July 2020 Newsletter

We continue to hope that you and your loved ones are healthy. If you are like us, you are enjoying some of this summer's beautiful weather and some of the local produce that is now becoming available. For many, it has been a very challenging spring with many restrictions still in place. Our whole team continues to work from home, and we are looking forward to additional restrictions being eased in the near future.

In this summary we discuss the importance of financial and estate reviews during important milestones, as well as a brief review of the markets globally and investment portfolios.

Milestones – A Good Time for Review

Milestones are generally considered as touchpoints in life. While many traditional milestones are changing, there are still some that can be considered common to most people, including: graduating and starting your career, getting married, buying your first home, and retiring.
Looking Forward to Life's Milestones discusses several of these common, major milestones, and provides financial tips to consider to ensure that you are better prepared to navigate your way through these important crossroads.

July Monthly Recap: U.S., Canadian Stocks Post Historic Surge in Second Quarter as Virus Cases Top 10 Million

North American stocks weathered a turbulent second quarter en route to their best three-month performance in at least a decade. The rally came even as global COVID-19 cases topped 10 million—a grim milestone in the half-year battle to contain the novel disease.

Wall Street Posts Best Quarter in Over 20 Years

Wall Street's major indexes finished moderately higher in June, but the gains were enough to catapult markets to their best quarter in more than 20 years. At the end of the first quarter, investors were lamenting the end of the longest bull market in history as the Dow Jones and S&P 500 Index plunged into bear-market territory.[1]

The S&P 500 Index finished June down only 4% for the year. The index remains roughly 9% below its all-time high set in February. By June's end, the Dow Jones Industrial Average trimmed its year-to-date losses to 9%.

Canadian Stocks Regain Their Footing

Canadian stocks were also winners in June, rounding out their best quarterly gain since 2009.[2] The S&P/TSX Composite Index ended the month with a gain of 1.8%. For the quarter, the Canadian benchmark rose 16%.

For the quarter, the TSX was the 21st best performer among 92 global stock markets. Gains were broad based, with ten of 11 TSX subgroups finishing in positive territory. Among the TSX's 222 individual companies, 194 saw positive returns.

Gold Notches 8-Year High

Rebounding equity markets did not prevent gold from notching new multi-year highs. The yellow metal topped $1,800 a troy ounce in late June, its highest in eight-and-a-half years.[3] Comex gold rallied more than 18% in the first half of the year, putting it within 7% of a new peak.

A combination of factors is fueling gold's bull market. Safe-haven demand, a volatile macro environment and concerns about record monetary easing from central banks have been the main drivers of the rally.

Pandemic Cases Top 10 Million

The coronavirus pandemic accelerated in June, with Latin America joining the United States and Russia as a major epicenter for the disease. By the end of the month, more than 10 million cases had been reported worldwide, with about a quarter of those in the United States. More than 500,000 deaths have been attributed to COVID-19, according to Johns Hopkins University.[4]

The International Monetary Fund (IMF) has warned of a prolonged economic downturn due to the pandemic. In June, the IMF downgraded its world economic outlook, calling COVID-19 a "crisis like no other." Global GDP is forecast to contract 4.9% in 2020, lower than the 3% downturn forecast in April.[5]

Although the global economy is expected to rebound in 2021, growth is expected to be significantly lower than pre-pandemic levels.

Portfolio Overview

I joined Burns Fry in 1987 months before the S&P 500 corrected more than 20% in one day in October. Since then, there have been many significant corrections in the global stock markets including the demise of hedge fund Long Term Capital Management, the "TechWreck" in 2001-2003, and the financial crisis in 2008-09 to name just a few. All were frightening at the time, yet the markets recovered eventually over time.

The peak to trough (top to bottom) correction of 37% during this February and March, while swift, was relatively brief as governments globally took action to support the financial markets and the economy as unemployment ballooned as a result of the spreading of COVID-19. U.S. and Canada introduced plans to provide funds to the recently unemployed and to businesses that saw drastic reductions in business activity.

