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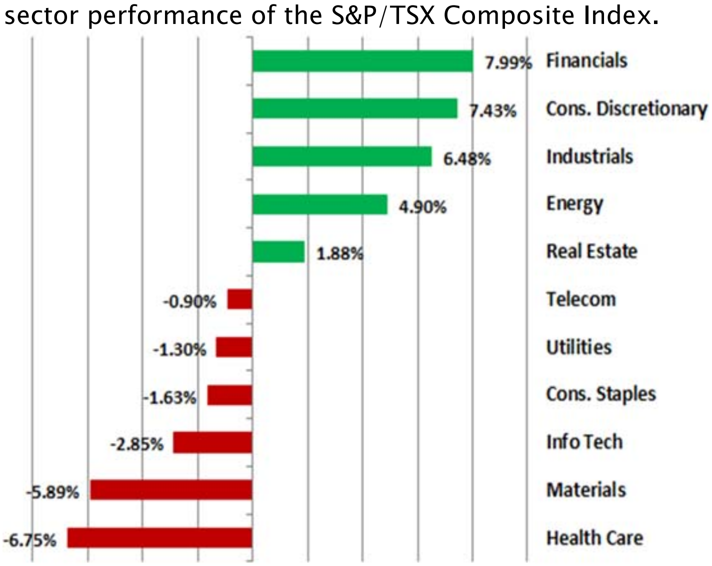
New Highs, New Opportunities

Not that 'The Donald' needs any more publicity, but it's been exactly one month since he was elected to become the 45th president of the United States. In this time, the S&P 500 is up 3.8%, copper is up 7.7%, and oil is up 13.5%. (The November 30th decision by OPEC to cut production was a concurrent positive to energy markets.) These are some big one-month moves, and to quote Trump, "I mean really big." Putting it in perspective, the average monthly price move over the past twenty years for each of these benchmarks is 0.6%, 0.7%, and 0.7%, respectively. Markets have definitely lived up to being forward looking, having run wild even before the president-elect takes his seat in the Oval Office.

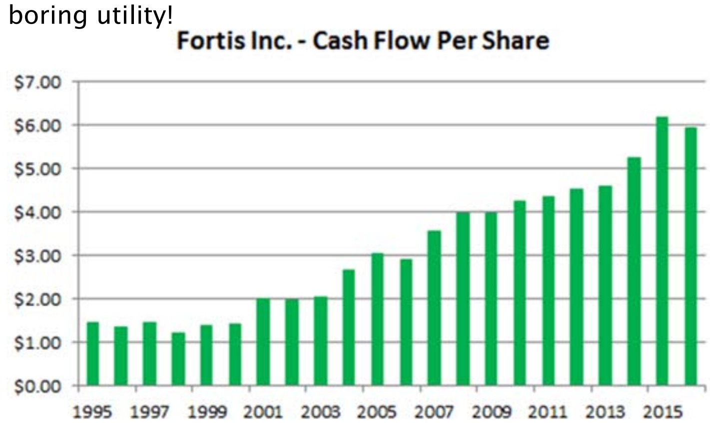
Equity markets have become more expensive in a very short period, with new all-time highs capturing headlines. Mr. Trump and his ideas have led to a 0.7x increase in the S&P 500's forward price-to-earnings (P/E) ratio, setting a post-2009 high valuation of nearly 19.0x. Not all areas of the market are likely to be winners under the Trump regime. Consensus has determined that the financials sector will outperform, along with other economically sensitive groups. Conversely, bond proxies like telecoms, REITs, and utilities stand to underperform as interest rates rise on the back of higher future inflation. For the most part, investors have reflected these expectations, as shown below in the one-month sector performance of the S&P/TSX Composite Index.



Source: Bloomberg

This may be justified if the future shapes up to what everyone expects. In such an environment, who wants to be invested in boring old utilities when growth will come from massive spending on infrastructure?

As a result, utilities companies like Fortis Inc., held in our Canadian equity strategy, have seen their stock prices decline. Fundamentally, nothing has changed at Fortis, except that it closed the acquisition of ITC Holdings, a large transmission company in the U.S. Midwest. This only solidifies Fortis' 5%+ rate base growth, and positions it to generate roughly 65% of its profits from the U.S. As an investment, Fortis' forward P/E ratio sits at 16.0x relative to its 15-year median of nearly 17.0x. The company has increased its dividend for 43 consecutive years, and it now yields 3.8% versus a Canadian 10-year government bond at 1.7%. You may question the comparison to government backed paper, but Fortis has been in business in its current form since 1977 and has grown its cash flow per share at 7.0% per annum since 1995 (the extent of available data - chart below). In other words, this business has witnessed at least six different American presidents, survived at least four different political party shifts, and still manages to grow well-ahead of historic inflation. Not bad for a boring utility!



Source: S&P Capital IQ, QV Investors

The 'Trump Rally' has made investing more challenging, as what were once value areas of the market have now rallied. We caution investors against betting too heavily on a future whose parameters remain largely undefined. However, we encourage taking advantage of short-term opportunities to own more of the strongest businesses that have quickly become unfavoured.