

Issue 7

OVERBOUGHT CONDITIONS

As we enter into the last week of the second quarter the markets could see some more volatility as Q2 GDP and more economic data is released. Stocks fell this past week across all the major averages. The Dow Jones Industrial Average dropped 855.91 points, or 3.3% to 25,015.55 this past week, while the S&P 500 index fell 2.9%, to 3009.05, and the Nasdaq Composite declined 1.9% to 9757.22. Those losses led to the major averages second weekly drop in three weeks. The optimism about a V-shaped recovery, powered by unprecedented monetary and fiscal stimulus policies and a reopening of states economies, is being challenged as new Covid-19 infections have topped 10M worldwide.

The week started off strong with big tech stocks lifting the market for no apparent reason. That was followed by a sharp tumble Wednesday as the markets finally started to pay attention to the spike in Covid-19 cases in places like Texas, Florida, and Arizona. On Thursday, stocks recovered thanks to hopes that states would take steps to reverse the spread of the virus, however, the Friday selloff started as the Federal Reserve released the results of its bank stress tests Thursday afternoon that was conducted to determine whether or not banks could survive a prolonged economic downturn. The Fed told banks they aren't allowed to buy back their own stock through the third quarter of the year, and imposed limits on how much they can pay out in dividends. Also, on Thursday, the Fed along with the Office of the Comptroller of the Currency and Federal Deposit Insurance Corporation – relaxed the Volcker Rule, a 10-year-old restriction introduced in the wake of the financial crisis that prohibited banks from making certain risky investment bets.

The Federal Reserve has relied heavily on the financial services industry to carry out the legwork of supporting borrowers during the Covid-19 pandemic. The banking sector is special in that it's providing liquidity to the economy and there are concerns with regard to bank health in particular, especially the way they've been used for some of the lending programs. Limits on capital distribution through buybacks and dividends may not do the job to ensure the banks are strong enough to withstand a prolonged recession. Debt defaults by consumers are expected to rise as the struggle with the economic impact of Covid-19 continues and the Fed is telling banks to keep a look out after releasing the stress test results. The question for the markets is whether continued monetary input from the Fed will be sufficient to offset the stalling, or even reversal, of the reopening of the economy.

Coronavirus cases are spiking and reopening's are being delayed as some states have begun to rollback their reopening to try and halt the massive increase in cases. Restrictions such as ending the on-site sale of alcohol at bars, cutting restaurant capacity, and banning outdoor gatherings over a certain threshold of people are being implemented in the states seeing the biggest climb in cases. Florida reported 8,530 new Covid-19 cases on Sunday after two straight days of record setting new case counts. As Covid-19 related cases continue to increase and reopening's are being delayed, at a minimum it will impact earnings. Q2 earnings seasons begins in one week and this will allow us to gauge the real earnings damage caused by Covid-19. For weeks now economists have been saying Q2 GDP is expected to be among one of the worst quarters the U.S. and Canada has ever seen. The brunt of the Covid-19 earnings hit is expected to be in Q2 2020, but declines are expected to continue in the second half of the year as well.



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MARKET SUMMARIES

(at Friday's close)

S&P/TSX Composite **down 1.66%** at 15,188.98 (**down 10.99% ytd**)

S&P/TSX Venture **up 0.47%** at 598.74 (**up 3.67% ytd**)

S&P 500 **down 2.42%** at 3,009.05 (**down 6.86% ytd**)

Dow Jones Industrial Avg. **down 2.84%** at 25,015.55 (**down 12.34% ytd**)

Nasdaq Composite **down 2.59%** at 9,757.22 (**up 8.74% ytd**)

Metals

Gold: \$1780.30

Silver: \$18.04

Copper \$2.66

Energy

Brent Crude Oil: \$39.46

WTI Crude Oil: \$38.49

Natural Gas: \$1.50



Total S&P 500 earnings are expected to decline -44.1% in Q2 on -10.9% lower revenues. Consensus earnings estimates shows that overall profitability for the S&P 500 index will not go back to pre-Covid levels even in 2021, with major sectors like Energy, Transportation, Consumer Discretionary, Industrials and even Financials, expected to earn less in 2021 than they did in 2019. Despite the lower earnings forecasts, the S&P 500's forward price-earnings ratio which is measured using earnings estimates for the next 12 months, has jumped to nearly its highest levels in almost two decades.

Elsewhere, in Canada, coronavirus cases stand at 103,000 as provinces continue forward with their reopening's. Canada April GDP will be announced on Tuesday with Statistics Canada estimating an 11% decline for April while consensus calls for a 12.3% drop. May and June economic data has shown some improvement, so April is marked as the low point for the Canadian economy. Prime Minister Trudeau addressed the proposals from the U.S. about the possibility of more tariffs on aluminum on Monday not confirming their validity. Trudeau did come out and say "The United States needs Canadian aluminum. They do not produce enough, nowhere near enough aluminum in the States to fulfill their domestic manufacturing needs." The report of the U.S. imposing tariffs on Canadian aluminum would go into effect on Canada day- the same day the new Canada-U.S.-Mexico (CUSMA) trade deal comes into effect. If the Trump administration does, in fact, impose a new round of tariffs on July 1st that would mark two years to the day since it last imposed steep tariffs of 25% on Canadian steel and 10% on Canadian aluminum. That move came as part of a bid to exert pressure in the renegotiation of the new NAFTA deal, now sometimes called CUSMA.

IN THE WEEK AHEAD

There's no doubt that the Fed stimulus has inflated P/E multiples leading to overbought conditions. Cash in money-market funds has reached almost its highest on record going back to 1992. This is a clear signal that investors are either waiting for market volatility to die down and for the economy to stabilize before putting cash to work or investors are leaving ammunition on the sidelines to deploy capital on any downturn. The near-term equity market downside could be closer than we think as some institutional players begin their portfolio rebalancing and adding the winners of the second quarter (window dressing).

Our quote of the week is from American investor, Philip Fisher.

"The stock market is filled with individuals who know the price of everything, but the value of nothing."

FINANCIAL PLANNING TIP OF THE WEEK

Who should I name as my executor and what are the following tips to look out for;

1. **Objectivity:** Choose someone who can be diplomatic and handle family dynamics.
2. **Location:** If you live in BC and must travel to another province, ensure you know the local laws.
3. **Flexible Schedule:** The role of an executor takes time which can be difficult for busy individuals.
4. **Age and Health:** Ask your executor if they are willing to take on the responsibility
5. **Handling Family Dynamics:** Is the person capable of keeping their emotions out of it.
6. **Knowledge of Financial Issues:** Being an executor is similar to being a financial advisor, accountant, and lawyer combined as one.





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