Interest rates were dropped to near zero percent and corporate bonds were purchased in a co-ordinated fashion in the open market to relieve a credit crunch that became even more severe than experienced in the financial crisis of 2008.

Our investment process utilizes a multi asset approach which may include Canadian equities, U.S. equities, developed international equities, emerging international equities, currencies, commodities, Real Estate Investment trusts (REITs), bonds, preferred shares and cash. We actively measure the supply and demand for each asset class, and allocate our investments to the strongest asset classes.

With the exception of our All Equity Portfolio, our Multi Asset portfolios consist of two primary components. One component consists of permanent positions in Canadian and U.S stocks, a bond Exchange Traded Fund (ETF), a GIC, as well as individual preferred shares and preferred share ETFs. The second component is flexible and can include any of the previous assets classes previously mentioned.

At the end of February, and again in the first days of March, we reduced our exposure to stocks in the variable component as the markets began to break significant support levels. This helped significantly in reducing the downside volatility of the portfolios. Our core position in stocks remained invested. After bottoming in March, equities advanced in the fastest recovery in the past ninety years. As a result, our core equity component participated fully in this recovery.

More than a year ago, we invested in a bond ETF managed by the world leader in bond management, Pimco. This ETF is a global ETF investing in government and corporate bonds and securitized debt. A large portion of the assets are invested in the U.S. During the market collapse, the bond market experienced a liquidity crisis more extreme than in 2008. As a result, the ETF experienced a swift decline in value as corporate bond market was essentially “frozen” until the Federal Reserve stepped in to purchase corporate bonds and provide liquidity. The ETF has recovered a large portion on the losses, but is still negative for the year.

As I have mentioned previously, we built a portfolio of preferred shares more than five years ago. Preferred shares provide a steady stream of income higher than generally available from bonds. During the market decline, the liquidity of the preferred market dried up causing the prices of the preferreds to decline substantially as investors sold in a panic. While the prices have mostly recovered, this component had a noticeable impact on the returns of the overall portfolios. Liquidity is critical for us to control risk in the overall portfolios. While the worst of the current crisis appears to be behind us, there will be other market shocks in the future. As such, we will be reducing our exposure to individual preferred shares in favour of a Preferred ETF. Doing so will allow us to participate in the preferred share market, yet provide us with significantly improved liquidity.

Much of the global government support during the COVID crisis has been financed by issuing massive amounts of debt. As a result, we added a gold position to the portfolio through an ETF directly investing in gold bullion – iShares Gold Bullion ETF.

We also added a position in a unique ETF, the AGF Anti Beta Market Neutral Fund. The objective of the ETF is to provide additional downside protection to the portfolio should the market experience severe downside volatility. The ETF is expected to appreciate in value under those circumstances.

You can view the first half results of the portfolios here.

We continue to be underweight stocks overall. While the recent stock market recovery has been fueled by government intervention, to support ongoing stock market growth, corporate earnings are what fuel the stock market over the long term. Corporate earnings have been significantly impacted by the virus and we expect overall earnings growth of the S&P 500 to be lower in 2020 and 2021.

Stock valuations today are high by historical standards. For example, Apple currently has the highest price earnings (PE) ratio since 2007, and Nvidia has the highest price to sales ratio ever. The average PE ratio of the S&P 500 in the past five and ten years is 16.9x and 15.2x respectively. It currently is 21.9x.

The market recovery has been fueled by technology stocks. Apple, Microsoft and Amazon have a combined market value greater than the bottom 300 stocks combined in the S&P 500. Tesla has a market cap more than Toyota, the world leader in auto production. While our stock portfolios have significant exposure to technology stocks, the valuations for many of these stocks are at historical highs. As such, we expect significant volatility for the sector going forward.

Looking Forward

We are optimistic about the economic recovery going forward as a treatment or vaccine appears probable. While many industries have been permanently negatively impacted by the pandemic, new and exciting companies offering world changing products and services are being created daily which will likely improve all of our lives well into the future.

As always, if you have any questions regarding this summary of your investment portfolio, please call us.

Sincerely,

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