Wealth Management
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Why Markets Don't Act The Way We Feel

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We are getting closer to summer by the day, and the weather is not the only thing that is heating up!

The S&P 500 closed above the 4,200 mark on Friday, May 26th for the first time since August of 2022. That is now a 20% bounce off the recent bottom of October, driven mainly by some of the largest companies in the world beating earnings expectations and forecasting solid growth (ie. Apple, NVIDIA, Alphabet, Microsoft). Despite this, the majority of market commentary continues to be skeptical of this rally, while media headlines are still mainly focused on factors that are bearish in nature: potential recession; sticky inflation; higher interest rates; and most recently: the game of "chicken" that politicians were playing with the U.S. debt ceiling. The question that may be running through the minds of many is:

"WHY WOULD THE MARKET BE DOING SO WELL WHEN I'VE FELT SO UNCERTAIN AND CONCERNED?"

The short answer to that question: That's more often than not what stock markets do! There is some logic to this as well. For fun, let's consider a scenario where a group of 1,000 investors create a market in a new company (let's call it Fake Inc. – ticker FAKE). 500 of them invest in the stock and are positive on its future, and 500 of them hold cash and not buying at the current price of $50. Now, let's assume that prospects for this company become more uncertain. It appears that they will have higher costs (as interest rates are beginning to rise); a weaker consumer base will spend less on their product (as inflation is picking up); and expectations are for the overall economy to go into a recession several months from now. Due to all of these factors, the investors in FAKE are forecasting a rough few quarters. Some of the previously positive holders of the stock change their minds and decide to sell. The most positive investors in the stock will buy the shares, but it takes a lower price to entice them to do so. When the trades are completed, there are now 250 holders of the stock, and 750 investors that are on the sidelines. The price of FAKE stock has gone down to $40 (a drop of 20%).

So far in our example, there are only expectations of what is going to happen to this company's bottom line. Nothing concrete has officially happened, yet the stock price has taken a 20% hit due to the market's view on what inflation and interest rates could cause (sound familiar?). Fast forward a few months in our scenario: inflation has peaked but is coming down from high levels, interest rate hikes are occurring but at a slower rate; and most importantly FAKE is churning out solid earnings that beat lowered expectations. Things still seem bad out there in the economy, but maybe not so bad next year?

Now, there are some brave souls that want to put their cash back to work, and 150 investors re-enter the market to buy FAKE.

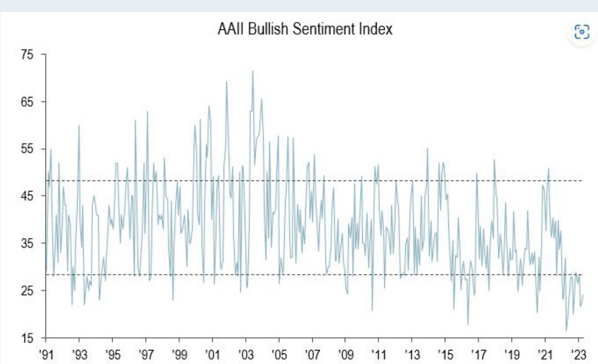
None of the 250 existing holders are looking to exit the stock at $40, so they demand a higher price to sell those shares, sending the price higher back to $50.

This very simplistic example is meant to highlight a few things about investing:

1. The stock market is heavily swayed by forecasts and not just the current situation
2. The most lucrative time to invest is when others are most fearful
3. It's easier just to remain invested and not try to guess on perfect market timing

Further on point #2, please see the attached chart that shows the investor sentiment reading for the S&P 500. Most recently, only 24.1% of investors surveyed considered themselves "Bullish". Historically, the best 12-month returns for the S&P 500 come at a time when this reading is below 29%, with a median return of **16.1%** over the next year when investors are at their **least bullish.** Conversely, the **worst** returns occur when investors are at their **most bullish** (as seen in the chart).

So, perhaps the question shouldn't be "Why is the market doing well right now?", but



"WHY IS IT CONSTANTLY A SURPRISE WHEN THE MARKET DOES WHAT IT USUALLY DOES?"

Finally, as we are quite possibly at the end of the rate hiking cycle in the U.S, we wanted to provide some information on what that can mean for the markets. As seen in the chart below, S&P 500 returns 6 months after the final rate hike are very strong (median return of 13.3% since 1990). Eventually, the Federal Reserve will start cutting interest rates as well. When they do, returns in the stock market are historically positive (median return of 9.0% 6 months after the first cut). Unless there is a renewed interest by the Fed to continue rate hikes, history will be on the side of investors. Enjoy the beginning of summer!

