2nd Quarter 2024 Commentary

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Schacter Palazzi | Wealth Management

TD Wealth

TD Wealth Private Investment Advice

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What can the Olympics tell us about investing?

While many of us feel chest swelling Canadian pride every Olympic cycle, not one of us believes that Canada can win more medals than our southern neighbours, the United States of America. It is similar with equity markets – while we have some fine, world class companies, it doesn't seem we will ever have as many as the United States does. Yet, we continue to feel both countries offer opportunities to invest albeit there are more choices in the US – particularly for those investors looking for growth over income. While that is our sense most of the time, we feel Canadian income investments have never looked more attractive despite the current political environment and its effect on economic efficiency and the overall Canadian business climate.

As always, our clients have asked some interesting questions over the last quarter so let's get right to them:

Q: Are you worried about the US election affecting valuations or causing further volatility in our portfolio?

A: The election season for the United States is just starting to come into focus now with the first direct face-off between the candidates, the CNN debate of June 27th,2024. As we watched President Biden face off against former President Trump in that live televised debate, we were happy to not have to make a choice here. And at this point, voters are also lukewarm on both candidates. Early indications suggest this will be a very close race. While the political winds of election season between now and November 5th 2024, may create a certain amount of volatility on any given day, we think the economy will play a much larger part in determining how we finish the year.

Markets in North America are in solid shape but, admittedly, investor sentiment (as reported by Argus Research) appears to be slipping of late. Reports from Argus Research show both business leaders and consumers in the United States are uneasy about the months ahead, and we are seeing clear signs of slowing consumer spending, and softer purchasing manager sentiment amid the pending US elections.

On the bright side, recent US and Canadian inflation data (both CPI and PPI) are finally showing improvements from recently stalled levels (especially in the US). These types of influence will have more pronounced effect on market returns in the long run relative to the US election results.

Q: What is the number one thing you and the team are keeping an eye on regarding the types of companies in our portfolio?

A: The biggest driver of economic activity in the US, and to some degree Canada, remains the consumer. In the US specifically, the consumer is responsible for over two-thirds of final sales. With the American consumer finally showing signs of exhaustion according to Argus Research, we do expect that growth will slow south of the border. Canadian households have a greater sensitivity to interest rates as our mortgages have a shorter duration and so the Bank of Canada has already begun to unwind things with a 25bps cut in early June 2024. Right now, the TD Economics long term forecast includes two additional rate cuts from the BoC by year end. The market is currently suggesting a 60% probability that an additional interest cut in Canada is coming in July 2024.

We are keeping a close eye on Gross Domestic Product (GDP) in both countries but also the Leading Indicators index (LEI) in the US. In May 2024, the LEI in the US fell 0.5% from a combination of a decline in new orders, weak consumer sentiment and lower building permits. Housing has been an ongoing drag on LEI. Existing home sales in the United States are currently running at 60-65% of peak levels achieved back in late 2020 through 2022. In Canada, housing is also showing weakness with the Globe and Mail recently reporting condo listings for sale in the Toronto market are up 94% from May of last year!

Q: How do you feel the interest rate cut from the Bank of Canada will affect our portfolios?

A: While the Bank of Canada is supposed to remain above politics, politician never do and many of them are pushing the message that low- and moderate-income consumers are coming under severe pressure from the combination of high prices and high interest rates. We have recently heard Chrystia Freeland and Doug Ford both literally asking the Bank of Canada for an interest rate cut, a posture that makes the job of the Band of Canada more difficult as they are trying to appear free from political pressure. As we have mentioned in previous commentaries, Canadians are much more susceptible to interest rates as mortgages are so low duration in nature in this country vs the 30-year mortgage rates available in the US.

The recent rate cut of 25bps in June 2024 and likely two more this year will certainly give income oriented companies a boost as dividends become more valuable. Those cuts should also cause bond prices to rise over time so long as the inflation genie stays in the bottle.

Conclusion

At the halfway point of 2024, the total return for the S&P 500 is 15.3%, the Dow Jones has returned a total of 4.8%, and the TSX Composite has shown a total return of 4.7% (source of index returns: Thomson Reuters). In the US markets it is the information technology and communication services sectors leading the way on the back of strong moves from US technology/communications giants and the Artificial Intelligence (AI) theme. If we had a fall wish list, we would like to see a broader market advance across all sectors. Until the AI spell is broken, market participation is likely to remain narrow.

If any of you have any questions or concerns about your own portfolios or your family situation has changed, please always feel free to reach out to any team member to set up a call or meeting. Have a great summer!

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