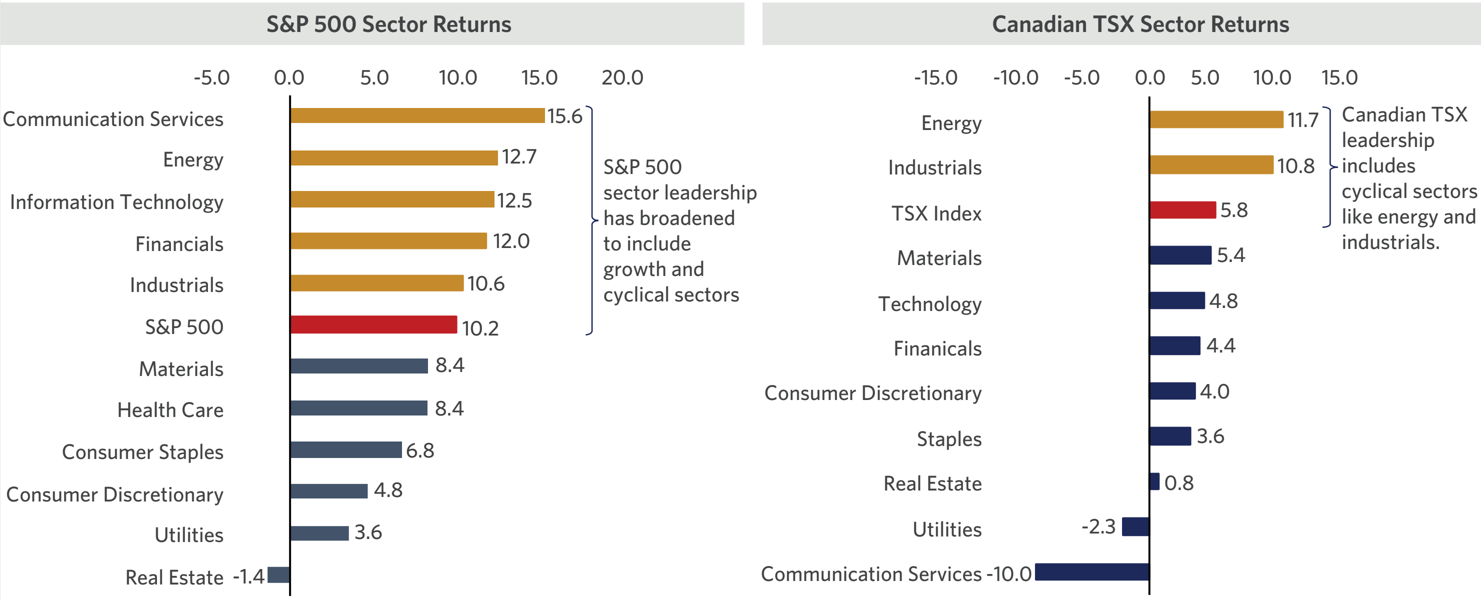
2024 YTD sector returns, S&P 500 & Canadian TSX (%)



Source: FactSet, as of 3/31/24

Equity outlook

Stock markets continued to rally in the first quarter of 2024, with the TSX up by around 6% and the S&P 500 higher by nearly 10%. Underneath the surface, we have started to see some broadening of market leadership alongside U.S. mega-cap technology stocks.

Market volatility may be likely after a strong rally – The TSX has rallied over 21% and the S&P 500 over 25% since late October through the end of the first quarter, without a correction of 5% or higher. After strong performance in the first quarter of 2024, we would expect market volatility or a pullback to emerge, perhaps as uncertainty around the path of inflation and the Bank of Canada (BoC) and the Fed lingers. However, we would not expect any market correction to morph into a more severe bear market (a pullback of 20% or more). These down markets tend to occur when the economy is headed towards a recession, or central banks are raising rates – neither of which is in place today. Thus, market volatility may be an opportunity to add to or diversify portfolios, particularly for those investors who may not have fully participated in the recent rally.

Continue to see broadening of market leadership – While the U.S. mega-cap technology theme has certainly continued to see momentum in the first quarter of 2024, there have also been encouraging signs that market leadership may be expanding. From a sector perspective, in the U.S., while technology and communication services are still top performers, cyclical sectors like energy, financials and industrials are also outperforming the S&P 500 index. Similarly, among Canadian TSX sectors, energy and industrials are both outperforming the broader index. These sectors tend to do well when economic growth is steady or improving, which we believe is the case for both the Canadian and U.S. economies in the back half of 2024. From a size perspective, small-cap and mid-cap stocks are starting to play catch up with large-cap stocks as well. In our view, this broadening in leadership may continue over the next year, especially as both the BoC and the Fed potentially pivot to rate cuts and earnings growth also broadens across sectors.

▶ Action for investors

We recommend overweighting U.S. equities in your portfolio, specifically U.S. large-cap and U.S. small- and mid-cap stocks, which we believe can continue to outperform in the year ahead, driven by both growth and cyclical sectors, as U.S. earnings growth continues to expand over the next twelve months. We would use periods of market volatility or pullbacks as opportunities to add to or diversify portfolios, as we see the broadening of market leadership continuing to play out in the year ahead.

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.

