

# The Long and Short of Equity Resilience

A Publication of BMO Capital Markets Economic Research • Douglas Porter, CFA, Chief Economist, BMO Financial Group

Equity markets slumped this week, with the S&P 500 down 1.7% and the TSX giving back 0.9%. More broadly, the market has held up remarkably well despite what would ordinarily be considered choppy waters. The S&P 500 is up 33.5% from a year ago, and momentum has held firm over the past three- and six-months, up 21% and 29% annualized, respectively. Meantime, the TSX is now routinely pushing record highs. Here is a look at three challenges facing stocks, and three factors that are helping to keep the market moving steadily higher. First, the challenges:

**Seasonal factors:** The market is currently right in the toughest part of the calendar from a historical perspective. Between 1950 and 2020, August (flat) and September (-0.5%) have recorded the weakest average monthly returns. If there was some concern heading into this period after a very strong spring and early summer (and not to jinx it with three weeks still to go in September), those concerns have eased so far.

**Delta variant:** Rising COVID cases across much of the developed world have slowed down some regional reopening and the travel that was expected to return with vigour in the second half of the year. As a result, growth has been coming in under expectations, and revisions have been tilted to the downside (we revised down our outlook for both Canada and the U.S. last week). Bloomberg's Economic Surprise Index, which measures data flow versus expectations, has turned negative for the first time since the pandemic started. True to form, areas of the equity market that thrived on a relative basis during 2020 lockdowns (e.g., technology and large caps) have been outperforming again versus areas like small caps and banks.

**Fed tapering:** Fed Chair Powell said in Jackson Hole that, "at the FOMC's recent July meeting, I was of the view, as were most participants, that if the economy evolved broadly as anticipated, it could be appropriate to start reducing the pace of asset purchases this year". The start of the road toward less-accommodative Fed policy has not spooked the market, unlike in some past episodes, but inflation concerns only seem to be mounting at this point. U.S. job openings, for example, are now at the highest level on record dating back to the early-2000s, by a long shot, and supply-side issues (growth negative and inflation positive) look to persist well into next year.

While that sounds like a pretty tough environment for equities, the market continues to push gradually higher. Here are a few reasons why:

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**Table 1 - Market Performance**

September 10, 2021		Performance (percent)					
	Current Price	1 Week	1 Mo.	3 Mo.	1 Year	Y-T-D	2020
NIKKEI 225	30,382	4.3	8.9	4.9	30.8	10.7	16.0
China CSI 300	5,014	3.5	-0.6	-4.9	9.4	-3.8	27.2
CAC 40	6,664	-0.4	-2.3	1.8	32.6	20.0	-7.1
S&P/TSX	20,633	-0.9	0.7	2.9	27.5	18.4	2.2
DAX	15,610	-1.1	-1.0	0.2	18.2	13.8	3.5
FTSE 100	7,029	-1.5	-1.8	-0.8	17.1	8.8	-14.3
NASDAQ	15,115	-1.6	2.2	7.8	38.4	17.3	43.6
S&P 500	4,459	-1.7	0.5	5.2	33.5	18.7	16.3
Dow Jones	34,608	-2.2	-1.9	0.4	25.7	13.1	7.2

Source: BMO Economics, Bloomberg

**Asset inflation:** Goods price inflation remains a key factor; wage inflation is a potential concern, but asset-price inflation is still very much alive too. While the focus on this front tends to zero in on areas like housing, commercial real estate and cryptocurrency/meme stocks, it is very much supporting the broader equity market as liquidity on both household and corporate balance sheets looks for a home and/or a hedge.

**Longer interest rate view:** While Fed tapering is the next major policy move on the radar, it appears the market is still comfortable assuming a low-for-long interest rate environment post-COVID. For now, 10- and 30-year Treasury yields have settled in slightly below pre-COVID levels. For equities, this has helped ease valuation concerns that were percolating earlier in the year. Indeed, with 10-year yields backing off more than 40 bps from the spring high, the spread between the S&P 500 earnings yield and 10-year Treasury has been able to hold steady around the five-year average, even as prices have continued higher.

