18
JPMorgan Global PMI	52.7	52.7	53.0	53.0	52.7	52.6	52.6	52.7	53.2	53.3	53.5	54.1	54.5	54.4	54.1	53.3	53.5	53.1	53.0	52.8	52.6	52.2	52.0	52.0	51.5
United States	54.3	55.0	54.2	53.3	52.8	52.7	52.0	53.3	52.8	53.1	54.6	53.9	55.1	55.5	55.3	55.6	56.5	56.4	55.4	55.3	54.7	55.6	55.7	55.3	53.8
Canada	51.8	53.5	54.7	55.5	55.9	55.1	54.7	55.5	54.6	55.0	54.3	54.4	54.7	55.9	55.6	55.7	55.5	56.2	57.1	56.9	56.8	54.8	53.9	54.9	53.6
Mexico	50.2	50.8	50.6	51.5	50.7	51.2	52.3	51.2	52.2	52.8	49.2	52.4	51.7	52.6	51.6	52.4	51.6	51.0	52.1	52.1	50.7	51.7	50.7	49.7	49.7
U.K.	56.1	55.7	54.5	54.2	57.3	56.7	54.3	55.3	56.7	55.9	56.6	58.2	56.3	55.3	55.0	54.9	53.9	54.3	54.3	53.8	53.0	53.6	51.1	53.6	54.2
Eurozone	54.9	55.2	55.4	56.2	56.7	57.0	57.4	56.6	57.4	58.1	58.5	60.1	60.6	59.6	58.6	56.6	56.2	55.5	54.9	55.1	54.6	53.2	52.0	51.8	51.4
Germany	55.6	56.4	56.8	58.3	58.2	59.5	59.6	58.1	59.3	60.6	60.6	62.5	63.3	61.1	60.6	58.2	58.1	56.9	55.9	56.9	55.9	53.7	52.2	51.8	51.5
Switzerland	56.2	54.6	57.8	58.6	57.4	55.6	60.1	60.9	61.2	61.7	62.0	65.1	65.6	65.3	65.5	60.3	63.6	62.4	61.6	61.9	64.8	59.7	57.4	57.7	57.8
Holland	57.3	56.5	58.3	57.8	57.8	57.6	58.6	58.9	59.7	60.0	60.4	62.4	62.2	62.5	63.4	61.5	60.7	60.3	60.1	58.0	59.1	59.8	57.1	56.1	57.2
France	53.5	53.6	52.2	53.3	55.1	53.8	54.8	54.9	55.8	56.1	56.1	57.7	58.8	58.4	55.9	53.7	53.8	54.4	52.5	53.3	53.5	52.5	51.2	50.8	49.7
Italy	53.2	53.0	55.0	55.7	56.2	55.1	55.2	55.1	56.3	56.3	57.8	58.3	57.4	59.0	56.8	55.1	53.5	52.7	53.3	51.5	50.1	50.0	49.2	48.6	49.2
Spain	55.3	55.6	54.8	53.9	54.5	55.4	54.7	54.0	52.4	54.3	55.8	56.1	55.8	55.2	56.0	54.8	54.4	53.4	53.4	52.9	53.0	51.4	51.8	52.6	51.1
Ireland	55.7	55.5	53.8	53.6	55.0	55.9	56.0	54.6	56.1	55.4	54.4	58.1	59.1	57.6	56.2	54.1	55.3	55.4	56.6	56.3	57.5	56.3	54.9	55.4	54.5
Czech Republic	53.8	55.7	57.6	57.5	57.5	56.4	56.4	55.3	54.9	56.6	58.5	58.7	59.8	59.8	58.8	57.3	57.2	56.5	56.8	55.4	54.9	53.4	52.5	51.8	49.7
Hungary	52.8	57.0	59.4	55.9	56.2	61.9	56.9	54.2	56.8	59.3	58.3	58.8	60.5	61.1	57.2	56.6	53.3	55.2	52.9	53.3	56.0	54.1	57.1	53.5	54.2
Poland	54.3	54.8	54.2	53.5	54.1	52.7	53.1	52.3	52.5	53.7	53.4	54.2	55.0	54.6	53.7	53.7	53.9	53.3	54.2	52.9	51.4	50.5	50.4	49.5	47.6
Greece	49.3	46.6	47.7	46.7	48.2	49.6	50.5	50.5	52.2	52.8	52.1	52.2	53.1	55.2	56.1	55.0	52.9	54.2	53.5	53.5	53.9	53.6	53.1	54.0	53.8
Australia	55.4	51.2	59.3	57.5	59.2	54.8	55.0	56.0	59.8	54.2	51.1	57.3	56.2	58.7	57.5	63.1	58.3	57.5	57.4	52.0	56.7	59.0	58.3	51.3	49.5
New Zealand	50.0	49.5	47.5	48.6	50.9	50.1	50.5	55.1	56.0	53.4	54.9	58.8	55.1	59.4	57.1	54.3	55.7	57.0	56.4	56.2	56.5	58.4	55.2	52.6	53.3
Japan	52.4	52.7	53.3	52.4	52.7	53.1	52.4	52.1	52.2	52.9	52.8	53.6	54.0	54.8	54.1	53.1	53.8	52.8	53.0	52.3	52.5	52.5	52.9	52.2	52.6
China (caixin)	51.9	51.0	51.7	51.2	50.3	49.6	50.4	51.1	51.6	51.0	51.0	50.8	51.5	51.5	51.6	51.0	51.1	51.1	51.0	50.8	50.6	50.0	50.1	50.2	49.7
South Korea	49.4	49.0	49.2	48.4	49.4	49.2	50.1	49.1	49.9	50.6	50.2	51.2	49.9	50.7	50.3	49.1	48.4	48.9	49.8	48.3	49.9	51.3	51.0	48.6	49.8
Taiwan	56.2	55.6	54.5	56.2	54.4	53.1	53.3	53.6	54.3	54.2	53.6	56.3	56.6	56.9	56.0	55.3	54.8	53.4	54.5	53.1	53.0	50.8	48.7	48.4	47.7
Vietnam	52.4	51.9	54.2	54.6	54.1	51.6	52.5	51.7	51.8	53.3	51.6	51.4	52.5	53.4	53.5	51.6	52.7	53.9	55.7	54.9	53.7	51.5	53.9	56.5	53.8
Indonesia	49.0	50.4	49.3	50.5	51.2	50.6	49.5	48.6	50.7	50.4	50.1	50.4	49.3	49.9	51.4	50.7	51.6	51.7	50.3	50.5	51.9	50.7	50.5	50.4	51.2
Malaysia	47.1	48.6	49.4	49.5	50.7	48.7	46.9	48.3	50.4	49.9	48.6	52.0	49.9	50.5	49.9	49.5	48.6	47.6	49.5	49.7	51.2	51.5	49.2	48.2	46.8
Singapore	52.0	51.6	51.4	52.2	52.6	51.4	50.7	51.3	53.2	53.7	54.2	54.4	52.1	53.6	55.3	53.7	55.6	56.8	56.0	53.0	51.1	49.6	52.6	53.8	52.7
India	49.6	50.4	50.7	52.5	52.5	51.6	50.9	47.9	51.2	51.2	50.3	52.6	54.7	52.4	52.1	51.0	51.6	51.2	53.1	52.3	51.7	52.2	53.1	54.0	53.2
Brazil	45.2	44.0	46.9	49.6	50.1	52.0	50.5	50.0	50.9	50.9	51.2	53.5	52.4	51.2	53.2	53.4	52.3	50.7	49.8	50.5	51.1	50.9	51.1	52.7	52.6
Turkey	47.7	48.7	49.7	52.3	51.7	53.5	54.7	53.6	55.3	53.5	52.8	52.9	54.9	55.7	55.6	51.8	48.9	46.4	46.8	49.0	46.4	42.7	44.3	44.7	44.2
South Africa	51.6	51.3	50.5	50.7	50.3	50.2	49.0	50.1	49.8	48.5	49.6	48.8	48.4	49.0	51.4	51.1	50.4	50.0	50.9	49.3	47.2	48.0	46.9	48.2	49.0
Saudi Arabia	55.0	55.5	56.7	57.0	56.4	56.5	55.3	54.3	55.7	55.8	55.5	55.6	57.5	57.3	53.0	53.2	52.8	51.4	53.2	55.0	54.9	55.1	53.4	53.8	55.2
Russia	53.7	54.7	52.5	52.4	50.8	52.4	50.3	52.7	51.6	51.9	51.1	51.5	52.0	52.1	50.2	50.6	51.3	49.8	49.5	48.1	48.9	50.0	51.3	52.6	51.7

Source: Manulife Investments, Bloomberg. As of December 31, 2018

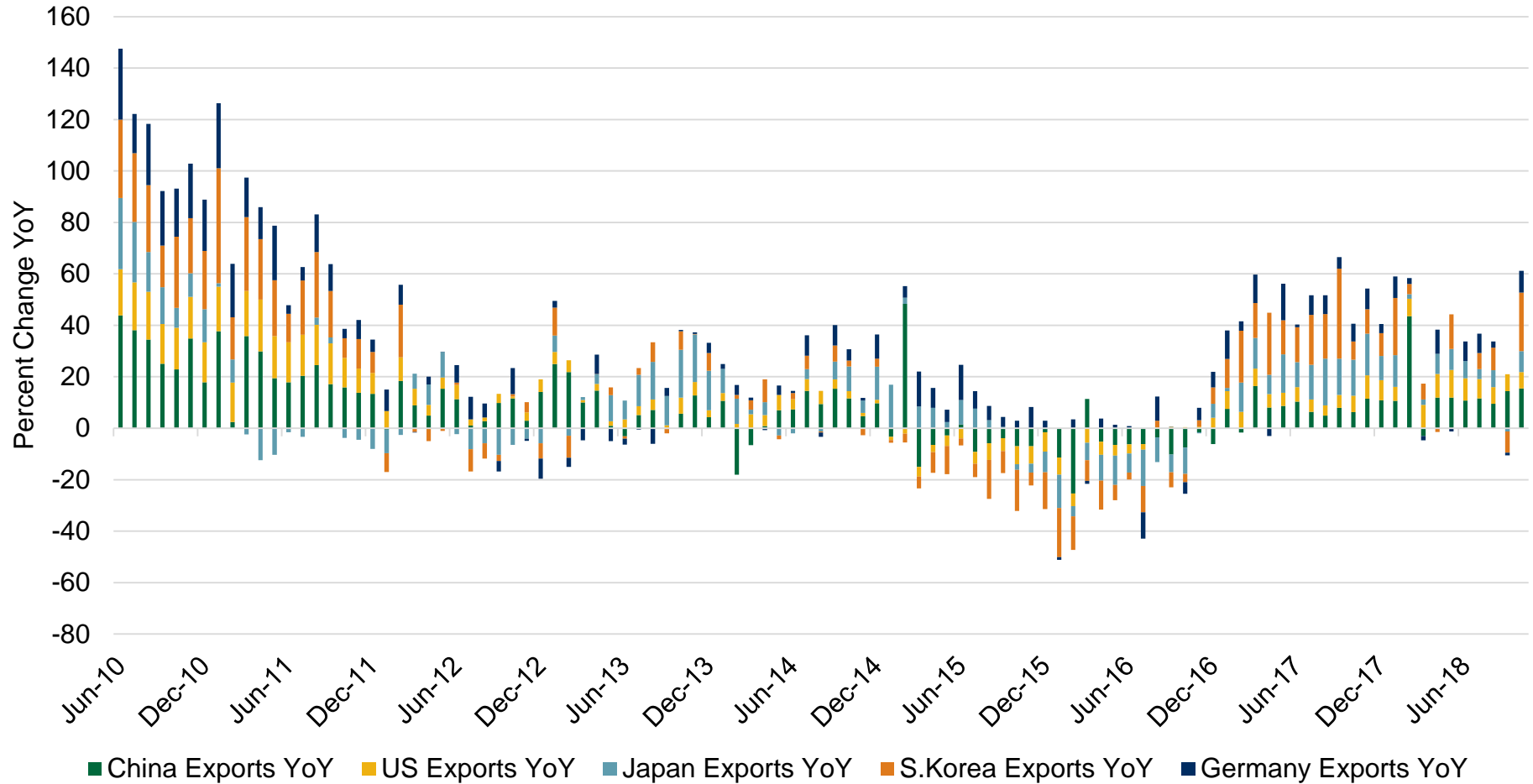
# Global Manufacturing PMI Over The Past Year



