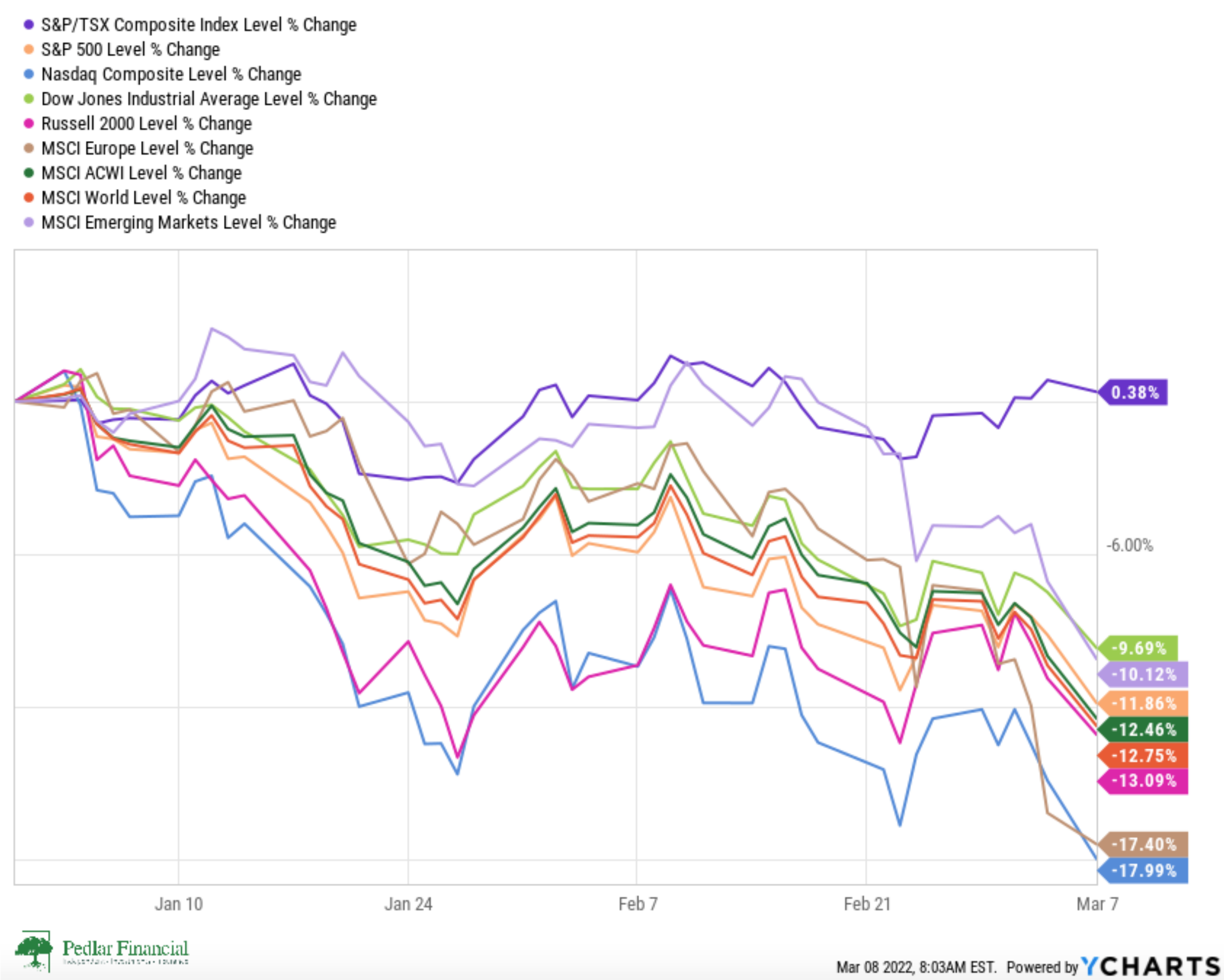
Market Perspectives

March 8.2022

The start of 2022 has been incredibly exhausting for investors. While Canada is level on the year solely in part to sky rocketing oil prices, global markets are down across the board. The S&P 500 and Dow Index have entered correction territory (down -10% from peak) while the Nasdaq, Russell 2000 and European indexes have entered or are getting near bear market territory. Investors who have been nervous about a potential policy mistake by the U.S. Federal Reserve have to now deal with the ongoing tensions between Russia and Ukraine. Over the past decade, only 2016 and 2020 saw a drop of more than 10% in the S&P 500 in the first quarter. Historically, we typically don't experience weak starts to the year, but the most recent turn of events has put additional pressure on markets.



