Wealth Management
Dominion Securities

Cooper Wealth Management of
RBC Dominion Securities

Thoughts on the market

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RBC Dominion Securities Inc.

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The Little Engine That Does

"I know I can, I know I can…"
– The Little Engine That Could

In the children's story "The Little Engine that could", a small train climbs a large hill because it believes in itself. Based on population, the US represents only 4.23% of the world, yet it has become the economic engine that pulls the world's markets behind it.

This month, we will review some of the key US economic metrics to attempt to gauge the extent of their economic dominance and its effect on the rest of the world, as well as discuss current market conditions and some portfolio names we will be looking to add in the coming months.

To begin with, let's look at the US stock market. At the end of last year, the US market accounted for 46.3% of all global market capitalization; in dollar terms over $50 trillion. In terms of growth in the last decade, the Dow Jones is up 138%, the Nasdaq is up 347%, while the next two largest indexes, China and Japan, were up 50% and 160% respectively. However, we would point out that while the other countries have climbed fairly consistently, Japan is now only getting back to the market high. The TSX grew by 50% also. As to relative size, if the top 7 US stocks were traded on a separate exchange, they would represent the third largest exchange, in a virtual tie with Japan. For a Canadian perspective, the market value of Microsoft alone is greater than the value of the entire TSX combined.

Moving on to the US dollar, it has been the world's reserve currency since World War II. The US dollar currently represents approximately 58% of global currency reserves. The dollar is also involved in 90% of all global foreign exchange transactions and is the trading currency for most major global commodities such as gold, oil, and copper.

From finance through any number of economic or social categories, the US holds globally dominant influence. The question we need to answer as Canadian investors is how to best position our investments to take advantage of US strengths while avoiding problem areas. To answer this question, we begin with a review of the US economy.

For the latest quarter, US Gross Domestic Product (GDP) was up a healthy 4.8%, unemployment remains at a low 3.7% and consumer spending remains healthy. US inflation is down to 3.1% and had been generally trending lower. One nagging concern has been the possibility of a recession due the delayed effect of interest rates but so far that has not occurred and seems less likely as time passes. The level of interest rates has been the main point of concern but there is relief on the horizon as the US Federal Reserve has forecast three interest rate cuts this year, likely to start in the summer.

On the corporate level, it was another quarter of solid earnings with 73% of S&P 500 companies beating estimates. The one area where we have to be selective is technology. The euphoria surrounding generative artificial intelligence has caused stock prices in this area to rise dramatically, making good value more difficult to find. The current technology boom has been compared to the boom and bust in 1999 but the current cycle has one major difference in that the majority of companies are extremely profitable unlike the Nortels of the last generation. That being said, we still have to be selective as to how best to participate. Microsoft remains a key investment as the current leader in the AI space. For data security, Palo Alto and Crowdstrike are our top choices. Companies will also need to maximize their data management so companies like Arista Networks and Datadog will benefit. Another way we are participating in the sector is through the chipmakers. Nvidia is the dominant supplier in the market, but the high share price and very high earnings multiple make it too expensive at this time. However, rival chipmaker Advanced Micro Devices and Applied Materials, which manufactures chip making equipment offer better relative value. For now, Nvidia is the bellwether for technology as a whole and we will monitor developments as this technology evolves. One further interesting way to invest in technology is Amazon. The company over expanded their delivery service during Covid and had to take some significant write offs but is now back on track and their unique blend of online retail dominance and cloud computing should allow them to grow significantly in the coming years.

The US market is primarily focused on growth and the challenge is finding growth at a reasonable price. We are also looking for strong management, financial strength, and companies with competitive advantages in diverse parts of the economy. A company we believe fits these criteria is Owens Corning. Owens is the leading manufacturer of insulation and roofing materials. With the housing shortage throughout North America, we expect the demand for building materials to remain strong and Owens provides a lower risk point of entry into the housing market.

One further name we like is the Progressive Corporation, a leading US Insurance company in multiple lines of home and auto insurance. Declining interest rates this year should improve overall economic results and allow this innovative company to increase both market share and profit margins.

In the Canadian market, the focus of our portfolio is primarily income, but we are adding one growth oriented name, Loblaws. As Canada's leading grocery retailer, they have managed to increase their market share since Covid and are completing a $4 billion expansion this year to build new stores.

For additional income to help reduce portfolio volatility, we are adding positions in two real estate income trusts to the portfolio: Choice Properties and Killam Apartment REIT. Choice is the property arm of Loblaws and given their expansion plans and forecast lower interest rates, we believe this to be a good entry point. Killam invests in rental apartments in major Canadian cities such as Toronto and with the current housing shortage, we expect their earnings to be steady over at least the next few years.

In closing, the US remains the global economic engine and for now, most things appear to be running well. With the market having been moving at full steam in the last few months, we have carefully selected a portfolio designed to balance income and growth, as well as US and Canadian stocks to help keep portfolio returns on track. Until next month, stay well.

As always, questions, comments, concerns, and feedback are always welcome.

Yours truly,

Trevor, Walter, and the Cooper Wealth Management team

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