Source: Manulife Investments, Bloomberg. As of December 31, 2018

# Exports Have Held Up Well Despite Trade Wars

Year-over-Year Export Growth by Country  
2010 - Current



Source: Manulife Investments, Bloomberg. As of October 31, 2018.

# Typical Signs Of Recession Are Not Present

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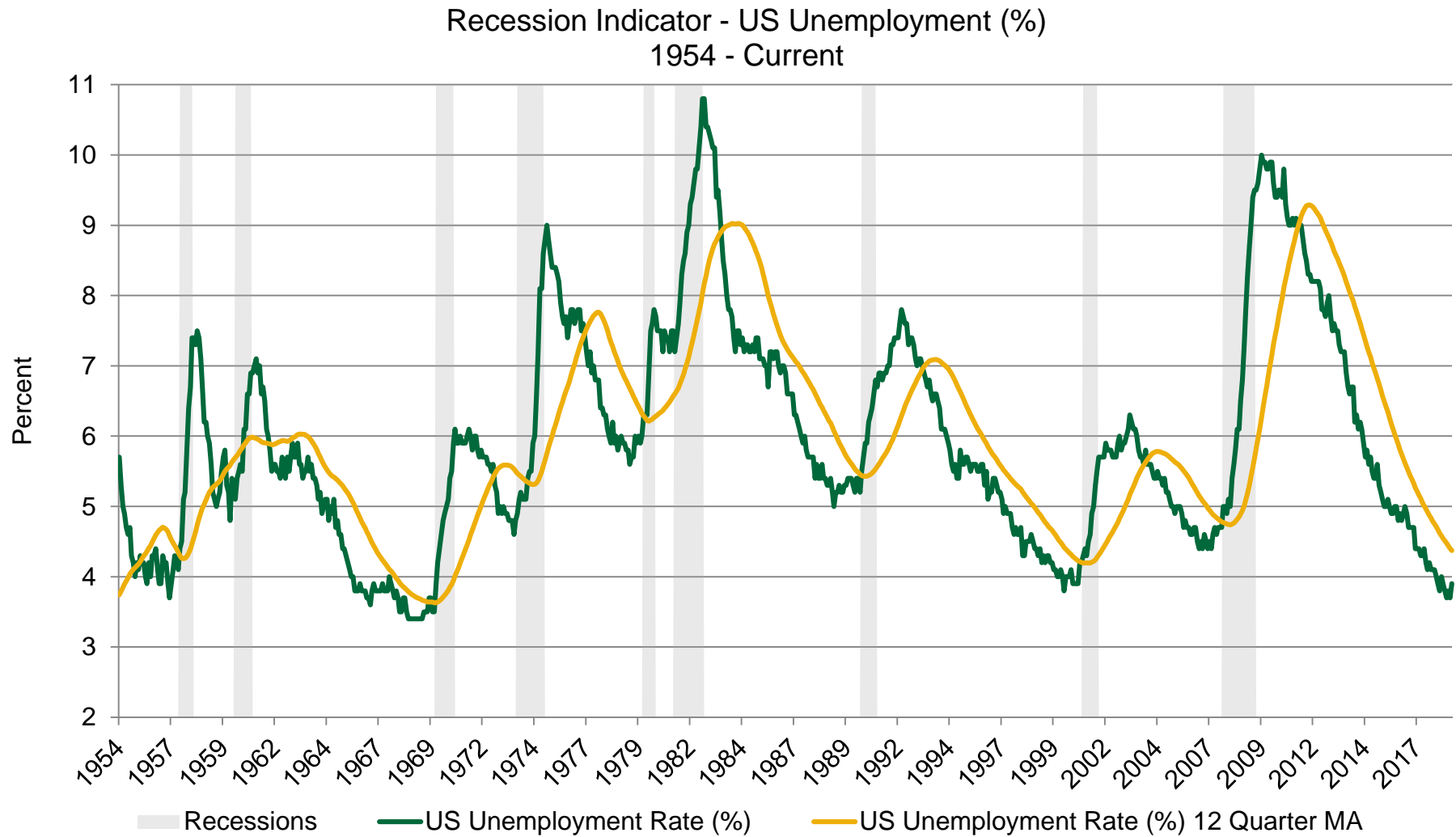
Sign of Recession	Present today
Inverted Yield Curve	No
ISM Manufacturing PMI Below 45	No
Positive Inflationary Trends	No
Capacity Utilization above 80% and peaking	No
Housing Starts Declining	No
Labor Market Weakening	No
Leading Economic Indicators Negative	No

- There are usually leading indicators to a recession, the most prevalent is an inverted yield curve.
- We continue to believe recessionary risks through 2019 remain low.
- Most bear markets coincide with recessions and therefore we do not anticipate the current market volatility to result in a bear market.

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Source: Manulife Investments. As of December 31, 2018

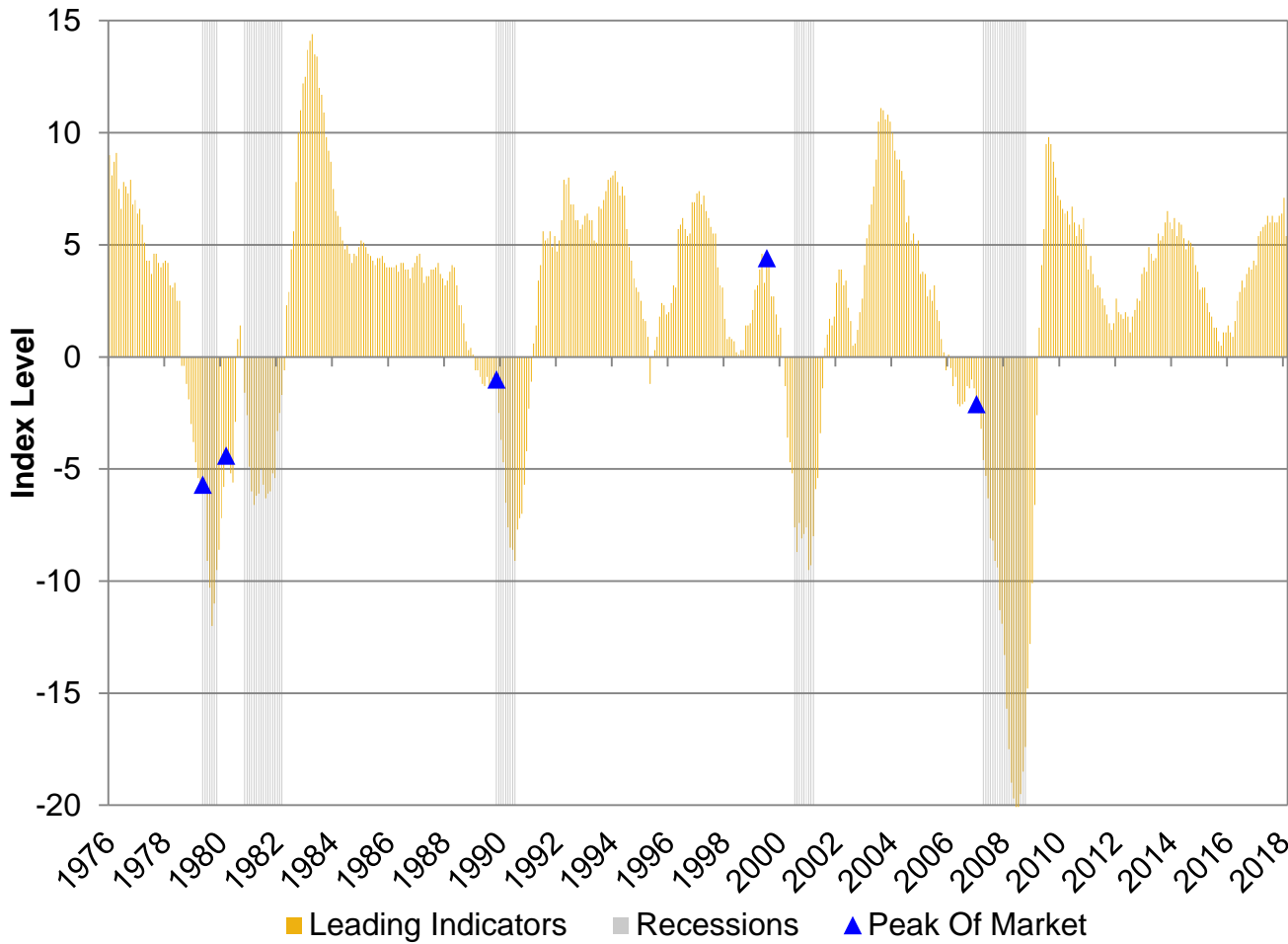
# Employment – No Signs Of A Recession



Source: Manulife Investments, Bloomberg. As of December 31, 2018

# US Expansion Remains Intact

Conference Board's Composite Index of Leading Economic Indicators  
1976 - Current