What do we do about it?

In short, nothing. In periods of heightened volatility, it is never prudent to do a complete overhaul of your asset allocation that has been carefully designed considering your risk tolerance coupled with your investment time horizon. In terms of the current geopolitical risks, if we let history be our guide, it would show that the impact of geopolitical military activities on markets are reasonably short lived. In 2014, when the Russian Federation annexed Crimea, the S&P 500 Price Index fell nearly 6% leading into the event, only to recover its losses a few months later.

Stock markets typically take geopolitical events in stride. History would suggest the geopolitical risk premium built into commodities and the negative market sentiment over the past few months will likely be short term. Uncertainty is the name of the game; risk premiums are rising – equity markets are see-sawing on the volatile situation. Bond yields are stable, providing some risk protection to balanced investors. And other safe-haven assets like the U.S. dollar and gold are also rallying.

In times like these it's important we rely on the weight of history to guide us and temper any knee-jerk reactions. Although memories are short, capital markets have faced these situations many times in the past decades, and they eventually recover. See below:

Market Crisis and Subsequent Returns

Crisis	Market Low	Related Market Decline	Months to Recover	1 Year Later	2 Years Later
The Korean War	13-Jul-50	-14.0%	2	31.7%	49.7%
Cuban Missile Crisis	23-Oct-62	-26.4%	10	36.5%	59.2%
JFK Assassination	22-Nov-63	-2.8%	<1	23.9%	31.6%
1969 to 70 Market Break	26-May-70	-36.1%	21	43.7%	59.7%
1973 to 74 Market Break	06-Dec-74	-45.9%	67	33.5%	59.3%
1979 to 80 Oil Crisis	27-Mar-80	-17.1%	3	37.1%	14.0%
1987 Stock Market Crash	19-Oct-87	-33.2%	21	23.2%	54.4%
Desert Storm	11-Oct-90	-19.9%	4	29.1%	36.3%
Soviet Coup D'état Attempt	19-Aug-91	-3.6%	<1	11.1%	21.2%
Asian Financial Crisis	02-Apr-97	-8.1%	1	49.3%	72.5%
Dot-com Bubble crash	09-Oct-02	-49.1%	55	33.7%	44.5%
Sept 11th	21-Sep-01	-11.6%	1	-12.5%	7.3%
Invasion of Iraq	11-Mar-03	-14.7%	2	38.2%	49.9%
North Korean Missile Test	17-Jul-06	-6.9%	2	25.5%	2.1%
Subprime Mortgage Crisis	09-Mar-09	-56.8%	47	68.6%	95.1%
US Debt Rating Downgrade	03-Oct-11	-19.4%	5	32.0%	52.2%
Crimea Annexation	03-Feb-14	-5.8%	<1	17.7%	9.8%
China Yuan Devaluation	11-Feb-16	-13.0%	3	26.6%	43.2%
2018 Global Recession Scare	24-Dec-18	-19.8%	4	37.1%	57.5%
COVID-19 Pandemic	23-Mar-20	-33.9%	4	74.8%	-
Average		**-21.9%**	**12.8**	**33.0%**	**43.1%**

Snapshots in time of significant negative international events from 1950 to January 31, 2022, and the subsequent change in market value from the stock market low in that calendar year to one and two years after. Source: Datastream and Bloomberg. Benchmark: S&P 500 Composite, US$ return.

For investors, all eyes should be on the U.S. Federal Reserve

Investors will refocus on central bank policy once the tensions between Russia and Ukraine dissipate, or as other market situations arise. Since the start of the year, there has been a material shift in market expectations regarding the path of Fed rate hikes. It's now expected to increase its overnight rate at least six times in 2022, from the expectation of three to start the year. Markets were weak leading into this event on fears of the U.S. Federal Reserve making a policy mistake causing a recession.

Over the past week, the odds of the Fed hiking 50 basis points at their next meeting later next week have plummeted, with the markets pricing in only a 25-basis-point increase. The market has recognized that the Fed needs to understand the implications of the Russian-Ukraine conflict on oil prices and global economic activity. The Fed is likely to be more cautious now than what it may have been a week or so ago. As the year progresses, we continue to believe that the Fed will raise interest rates less than what the market expects leading to a pivot in the narrative that unfolded in January and February. A change toward less hawkish sentiment coupled with a good fundamental backdrop provides a positive path forward for returns.

