3rd Quarter 2020 Commentary

October 2020

Schacter Palazzi | Wealth Management

TD Wealth

3rd Quarter 2020

TD Wealth Private Investment Advice

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Can we finally forget 2020?

The past 12 months have been historic. There was the impeachment of a president in the United States followed by an acquittal of that president in the Senate and of course the thing most of us wish would just go away – a global pandemic that caused many governments to at least temporarily shut down their economies. The imminent event at the top of our clients minds now is the most contentious election in recent US history. Our investors want to know if they should do something now to protect their portfolios from a negative election result. But does anyone really know what a negative outcome looks like? Using 2008 as an example, the S&P 500 fell 21% in the 2 weeks after Barack Obama won the election. Was this reaction really about the election outcome? Or was it tied to the fact the world was in the biggest financial crisis since the Great Depression? In 2016, when Donald Trump was elected many felt the market would falter but instead the S&P 500 rose. And it continued rising, gaining almost 10.5% by the end of February 2017.

All of this is to say that while it is interesting to pontificate on the election outcome and the impact that the policies of the mooted winner may have, market trajectories are most often dictated by the economic outlook and corporate earnings. At this stage whoever wins the U.S. election will adopt an economy that appears to be recovering from the global health crisis caused by Covid-19. We would say the recovery will dictate the longer-term direction of stock prices and our economy.

Below are the most common questions from our client's during the quarter. Each member of our team has selected one question and provided their response:

Q: What conviction do to you have that the markets will continue to recover from their lows and will the dividend paying stocks start to participate or is dividend investing dead?

Jeff: Even as Covid-19 news alternates between fresh outbreaks and positive vaccine developments, the economy continues to get back to work. So far, third quarter data has been strong across the consumer side of the economy, including retail sales, personal income and housing. The industrial economy is also recovering, and we are seeing increases in both durable goods and capital goods orders. (based on Research by both Argus (U.S. based) and TD economics (September 2020 publications).

Indeed, dividend paying stocks have tested the patience of both ourselves and many of our clients. Growth stocks, many of which have high valuations and a technology bias, have been stand out performers from the March lows. On the contrary, we see many dividend paying companies in sectors such as real estate, pipelines and financials that have significantly lagged the major indices and many names remain down on a year to date basis despite paying healthy dividends. We have focused on positioning the portfolio in dividend paying stocks that we believe have a sustainable and growing dividend profile, manageable debt load and relatively good growth prospects. We feel these should perform well over time on a total return basis.

In addition, with interest rates at historic lows, the dividend yield of many stocks are at historically high wide premiums compared to the 10- and 30-year government bond yields. While we cannot predict when those premiums will begin to narrow, we believe dividend investing is currently offering a compelling opportunity to generate tax efficient income that many of our investors need for either retirement or for lifestyle maintenance. Focusing on income alone can be difficult particularly when the original investment has been subjected to some of the large valuation changes we saw during the initial onset of Covid-19. During periods of volatility it is important to review the financial implications of market volatility before making any rash decisions - quite often there is little impact on the income generated from the portfolio and a decision to sell results in a reduction to income and lost opportunity to participate in a price recovery. If any of you feel the need to review your financial situation to help understand in more detail your capacity to handle market volatility, please feel free to reach out to anyone from our team to book and appointment to review your financial priorities.

Q: How much more volatility can I expect for the rest of 2020 and beyond in my portfolio?