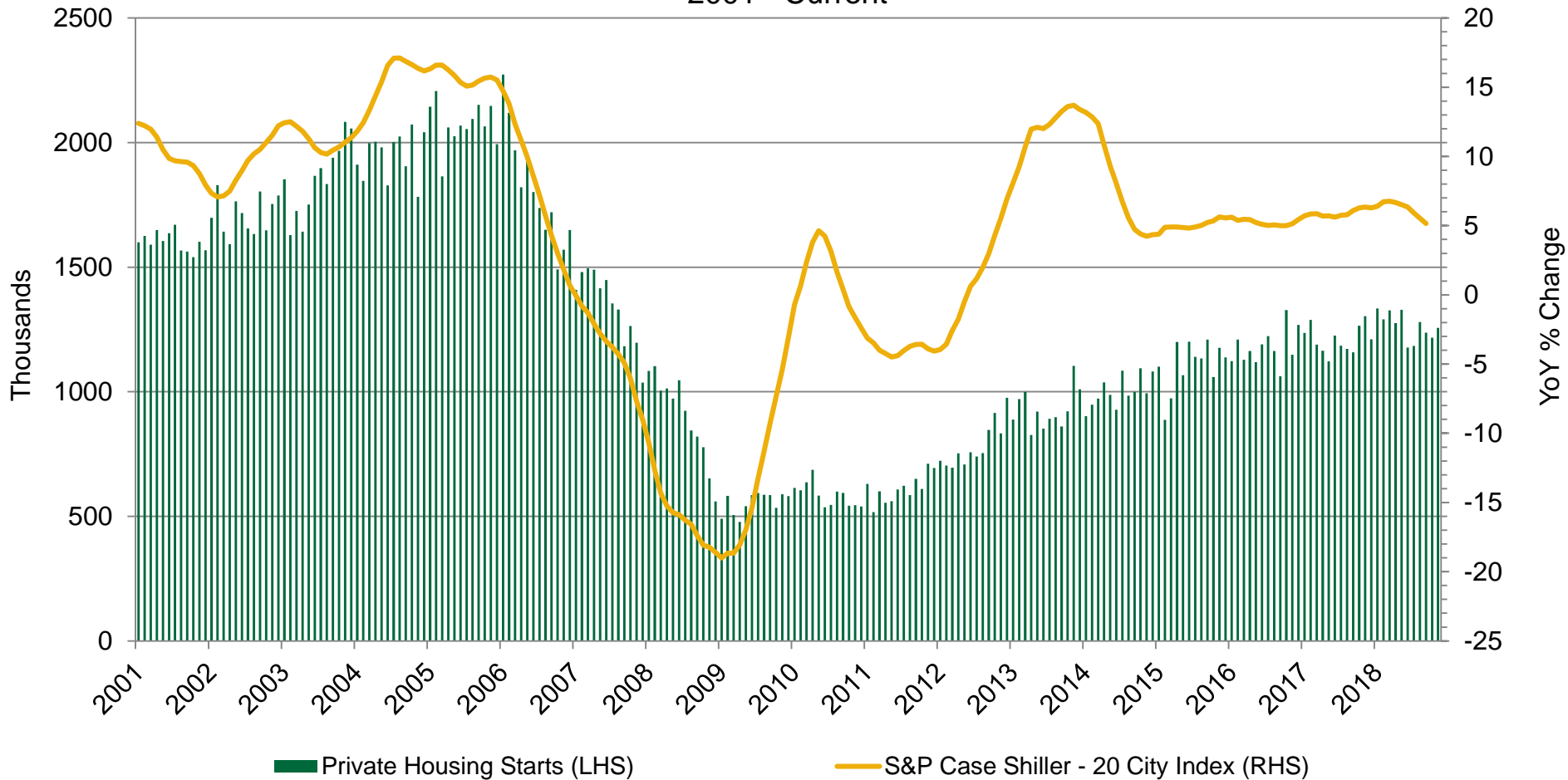
The Conference Board's  
Composite Index of Leading  
Economic Indicators  
(positive/neutral/negative)

1. Average weekly initial claims for unemployment insurance
2. Average weekly hours, manufacturing
3. Manufacturers' new orders, consumer goods and materials
4. ISM® Index of New Orders
5. Manufacturers' new orders, non-defense capital goods
6. Building permits, new private housing units
7. Stock prices, 500 common stocks
8. Leading Credit Index™
9. Interest rate spread, 10-year Treasury bonds less federal funds
10. Average consumer expectations for business conditions

Source: The Conference Board, Bloomberg. As of November 30, 2018

# US Housing

U.S. Housing Starts vs. YoY Housing Price % Change  
2001 - Current

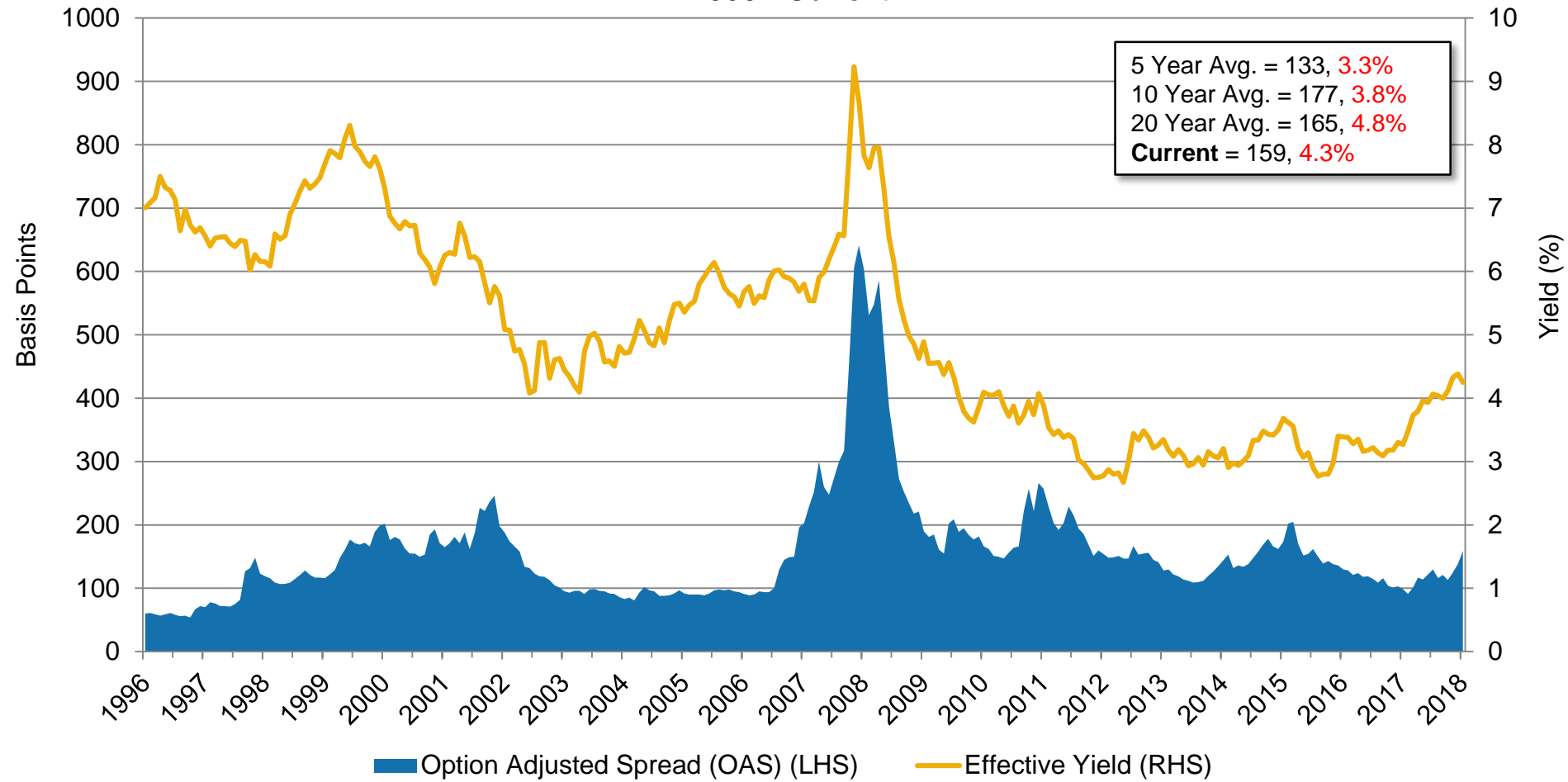


Source: Manulife Investments, Bloomberg. As of November 30, 2018



# 2019 Returns Will Be Driven By Yield

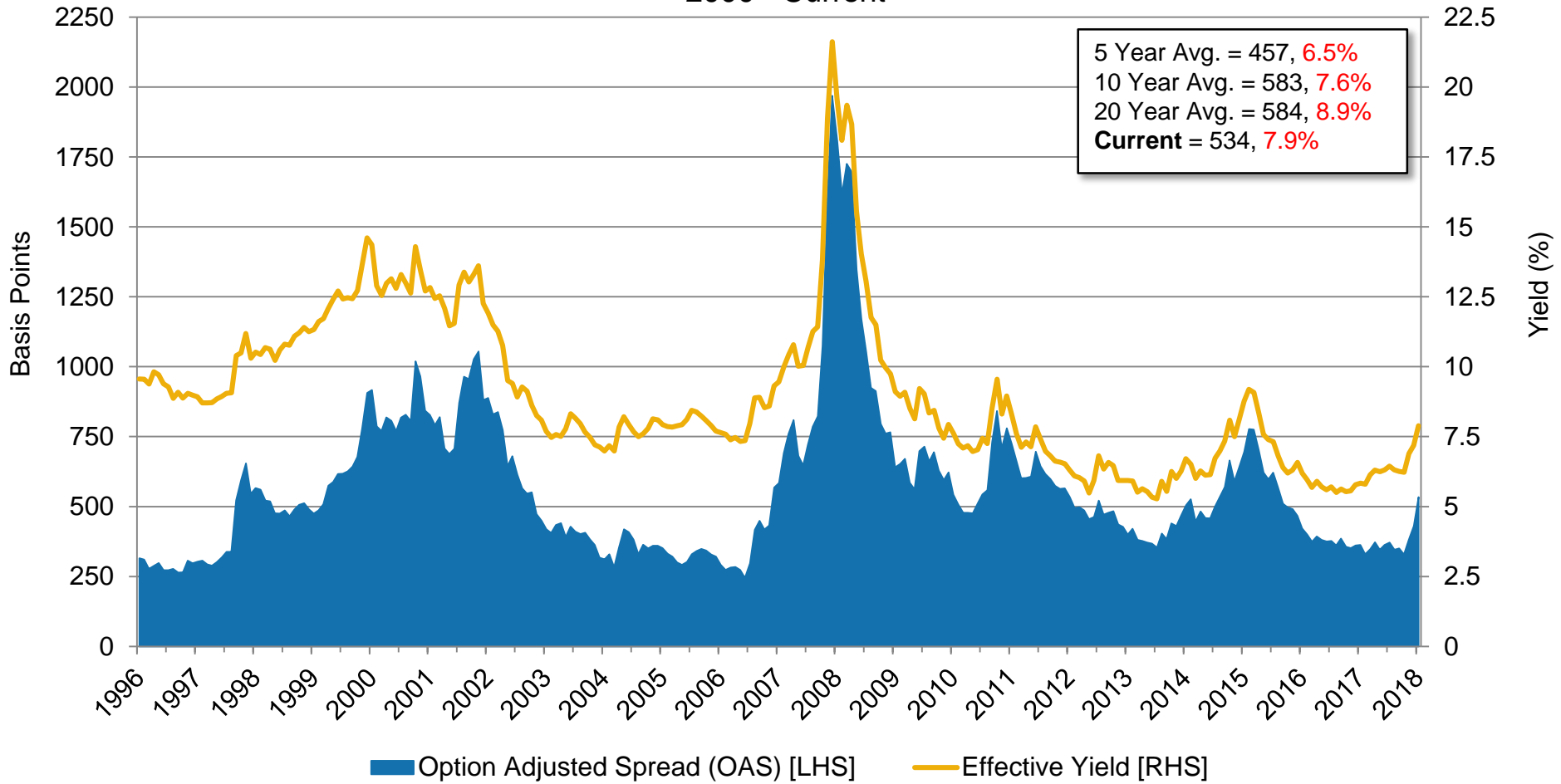
U.S. Investment Grade Corporates - Spread (OAS) & Yield  
2000 - Current