S&P 500 Index

Bullish Sentiment Quintile	1st <29	2nd 30-35	3rd 36-40	4th 40-46	5th 47+
Median Fwd. 12m Total Return	16.1%	11.0%	13.0%	9.9%	7.2%
Median Fwd. Change in P/E	1.1x	0.5x	-0.1x	-0.3x	-0.5x

Current: 24.1

Historical U.S. market performance when Fed policy shifts

Before and after the final rate hike in a Fed tightening cycle:
Downside risk right before the Fed pauses, but typically gains afterward

S&P 500 performance	Before final rate hike			After final rate hike		
Final Fed rate hike	6 months	3 months	1 month	1 month	3 months	6 months
Median 1970 – 1979	-1.0%	-2.5%	-4.5%	2.6%	-4.4%	2.8%
Median 1980 – 1989	9.0%	7.3%	-0.5%	1.2%	1.4%	8.0%
Median 1990 – 2018	2.4%	2.3%	1.0%	0.6%	7.2%	13.3%
Median since 1970	**2.9%**	**0.5%**	**-0.7%**	**1.0%**	**1.7%**	**5.9%**

Before and after first rate cut in a Fed loosening cycle:
Stocks typically rise, including at an above-average rate 6 months later

S&P 500 performance	Before first rate cut			After first rate cut		
First Fed rate cut	6 months	3 months	1 month	1 month	3 months	6 months
Median 1970 – 1979	0.1%	-0.1%	-0.2%	1.2%	9.6%	8.5%
Median 1980 – 1989	7.1%	4.5%	1.9%	-0.2%	7.5%	10.0%
Median 1990 – 2020	5.9%	0.5%	1.7%	0.1%	1.7%	8.8%
Median since 1970	**5.7%**	**1.3%**	**1.2%**	**0.1%**	**4.2%**	**9.0%**

Source - RBC Capital Markets U.S. Equity Strategy, Bloomberg; periods of positive performance shaded in green, periods with negative performance shaded in red

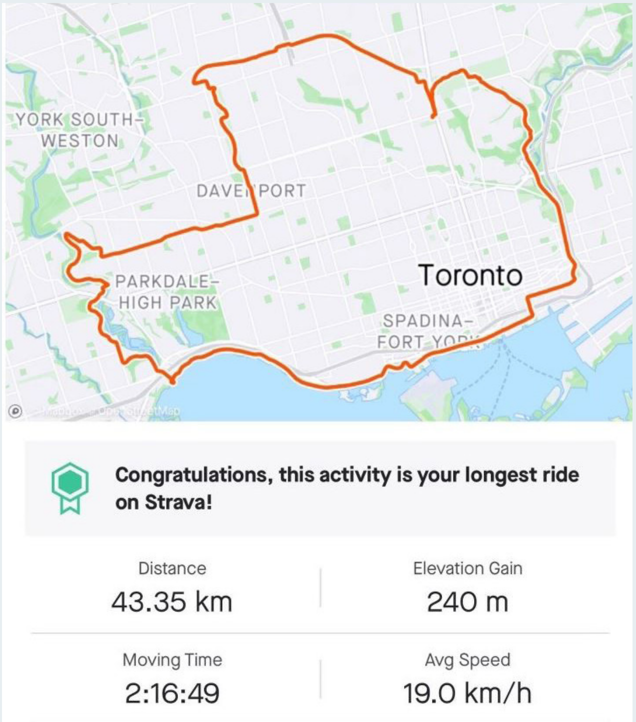
Have you given enough thought about your Power of Attorney?

This month we wanted to touch on an essential component of your financial and estate plan; **your Power of Attorney (POA).**

For any that are unfamiliar, a POA is a legal agreement whereby one person, gives another person or persons, the power and authority to act on their behalf. The POA usually falls under one of two categories: property or personal care. A POA for property is used to grant the attorney authority to make decisions about financial and property matters. A separate legal document may be used to make personal care decisions, generally referred to as a POA for personal care. Due to the nature of the business that we conduct at RBC Dominion Securities, we deal with POAs for property and financial matters, which is why the following article focuses on that topic. This is not to say that a POA for personal care is not equally important and should also be given careful thought.

Typically, POAs are drafted to allow the attorney to act for the donor after their incapacity but that does not necessarily have to be the case. While this may seem like something that would only be applicable to older clients, **having a plan for your POA is something that is useful to consider at any age.** Please take a look at this Navigator article which is full of useful information, and may raise questions that you had not previously considered.

Please contact us or a qualified legal advisor if you have further questions about setting up a POA. If you already have one and are curious about having your POA added to your accounts with us, we are always available to discuss that process as well.



One way to explore Toronto

One may think that Toronto is all homes, skyscrapers and roads, but one may not realize **Toronto has more parks, ravines and bike trails than most major cities.** Every Thursday morning at 7am, John and a group of friends from the Badminton and Racquet Club explore these bike trails on a 20 km ride. This past Tuesday the group decided to take a longer 43km route and passed many interesting sites along the way. There was a display of inukshuks plus a yacht club and kayak adventure outfitter as the trail took us north along the Humber River. Queens Quay is newly revitalized with many new developments. There we so many sailboats that lined our ride along the lake towards the Humber.

AS ALWAYS, PLEASE REACH OUT TO US DIRECTLY IF YOU HAVE ANY QUESTIONS OR CONCERNS RELATED TO YOUR PORTFOLIO.

ORD PRIVATE WEALTH MANAGEMENT

Best regards, John, David, Tim, Liam & Mikail

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