Year End 2025 Commentary

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Schacter Palazzi | Wealth Management

TD Wealth

TD Wealth Private Investment Advice

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What Netflix and Stock Market Returns Have in Common!

If 2023–2025 were a Netflix series, 2025 was the season where the Canadian market finally got more screen time than the flashy U.S. tech stars—and then promptly left investors wondering if there would be a plot twist in 2026. Canadian equities quietly delivered standout returns, while U.S. markets posted a solid but more "normal" year by recent standards, all against a backdrop of cooling inflation, central banks easing off the brake pedal, and nonstop headlines about Artificial Intelligence (AI), politics, and interest rates

Before we get to the most popular questions last quarter, one question stood out the most: How much farther can this bull market go?

A: We looked back on the U.S. market due to its influence (sorry Canada) and we found that approximately 13 bull markets have occurred since the end of World War II. On average, the S&P 500 gained 164% during these 13 periods, which averaged 57 months in duration, or just about five years. We also note that the recent bull markets have generated higher returns over longer periods. On average, the five bull markets since 1980 have seen stocks advance about 240% over a period of almost six years (Source: FactSet Research Systems Inc.)

But there are risks in 2026. Of the four years in a presidential term, the second year -- the mid-term election year – has, on average, been the worst for investors. Consider that since 1980, returns in the second year of a presidential term have averaged 3.3%, compared to average returns of 15.6% and 16.5%, respectively, in the first and third years. Even the fourth year, with all the drama of the election itself, outperforms the second year, with an average gain of 7.2%. What is more, the "batting average" of positive second years for the S&P 500 is only 55%, compared with 80%-plus averages for the other three years. Why? The reason is uncertainty, and the likelihood of change. Investors favor predictability and continuity, and a mid-term election year offers a real opportunity for a significant shift in direction -- whether it is in fiscal policy, antitrust philosophy, or a certain regulatory focus. We note that incumbent parties typically lose seats in mid-term elections, and even the loss of a few Republican seats in the House could tip the chamber Democratic and then lead to gridlock in Washington D.C. (Source: FactSet Research Systems Inc.).

So, to sum up with a potential rate of return, we would suggest a range of 5%-10% might not be out of the realm of possibility in 2026 on the U.S. side. A Canadian forecast might be a bit trickier, as government spending and policy seems to change daily. We do expect volatility to show itself as some of the themes I mentioned above take place in real time.

Now let's get into the most popular questions during the last quarter of this year!

Q: We were pleasantly surprised to see the Canadian markets outperformed U.S. markets this year. Should we expect that outperformance to continue?

A: While Canadian outperformance could continue in the near term, it is unlikely to be a straight-line, multi-year trend. The TSX's 2025 leadership reflected its sector mix: more heavily weighted to financials, energy, and resources, all of which benefit from stable growth, reasonable commodity prices, and a move away from extreme rate-tightening. The U.S. market remains structurally advantaged in terms of earnings growth, innovation, and sector composition (technology, communication services, health care), which historically has driven higher long-term total returns despite shorter bursts of non-U.S. outperformance. The base case is that Canadian equities can remain competitive—especially if commodities and financials stay bid—but over a full cycle, we believe investors should still assume U.S. markets will be a key driver of long term portfolio growth due to higher aggregate earnings growth and innovation exposure.

Q: Last year you and the team mentioned you thought the Canadian Dividend model was the best value. What model do you favour the most this year?

A: It is great to see that many of our audience (and not just our mothers and fathers) are not just reading but also remembering what we have written – Thank-you!

We feel if an investor is looking for income our Core Dividend model is still the way to go but in terms of value, especially in light of a stronger Canadian dollar we are, at the moment, leaning in favour of our North American model and U.S. Equity model going into 2026. Admittedly, we did move a bit more defensive in our U.S. Equity model in 2025, and to some extent our North American model, but feel they are most attractive based purely on valuation and movement of the Canadian dollar versus the U.S. dollar. The recent release of third quarter GDP growth in the United States can be read to suggest that economic growth will continue for the next few quarters although not without risk along the way..

Q: You recently added a position in Google while reducing Oracle. Why, and what do you see ahead in Artificial Intelligence (AI)?

A: The shift from Oracle toward Alphabet (Google) is essentially a move to take advantage of what we believe to be broader AI monetization potential and more diversified growth levers.

Alphabet has multiple AI monetization channels—search, YouTube, cloud services, and emerging productivity tools—which tie directly into advertising and cloud workloads, two very large profit pools. While Oracle remains important in enterprise databases and has made progress in cloud and AI infrastructure, its growth profile is more concentrated and dependent on winning large enterprise contracts versus Alphabet's more diversified consumer and cloud ecosystem.

Looking forward, AI is likely to evolve from a "hype phase" to a productivity and profitability phase, where earnings growth is driven by:

- Higher cloud and data-center spending,
- AI-enhanced software pricing power and upsell,
- Efficiency gains inside non-tech sectors (financials, industrials, healthcare), where as these environments typically reward platforms with scale, data, and distribution—traits more associated with the largest cloud and consumer-tech ecosystems.

Q: Do you think interest rates will remain the same in 2026, and will inflation finally be under control?

