

By the Way

Monthly commentary from Jack Way

The S&P 500 is up 12½% this year, in the process making several new all-time highs. There remains a concern that so much of that strength continues to come from a few technology related, high market weight stocks. NVIDIA on its own has accounted for 1/3 of this year's increase. The top 10 market weights in the Index still make up over 75% of the total, and Microsoft, NVIDIA and Apple each are over 6%. Hedge fund ownership is heavily skewed to that group with their 6 largest holdings being: Amazon, Microsoft, Meta (Facebook), Alphabet (Google), NVIDIA and Apple. It continues to be a fear of mine that if for any reason those positions needed to be unwound, the exit door would get very small in a very big hurry. As of today, there is no sign that such an eventuality is imminent. Another nagging worry is market breadth, or how many market participants are also enjoying the profits. There has been a modest, but not trivial weakness in this area. At the new high in March, 85% of the stocks in the S&P 500 traded above their 200-day moving average; at the most recent all-time high that number was 70%. That is not necessarily reason for alarm, but such divergences need to be monitored. There are several short-term internal factors that should be positive for equities, among them: corporate buybacks of a company's own stock, especially among the "Magnificent 7", remain a significant source of demand; passive and index funds will likely need to be buyers of equities at their mid-year rebalancing; and July is historically a seasonally strong month. Here's a statistic I hadn't seen before, since 1944 the average increase in the market has been 15.8% in re-election years (likely due to the sitting President having a more than casual interest in ensuring a strong economy). That is a good segue to my bottom line; as long as the President, Congress, the Treasury Department and the Federal Reserve are prepared to use whatever tools are available to support the economy, it is hard to argue markets will decline significantly.

Mixed economic releases are making predictions dangerous. This is especially so for the FED as it develops interest rate policy in an uncertain world. For example, non-farm payrolls in April missed badly to the downside indicating a weakening economy but rebounded sharply in May to above projections. Our old friend, the Purchasing Managers Index in May showed the service sector strong, but manufacturing was weak. The FED seems to have developed a "wait and see" strategy until more data is available, which probably reflects a what else can we do attitude. At any rate, consensus is still looking for a quarter point decline in the FED funds rate in each of September and December, but there's no guarantee. We've come a long way from 2023 expectations for six rate cuts this year, but the market seems okay with that as long as there is no sign of any rate increases. Other countries, Canada for one, have already started to cut given a weaker economic outlook than the U.S. Not that it means anything, but this is the first time the European Central Bank has reduced rates before the FED. Perhaps most importantly when the FED does act, the market will want to see the Board as in control and not reacting to the unexpected.

I have held a belief that investors were not giving sufficient importance to the upcoming elections in the U.S., which are now only five months away. The recent Trump guilty verdicts plus the realization that the first Presidential debate will take place in only two weeks has brought discussion of potential repercussions more to the fore. As I've said before; the country and the world could look vastly different in 2025 depending on the results. Much as I try, I can't get my mind around what this debate will look and sound like, despite the fact the perceived winner will gain an important early lead heading toward November. Some commentators have suggested that the guilty verdicts won't change voter's perception of Trump (it's too entrenched already) but could impact his perception of

himself. As such, he could become even more strident, and so far recent speeches have confirmed that possibility as his rhetoric and name calling are nastier than ever. Will he ease up for the upcoming debate? It remains to be seen, but that's certainly not his style. Biden, on the other hand, can't wilt in front of any invective, although his recent public speaking performances in France don't fill anyone with confidence. There is a reasonable expectation that the two men running for the most important job in world could turn the whole thing into something of a fiasco.

The results of the European Parliament elections are now in and are adding to the geopolitical chaos. Populist and far-right political parties soundly trounced incumbents in Germany and France (and other countries). French President Macron felt it was a significant enough disaster to call a snap election. That's a tactic already being implemented by U.K. Prime Minister, Rishi Sunak, who is also under pressure from all sides. There is a general dissatisfaction around global democracies that political parties do not represent the needs and wants of voters and it's promoting a "throw the bums out" mindset. The governments of both India and South Africa have already lost majority positions; which exit interviews reveal was based on voter's disapproval of policies dealing with three main issues: inflation, immigration and inequality. Those issues loom large in the U.S. as well, and don't speak well for President Biden's chances in November. Not to run around yelling "the sky is falling", but it's no longer just people in tin hats that are concerned about the future of democracy as we know it. (OK that is yelling "the sky is falling". Sorry.)

The Supreme Court of the U.S. (SCOTUS to many) will be releasing many impactful decisions over the next several weeks. Number one in the eyes of the public will be the two dealing with abortion. I think people need to realize that this is a very Conservative court (6-3) packed by Trump while he was in office, but the decisions are not just based on moral issues but Constitutional interpretation of state rights vs. federal oversight, and this court definitely favors states rights. Other decisions will deal with: the definition of income, does it need to be "realized" or not; social media content, is it "awful but lawful"; do environmental regulations only apply to specific things mentioned in Congressional law; and of special importance to Trump – Presidential immunity.

The U.S. two party system allows for only a "winner takes all" outcome. Other democracies approve coalitions that allow for a way forward by a compromise not just "you lose you're out" which has only amplified anger and distrust.

Marjorie Taylor Greene may be the poster woman for the divisiveness in U.S. politics. The Republican Representative to the House from Georgia brought an amendment to the floor to defund NATO the day before D-Day remembrances and got 46 other Republicans to vote with her. As a staunch Trump acolyte, she also went so far as to compare him to Jesus as she said both are "convicted felons".

President Biden's executive order to restrict the number of asylum seekers at the southern border reads almost identically to Trump's 2018 proposal that was thrown out by the courts. It seems an empty attempt to win votes.



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