



## Rallying Stocks Mask the Growing Risk of a Market Correction

### Description

Stocks continue to defy gravity, rebounding from last week's minor market correction as investors pile into stocks in the anticipation of a stronger economy.

Nonetheless, growing fears of an impending major market correction just got a shot in the arm because controversial investment bank **Goldman Sachs** recently stated that equities are facing a high risk of a correction.

Surprisingly, Goldman Sachs believes that it won't be politics that trigger the next correction, but rather a decline in the momentum of economic growth.

You see, there are signs that equities are overpriced with the exuberance surrounding Trump's proposed economic stimulus, propelling them to record highs, despite not yet having any significant policies introduced. It also appears that markets have priced in some steep valuations for equities, while ignoring the potential impact of Trump's more radical policies, the difficulty of implementing the planned stimulus, and the underlying economic data.

### Now what?

In an [earlier article](#), I discussed that equities are expensive because valuations have decoupled from economic reality. If anything, it appears that markets have overestimated Trump's ability to boost economic growth through the implementation of extensive fiscal stimulus, considerable deregulation across many industries, and hefty tax cuts.

In the words of a Goldman Sachs analyst: "If you look at some of the more cyclical parts of the market which are very sensitive to these valuations, they really ran ahead of macro data."

The bad news doesn't stop there.

Trump's economic vision is certainly not a coherent, well-thought-out program. The contradictions are clear with his stance on trade and immigration likely to impact the U.S. economy.

Any attempt to significantly increase spending while aggressively slashing taxes would cause a massive blowout in the U.S. federal deficit, which some analysts have estimated to be as high as US\$10 trillion over the next decade. If this occurred, it would drive interest rates higher, raise the spectre of stagflation in an economy already close to full employment, act as a drag on private sector investment, and possibly even trigger a full-blown financial crisis.

Any of these events would not be good news for stocks with the fallout affecting global financial markets.

There are also significant impediments to the implementation of many of Trump's economic policies. While he can enable many through executive orders, he can't do so with the federal budget. It is controlled by Congress; despite being a Republican-dominated house, it has shown itself to be notoriously resistant to incurring massive budget deficits.

A lapse in the implementation of any of these policies would dull the momentum for economic growth, and this would be further magnified by a stronger U.S. dollar, higher interest rates, and trade tariffs all causing inflation to spike. This will be the catalyst for the next major correction as real economic fundamentals fall short of the overoptimistic expectations priced in by the market.

### **So what?**

As investors are all too painfully aware, any correction in U.S. equity markets would spill over into markets across the world, including Canada. Investors need to prepare themselves for a sharp market correction.

Businesses that provide necessary goods and services, such as water and electric utilities, are typically resilient to economic downturns and market crashes. This is because they operate in highly regulated industries with steep barriers to entry which enjoy regulated or contracted cash flows.

Furthermore, the goods and services they provide remain in demand regardless of the state of the economy.

A classic defensive stock which possesses these attributes is diversified electric and natural gas transmission utility **Canadian Utilities Limited** ([TSX:CU](#)). It derives a considerable proportion of its earnings from regulated sources, giving them a degree of predictability. This certainty has allowed Canadian Utilities to hike its dividend for an extremely impressive 45 years straight. It now rewards investors with a tasty and sustainable yield of just under 4%.

### **CATEGORY**

1. Investing

### **TICKERS GLOBAL**

1. TSX:CU (Canadian Utilities Limited)

### **PARTNER-FEEDS**

1. Msn

2. Newscred
3. Yahoo CA

**Category**

1. Investing

**Date**

2025/08/26

**Date Created**

2017/03/31

**Author**

mattdsmith

default watermark

default watermark