

PENDER MARKET INSIGHTS

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There are decades when nothing happens, and then there are months when decades happen. That is what June felt like. Every day it seemed like a new, more extreme headline was coming across the screen. Yet remarkably, equity markets continued their rebound from the April lows, to close the first half of the year at an all-time high. That is called 'climbing the wall of worry' and has been impressive to watch.

The backdrop is still wildly uncertain and headline risk remains elevated. A trade war between the world's largest trading partners is disrupting global supply chains. The largest ground war in Europe since WW2 continues with no end in sight. And the proxy war in the Middle East between Iran and Israel began, with US involvement for a few hours. Yet none of that has affected investors' risk appetite as cash continues to be pulled back into the market from the sidelines.

When President Trump was re-elected last November, investors cheered the outcome and rallied markets into year end. While it wasn't the smoothest path, his first term was very positive for wealth creation as he focused on growth over conflict, and many were looking forward to a repeat of that performance. However this term has started off on a very different note. Almost immediately tariffs were imposed on both friend and foe, trade agreements were shredded and executive teams everywhere slammed the brakes on capital plans until able to get a handle on the operating landscape. Markets are well known to hate uncertainty, and uncertainty is what we have in record amounts.

One of the fears coming into this year was the ability to avoid an earnings recession. After several years of strong markets, valuations had become stretched, and for markets to move higher, earnings need to grow. Tariff and trade uncertainty put a damper on this as corporations announced Q1 results. But these initial fears appear to be receding. The consumer appears to have adjusted to higher prices and resumed normal activities. This has allowed companies to relaunch previously stalled capital expenditures and growth plans. Corporate activity is picking up which has resulted in several takeovers and IPOs. All healthy outcomes and a primary reason banks and other financial players have led equity returns recently.

But what does the second half hold? The risk is this recent market surge has pulled forward all the good news we could have expected. With markets at these levels, we are now pricing in earnings growth. There is also the expectation that trade wars will end shortly with a flurry of deals over the summer. In addition, markets are now expecting President Trump to return to his promise of cutting taxes and government regulation to become more business friendly. Those would all be a great outcome, but can it all happen?

One area to focus on for signals will be the bond market. This was expected to be the year of rate cuts, and we are still waiting for the first cut from the FOMC. Bond yields have remained higher than many expected as inflation has not cooled to the extent anticipated. Bond auctions

and debt refinancing will be a key story over the summer as well as the growing risk from President Trump's attempts to force rate cuts or undermine Fed Chair Powell.

Back in Canada, it feels like a complete reset. Gone is a government that seemed to do everything in its power to stifle growth, replaced with one that is saying all the right things to turn the ship around. This has caught global attention with the C\$ off to a strong start and increased optimism for future growth. Infrastructure building looks like a theme that could be with us for a while. The S&P/TSX is enjoying a nice start to the year, outperforming other North American markets for the first time in a while.

Yet this isn't the time to be complacent. Summer markets are risky and strange things happen with low volumes. It does need to be pointed out that even though markets are at all-time highs, one of the best performing assets this year has been gold, the original defensive asset. A 25% rally off the 'Liberation Day' lows is making everyone feel a little better heading off for summer vacations. But like all roadtrips, you need to keep the fuel topped up for future gains and I wouldn't be surprised if the warning light starts signaling there is a pause on the horizon.

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