Source: Bloomberg, Manulife Investments. As of December 31, 2018

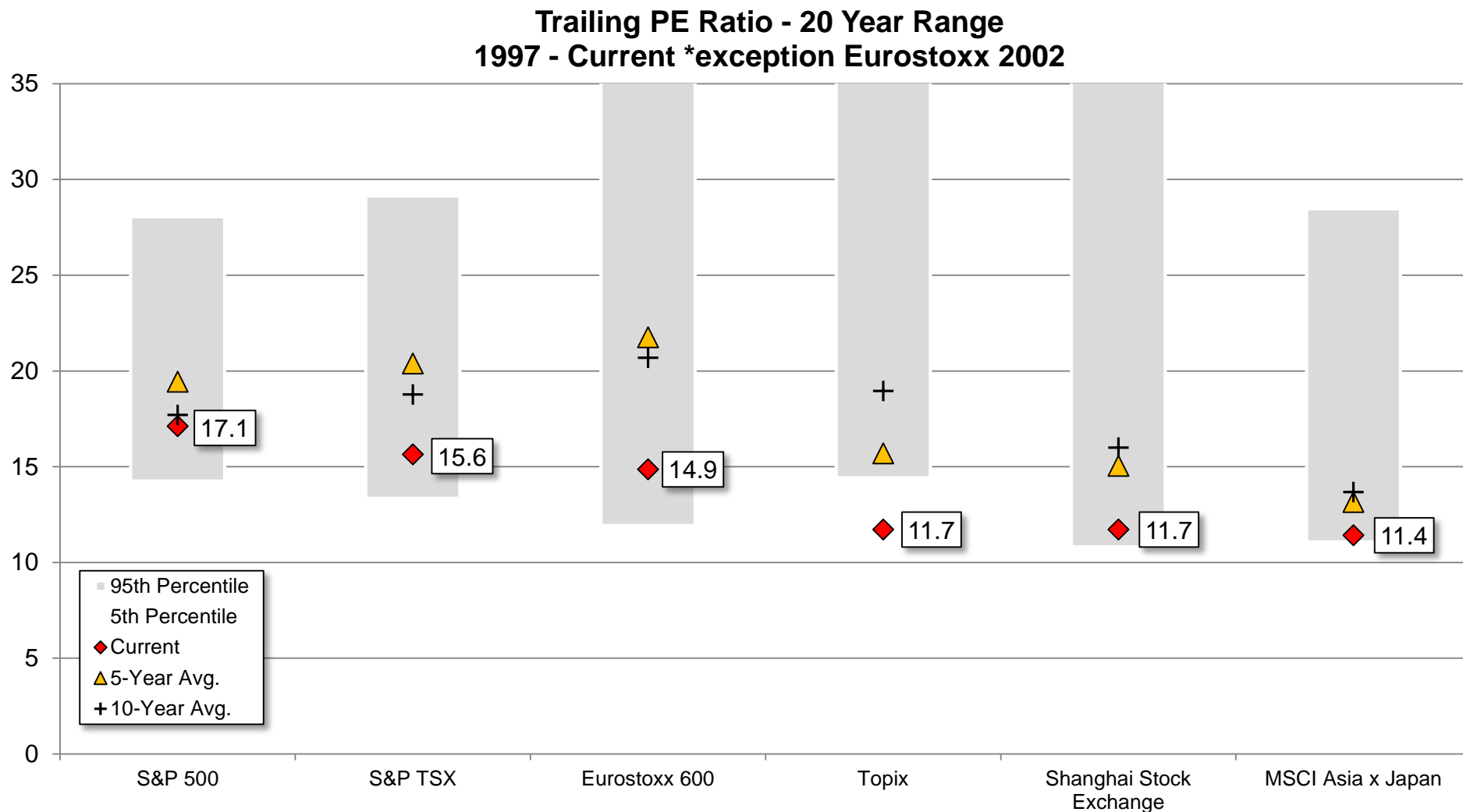
# Spread Widening Not Indicative Of Credit Event

U.S. High Yield - Spreads (OAS) & Yield  
2000 - Current



Source: Bloomberg, Manulife Investments. As of December 31, 2018

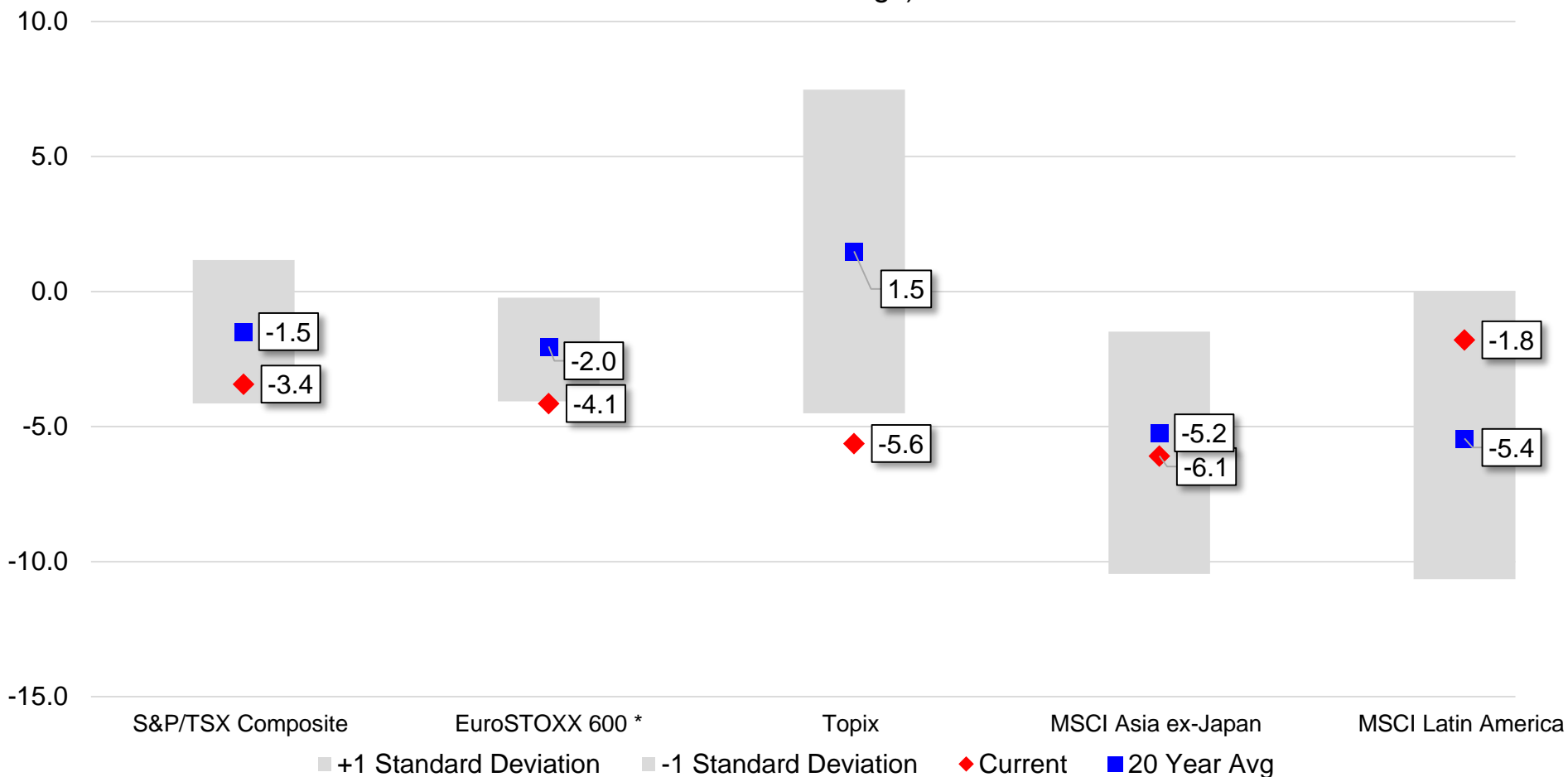
# Trailing PE Ratio From A Historical Perspective



Source: Bloomberg, Manulife Investments. As of December 31, 2018. \* 1996 – current, \* exception Eurostoxx 2002

# Canada, Europe And Japan Trading At Historical Discounts Relative To The United States

Relative Value of Global Indices to the S&P 500 Index Trailing 12M PE Ratios (Adjusted for Positive Earnings)



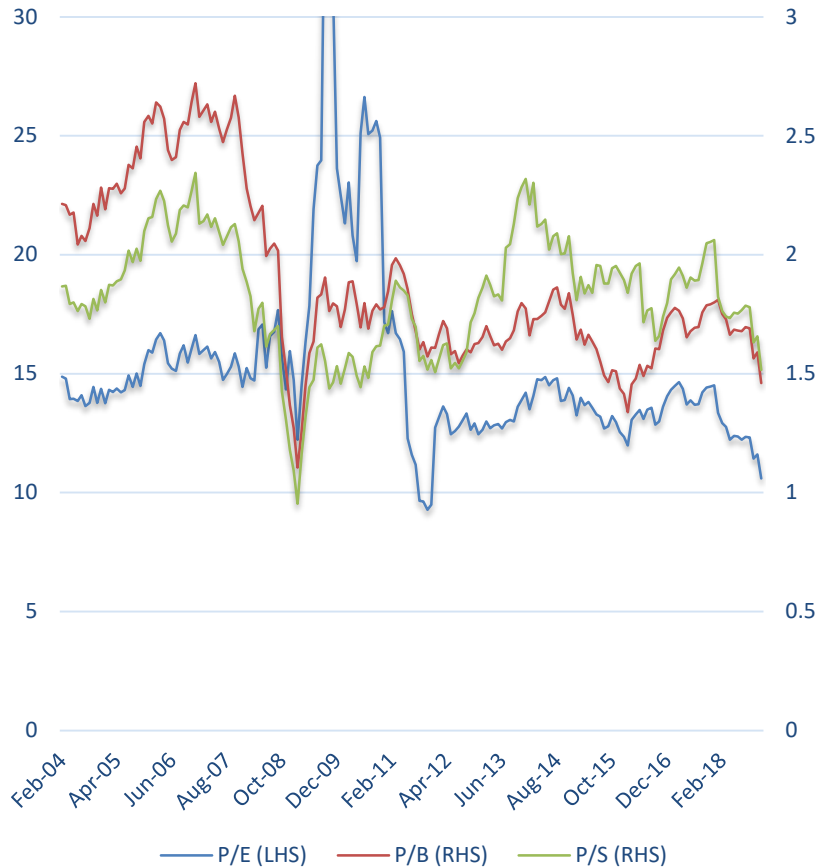
Source: Bloomberg, Manulife Investments. As of December 31, 2018. \* Eurostoxx 600 is 15 year average.

