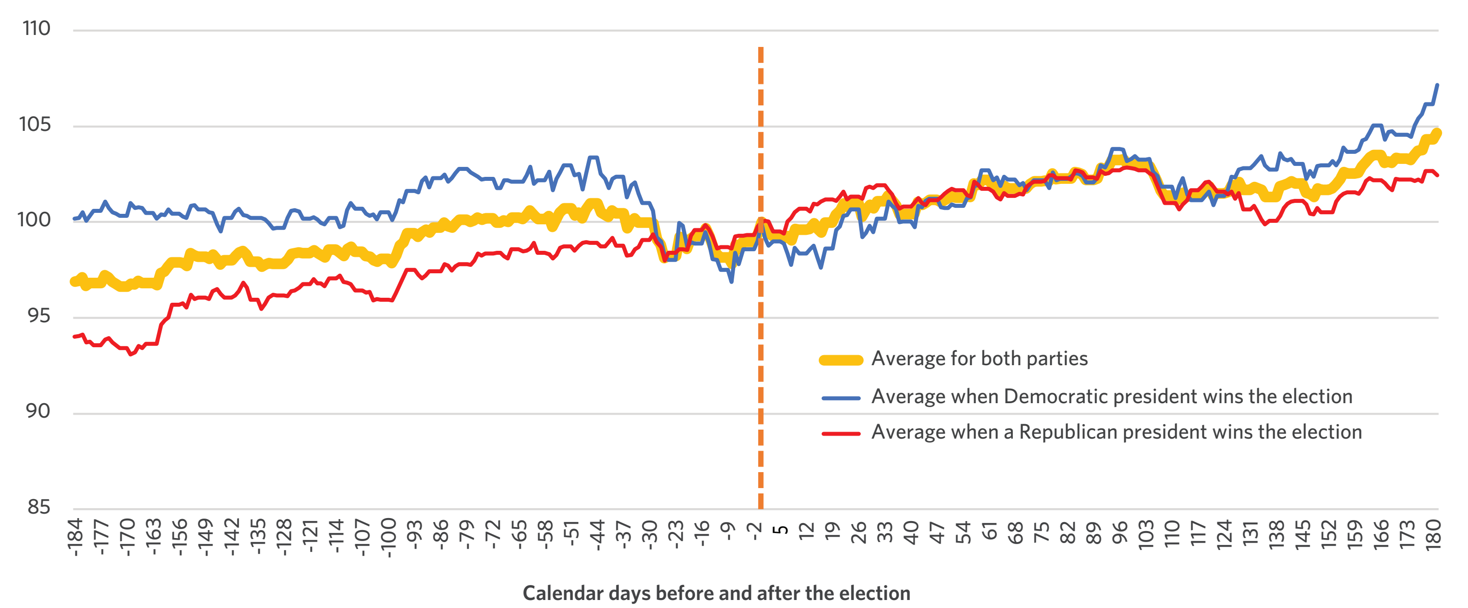
Average S&P 500 Price Return: Indexed to 100 on U.S. election day (1964 - 2020)



Source: MorningStar
Past performance is not a guarantee of future results.

Equity outlook

The U.S. and Canadian stock market performance was mixed in Q2. The U.S. S&P 500 was up about 4%, driven by technology and artificial intelligence (AI) sectors, while the Canadian TSX was down about 1%, given its higher exposure to areas like financials and industrials. For the full year, however, the U.S. market is up by about 14%, and the Canadian equity market is also higher by over 4%.

Can market leadership broaden beyond U.S. mega-cap technology? Given our view that AI is in the early innings of a long-term growth phase, we believe U.S. technology sectors will continue to play a meaningful role in portfolios. Keep in mind that the S&P 500 has nearly a 50% weight to three growth sectors — technology, communication services and consumer discretionary — all of which house mega-cap AI stocks. These companies not only have delivered on earnings but have fortress cash positions, allowing them to reinvest in their businesses and return value to shareholders.

But we continue to believe market leadership should broaden beyond U.S. mega-cap technology for a few reasons. First, we see S&P 500 earnings growth broadening in the back half of the year. While the contribution to earnings growth in Q1 came largely from technology sectors, by Q4 we expect earnings growth will be driven equally by sectors outside of technology, which should support these sectors as well. Second, we believe that as we get closer to Fed rate cuts, and the Bank of Canada (BoC) continues its rate-cutting cycle, cyclical areas of the market may play catch-up as yields moderate. And finally, while the enablers of AI like semiconductors have gained most thus far, we believe that over time, the efficiencies from AI will be felt across sectors, which should support broader stock leadership in both the U.S. and Canada.

Will the U.S. presidential election trigger volatility? Historically, stock markets have experienced volatility in the six to eight weeks prior to U.S. election day, which is slated for Nov. 5 this year. However, markets typically recover in the weeks following the election.

In this election cycle, we expect Congress to remain divided, which means no major new regulation or legislation is likely, regardless of which party wins. Markets tend to prefer this environment of political gridlock, as it means a more transparent operating environment for companies to run their businesses. Over the long run, markets tend to follow the fundamentals — including inflation, interest rates and economic growth — more so than politics and elections.

▶ Action for investors

We recommend using bouts of volatility as opportunities to rebalance and diversify portfolios. We remain overweight on U.S. large- and mid-cap equities, both of which can benefit as the Fed and BoC implement interest rate cuts and earnings growth broadens.

Investing in equities involves risks. The value of your shares will fluctuate and you may lose principal.
Mid- and Small-cap stocks tend to be more volatile than large company stocks.
Diversification does not guarantee a profit or protect against loss in declining markets.

