Commentary for the Third Quarter of 2020

September is often referred to as the cruelest month for stock markets and it played out that way again this year as most equity markets finished in negative territory for the month. In Canada, the S&P/TSX Composite Index was down -2.1% with nine of eleven sectors finishing the month with negative returns.

Despite the downbeat ending, the third quarter – July, August and September – largely saw stock markets continue the remarkable run they've been on since the end of March. The TSX was up 4.7% during that timeframe.

The benefits of diversification were on full display in the third quarter, too, as both Asian and U.S. equities outperformed Canada while European equities were a bit of a laggard. China's extraordinary turnaround from COVID-19 lockdowns has helped fuel strong performance by Asian markets.

In the U.S., growth stocks led by mega-cap technology companies, which benefited from the move to online caused by the pandemic, saw a sell-off in early September, after having enjoyed a good quarter prior to that point. In the fortunate event that a vaccine is approved and widely accessible, we could start to see a rotation to cheaper, value stocks with Financials and travel & tourism related companies returning to favour. However, if lockdowns return due to a resurgence in the virus, the run-up by tech stocks and others may continue.

Central banks have done just about everything they can do, affirming that they will keep rates at their current ultra-low levels for at least the next two years, with the U.S. Federal Reserve pegging any future rate increases to achieving targeted inflation and employment numbers – which are likely many years off.

While this ultra-low rate environment may make it seem like bonds won't have a use in effective portfolio construction in the future; to the contrary, we still see the benefits of fixed income in providing a buffer to equity volatility. We also continue to diversify our fixed income exposure both by credit type and geography to increase returns and diversification without taking on any significant added risks.

In our Portfolios

In the Portfolios, with markets having their first down month in September since March, the defensive strategies took a bit of equity off the table in the IPC Essentials and the Counsel Strategic Portfolios, which may prove fortuitous in the short run given the shocking positive COVID-19 tests of the U.S. President and the First Lady.

The trend-following model in the IPC Essentials Portfolios reduced Canadian and International equity in the Balanced, ESG Balanced and Growth Essentials Portfolios, adding between 0.5% to 2% back to the short-term bond position. There were no changes in the Income Essentials Portfolio. We continue to hold short-term bonds only, given the higher volatility among longer-term bonds.

For the Counsel Strategic Portfolios, the Global Trend model decreased equity holdings at the end of the quarter to 63%, increasing the 'safety bucket' of short-term U.S. bonds to 37%. The North American sector holdings in the model remain at 40% and are now spread over eight sectors: Technology, Health Care, Communications, Materials, Consumer Discretionary and Staples and Industrials with Real Estate added last week. The model is not holding Energy or Utilities. There are selected holdings in Japan, Europe, Emerging Markets (EM), commodities and credit strategies.

In the income-oriented Strategic Portfolios, the income trend strategy is back up to 49% in short-term bonds from 46%, while reducing its U.S. high yield exposure. There are additional holdings in longer-dated investment grade bonds, high yield international and EM bonds and alternative sectors such as U.S. and International preferred shares, U.S. convertible bonds and senior loans.

In the Counsel Retirement Portfolios, the Defensive Global Equity strategy remains at 100% equity exposure, and the Retirement Portfolios are all invested at target allocations.

Outlook

There are many global events that will bear watching over the coming quarter, including the recovery of President Trump. In the next couple of weeks, we may see the U.S. congress reach a deal on another stimulus package, which will help buoy consumers – who comprise about 70% of the U.S. economy. Good news on a vaccine or a viable COVID-19 treatment would also provide a lift to markets. On the other hand, a contested U.S. election result would add some short-term volatility, as would a no-deal hard 'Brexit', which is increasingly looking like a strong possibility.

We believe that effective diversification remains your first and best defense against this highly uncertain environment. Whether it's by asset class or by region, a properly constructed portfolio can give you the protection you need in down markets and the ability to participate as markets rise. I like to think of this as a "winning by not losing" strategy. In an environment with high levels of uncertainty and high valuations, there is an asymmetric payoff for taking on excessive risk. Although "winning by not losing" is not nearly as appealing to our emotions as a "winning by winning" strategy, it is a better strategy for the long term.

As always, we encourage you to follow a sound financial plan, and to speak with your Advisor to ensure you are on track to meeting your investment objectives.

Sincerely,

Corrado Tiralongo,
Chief Investment Officer

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