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# Canada looks attractive

**S&P/TSX Financials Sector  
2004-2018**



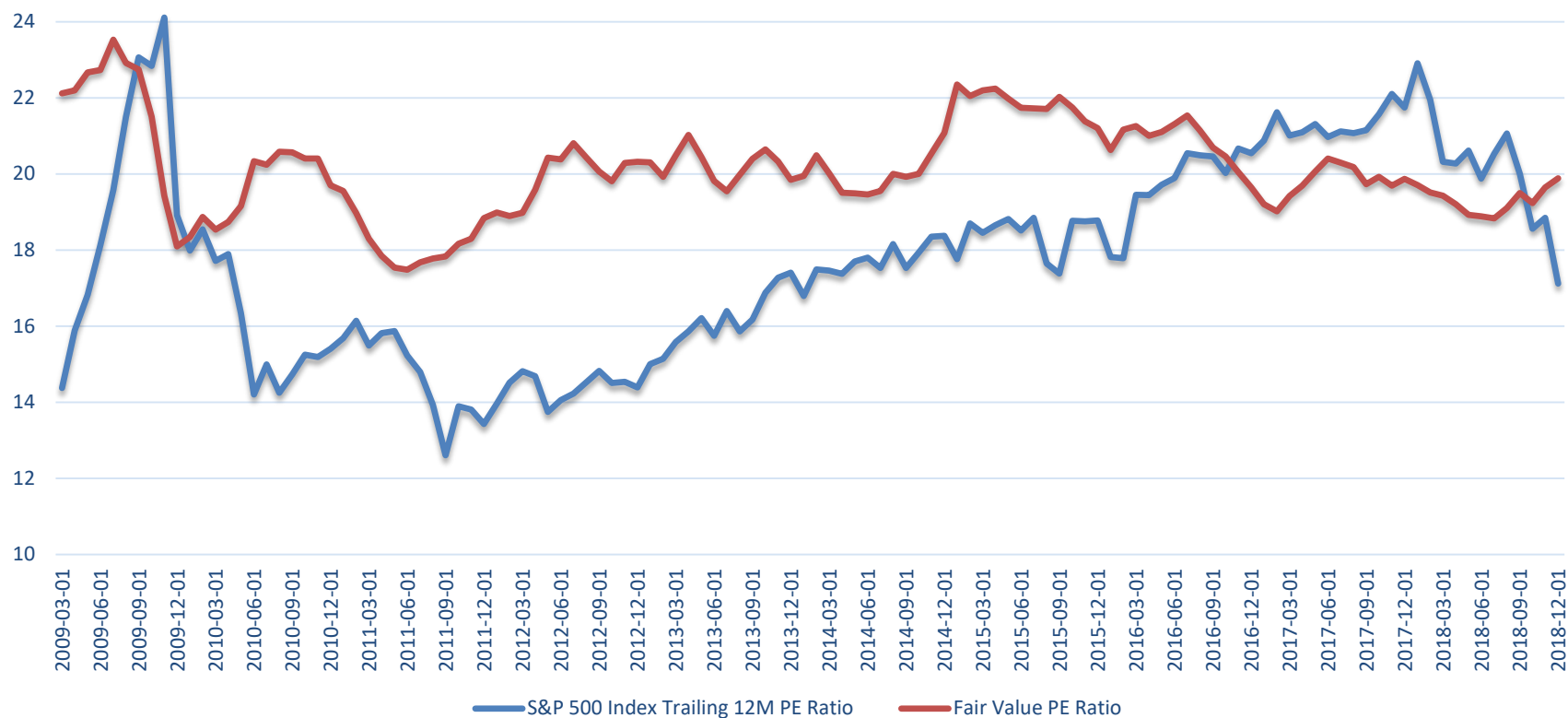
**S&P/TSX Energy Sector  
2004-2018**



Source: Bloomberg, Manulife Investments as of December 31, 2018

# The valuation pendulum has swung too far

**S&P 500 Index  
Trailing 12M PE Ratio vs Fair Value Model  
March 2009-2018**

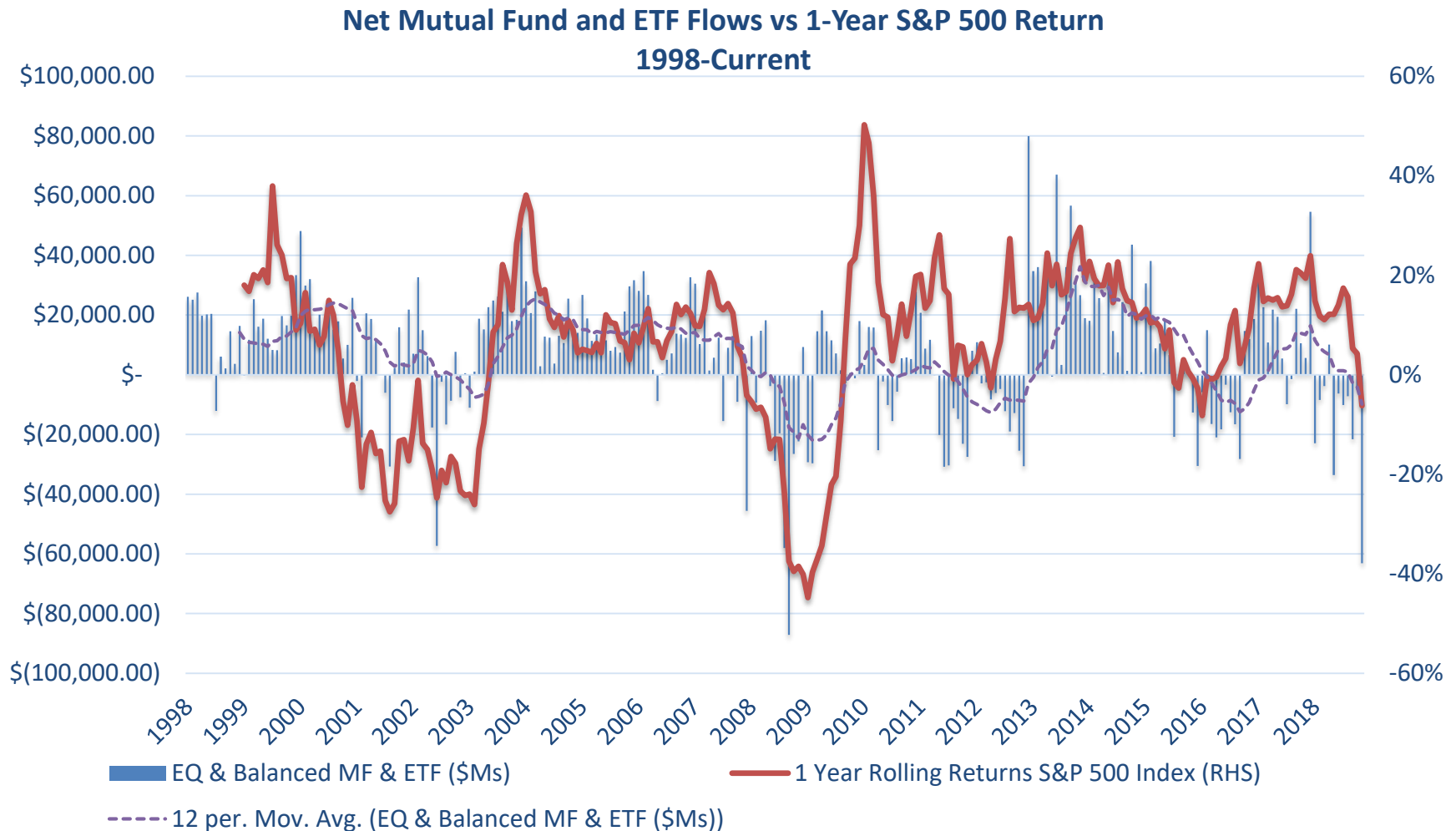


Source: Bloomberg, Manulife Investments. As of December 31, 2018.

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# Retail Investors are acting as if its 2008

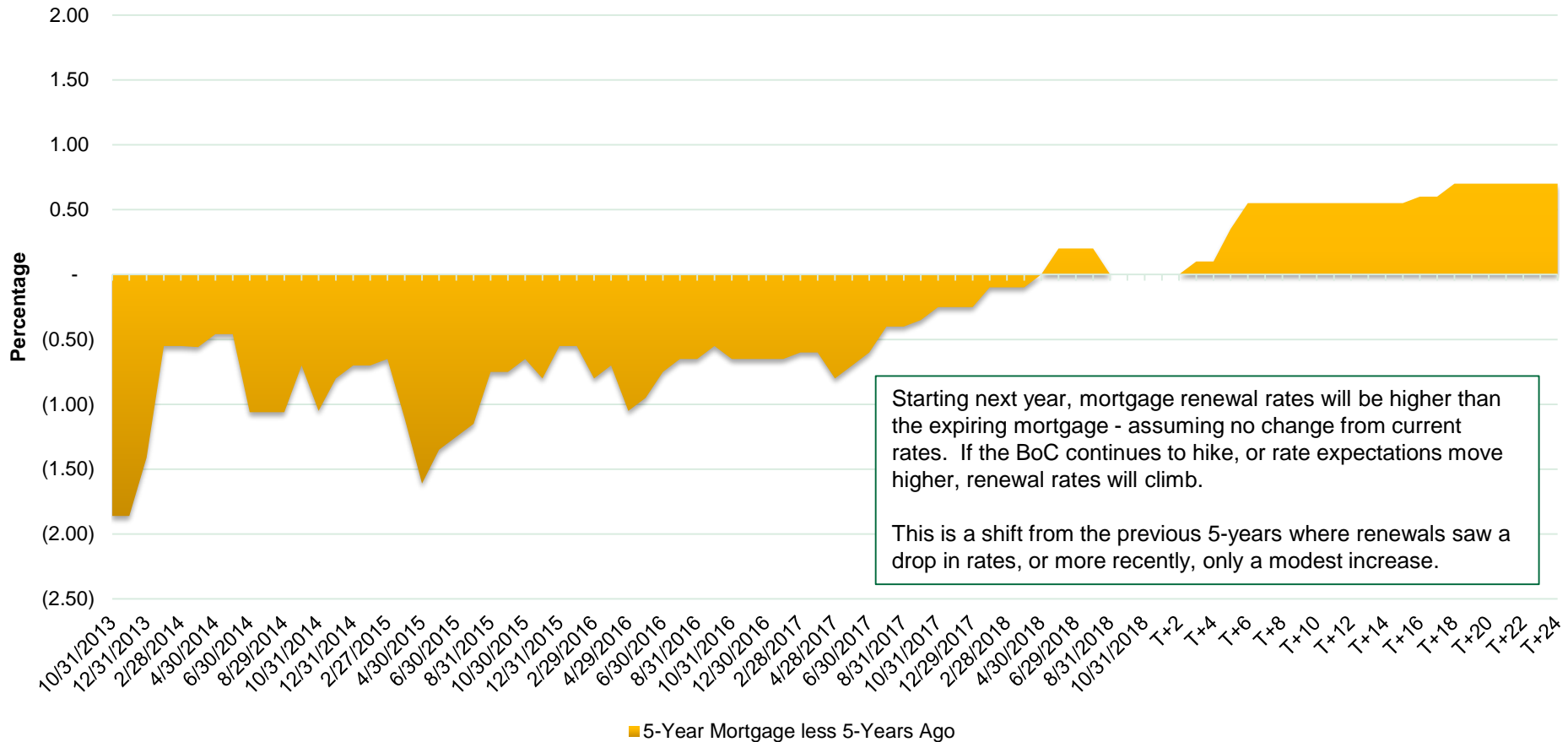


Source: Bloomberg, Manulife Investments. As of December 31, 2018.

