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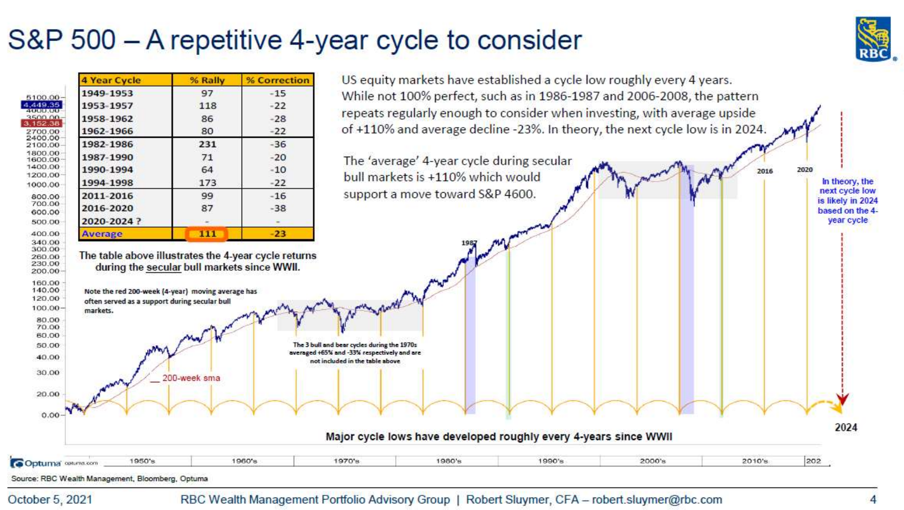
# Third Quarter 2021

September is the only month of the year that the stock market has had, on average, negative returns, in the order of roughly -1.0% since 1960. There does seem to be something of a seasonal pattern in the stock market and the 4.2% decline in the S&P 500 in September would fit the pattern. October, on the other hand, has a fierce reputation, because of some spectacular stock market crashes, notably in 1929 and 1987, but on average it has been a positive month. The 4th quarter has generally been a pretty good one. I'm not sure if Seasonal Affective Disorder explains fall's stock market weakness or if some other factors are at work but as I've often said, I sometimes find good bargains in the fall.

Bull markets are said to climb a wall of worry and in the last weeks perhaps the wall just became a little too steep; Delta variant, peak everything, shortage of everything from natural gas to shipping containers, rising bond yields, surging oil and gas prices and Washington's self-inflated crisis of the debt ceiling. Perhaps it was all getting to be a bit too much.

Beyond the seasonal pattern, there also seems to be a 4-year cyclical pattern to the stock market. RBCDS recently rehired Robert Sluymer, CFA, who for many years was our Technical Analyst but who spent a couple of years working elsewhere. I'm happy to be able to borrow his charts again and one that I've used several times in the past is his 4-year cycle chart. I must say I'm generally not a believer in stock market charts. I actually find them more useful for explaining the past than in predicting the future. However there is something psychologically reassuring about the idea that the future is predictable and I am more or less persuaded that there is something of a 4 year pattern in the stock market, perhaps linked to the presidential cycle. For many years Robert has been illustrating this pattern with this chart:




| 4 Year Cycle | % Rally | % Correction |
|---|---|---|
| 1949-1953 | 97 | -15 |
| 1953-1957 | 118 | -22 |
| 1958-1962 | 86 | -28 |
| 1962-1966 | 80 | -22 |
| 1982-1986 | 231 | -36 |
| 1987-1990 | 71 | -20 |
| 1990-1994 | 64 | -10 |
| 1994-1998 | 173 | -22 |
| 2011-2016 | 99 | -16 |
| 2016-2020 | 87 | -38 |
| 2020-2024 ? | - | - |
| Average | 111 | -23 |

As Robert says, in theory the next 4 year cycle low should come in 2024. In practice, I will continue taking one day at a time.

Last month for Team Stedman's regular feature article we used Dan Chornous's quarterly slide show, The Global Investment Outlook, without much explanation as it was hot off the press. Dan Chornous, CFA, is Chief Investment Officer at RBC Asset Management, a position he has held for some time. Before that he played a similar role at RBC Dominion Securities. He regularly uses a chart ***S&P 500 equilibrium Normalized earnings and valuations***, that I have borrowed from time to time over the years:


It was first developed 40 years ago by Bill Moriarty when he and I both worked at a small company that was called R.A. Daly. Coincidentally, we both moved to Dominion Securities in 1982 and, as our Chief Strategist, Bill brought the chart with him. In the years since Dan has kept using it. The chart shows the S&P 500 from 1960 to today moving within a fair value band. The band is based on normalized earnings (normal profit margins) and today's low interest rates and low inflation. There are several things about this chart I would like to bring to your attention. Firstly, notice that the stock market index moves from the bottom left corner of the chart to the top right corner. In other words, in the long-term at least, stock prices move up. Secondly, notice that since 1960 there have been only two times when the S&P 500 has moved above the upper boundary of the fair value bond, and, that this is one of those times. Granted the extent of the over valuation today is nothing like it was during the technology stock craze of the late 1990s, which resulted in three quarters of Internet companies going bankrupt. Still, the overvaluation of U.S. stocks is at least something to be mindful of. Overpriced stock markets are vulnerable to shocks. During that earlier period of technology craziness value stocks were greatly underappreciated and today, similarly, there seems to be pockets of speculation that can be avoided.

Although I might like to think that there are patterns to the movement in stock markets, my investment philosophy is firmly based on the principle that the future is uncertain. When I'm asked what the stock market is going to do I might say it is going to go up 9.2% in the next year, because that is the 50 year average (in truth I would haircut that guess by a percentage or two today because interest rates have already fallen for 40 years). When asked, when is it a good time to buy? I might quote Sir John Templeton and say the time to buy is whenever you have the money.

Elena Venneri has kindly agreed to become a full time member of our team and Margarita Martinez Elizondo is back from maternity leave and, for that I am grateful. For all of you I am thankful for helping me get through this worrisome time and for helping to make our work fun. Thank you for reading this letter. Happy Thanksgiving.

Sincerely,

George Stedman, CFA
Senior Portfolio Manager
*Please visit us at* [www.georgestedman.com](http://www.georgestedman.com)