QUARTERLY COMMENTARY

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Full of Ups and Downs

You would think that I would be happy with every stock market rally, wouldn't you? That's not always the case however. When the markets move up in a broad fashion with most sectors and companies participating – that's a reason for optimism. But when it's led by a narrowing number of impactful stocks it's more a reason to be a little wary. Bespoke Investment Group reports that just eight stocks have accounted for more than half of the S&P 500's gain since May 12.

Last quarter the S&P/TSX Composite moved up by 8.1%. However, the small caps are still about 4% lower than they were on March 15 and only about 40-45% of stocks on the NYSE and NASDAQ are even above their 50-day moving averages. It can make reducing risk feel like the wrong decision when you see indices like the S&P 500 and NASDAQ keep pressing to new all-time highs, yet in my experience these moves are often followed by sharp retracements that can seemingly come out of nowhere if one is not paying attention. So, I feel that it doesn't hurt to be a little more cautious now even if it has sometimes felt "wrong." When we begin to see more companies participating in this steady churn upwards my confidence will increase. Historically August and September are the two weakest contiguous months of the year. Of course the stock market can also rally higher during that time - last year the S&P 500 rallied 2.8% as the result of aggressive stimulus from both the

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government and central bank. But this year government relief spending is moderating and if investors start to believe that the stimulus is set to dry up in the future, the stock market will lose some of the tailwinds that has helped it to reach all-time highs. The NASDAQ 100 has been the indisputable leader lately, thanks to it being dominated by the handful of mega-cap companies that have become this generation's "safer" blue chip stocks (AAPL, MSFT, AMZN, FB, GOOG/L, TSLA, NVDA, PYPL now account for around 50% of the NASDAQ 100). Despite US earnings season bolting out of the gate with a series of very strong reports from some of the largest US banks and industrial companies, their stocks not only failed to respond to the good news, in many cases, they turned downward as investors took profits against the news. This suggests that the advances of the last year have already priced in anticipation of strong results leaving some to wonder what it will take to reignite equities.

Over the last 20 sessions, while the S&P 500 has been making regular new all-time highs, the only three sectors that have outperformed the index, itself, are technology, discretionary, and health care. All of the other S&P sectors show negative relative performance over the past four weeks.

On July 13 the updated CPI numbers (the gauge for inflation) for the U.S. came out and they were once again higher than expected. There continues to be a tug of war regarding inflation expectations, with some arguing (like the Fed) that it will be transitory before settling back to normal, others believing that it will stay higher for longer, and then still others (like ARK's Cathie Wood) actually expecting deflation thanks to factors like technological innovation and the reversal of inventory build-ups after companies ramped up to produce goods during COVID-19. The Fed's Powell has said that the economy in the U.S. is quite a ways off before they begin to increase interest rates and they expect

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that inflation will ease in the coming months. Government relief stimulus is moderating and is expected to be reduced in late Q3 and Q4. The Bank of Canada held its policy rate steady at 0.25%, as expected but the pace of 'quantitative easing' (asset purchases) is being reduced from $3 billion per week to $2 billion per week. With regard to inflation, property owners everywhere will attest to the idea that we are in a very inflationary environment. It's great for our personal balance sheet but whether the rise in valuations continues remains to be seen. My approach to the "inflation question" is to own some companies/themes that should benefit from inflation while also holding the innovative "deflators" that have high growth prospects and should dominate if that approach proves correct. It's not out of the question that both sides may very well see their preferred groups appreciate over the next year, even if the near term looks a little bit dicey.

If you have any questions about your portfolio or any changes you would like to discuss, please don't hesitate to contact my office at any time.

Sincerely,

Richard