**Lots of earnings support:** The Q2 earnings season was pretty much a blowout. According to Refinitiv's tally, 87% of the S&P 500 topped analyst expectations, which is well above historical norms. Earnings growth topped 95% y/y and, beyond base effects, the level of earnings on the S&P 500 has surged more than 20% above pre-COVID levels. Combined with the decline in longer-term interest rates, this has helped justify the move in prices. And, it reinforces that, even as Main Street continues to face some challenges, big businesses that trade on the S&P 500 can still thrive.

## North American Sector Performances

(% change over period)

**Table 2 - S&P 500 Sector Performance**

September 10, 2021						
S&P 500 Sectors	1 Wk	1 Mo.	3 Mo.	1 Year	Y-T-D	2020
Cons Discretionary	-0.3	1.1	5.8	21.8	12.2	32.1
Banks	-1.1	-3.2	-3.2	61.3	27.0	-16.8
Telecom Services	-1.2	2.8	8.6	42.8	27.7	22.2
Cons Staples	-1.3	0.4	2.5	13.2	7.0	7.6
Financials	-1.3	-2.1	0.7	53.4	27.1	-4.1
Utilities	-1.6	0.9	3.8	16.7	8.4	-2.8
Materials	-1.7	-1.8	-2.2	30.5	15.4	18.1
Info Technology	-1.8	2.1	10.9	37.4	19.9	42.2
Energy	-1.8	-4.7	-13.9	47.1	24.9	-37.3
Industrials	-2.5	-2.4	-1.3	33.3	14.7	9.0
Health Care	-2.7	-0.1	6.2	27.9	17.0	11.4
S&P 100 Large Cap	-1.6	0.8	6.3	32.1	19.1	19.3
S&P 600 Small Cap	-2.1	-1.2	-3.0	54.5	19.8	9.6
S&P 400 Mid Cap	-2.7	-1.2	-1.6	44.7	16.5	11.8
<b>S&amp;P 500</b>	<b>-1.7</b>	<b>0.5</b>	<b>5.2</b>	<b>33.5</b>	<b>18.7</b>	<b>16.3</b>

