Fourth Quarter 2021

Groundhog Quarter

The Numerous Investor Worries That Popped Up in Q3 – COVID and Related Lockdowns, US Government Gridlock, Chinese Growth, Inflation – Grew in Q4 (and Subsequently Q1 2022), Stalling Riskier Assets

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Quarterly Summary and How We're Positioning for Q1

Boy did Q4 2021 feel a lot like Q3 2021! Concerns about a new, highly contagious Delta variant in Q3 were subbed out for concerns about a new, even more contagious Omicron variant. Haggling over the US Build Back Better legislation continued, with no solution, and for virtually the same reasons that prevented its passage in Q3 (moderate Democrats blocking progressive policies). Price inflation of nearly everything continued to push higher. Chinese economic growth continued to fade as its property sector remains on the ropes.

Thankfully there were some mandatory differences in Q4 thanks to there being no holiday season in Q3, but with COVID cases spiking to all-time highs and strict government recommendations and requirements for gatherings, it sure did feel a heck of a lot like last year. Hopefully, you got through it all with more poise than Bill Murray during his run-in with a time loop, and if you didn't that's okay too!

Of all of the concerns, inflation seems to have grabbed the world's attention. Annualized inflation hit 4.8% in Canada in December, a thirty year high, while it hit an eye-melting 7% in the US in December, nearly a forty year high. Unless you haven't purchased anything in the past few months, this should come as no surprise. While inflation is tough for any household or business to deal with, inflation can be especially trying for lower-to-middle income households that were already struggling to make ends meet. This is especially true when prices of products like food and shelter are rising faster than most other products. This concern is so pervasive that in the UK, policymakers are creating a new price index to track prices related to lower income households in an attempt to understand and rectify troubles these households uniquely face, as well as prevent the greater economic damage caused due to that hardship.

If you are feeling charitable, we are confident that donations to your local food bank would go a long way these days.

In response to this high inflation, and with employment levels closer to pre-pandemic levels, investors now expect central banks to raise interest rates several times in 2022. The odds of higher interest rates in 2022 triggered a selloff in the most speculative corners of the equity markets, specifically "meme" stocks GameStop (GME) and AMC Entertainment (AMC) as well as other stocks affected by meme stock sentiment like DocuSign (DOCU), Zoom (ZM), BlackBerry (BB) and many others. Subsequent to the end of Q4, it appears this negative sentiment toward growth stocks has expanded to include larger growth names. How far the negative sentiment travels will be a matter of debate throughout Q1 2022.

As for the other investor concerns in Q4, progress and ultimate economic impact remains unclear.

Chinese economic growth is likely to be lower going forward than in the 2000s or 2010s, simply due to slowing or possibly soon to be negative population growth. As a result, China's seemingly overbuilt property sector will likely be under stress for quite some time though the government's involvement will help tamper concerns related to the Chinese property sector and economy.

The COVID Omicron variant has been hailed as a potentially positive development due to its low associated hospitalization rates and its high rate of transmissibility which helps build our society's natural immunity against the virus. How the virus continues to evolve is anyone's guess and we may continue to see government lockdowns and restrictions which impact global economic growth but a less deadly variant is an encouraging surprise for the long-term economic outlook as well as our personal day-to-day wellbeing.

The US stimulus bill remains in limbo as moderate Democratic members of congress continue to reject the party's more progressive policies. The last iterations put forth in Q4 removed many of the more radical policies and yet passage of the bill was still unsuccessful. It is now unclear whether a stimulus bill will be passed before the US mid-term election in November 2022, and depending on how that election goes, a stimulus bill may not be enacted anytime soon. With global economic growth starting to wane, the lack of a US stimulus bill may push global economic growth to pre-pandemic levels fairly soon and investors may become concerned about the lack of fiscal support.

Equities performed well in Q4, with the S&P 500 and TSX composite index finishing up 11.0% and 6.5%, respectively, perhaps as investors became numb to the concerns that initially arose in Q3 and with no new major shocks.

How To Position Portfolios Going Forward?

Our investment philosophy remains unchanged with our core tenets being diversification and value. We build portfolios to participate in strong markets but also weather tumultuous times, like the times we are seeing now in early 2022. Our philosophy allowed us to participate in market upside in Q4, largely avoid the Q4 selloff in the more speculative areas of the market, and subsequent to year-end, avoid much of the broader selloff in equity markets so far in 2022.

The specter of higher interest rates and a selloff in many growth stocks, pushed investors into low volatility, blue chip stocks in Q4. Some names that we hold that outperformed in Q4 were Cisco Systems (CSCO), Constellation Brands (STZ) and Pfizer (PFE). Pfizer continues to benefit from the longevity of the pandemic as it is now the clear COVID vaccine winner and the front-runner for most promising COVID treatment. Two stocks we hold that struggled in Q4 were Saputo (SAP) and Intel (INTC), both of which struggled from supply chain bottlenecks and cost inflation. Walt Disney (DIS) also came under pressure in Q4 as it indirectly got caught up in the meme stock selloff due to its association with Netflix, the key competitor for its Disney+ streaming service.

We continue to focus on owning an equity portfolio consisting primarily of high quality businesses whose valuation is much less extreme than average. That said, the growth stock selloff has made some of the more established growth names appealing. We will look to add some growth to portfolios when the valuations become compelling relative to long-term growth expectations.

As always, we are working constantly to position your portfolio appropriately to maximize return, while managing your overall portfolio risk exposure. Please feel free to reach out if you have any questions or concerns.

Sincerely,

Steele Wealth Management

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