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# The Canadian consumer faces headwinds

## 5-Year Change in Bank of Canada 5-Year Conventional Mortgage Rate 2013 - 2020 (estimated)

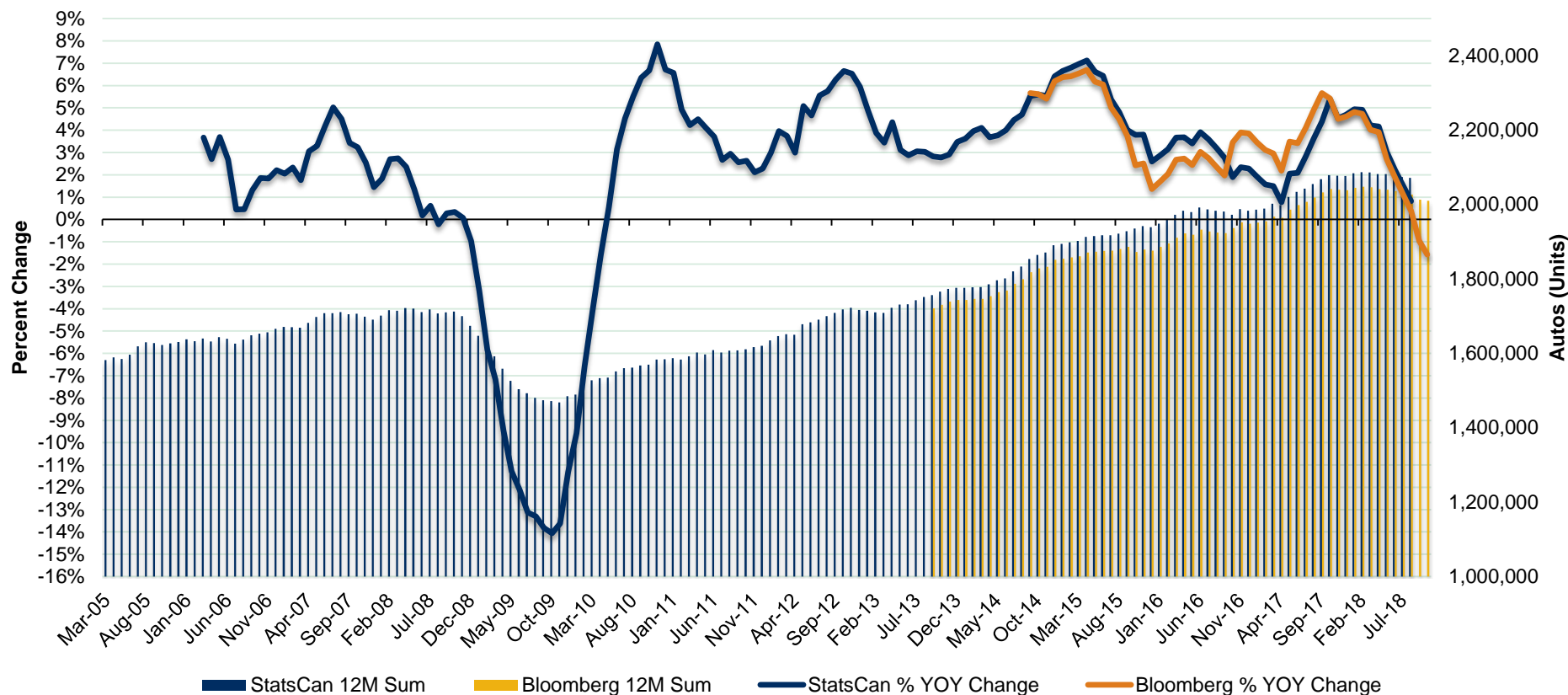


Source: Manulife Investments, Bloomberg. As of October 31, 2018



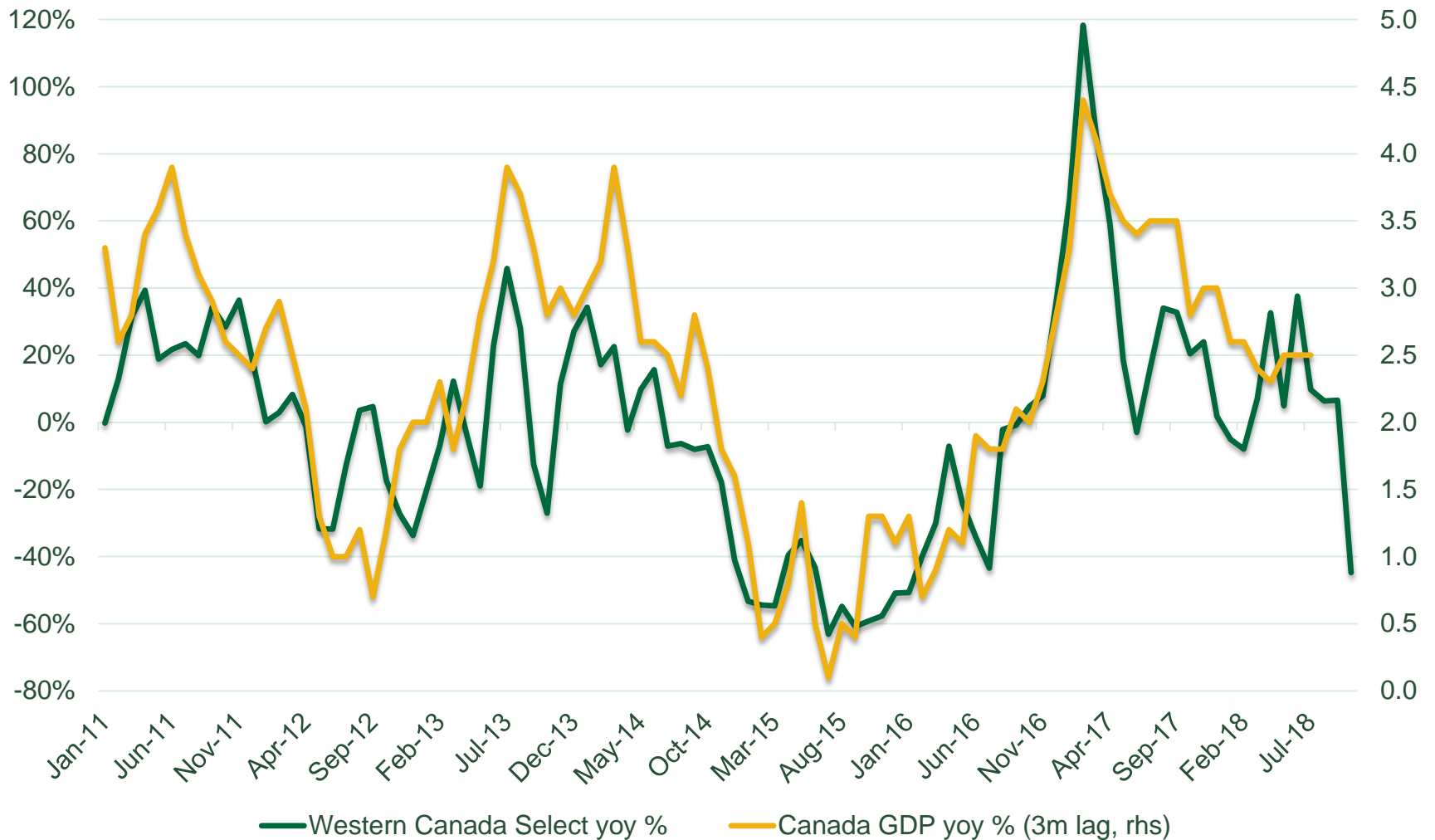
# Auto sales - the “Camry” in the coal mine

**Canadian Auto Sales  
12M Sum vs YOY Change  
2005-Current**



Source: Manulife Investments, Bloomberg and Statistics Canada. As of October 31, 2018.