Source: BMO Economics, Bloomberg

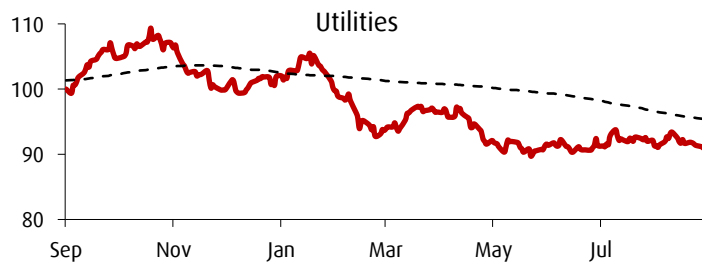
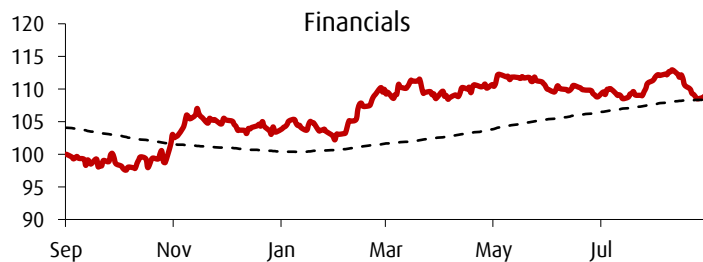
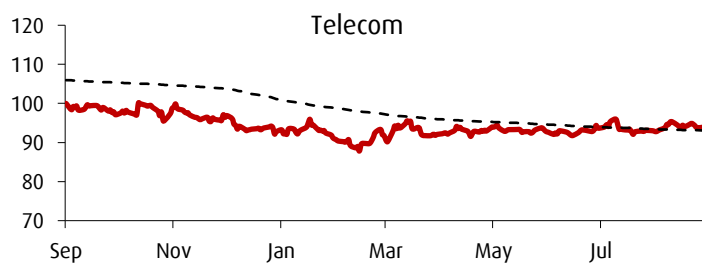
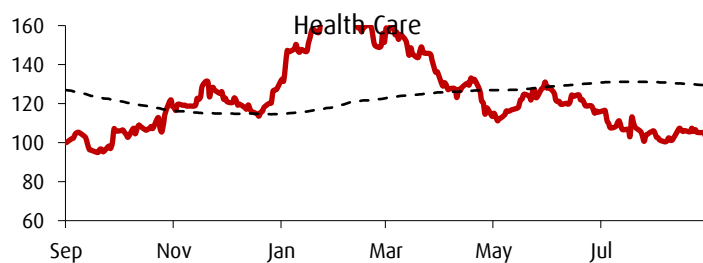
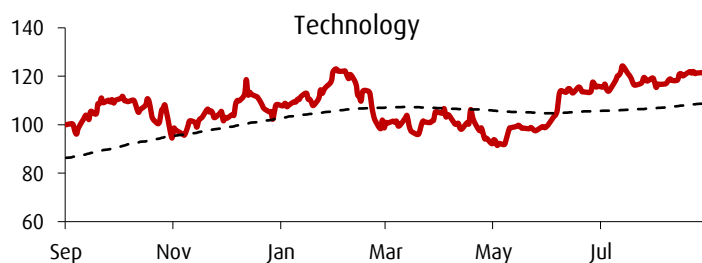
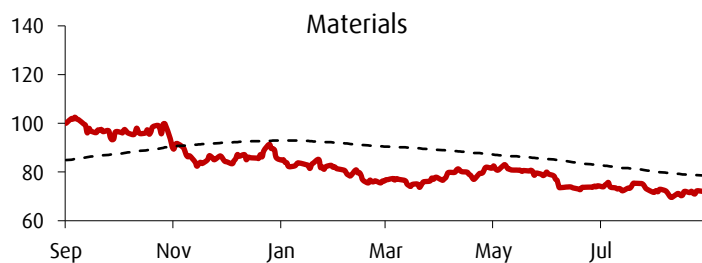
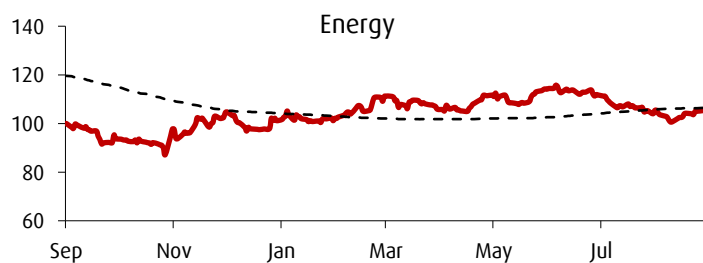
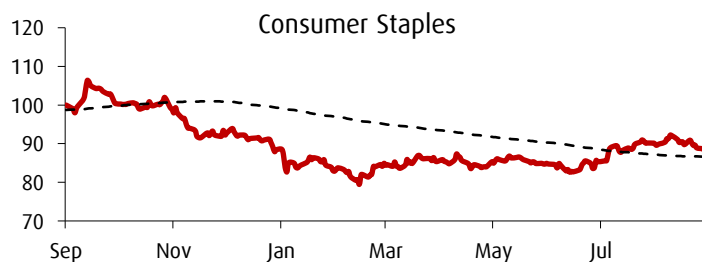
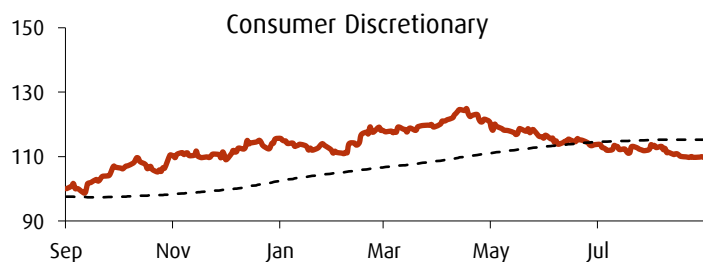
**Table 3 - TSX Sector Performance**