James: Market volatility is a fact of life and is a healthy and normal part of investing and economic cycles. The pandemic we are living through adds a new set of circumstances never experienced by investors and policy makers of our time. Very simply, volatility will continue to be a part of investing in 2020 and beyond. Despite a myriad of other concerns in the world, the pandemic is the most important near-term issue facing us. I believe it is important to assess the response by governments and central banks around the world, with their "Whatever it takes" attitude to gauge how to approach volatility in the near term. It is important to look beyond the moment and into the future, and there I see a prolonged period of low interest rates, support from government to grow the economy, material amounts of investors' cash on the sidelines and a potential vaccine as several of the key catalysts that should remain top of mind even if it is a choppy ride until we get an "all clear" signal from the national and global health authorities. Periods of market volatility are totally normal! While most of us do not like volatility, it is a normal, healthy feature of the markets and it helps to restore balance by finding the correct price level for assets. In general better managed companies which have quality business see less volatility in day to day trading. It is quite possible that the economic solutions being put in place today will bring a new set of concerns and market distortions, engendering volatility in the future. However, with accommodative policies on both the fiscal and monetary front, and with the economy on a path to normalization, , I think there is a lot to look forward to. We will have to wait and see, but for the moment, be prepared for volatility—but remember that it will pass.

One thing I would like to point out is that, for the past year or so, we have been using the "Discovery" survey with clients. This application is a sort of psychological survey which uncovers your response to certain conditions. Sometimes, knowing how you react to certain stimuli can help you make better decisions in the moment rather than letting emotion rule the day. Let any of us know and we can send you the survey directly to your email inbox and discuss your results!

Q: Will Covid-19 continue to be an issue for all my investments and how will it affect the income I receive?

Andrew: we have already seen a very strong recovery in stocks since they hit their lows in March of this year. Granted that the rebound has not been as strong in all segments of the market, this is nonetheless a positive sign and it has been a result of a significant rebound in economic activity from the government induced "coma" the economy was put in through April and May. There are many reasons to explain why economic activity has returned from the lows of the spring but the key items are that virus testing and tracing has improved across North America, and also that doctors and researchers are learning better techniques and discovering which drugs can be used to diagnose and treat Covid-19 symptoms. As well, I believe that people and businesses have embraced mask-wearing and social distancing and that workplace alterations have allowed many people to return to work including our students. This has helped the population regain some confidence that Covid-19 can be managed and we all hope ultimately reduced to having effects no more severe than a common cold. As such, the increased (from the spring) level of economic and personal activity that is seen today will likely continue despite the threat of increasing Covid-19 cases in the now started second wave. I believe governments have learned shutting down an entire economy is no longer the "best option". That all having been said, there always is the risk that economic recovery can and likely will slow at times in the future.

I do not think that Covid-19 will be with us indefinitely and continue to believe that the very accommodative monetary policy provides a good opportunity to invest during a period where many investors feel uncertainty with our current circumstances. Looking into the future, I see many investment opportunities developing in the renewables and environmental sectors and also with companies positioned to resume growth in areas of the economy that have been held back by the pandemic. I believe that the majority of companies that have been severely impacted by the pandemic and have seen curtailed cash flows have already cut their dividends and now the focus shifts to life beyond the pandemic and those business ready to resume their growth, profits and eventually dividends and dividend growth as we emerge from a moment in history we will never forget.

Final Thoughts to Everyone

We recently emailed out an article from TD Wealth's Chief Wealth Strategist, Brad Simpson, which does a great job outlining the possible election outcomes and presents some historical data on market performance depending on the party in power. If you are interested in reading the article and missed it the first time please let us know and we would be happy to resend you another copy.

We would like to take this opportunity to thank all our clients for adapting to new methods of communication and correspondence. Webex, our video conferencing service, and e-sign have been two very popular and accepted methods of communication. With offices not fully operational until likely January 2021 at the earliest, people are adapting to this new normal and that is very encouraging. If you would like to schedule a Webex meeting or if you have further questions surrounding the ideas presented today please feel free to reach out to Jeff, James or Andrew over the next few weeks to discuss any issues or if you feel any long range planning should be revisited.

All of us here at the Schacter Palazzi team wish everyone health and safety as we head into the final quarter of 2020.

Thanks again for all of your questions this quarter and if you have a question that was not covered here, please don't hesitate to reach out to us directly.

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