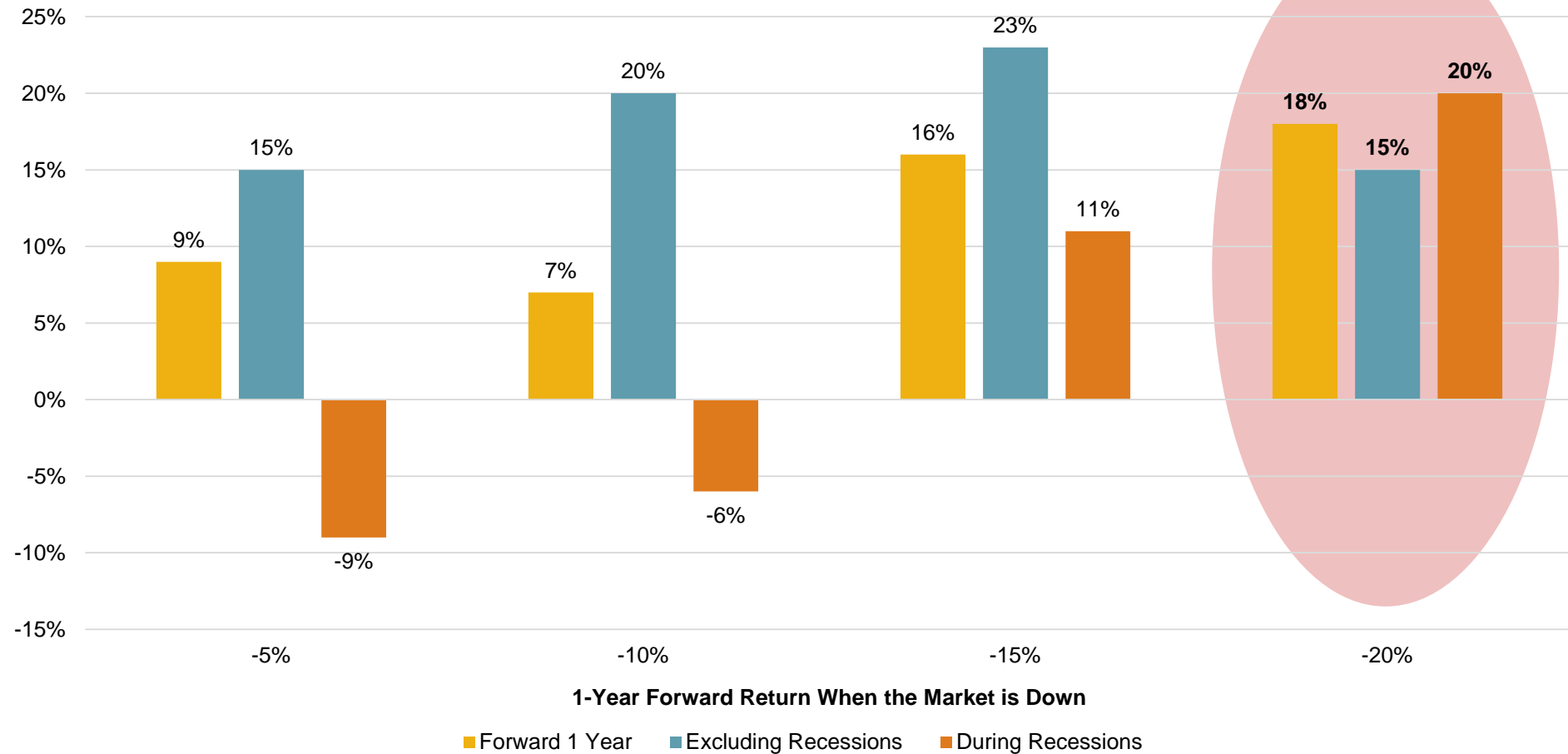
# Canadian Economy Correlated With WCS



Source: Manulife Investments, Bloomberg. As of October 31, 2018

# History Would Suggest Investors Can Profit From The Dip

Average 1-Year Forward Return following Corrections  
1987-2017

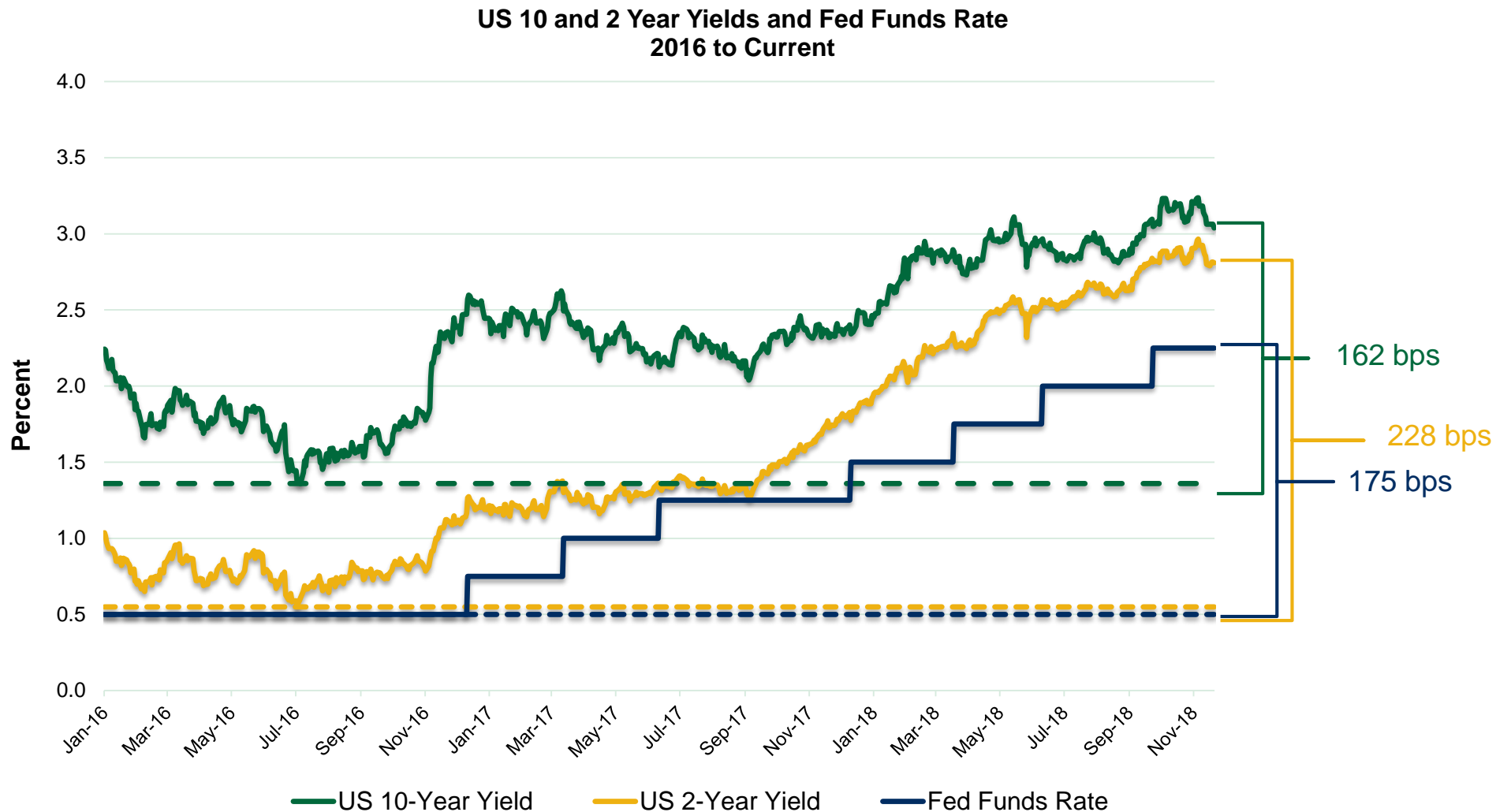


Source: Manulife Investments, Bloomberg. As of January 31, 2018

# Fixed Income - The Return Profile Looks Much Improved In 2019 And Beyond



# Do You Believe Rates Will Go Up As Much As They Have Come?



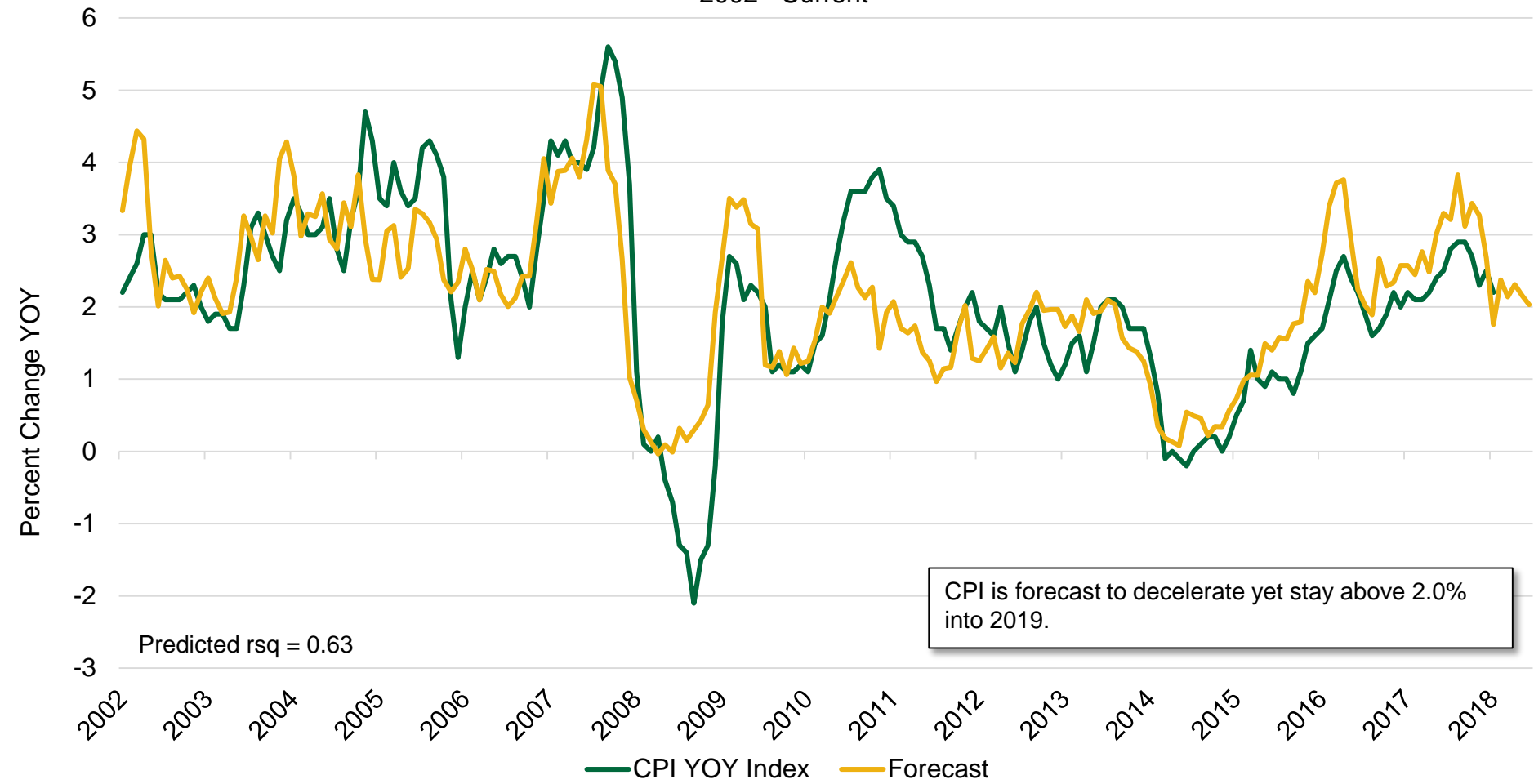
Source: Manulife Investments, Bloomberg. As of November 30, 2018

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# The Inflationary Impulse Is Behind Us