You'll most likely feel the longer-term impacts when filling up your car

Oil prices (measured by WTI) have increased approximately 65% since the beginning of December on concerns of a disruption in Russian energy supplies. While oil prices are likely to remain at these levels until tensions decrease, it's likely a low probability event that Russian energy exports be cut off entirely from global consumers. In a worst-case scenario, oil prices would spike even more, impacting the global economy.

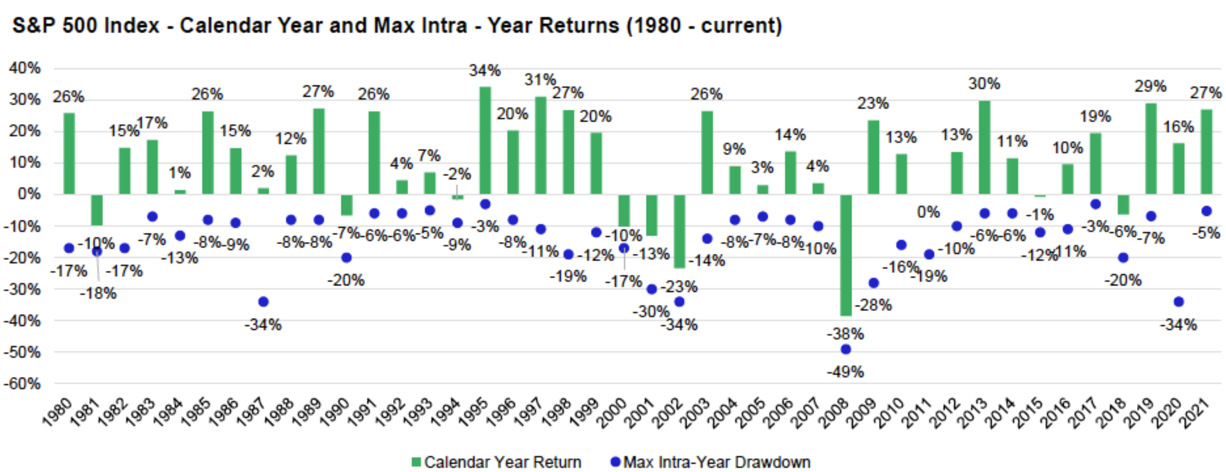
Russia has a strong economic interest in continuing to sell its energy. Its government budget is supported by oil revenue, which makes up nearly 40% of its exports. On the flip side, Europe depends on Russian energy. Germany and Italy's share of gas supply from Russia is almost 50%, according to the European Union Agency for the Cooperation of Energy Regulators. Both sides lose, increasing the odds of it not happening.

Over the next few months, the geopolitical premium built into oil prices today will likely go away but supply-and-demand dynamics will continue to support oil prices above US$100/bbl as global economies continue to fully reopen leading into the summer.

Keep in Mind – Corrections are Normal

Markets have been through 30+ pullbacks since 2009 – we have recovered through every single one. 10% corrections happen often, in fact 50% of the time. 20% corrections happen 20% of the time.

Stock market corrections are very common and very difficult to predict. Since 1980, the S&P 500 index has fallen an average of 14.3% in any given calendar year but is positive 78% of the time with an average return of 10.3%



In **2021**, the S&P 500 returned 26.89% (in USD) on the calendar year while never exceeding a drop the entire year of 5% (see chart above). Although a drop from the high of only 5% is extremely uncommon consider that if an investor missed the 10 best trading days of the year by trying to time the market that return would get dwindled down to 9.09%

2020 provides a better example as the S&P 500 had a very sharp and concentrated selloff. The S&P 500 returned 16.26% (in USD) on the calendar year while experiencing an intra-year correction of 34% as the COVID pandemic sent a risk off environment across the board. In hindsight, this selloff lasted 25 trading days (Feb 19 – Mar 23) but who would have guessed on the close of March 23rd, 2020 that we reached the bottom? If an investor missed the 10 best trading days of 2020 by trying to time the market their return would be negative -42.2%. Those best 10 days were between March 2nd to April 8th. In comparison, 7 of the worst 10 days on the year were during that selloff. Reality is, it doesn't matter how you spin it; an investor would have been in a materially worst place by trying to time the market during this period of incredible uncertainty.