A: We think that rates are more likely to stabilize with a slight easing bias rather than move dramatically in either direction, as long as inflation remains near target.

The Bank of Canada (BOC) is currently holding its policy rate at 2.25%, after cutting rates earlier in 2025. The BOC has explicitly signaled that this level is "about the right" setting to keep inflation near its 2% target, assuming inflation and other economic data cooperate. Headline inflation in Canada is running around 2.2%, with core inflation measures drifting back toward the 2% target, suggesting that the worst of the inflation shock is behind us, even if individual prices do not "go back" to pre-COVID levels. In the U.S., the Federal Reserve has cut rates to a 3.5%–3.75% range and is signaling a slower pace of future reductions, reflecting cooling inflation and a softer but still resilient economy. Barring significant growth or geopolitical shocks, both central banks are positioned for modest tweaks rather than big swings, with inflation likely to oscillate around target rather than reaccelerate meaningfully.

Q: If there was a major pullback after three strong years, how bad should people expect it to be?

A: After three solid years of gains, a pullback in major indices would be well within historical norms, even without a full-blown crisis. With the S&P 500 having delivered strong positive returns in 2023, 2024, and 2025, and history shows that multiyear advances are often followed by corrections in the mid-teens to low 20's percent corrections, even within ongoing bull markets.

The TSX, which returned close to 30% over the past year, could also be vulnerable to a sizeable correction if growth slows, commodities wobble, or credit spreads widen, particularly given its cyclical sector tilt. For long-term investors, the more relevant question is duration and earnings impact:

- A quick 15%–20% pullback with stable earnings and no recession tends to be an opportunity.
- A deeper drawdown (25%+) usually requires a recessionary or systemic shock, which would likely be accompanied by falling earnings estimates and wider credit stress.

We believe constructing a portfolio of companies with quality balance sheets, and adequate liquidity, and then diversifying amongst asset classes, is more important than trying to guess at the timing of the next market reset.

One important thought to make note of is to imagine if your portfolio had grown from $2 million to $3.5 million over the past 3 years. Now assume your portfolio fell in value by $525,000. If this thought keeps you up at night, then your asset mix clearly needs to be revisited. But remember, an investor's time horizon is one of the most important factors when looking at the impact of economic volatility. We also want to remind you all that, when we speak about pullbacks, we mean in an equity sense not short-term cash or fixed income investments which are more sensitive to interest rate changes than earnings and cash flows.

Q: Does dividend investing still have legs, or will the "Magnificent 7" dominate again in 2026?

A: Dividend investing still has plenty of long-term merit, but leadership between high dividend stocks and mega cap growth will likely continue to rotate.

In 2025, Canadian banks, pipelines, and other dividend payers participated meaningfully in the TSX rally, helped by more stable rates and a bid for value and income. In the U.S., while the "Magnificent 7" no longer dominated index returns to the extent they did in 2023, mega cap tech and communication names still contributed a disproportionate share of S&P 500 earnings and market cap gains. For 2026, we believe a balanced approach remains prudent:

- Dividend strategies can provide income, lower volatility, and partial inflation protection, especially in an environment of moderate growth and range bound rates.
- Growth and AI linked leaders remain crucial for long term capital appreciation, particularly if productivity gains from AI continue to flow through earnings.

The sweet spot is often a barbell, a diversified equity portfolio with quality dividend payers on one side and selected structural growth names (including AI beneficiaries) on the other. Why choose just one camp when you can have a foot in each? This is why we much prefer our North American model in 2026 as the combination of both Canadian and U.S. markets can give our investors the best of both worlds if income isn't a priority.

Q: How much will politics affect markets in the upcoming year?

A: There is no doubt that politics will generate headline risk and volatility, but it is fundamentals—earnings, interest rates, and growth— which tend to dominate over time.

In the U.S., the political debates over fiscal policy, regulation (especially in tech, energy, and health care), and trade will continue, but historically, markets have often looked through election-related noise and political debate unless it changes the trajectory of taxes, regulation, or spending in a material way. In Canada, political developments around housing, energy policy, and fiscal discipline may affect specific sectors (banks, real estate, pipelines, and producers) but are less likely to drive the overall market than global growth, commodities, and, oddly enough, U.S. policy. Investors should expect short term swings around major political events, but anchoring decisions on valuations, earnings power, and balance sheets—rather than on headlines—typically leads to better outcomes than trying to trade every policy twist and tweet.

Final Thoughts

Tax efficiency has been a top discussion topic among many of you, and we don't think that will change in 2026 based on current government policies. Health care planning is also an important topic that has been discussed amongst our client base as of late. You need to plan for scenarios and extra savings to meet possible supplemental health care services like private health clinics, assisted living support, and caregiving costs. All these important factors can change and evolve over time, so its best to discuss with our team to update investment and wealth plans continually. Please contact Jeff, Andrew, Jessica, James, or Chris to discuss further.

Thanks to everyone for your questions and thank you to all our clients and their family members for placing your trust in Schacter Palazzi Wealth Management in 2025. We look forward to helping everyone navigate 2026.

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Source for index returns and data: 2025 FactSet Research Systems Inc.

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