March 5, 2021

We hope that everyone is well and looking forward to some warmer weather.

The pandemic continues to be the central focus of the markets, but the recent volatility has caused us to concentrate on the re-opening of the global economy. The news about the pandemic appears more positive with the death rate falling and injections beginning at a steady pace in the United States, the developed world and hopefully soon in Canada. The come back from Covid should be very different than the protracted recovery coming out of the global financial crisis. This is because the emphasis has been on deficit spending as opposed to austerity. The 1.9 trillion American Rescue Act, if passed will act to put gasoline on simmering coals and should propel the U.S. economy forward, taking Canada and the developed world with them.

The concern now is inflation and whether the Central Banks can contain it and keep rates in check. If inflation rises rapidly it will slow the recovery and raise borrowing costs. This is particularly concerning to many because of the massive debts accumulated during the pandemic. We have recently seen a rapid rise in the U.S. 10-year treasury yield that acts as a key borrowing rate followed by professionals. The rate surpassed 1.5% which many analysts didn't expect to see until 2022. It wasn't so much the rate itself that spooked the markets, but the rapidity that it got there.

This spilled over into the stock markets as investors looked at valuations. This re-evaluation is positive for the longer term as it takes away some of the euphoria that many investors have showed recently with the rise of speculative currencies, new issues, green energy and what has been called the gamification of investing. As these themes abate and the focus shifts to earnings, equity markets should gain strength and build momentum based on fundamentals. It is important to remember that the inflation fears stem from what may be historic economic growth as we open the global economy. There are projections of 5-7% growth in GDP this year in the United States which will be reflected by the Canadian economy. Indicators lead to a very strong second half of the year.

We are now seeing a rotation away from high flying technology stocks and new issues, into cyclical stocks like financials, materials, energy and industrials. This is consistent with the beginning of an economic cycle coming out of a recessionary period. As we reopen, we need to build and maintain infrastructure and allow for consumers to spend on travel, leisure and goods. This bodes well for employment recovery. Technology will pave the way for the future, but valuations became very high based on the stimulus provided especially for newer companies without a track record. This is the reason for the pressure on the NASDAQ market and the relative outperformance of the DOW and the TSX. The large cap tech stocks and select green energy producers should continue to perform well once the focus shifts back to earnings.

We see the economy as recovering and we believe that the equity markets will reflect this. We will likely see short term volatility and a possible correction as we grapple with rising rates and the pressure on the bond markets. If inflation comes from a growing economy and a stronger consumer it is ultimately constructive and should lead to better days ahead over the longer term.

As always if you have any questions or just want to touch base, we are just a phone call or email away.

We're here to help!

The Andras Group