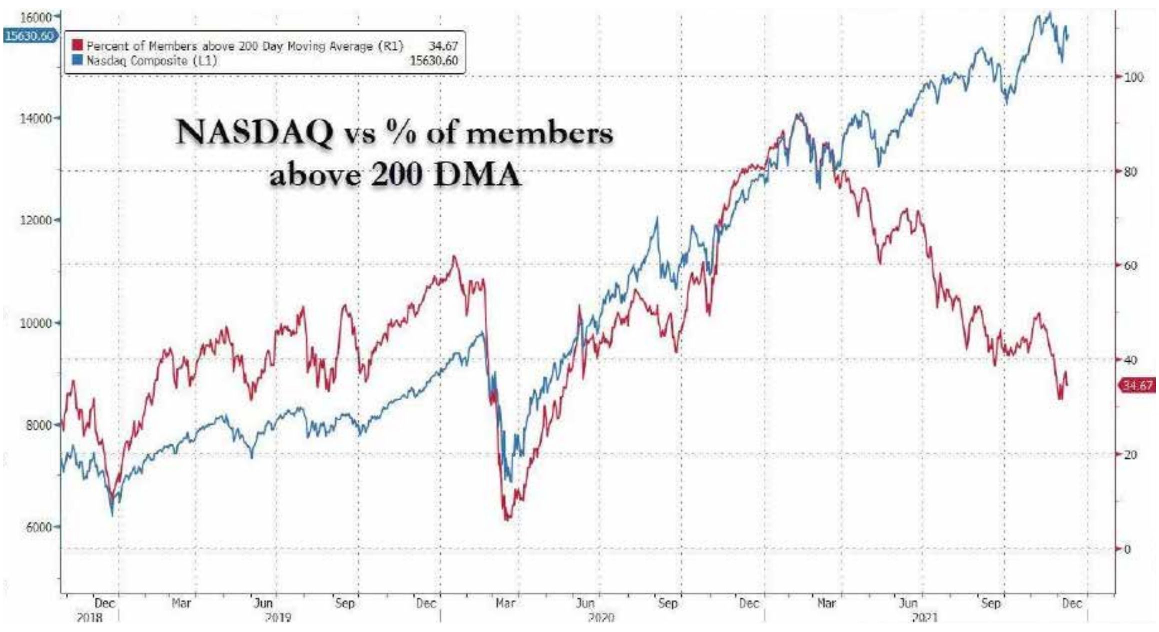
Green Private Wealth of Harbourfront Wealth Management is a discretionary portfolio management group focused on helping investors achieve their goals through building wealth and managing their risks.

Month in Review - December 2021

Volatility crept into equity markets in December when the US central bank (the Federal Reserve) admitted they've been wrong on inflation. This thereby caused some volatility in the markets as they signalled, they will likely be raising interest rates in 2022, resulting in a much tighter (restrictive) monetary policy than what is currently in place. After digesting this news mid-month with a pull-back, the market went on to rally the last ten days, with the TSX Composite rising 2.2% and the S&P 500 (in CAD) rising 2.5%. With the market expecting rate hikes on short-term interest rates (variable rates) in 2022, the Canadian Bond Universe Index finished the month up 0.9%, driving the 10-year Government of Canada lending rate down to 1.43%. Interest rate increases on short-term debt have historically slowed down the economy, as credit ends up contracting. The Canadian Bond Index recognizes this by lowering rates on longer-term debt to reflect the lower future growth.

Markets

FED policy decisions continue to cause volatility on equities, with their admission that inflation is now persistent and not transitory, causing large moves in equities underneath the main indices (Dow Jones, S&P 500, S&P TSX). High growth stocks such as those in the US ETF ARK Innovation peaked back in February, as the market was likely adjusting to higher interest rates and inflation back then (six to nine months in advance). As shown by the red line below, 65% of the companies inside the NASDAQ Index are trading below their 200 Day moving average, an indicator that shows if the price of a stock is increasing and should be bought or falling and should be sold.



However, the blue line, the Nasdaq Index, continues to move higher, with 70% of the gains in the Index in 2021 from just four stocks (Microsoft, Apple, Nvidia and Alphabet), which explains why it continues higher even though 65% of the companies peaked in February. The S&P 500 is almost identical with five companies contributing 50% of the gains since April as we can see below:

Goldman then calculates that just *the five most popular tech names - AAPL, MSFT, NVDA, TSLA, GOOGL - have contributed 51% of S&P 500 returns since April*. After contributing over double their starting weight to the index's return, these stocks now make up 22% of the S&P 500 by market cap, a 4% increase from the start of the year.

Exhibit 2: 35% of the S&P 500's YTD return has come from five stocks
as of December 9, 2021

Source: Goldman Sachs Global Investment Research

These mega-cap companies have been the largest beneficiaries of the easy monetary policy, as they have soaked up most of the liquidity. However, in soaking up this liquidity, the valuations on these companies have risen to the very high end, and when prices pull back to more reasonable valuations, it should cause the Indices to pull back too.

We continue to focus on FED policy, as the number one rule continues to be "Don't Fight the FED". This means to be aggressive when the FED is providing liquidity/keeping rates low, and then when they pivot to tighter economic policy, you should be more conservative. The FED announced in mid-December that it would accelerate the reduction in bond purchases starting in January to $60 Billion from $90 Billion in December. We expect bond purchases to be completed by late winter or early spring. Next up will be interest rate increases and forecasts for three rate hikes of 0.25% mid-late 2022. The Bank of Canada has also indicated it is taking similar action.

From a portfolio management perspective, our fund allocations did not change but within our equity pools, we saw managers taking profits in some of their technology holdings in favour of more conservative investments purchased at lower valuations. Think Advanced Micro Devices (AMD), a major maker of computer processors, which was up 56% in 2021 being sold, and Royal Bank adding in the Northgate fund. The Fidelity Long/Short Alternative fund shone in December with a return of 6%. This move to more defensive holdings is prudent given the path to tightening as outlined by the Federal Reserve.

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