Market Commentary
Third Quarter 2018

PICTON MAHONEY Asset Management

Synergy American Corporate Class

The U.S. economy appears to be firing on all cylinders. Leading indicators like Institute for Supply Management (ISM), Manufacturing Purchasing Managers Index (PMI) and consumer confidence are at cycle highs while small business confidence hovers at an all-time high. In labour markets, the Job Openings and Labor Turnover Survey (JOLTS) quit rate (rate of people quitting their job, presumably to pursue a more rewarding one) is at a cycle high, responding to JOLTS job openings which are at an all-time high. Commensurately, initial jobless claims are the lowest since 1970 and, adjusted for population differences, are at an all-time low. Tightness in the labour market could be the last shoe to drop in an inflation watch that has been ongoing far longer than once thought.

As the world slowly moves from Quantitative Easing (QE) to Quantitative Tightening (QT), it would be much easier if the transition occurred in an environment of sustained global synchronized growth. But not everyone is on the same footing. Growth rates in the Eurozone and emerging market economies have slowed notably, quelling any urgency to normalize monetary policy by moving in lockstep with the U.S. Federal Reserve (Fed) on the rate hiking path. A strengthening U.S. dollar is an obvious concern, but we believe rising interest rates on their own may prove a more systemic concern.

Should the Fed see continued inflation risks, short-term rates could exceed the neutral rate and the risk of yield curve inversion is front-and-centre. We will be closely monitoring the market's expectations for future Fed rate moves via the ratio of 18/3-month Fed Funds Futures. When this ratio turns negative, market participants are reflecting the view that the Fed has hiked too much and the implications could be grave.

Synergy American Corporate Class (Class F) returned 5.8% during the quarter. Our underweight positioning in information technology and overweight in real estate detracted from performance. The largest individual detractors were E*TRADE Financial Corporation and Wynn Resorts. Our underweight positioning in consumer staples and overweight in health care added to performance. Top performing holdings were HealthEquity and Progressive Corporation.

In broader macroeconomic trends, for some time now, we have noted divergences in the global synchronized growth narrative that was prevalent in 2017. The U.S. economy seems to be firing on all cylinders while many developed and emerging economies worldwide exhibit some unease in marching along the interest rate hike path which the U.S. Federal Reserve seems to have set. Issues in emerging economies like Turkey and Argentina and in developed economies like Italy should not be thought of in isolation – rather, they are indicative of the trouble the world may have adjusting to higher interest rates. In this context, we continue to believe there will be ample opportunity for decisive allocations in the near-term, but a broader risk management mindset will ultimately benefit investors as the world bides time until the next global recession. For now, we remain constructive, but are increasingly vigilant given our observation of deteriorating market leadership and other telltale signs of an eventual market top.

Class F Returns (in %) as at September 30, 2018	Year-to-date	1 year	3 year	5 year	10 year
Synergy American Corporate Class	14.3	22.1	12.3	15.8	10.9

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Published October 2018.