September 10, 2021						
TSX Sectors	1 Wk	1 Mo.	3 Mo.	1 Year	Y-T-D	2020
Energy	0.3	1.6	-4.1	35.4	28.9	-30.8
Banks	-0.1	-1.8	-0.2	38.5	22.4	-1.6
Utilities	-0.1	1.5	3.5	17.5	6.9	10.6
Financials	-0.1	-1.5	2.3	40.1	23.2	-2.9
Telecom Services	-0.4	2.2	4.6	20.3	19.3	-8.3
Cons Discretionary	-0.5	-2.4	-2.0	40.3	14.0	14.4
Cons Staples	-0.9	-0.6	7.7	14.1	16.0	2.8
Info Technology	-1.6	3.0	24.8	50.8	31.9	80.3
Industrials	-2.0	4.8	7.8	26.4	14.7	15.3
Materials	-2.6	-0.2	-8.6	-9.9	-2.5	19.5
Health Care	-4.8	-3.3	-18.7	26.9	3.1	-23.6
S&P/TSX Preferred	-0.1	0.7	0.1	19.4	12.2	0.1
S&P/TSX REITs	-1.1	0.8	4.9	37.9	24.7	-17.6
S&P/TSX Sml Cap	-1.5	1.5	-4.1	38.8	15.8	10.0
<b>TSX</b>	<b>-0.9</b>	<b>0.7</b>	<b>2.9</b>	<b>27.5</b>	<b>18.4</b>	<b>2.2</b>

