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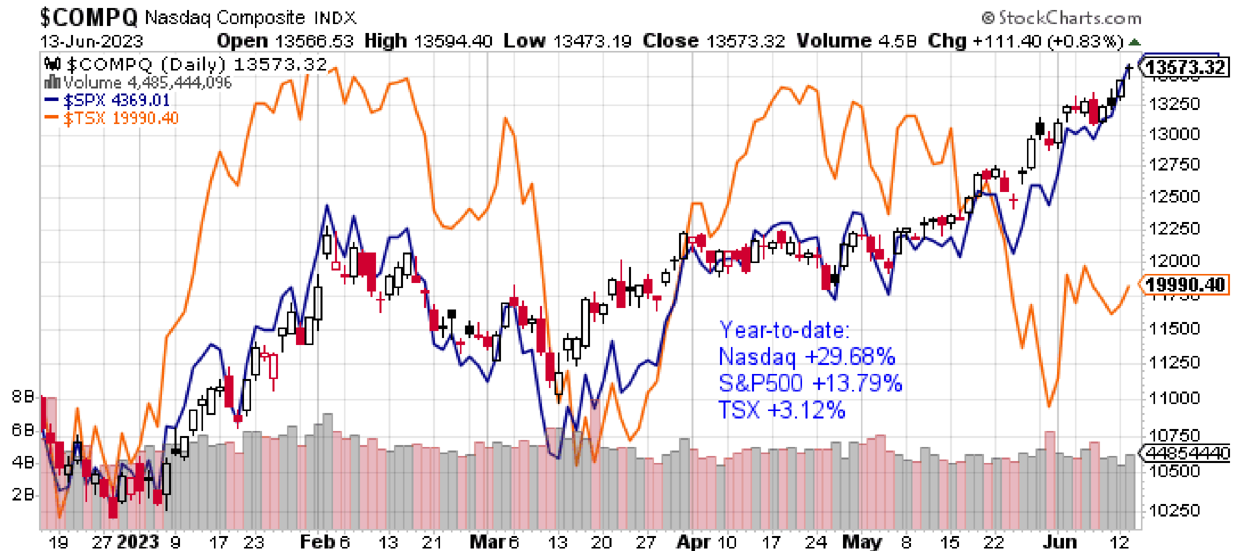
Market Update June 2023



The American indices look impressive this year but for the fact that they are not broad based in terms of participation. The S&P 500 (SPX) is the broad-based American index. Most of movement in that index is the result of just seven stocks: Microsoft, Amazon, Alphabet (parent of Google), Apple, Tesla, Meta (formerly Facebook) and Nvidia. The other 493 stocks in the index haven't moved much.

These stocks frame in part, the development of Artificial Intelligence.

One of two things will occur. Either that rest of the participants in the index (493 stocks) will start to participate or these names may be subject to a pullback or retest of lower prices at some point.

The U.S. market is outperforming Canada this year despite strong economic data in Canada where GDP growth came in at 3.1% last quarter. The volatility in the Canadian market is much more pronounced (see gold line above).

Canada.

Energy. Conflicting direction as the Federal Government on one hand is the builder of the Trans Mountain Pipeline to tidewater (2024 completion) while at the same time it appears dogmatic in its desire to remove fossil fuels. With Canada representing 1.5% of global C02 emissions. perhaps the world would be better served if we sold China oil and gas to replace dependence on coal. China currently controls 33% of global manufacturing and its dominant source of power is coal. The wind blows east.

Banks. The banks are trading at discounted valuations for months. Last quarter they added to loan loss provisions for 'performing loans' as a precautionary measure. When they do that, it draws from earnings. When they reduce loan loss provisions, earnings are enhanced. If you factor out loan loss provisions for 'performing loans' last quarter, collective earnings performance was pretty good. Of

course, one concern that has had plenty of play in the media is variable mortgages and potential for the inability to refinance all those variable mortgages out there should interest rates stay higher – for longer. Approximately 1/3 of Canadian rent, 1/3 are owners that own free & clear and 1/3 own with mortgages. Of those with mortgages, approximately 75-80% are fixed rate mortgages and the remaining 20-25% are variable rate mortgages.

Interest rates.

While central bankers on both sides of the border had suggested a pause in interest rate hikes, we are seeing them initiate rate hikes again – last week here in Canada. This has led to the notion that interest rates will likely stay higher for longer to decelerate the economy and achieve central bankers' inflation goals.

Inflation is no longer just about supply chain but other issues, as well as a less talked reality that money supply has increased about 28%.

Here in Canada we are starved for labour. Canada has an enviable track record when compared to the U.S. of seeking educated migrants that can mesh into our economy. Last year we had one million migrants and expect another million this year. The problem of course is housing and the lack of it, is inflationary. Canada has never been able to build more than 240,000 units in a year, so even if we had half the migrants, we would still be short on housing. Builders are antsy too, about preselling new projects when they have less certainty about their costs.

That all said, if risk is what we don't know, an imminent recession is the most over advertised secret I can recall. Layoffs at tech companies suggest they were overstaffed in the first place during more flush times, and many are more efficient as a result of downsizing. Regardless, unemployment overall, remains very low. Recent economic data out of the U.S. suggests a resilient economy despite the size of interest rate hikes.

Watch the consumer. Are they spending? My guess is that they still are and that may mean interest rates remain higher for longer and if that imminent recession ever occurs, I expect it may mean a hiccup in the rear-view mirror of investors.

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Best,

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Senior Wealth Advisor

Sources: NBF Economics, Stockcharts.com, Reuters

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