TD Wealth

Q1 2018 Market Commentary

It's been a tough start for global stock markets so far in 2018. The Canadian stock market as measured by the S&P/TSX Composite Index was down 4.52%, the U.S. stock market as measured by the S&P 500 Index (S&P 500) in USD was down 0.76% and the international markets as measured by the MSCI (in USD) was down 1.41%. The primary culprits for the decline and increase in volatility are: the threat of rising interest rates, mounting trade tensions and a revaluation of technology companies.

Interest Rates

Globally, we are seeing interest rates start to increase. The resulting impact on the stock market is two-fold: **(1)** For conservative investors looking for income (both individuals and pension funds), it creates investment options beyond the stock market. For example in the U.S., the dividend yield on the S&P 500 is 1.89% versus the return on a 10 year bond which is 2.75%. The shift from stocks to bonds by investors puts pressure on the stock market. **(2)** Heavily indebted companies will see their valuations decline. These companies with heavy debt loads will see their interest expense increase thereby reducing potential profits. Lower profits result in lower stock prices. Although we are mindful of rising rates, I believe the trajectory of the increase will be very moderate and should not further disrupt stock market valuations.

Trade Tensions

The NAFTA negotiations and the impact on the Canadian economy have been well covered in the media. The cancellation of NAFTA would hurt industries in both countries. However, the impending threat of a cancellation has had a greater impact on the Canadian stock market than the U.S. The overwhelming issue having the greatest impact on our stock market is the tariffs that the U.S. is placing on Chinese goods and vice versa. An all-out trade war between these two countries could lead to two outcomes – slower global growth and lower stock valuations. The hope is that rather than escalating to a trade war, the initial tariffs levied will start a dialogue resulting in a new trade deal between the countries. Considering this politically, President Trump cannot afford to have the U.S. economy fall into a recession and implode the U.S. stock market. He needs to be able to tell the electorate that he struck a "better deal", like he had promised. This would be a positive to help set him up for the election in 2020. Based on this, I am using market volatility to help build positions in companies that are being unnecessarily punished.

Technology Turmoil

For the past two weeks, large-cap technology stocks have sold off significantly. The main catalyst for the market angst is the crisis at Facebook. An independent researcher gained access to detailed personal information of millions of users and then provided it to a company that turned it into psychographic profiles employed in targeted political ads, including the 2016 U.S. Presidential Election. Technology companies with a business model based on collecting and selling information to advertisers have all come under pressure recently. I believe we've hit an inflection point where the companies that use social media to collect data and have an ad-based model could become regulated, causing some businesses to be worth significantly less than they are today. However, I'm still very confident in the technology industry. The focus could switch to companies involved in Artificial Intelligence (AI), the Internet of Things (IoT) which is about connectivity of devices and the development of electric vehicles, which I believe will have much higher adoption rates than currently forecast.

I was told early in my career that stock markets go up in escalators and down in elevators. It certainly feels like we are in an elevator right now. This is the time to patiently build long-term diversified portfolios that maximize the potential for growth and minimize downside risk.

Ashit Dattani
Portfolio Manager and Investment Advisor
T: 604 482 8336
ashit.dattani@td.com

Borzo Salehi
Associate Investment Advisor
T: 604 659 8136
borzo.salehi@td.com

Kristen Vilbrunt
Client Relationship Associate
T: 604 482 8446
kristen.vilbrunt@td.com

Kim Dadgar
Client Service Associate
T: 604 482 8488
kim.dadgar@td.com

Dattani
Wealth Advisory Group

Source for Stock Market Index Returns: http://w3.td.com/public/Intranet-Portal/Wealth/Wealth_Main/documents/March_Performance_Monitor_2018.pdf