

# SV WEALTH - NEWSLETTER



**Sabu Varghese, MBA, CIM**  
*Portfolio Manager*



**Ramzy Saad, CFA, MBA**  
*Associate Portfolio Manager*

**SV Wealth**  
**Raymond James Ltd.**

[www.SVwealth.ca](http://www.SVwealth.ca)

416-499-1555

8500 Leslie St, Suite #450  
Markham, ON

## Trick or Treat?

October is historically the worst month of the year for equity markets. After markets took a dive in September, many were fearing the worst for the month ahead, as inflation concerns and worries about defaulting Chinese property developers threatened turbulence.

In the end, October turned out to be more treat than trick, posting the best returns since November last year, when economies first started reopening from the pandemic. Not only are markets strong but they also remain at record levels; the wide-ranging S&P 500 notching its 59th record close for 2021 on the last trading day in October.

## The Good: Corporate Earnings Remain Strong

A strong quarter of corporate earnings propelled the market higher in October, with 82% of companies beating analyst expectations. The strong profits come as many companies raise prices without seeing a consumer backlash.

The waning spread of the Delta strain also added optimism that the worst of the pandemic (i.e. lockdowns) may finally be behind us.

## The Bad: Supply Chains Remain Tangled

While inflation remains stubborn and elevated, it is not intensifying, providing some support to the central bank's assertion that it remains "transitory".

Despite remaining stable, inflationary pressures appear to be broadening to more areas of the economy, especially wages. That persistence and broadening remain something to keep an eye on.

The issues with supply chains are well-known by this point. The restrictions that accompanied the pandemic resulted in clogged ports, which upset the delicate balance of international logistics. The computer chip shortage, which began after manufacturers slashed production in March 2020, is now beginning to impact larger companies that tend to have deep relationships with suppliers.

These issues are now starting to show up in weaker earnings for some of the largest corporations. As an example, Apple's earnings for Q3 missed expectations, with the company blaming supply-chain disruptions for hindering manufacturing of the iPhone. Worse yet, Apple warned that these disruptions would bring challenges during the important holiday-shopping season.

As for automakers, the chip shortages have slowed factory output and contributed to a steep drop in third-quarter profits for both General Motors and Ford Motor. Even Tesla, which makes a portion of their own chips, is warning that supply-chain woes are going to be having a larger impact going forward.

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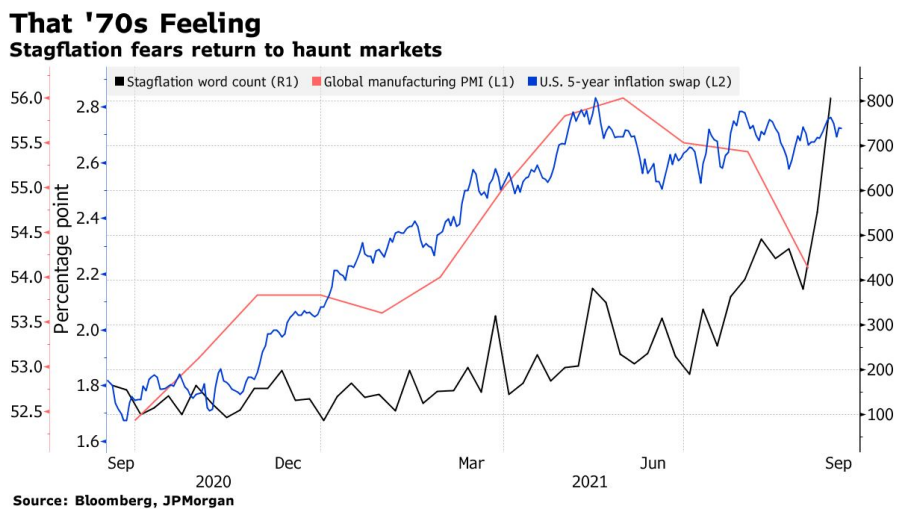
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## The Ugly: Wage Inflation and Slowing Economic Growth

The argument that inflation is transitory has centered on the understanding that the supply chain will eventually sort itself out at some point in the first half of next year. Of larger concern is the labour shortage, which is also pushing up prices but more importantly, wages.

Wage inflation is problematic because once an employee is given a raise, it's usually permanent and not easily taken away. Fast-food chain McDonalds has raised wages 10% this year and is still struggling to adequately staff restaurants. To compensate, McDonalds expects menu prices in the US to increase 6% this year.

As supply chains continue to create shortages, and as wages climb, the cocktail that is inflation coupled with a softening economy is the recipe for stagflation (stagnant growth and inflation). Stagflation is problematic because it becomes hard for the central bank to control once it manifests itself.



## Looking Ahead

Despite the troubles we're seeing in the economy, equities remain the best asset class to be invested. The key will be to rotate to those sectors who are poised to benefit from rising interest rates, something that the central bank is now hinting will be coming mid-next year rather than the 2023 timeline they previously discussed.

Like always, we remain your trusted partner in financial matters and will guide your portfolio to help you meet your life goals, which is what really matters at the end of the day.

We wish you a wonderful November!

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