

ROYDS REPORT

October 2024

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October just flew by. Elaine got home from Papua New Guinea (over 14,000 km away, and in some ways, many centuries away). Jordan and Elaine joined iA Private Wealth. We and our staff (Sarah, Marissa, Paulene, Samantha and Dharini, who is just back from maternity leave, not to mention our 4 footed greeters, Holly, and her new little sister, Ella, to replace the late Piper) have been busy transferring our clients' information onto new iA Private Wealth forms, so we could continue working with everyone. We'll be working hard on this for some time to come. So, this will be a short Royds Report for October with only 2 topics.

Election

By the time you get this, the US election day will be only days away. Sadly, it may not be known who the next president will be for some time after election day. Any uncertainty around this may upset markets and make them choppy, or extra volatile. It's important to remember that the value of a company is related to how much money it makes or has the potential to make. The price of a company's shares often disconnects from its value and the price reflects investors' emotions, particularly fear and greed. Warren Buffett is well known for paraphrasing his mentor, Ben Graham, in saying that in the short run, the market is a voting machine, but in the long run, the market sees the true value of a company and acts like a weighing machine assessing the company. We may see emotions swaying market prices more than usual around the time of the election, but except to the extent that a president truly affects a company's profitability, we need to keep our eye on long-term value and not react to any crazy short-term pricing.

That said, each presidential candidate is expected to have some impact, to the extent the house and senate support their ideas. In Picton Mahoney's Q4 2024 Investment Review and Outlook, they point out that "If Donald Trump wins, his promised tariffs on Chinese goods could result in materially higher U.S. inflation. And if Kamala Harris wins, her promise of tax hikes could cause more economic weakness." Neither candidate has announced any intentions of tackling the US government debt issue. More on that in the next section. Source: Picton Mahoney Asset Management Q4 2024 Investment Review & Outlook.

Economic Outlook

The US Economy is doing very well. You may have guessed that by the stock market behaviour this fall. Briefly, the US Federal Reserve cut interest rates by .5% (usually call 50 bps, pronounced beeps). That's a signal that it doesn't think the economy is overheated and it isn't as afraid of inflation as it has been. Inflation hasn't been conquered though. There are still some stimulants for inflation: expected strong US federal government spending funded by new debt, a decline in the immigrant labour supply which could lead to wage inflation, more restrictions/tariffs, and the clean energy agenda. Too high inflation is always a worry, because it can bring about market corrections. "However, this time may be different because the economy is **on the brink of an AI-driven productivity boom**. The Atlanta Fed's GDPNow tracking model

raised Q3's real GDP growth rate from 3.2% to 3.4% on Thursday, **suggesting that an 2.1% annual rate of increase in labour productivity had likely been achieved.** Productivity gains and rising inflation, combined with more wealth transfers to the public, stemming from the government deficit spending, should bring higher before-tax corporate earnings. Not fearing the potential nefarious effect of the growing national debt, stocks have kept on rolling up. The S&P 500 closed at 5865 - a new all-time high -on Friday... **"American Exceptionalism"** has incentivized an avaricious foreign appetite for U.S. assets. ... (As an aside, wealthy foreigners, who have decided to leave their country, are choosing UAE, US, Singapore, Canada, and Australia.)"

"An adult discussion on the national debt is needed. **The US federal budget deficit for the fiscal year ended September 2024 stands at \$1.8 trillion representing 7.2% of the gross domestic product, the third highest in history.** Unfortunately, we are not about to get a political response. It is indeed striking to observe that solutions used in the past to fix possible public debt crises like inflation, spending cuts, capital controls, or interest cancellations are left out of the political debate. The balance of power between taxpayers, wage-earners, pensioners and bondholders is just too chaotic to resolve the issue. **The last time the US government had a surplus was 23 years ago under Clinton's administration.** It was engineered by a bipartisan approach and effort. Today, there is no apparent political commitment to narrow the deficit, let alone the \$36 trillion debt. Are there concerns about this? Definitely." Source: Marleau, Hubert (October 21, 2024). The U.S. Economy is Red Hot, [advisoranalyst.com](https://www.advisoranalyst.com).

Picton Mahoney's 4th Quarter Investment Review echoes many of the same sentiments. Here is some additional information from them that you may find interesting.

"Virtually every correction in a bull market can feel like the end of the run when you're in the middle of it. The sell-off experienced by equities in early August was no exception, and certainly seemed more dire than the correction that occurred in the previous quarter. This time the CBOE Volatility Index (VIX) spiked to extreme levels, suggesting that panic was spreading and that a recession was finally at hand. However, markets yet again shrugged off the negativity and rallied back to new highs by the end of the quarter, suggesting that the soft-landing narrative [this is where an economy goes from being overheated to a safer level of production without going through a recession to reset the economy] was back in vogue. To the bulls' credit, economic data (although somewhat mixed) still seems to favour a Goldilocks outcome, especially as central banks around the world come riding to the rescue. ... **the always critical U.S. economy does not appear to have any dangerous excesses that could lead to a deep or prolonged recession. On the contrary: solid household balance sheets, significant wealth effects and structurally tight labour markets could limit any real economic downturn to something shallow and quick to recover from.** Meanwhile, the higher interest rate sensitivity that created significant drags on much of the rest of the world's economy will likely start becoming a tailwind as most central banks continue their easing. **The Chinese authorities' recently announced bazooka-sized fiscal and monetary stimulus programs should likely contribute to shore up flagging growth in China and the world as well.**

While markets have responded bullishly to these developments, the problem for investors at this time is that the set-up for boosting risk in most markets isn't great. Valuations are rich, with a lot of the soft-landing narrative already priced in, investor positioning is stretched, and unfriendly autumn seasonality, combined with U.S. election concerns, may create near-term downside pressures on markets. And **before the economy starts responding to the lagged effects of the new monetary stimulus, investors will likely have to look past labour markets that are cooling, manufacturing output that is heading in the wrong direction and new bankruptcy filings that are steadily rising. Given these near-term hurdles, we believe patience is currently the best approach for investors.**" **"S&P 500 Index earnings are still forecast to grow 12% in the coming year, even as a new Fed cutting cycle is underway."** "So, while equity valuations are

expensive at this time, it is possible that they could get even more expensive, if investors really embrace the stock market, given falling interest rates and stable to potentially accelerating economic growth”.

“U.S. inflation has become decidedly bifurcated since 2022. **Goods prices have been in outright deflation as of late**, aiding the Fed’s efforts to bring consumer prices back to target. Complicating matters, unfortunately, is **services inflation, which has proven to be both elevated and stickier**. Just as in the 1970s, the U.S. faces potential shortages in key parts of the economy that could become an issue once the U.S. and global economies begin to reaccelerate. **Electricity and copper are examples of commodities that are already in short supply and that could become even more scarce when the economy reaccelerates and/or recovers in the next cycle. A structural shortage of U.S. housing also poses challenges** for the Fed. U.S. home prices and rents continue to increase. But as a result of high interest rates, the housing completion rate is stalling, and the problem of the underlying supply shortage is not being addressed. Instead, it is likely being exacerbated. Source: Picton Mahoney Asset Management Q4 2024 Investment Review & Outlook.

So as usual, everything is not all positive. There are still some dangers on the horizon, but there are also lots of strengths in the U.S. and world economies. We think things look good for markets, but curve balls can come anytime. As usual, it’s important to stay invested for the long-term and not have knee-jerk reactions to any news or market volatility.

Call us if you have any questions or concerns. Our phone numbers are the same and so is our address. Our new email addresses are shown below. We look forward to continuing to work with you.

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