# QUARTERLY COMMENTARY

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## Brighter Skies

As expected, North American markets have powered through all of the negative news in the last quarter so that they are now making all-time highs. While a strong third pandemic wave is upon us and lockdowns abound, investments continue their positive run. There are always going to be problems that investors can focus on – China's aggressive moves in the Far East, attacks on the Natanz nuclear facility in Iran, the pandemic continuing to rage on in many countries and Canada being far behind many others with regard to the vaccine rollout. Barring an unforeseen event though, I think it should be clear by now that the economy and stock market have moved on from COVID. Even though we're nowhere near being back to normal, the markets which forecast what's to come see brighter skies ahead.

The most recent news of the Johnson & Johnson and AstraZeneca vaccines having potentially serious side effects in a small population of recipients hasn't put a damper on things. The market didn't seem to care and the U.S. authorities quickly switched to administering other vaccines instead. It's a far cry from times last year when any negative COVID news could cause stocks to tank. Of course that doesn't mean that we're all the way back – there's a lot of work to be done still but once the majority of the population is vaccinated in the next few months we will see more of a return to normalcy as far as business is concerned. There has been an improvement in the economy and we are now seeing a pickup in inflation data with CPI in the U.S. for March coming in at a 2.6% 12-month change and in Canada a 1.5% increase but, again, the market seemed to be expecting it and it didn't produce much in the way of concern. That's a good sign since other than a true black swan event that can't be predicted, I think inflation is the number one risk to the stock market.

It can eat into company earnings and raises the risk that the Fed will have to raise rates sooner than the market expects, but Powell and Yellen continue to say the right things to keep investors happy.

I admit that I have had some concerns about the market especially after such a huge comeback from last March. Stocks have become pretty expensive and it’s difficult to find good value. But the resilient grind higher that we’ve seen over the past couple of weeks is consistent with a strong bull market and as they say – “the trend is your friend”. Indeed, the stock market has had every opportunity to decline from a valuation, technical, and sentiment standpoint this year, and while that has produced pockets of severe selling, it has not resulted in the kind of broad market correction that is typical. What is happening is what we call rotation – when certain sectors start to sell off and others become the focus of buying – such as the large cap tech stocks coming down a little and financial companies and resource stocks going up. These underlying moves are providing a decent support for the market as a whole and it’s actually very healthy. When everything moves higher at the same time, that’s when I get more concerned.

Technology stocks almost single-handedly saved the market from disaster in 2020. It's been a different story so far this year. The Nasdaq index where most technology companies are listed gained less than 3 per cent in the first quarter. The S&P 500 Information Technology Index was up only 1.7 per cent. The Dow Jones Internet Composite Index added just 2.7 per cent. Many high-profile tech stocks lost ground during the quarter, including Amazon.com Inc., Apple Inc. and Zoom Video Communications Inc. When you compare those to the other indexes you can see the effects of sector rotation.  The Dow was up 7.8 per cent in the quarter, the S&P 500 up 5.8 per cent and here at home, the TSX gained 7.3 per cent.

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In Canada, we expect the slow progress on vaccinations and renewed lockdowns following a third wave of COVID-19 to likely hold back the economic recovery in the first half of 2021. However, we expect robust fiscal support provided to date, highly accommodative monetary policy, and strong gains in commodity prices, to bode well for the outlook in H2/2021. The consensus expectation for real GDP growth in Canada is 5.0% in 2021 (versus the 30-year average of 2.0%). Even though we are now totally mired in debt with all the support that has been doled out, in the upcoming budget I would be surprised to see any major change in taxation to capital gains – that will probably come in the next budget <u>after</u> the next federal election.

The quarterly Bank of Canada business survey painted an upbeat picture of the economy. Business sentiment has been improving steadily after a very difficult year. It seems hard to believe especially with all of the shutdowns, but consumers have adjusted incredibly fast to the conditions imposed by Covid with online purchases and shopping in person within the more restrictive store schedules.

If you talk to most individual investors, many of them are scared to death believing a recession or even depression is just around the corner. Therefore, they are sitting on WAY too much cash as they watch the equity markets dance higher. As Stan Salvigsen (Comstock Partners) used to say: If you want to catch a wave, you have to grab a surfboard and get into the water. The same can be said about the stock market – you have to grab a "board" and get wet! Jamie Dimon, the famous CEO of JP Morgan Chase said in his letter to investors released this week, because of massive stimulus and pentup demand from the pandemic, the U.S. is looking at potentially historic acceleration in economic growth over the coming quarters, and that growth should lift those companies in cyclical sectors most, but it should also create a rising tide that helps all risk assets (including tech).

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Sometimes investors gravitate toward what’s worked for them in the past or they see the hottest trend and want to jump onboard with everybody else. This happens especially when they have doubts about the strength or timing of an economic recovery; they’ll buy back into growth and expensive tech stocks that benefited during lockdowns. That tendency though is often the wrong approach to take – I look at markets as live and constantly changing. You always have to look forward and if you can, recognize attractive trends that are just starting to take hold. One of those big changes is ESG which stands for environment, social and governance. All companies are becoming more aware that embracing responsibility in these areas is not only good for business, it helps them manage risk and it’s good for the planet. I’ll be talking more about this area of investing in future newsletters.

Thank you for your continued trust and confidence. Should you have any questions or concerns at any time or if you would like to have a detailed discussion of your personal portfolio please do not hesitate to let me know.

Sincerely,

Richard



RAYMOND JAMES