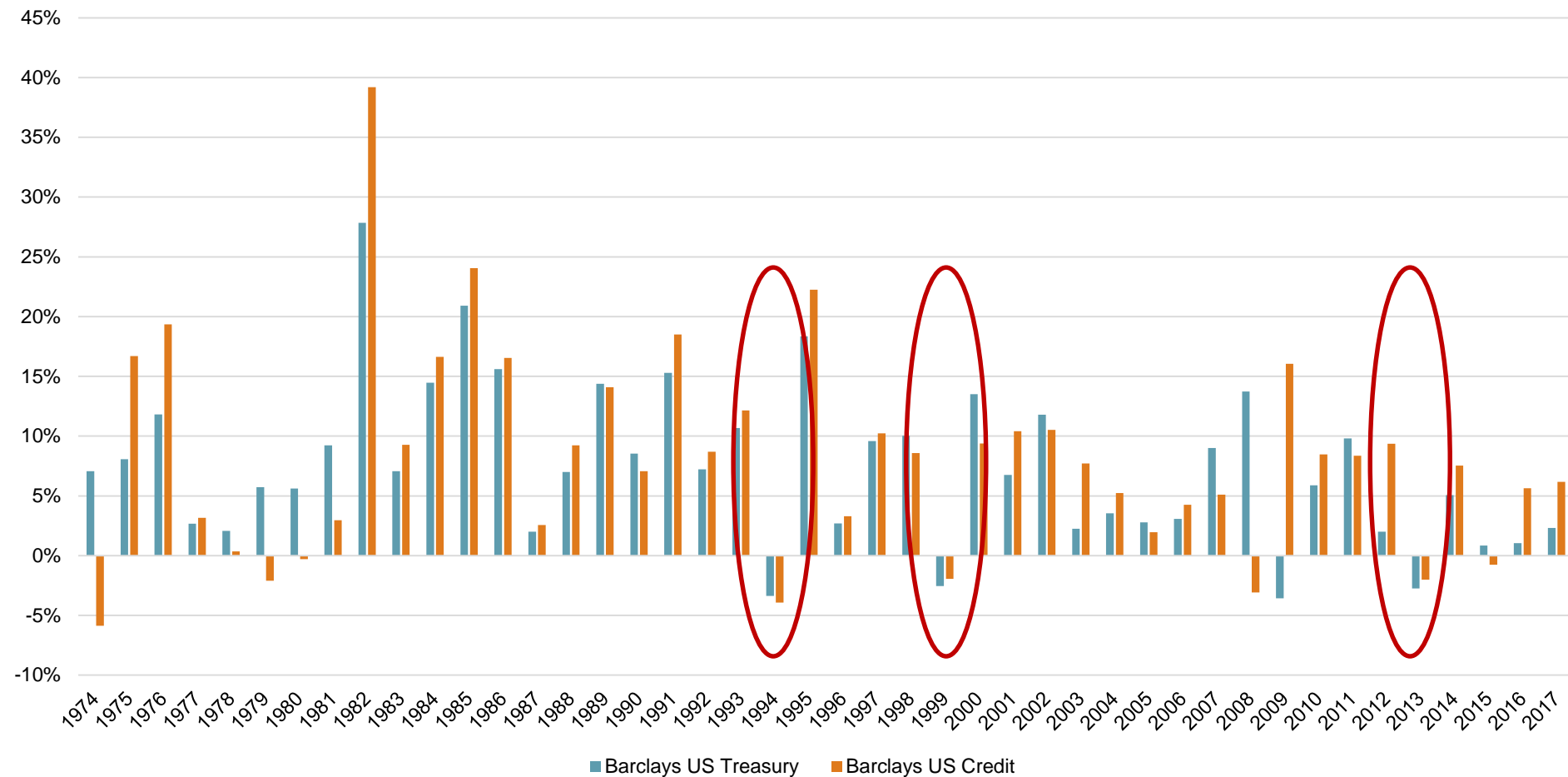
Forecast CPI vs. Actual CPI  
2002 - Current



Source: Manulife Investments, Bloomberg. As of November 30, 2018

# Can You Spot The Bond Bear Market?

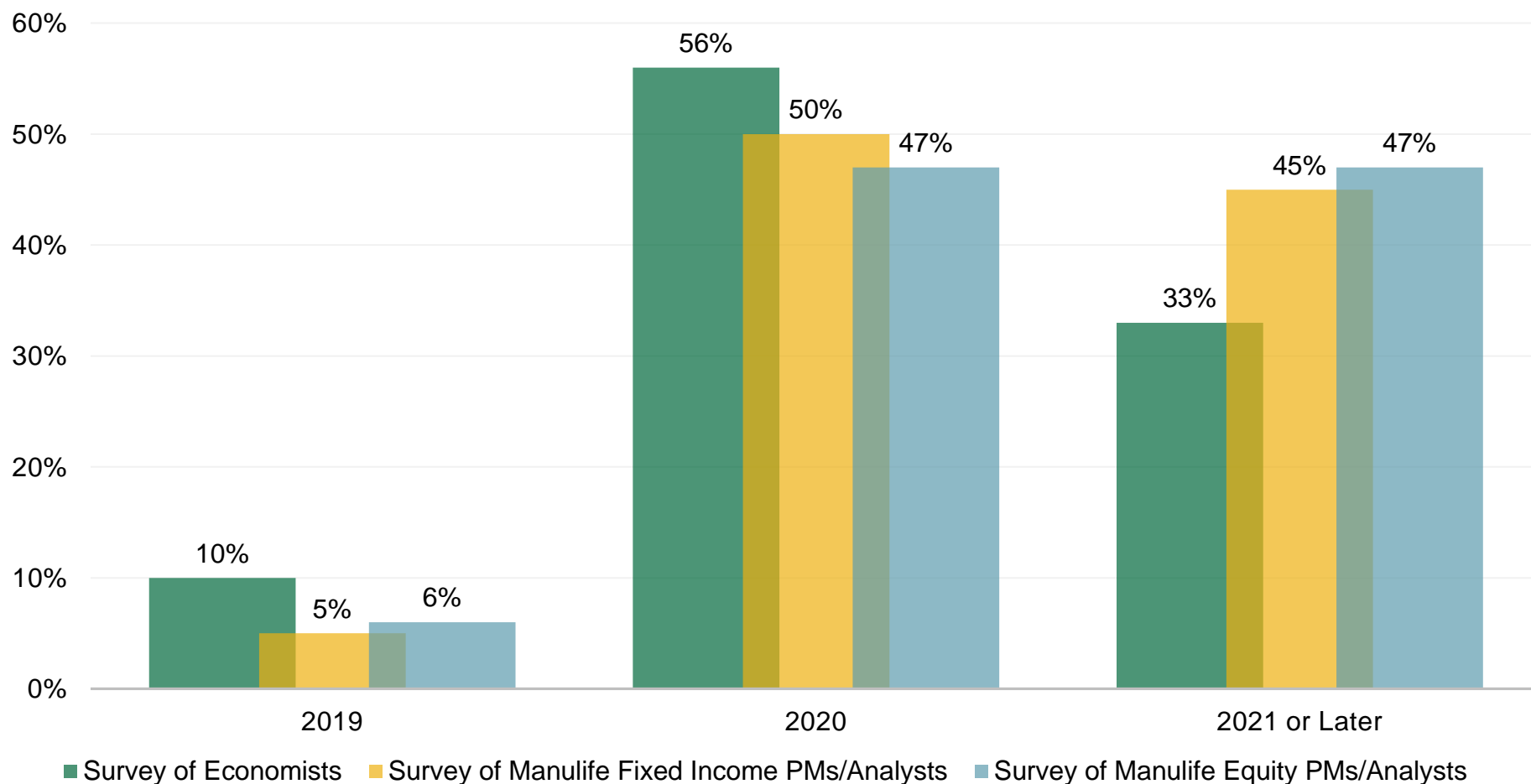
US Treasury and Credit Index Returns  
1974-2017



Source: Manulife Investments, Bloomberg. As of September 30, 2018

# When Do You Think The Next Recession Will Begin?

Survey: “When will the next recession begin?”



Source: National Association of Business Economics, Manulife as of November 2018



# Travel with Caution, Not Fear

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Fundamentals have slowed but are NOT recessionary

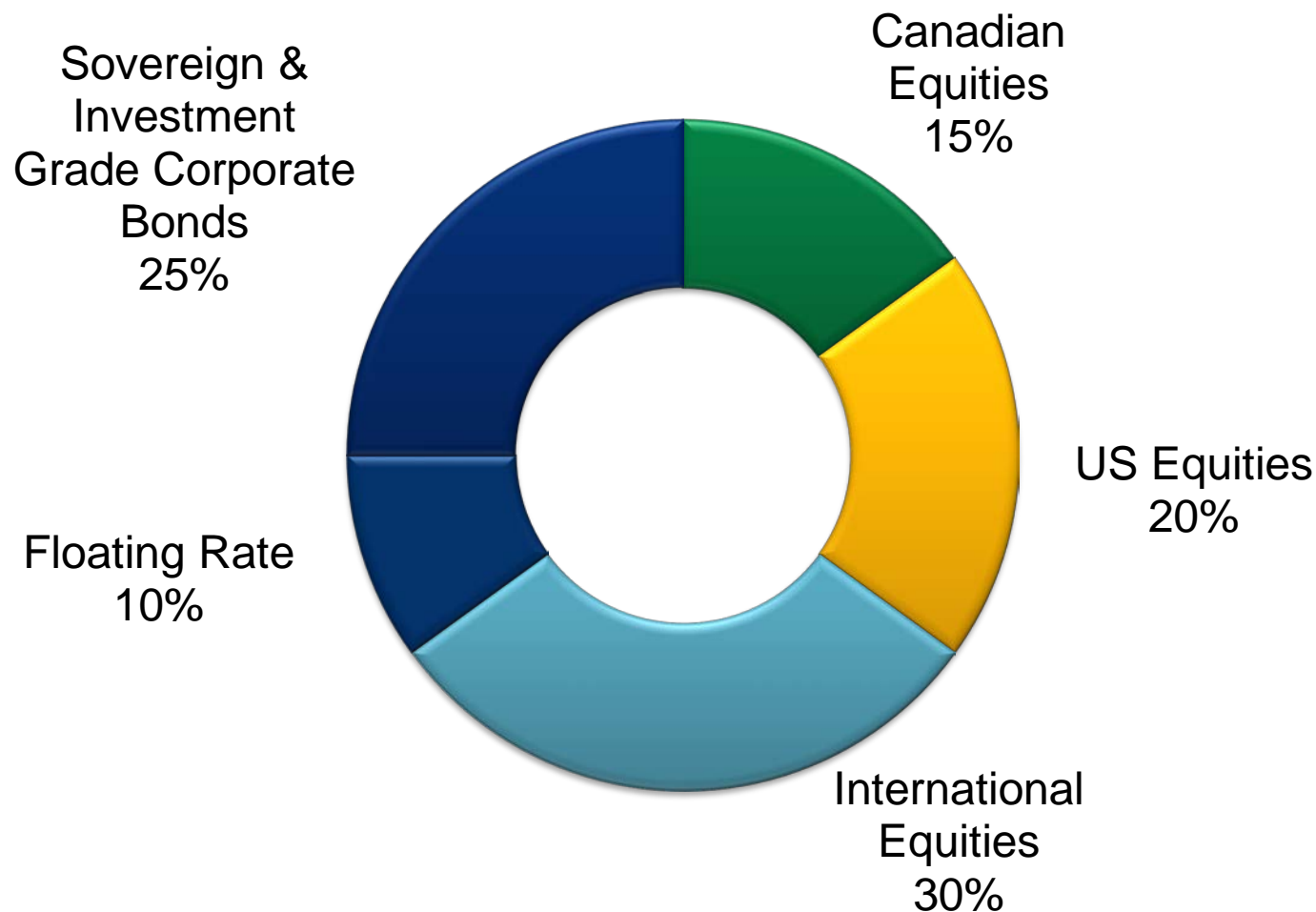
Earnings have peaked, but will NOT be negative

Valuations are attractive

Investing is a probability based decision – probabilities are on investor's side at this point

# Capital Markets & Strategy Model Asset Mix

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Source: Manulife Investments. As of December 31, 2018

# How to Stay In Touch



## Market Intelligence

Client friendly quarterly market overview (PDF)



## Exclusive Monthly Email

Contact us to be added to the distribution list



## in\*vest\*ments : Unplugged

Podcast



## Quarterly Market Intelligence videos

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