QUARTERLY COMMENTARY

Richard Liss, CFP, CIM®, FCSI®
Senior Portfolio Manager
Private Client Group
(416)777-7041
richard.liss@raymondjames.ca

Gala Petrenko
Financial Advisor Associate
(416) 777-7154
gala.petrenko@raymondjames.ca

Raymond James Ltd.
Scotia Plaza - Suite 5300, 40 King Street West, Toronto, ON M5H 3Y2
Phone: (416) 777-7041
Fax: (416) 777-7020
www.raymondjames.ca/richardliss

A Colourful Time

Third-quarter performance was strong for equities, with U.S. and Canadian equity markets posting all-time closing highs to finish out the quarter and bonds delivering positive returns, but not without a pickup in volatility at the start. Developed market equities delivered a 6.5% return over the period. As expected, the parts of the stock market that had previously suffered most from high interest rates generally outperformed, with small caps delivering 9.5% and global REITs returning an impressive 16.2%. Conversely, growth stocks gave up some of their recent outperformance but remain up more than 20% year to date.

But the stock market rally was not without volatility in late July/early August, as investors reacted to a weaker-than-expected jobs report, fueling concerns that a stumbling labour market implied a recession may be looming on the horizon. With the potential of lower rates, fixed income markets were buoyed with global bonds returning 7.0% in the third quarter.

After retracing 8.5% by early August, the S&P 500 had just about fully recovered by the end of the month, and subsequently powered to new highs after the Federal Reserve delivered a jumbo 50-basis-point rate cut. Overseas, China delivered its largest stimulus since 2015 and Japanese policymakers adopted a less hawkish tone, helping fuel strong global equity market returns. During the quarter, the Bank of Canada reduced its interest rate to 4.25% after seeing a slowing of the economy and a reduction in inflation. The BoC is expected to continue to lower interest rates quickly, as the level for inflation is now at 1.6% - below the 2% target.

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Our economy can certainly use some support, which is why interest rates will continue to drop (expect a 50 bp cut this month). Lowering interest costs helps boost household spending, which in turn helps the economy. Canadian households bear more debt, relative to income, than anywhere in the G7 club of large, rich countries.

It's interesting to note, though, that a well-known fixed income manager I use for some client exposure to that space is bracing for a "hard landing" here in Canada. They expect that it won't be that easy for government policy to reduce the chances of a recession. They are the most defensively positioned they've been in 23 years – holding a high weighting in government bonds and highly-rated corporates as opposed to riskier types of fixed income.

With their interest rate cut of 50 bps, Fed officials in the U.S. made it clear that they do not welcome any further weakening in the economy and are keen to quickly move interest rates back to less restrictive levels. Later in September, the Fed's more circumspect view on the economy was vindicated by the largest monthly decline in consumer confidence in over three years.

So, what now for Q4? The good news is that positive expected earnings growth (especially in the U.S. anyway), cooling inflation, and easing central banks create a robust backdrop for markets. That said, geopolitical risks and election uncertainty will be at the forefront for the rest of the year, suggesting investors should be prepared for a bumpy ride. Although the historical norm for September (a drop in equity performance) didn't materialize this year, there's a lot of geopolitical events that might throw things off course this quarter. For instance, even though Biden has certainly attempted to dissuade Netanyahu from attacking Iranian oil fields, Israel's promised retaliation for the latest attack on the country could upset energy markets if he continues to chart his own course on how to respond. And, of course, there is the upcoming U.S. election, the result of which will have huge ramifications on the U.S. economy and the country's approach to trade. Should Trump win, it won't be a positive for Canada – his protectionist instincts and stated desire to impose tariffs on all imports could be disastrous for Canada as 75% of

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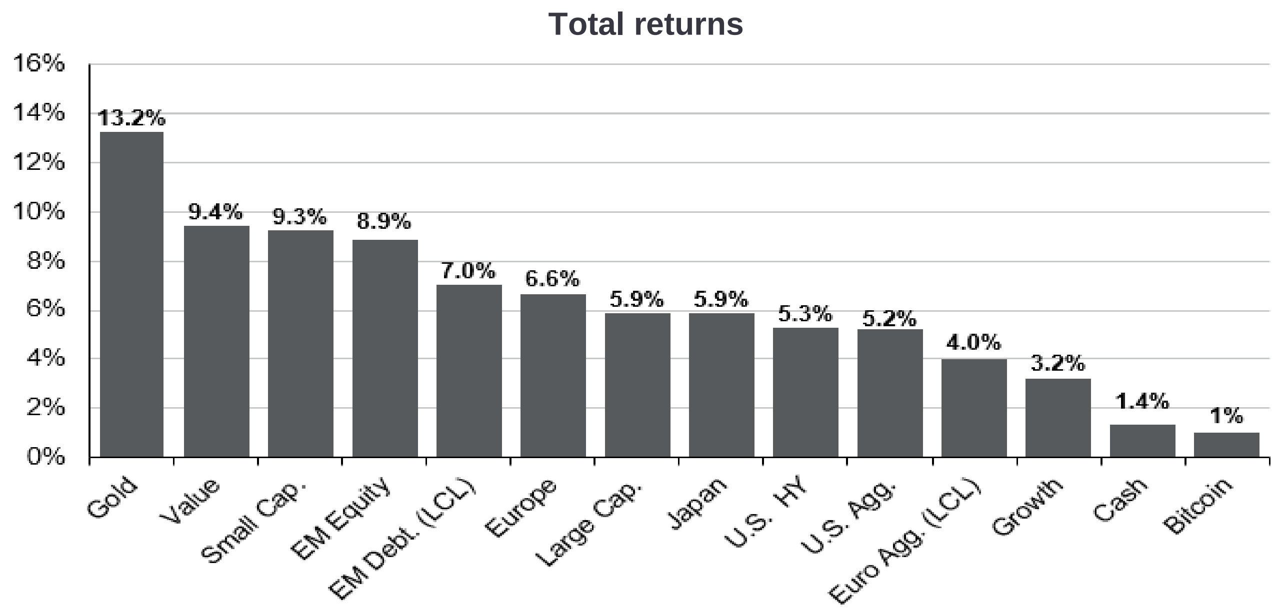
3Q 2024 asset class returns



Source: Bloomberg, FactSet, MSCI, Russell, Standard & Poor's, J.P. Morgan Asset Management.

our exports go to the U.S.

There are some interesting statistics regarding election-year equity outcomes. During years where the presidency stayed in the same party, the S&P 500 averaged an annual return of 16.0%, but when the presidency switched parties, the annual average return was only 6.3%. I believe that most election outcomes are decided by how the electorate perceives the economy is doing, and so, it makes sense that a change in administration might occur if the U.S. economy isn't particularly strong. I could cite all kinds of statistics regarding equity returns and elections, but I do note that one stands out in particular - there is

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a definite occurrence of increased volatility during campaign seasons. Does it make sense then to stay completely on the sidelines until election results are in? Not really – in the end, it's simply the cost of being invested in the stock market. We know that, in the short term, returns are going to be noisy and this is just one more manifestation of that. It would be prudent though to keep some cash available for when opportunities arise, in order to buy at lower prices, since markets are definitely not inexpensive right now.

As always, if you have any questions, are interested in a particular investment or you would like to have a comprehensive financial plan created for you, please don't hesitate to call. In the meantime, enjoy the colours of autumn!

Regards,

Richard