Source: BMO Economics, Bloomberg

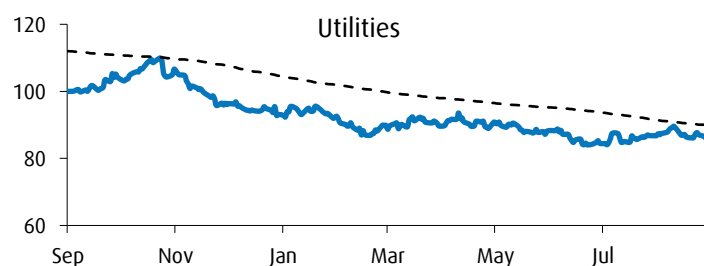
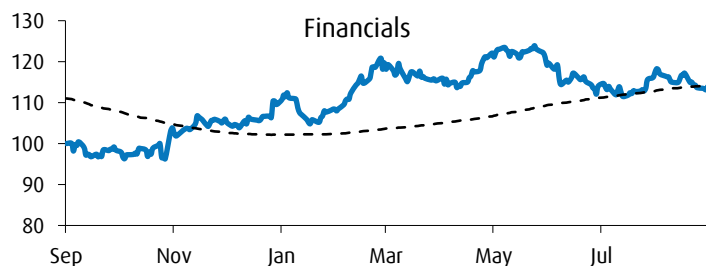
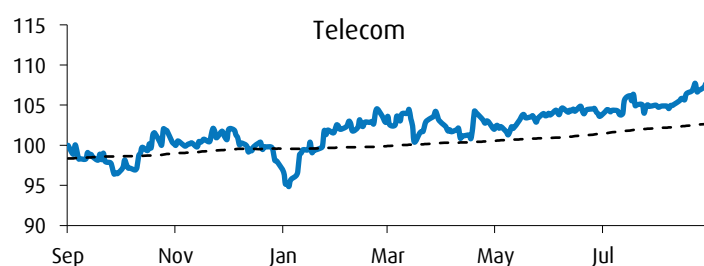
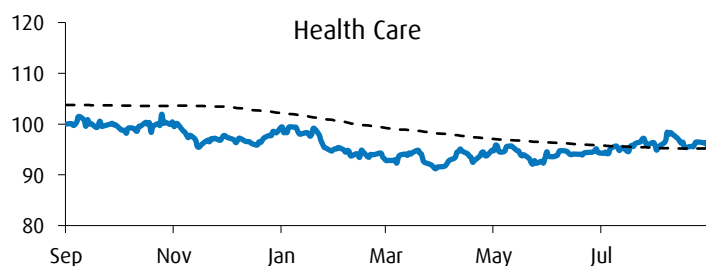
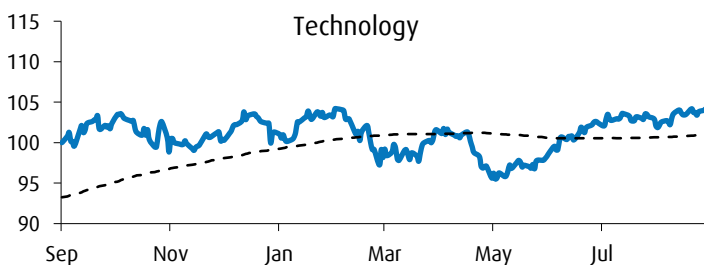
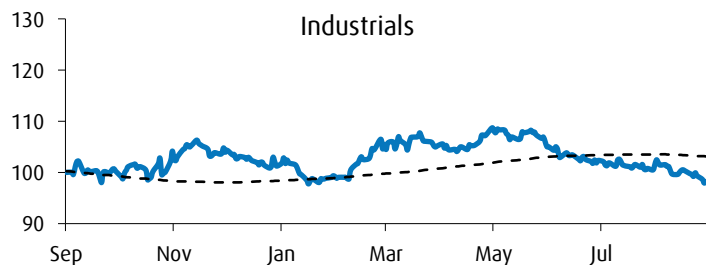
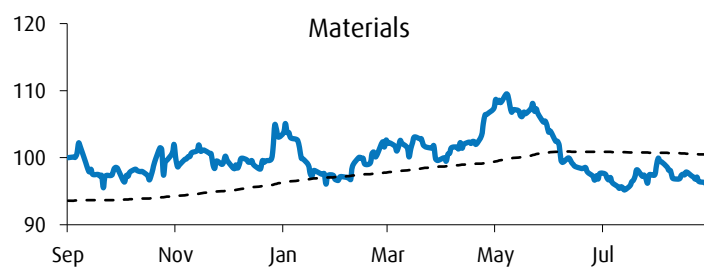
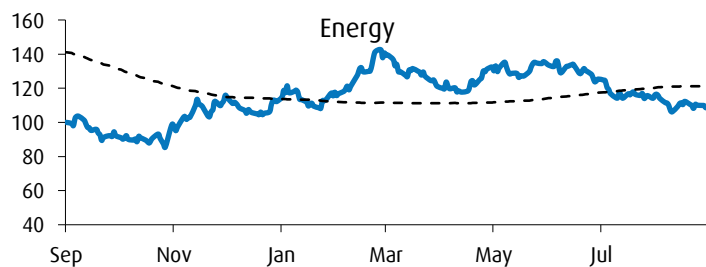
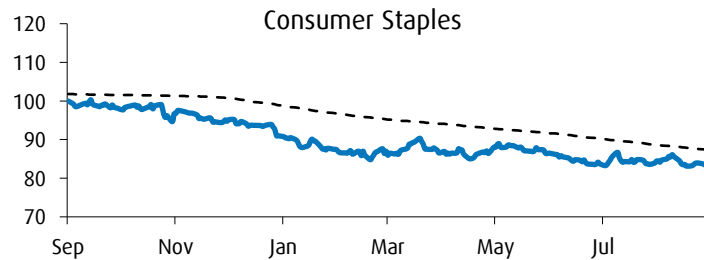
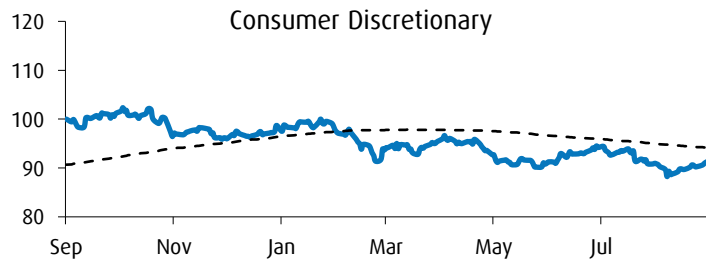
## TSX Relative Sector Performance

(relative to the index, year-ago = 100; dashed line = 200-day m.a.)



## S&P 500 Relative Sector Performance

(relative to the index, year-ago = 100; dashed line = 200-day m.a.)



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