You can do this experiment with any calendar year and get similar results all pointing to the fact that timing the market never works. Reality is the best days in the market most commonly occur in time periods with the largest down days. You cannot time equity markets rather thoughtful long-term investors reap rewards by the "time they spend in the market." In the big picture; news headlines, short-term volatility and market fluctuations serve nothing short of little detours on the way to long term success. History has proved that there's always some element of background noise in the world trying to distract us:

1962	Cuban missile crisis	**1981**	Market slumps	**2002**	WorldCom accounting scandal
1963	Kennedy assassination	**1982**	Worst recession in 40 years	**2003**	War in Iraq
1964	Gulf of Tonkin	**1983**	U.S. Embassy, Marine barracks bombed	**2004**	Madrid terrorist attacks
1965	Civil rights marches	**1984**	Record federal deficits	**2005**	London train bombing
1966	Vietnam War escalates	**1985**	Economic growth slows	**2006**	India, Israel, Lebanon bombings
1967	Newark race riots	**1987**	Record-setting market decline	**2007**	U.S. housing bubble bursts
1968	USS Pueblo seized	**1988**	Junk bond scandal	**2008**	Global financial crisis
1969	Money tightens – markets fall	**1989**	October "Mini-Crash"	**2009**	Financial crisis lingers into early 2009
1970	Cambodia invaded – Vietnam War	**1990**	Persian Gulf crisis	**2010**	European debt issues emerge
1971	Wage/price freeze	**1991**	Recession	**2011**	Japan, Fukushima earthquake
1972	Largest U.S. trade deficit ever	**1992**	Riots sweep Los Angeles	**2012**	China slowing growth concerns
1973	Energy crisis	**1993**	Bombing of World Trade Center	**2013**	U.S. government temporarily shuts down
1974	Nixon resigns	**1994**	Rising U.S. interest rates	**2014**	Russia and Ukraine conflicts
1975	Clouded economic prospects	**1995**	Oklahoma City bombing	**2015**	Paris terrorist attacks
1976	Economic recovery slows	**1996**	Taiwan Strait crisis	**2016**	Brexit – U.K. votes to exit the EU
1977	Market slumps	**1997**	Collapse of Thailand economy	**2017**	Britain triggers Article 50
1978	Interest rates rise	**1998**	President impeachment proceedings	**2018**	U.S. – China trade tensions
1979	Oil prices skyrocket	**1999**	Y2K 2000 Internet stocks plummet	**2019**	U.S. – China trade tensions continue
1980	Interest rates at all-time high	**2001**	September 11 terrorist attacks	**2020**	COVID-19 pandemic

If you had invested **$100,000** in the U.S. stock market on Jan. 1, 1960, it would be worth **$ 49,669,300** on Dec. 31, 2021!

If you stayed invested!

*Invested in the S&P 500 Index in local currency terms. Source: Market events – Ned Davis Research, Bloomberg, Fidelity Investments Canada ULC.

Final Thoughts

- We are not “market timers” rather we understand long term success involves “time in the market”. As thoughtful long-term investors it’s important in these moments we take a breath and put these issues into perspective.
- In terms of monetary policy and interest rates - this transitory period where rates are moving up should be put into context that we are coming off the floor (essentially 0). We are moving from an ultra-accommodative monetary policy to a less accommodative monetary policy - still “Accommodative”.
- This too shall pass. We have been through periods of geopolitical issues, increasing interest rates, inflation, trade wars… Good news is markets have historically continued to chug higher in every single scenario. The market is a forward-looking mechanism and good, quality businesses will never go out of favour.

‘We’ll get to our destination but there will be pit stops along the way’

Throughout the pandemic and as we navigate through this challenging period we find ourselves in today, I have consistently advocated that the best way to proceed for putting money to work is implementing a dollar-cost averaging strategy. Nobody knows with certainty what the market will look like tomorrow, next week or next month. While market volatility creates uncertainty, we need to take these pit stops in stride and focus on the road ahead to make sure we arrive at our destination.

What we do know is that markets are resilient, downturns don’t last forever and the longer we extend the time horizon out - the higher the probability a dollar invested today is worth more in the future.

Nobody likes market corrections but trust if we stay committed to our long-term goals, process, and fundamentals - together we will go far. Thanks for the continued trust to help you navigate the complexity of financial markets.

Regards,

Aaron Pedlar