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The Markets

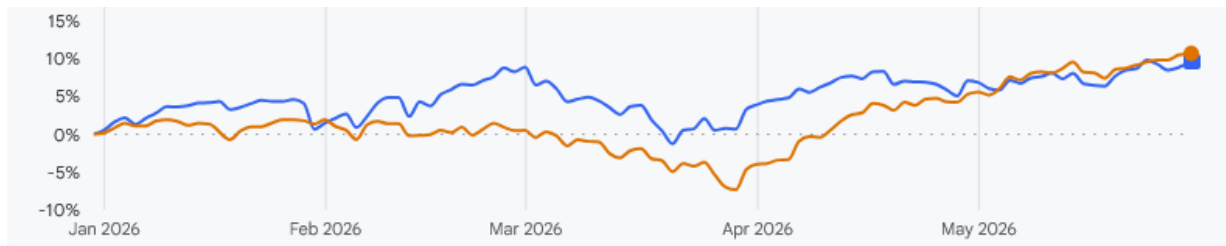
	May	Change in Month	Year -To-Date
S&P TSX	34769	2.4%	9.6%
S&P 500	7580	5.1%	10.7%
Dow 30	51032	2.8%	6.2%
Oil	\$87.36	-17.1%	52.1%
Gold	\$4593	-0.8%	6.2%

You do not need to read much further to know the market was driven by two factors, AI and the potential truce in Iran. Investors returned to the AI related stocks as companies reaffirmed their commitments to the new technology. The on again, off again situation in Iran caused gyrations in the markets. The hope that deadlock in the Strait of Hormuz would soon end led the price of oil to collapse and the broader markets to rally. Investors believed that lower oil prices would lead to lower inflation and a stronger consumer. I would say the market traded on emotion more than facts.

Gains were VERY broadly based in May. Only 2 sectors had negative returns. As you would expect, the Energy sector declined based on lower oil prices. That said, a 17% decrease in the price of oil led to less than a 5% decline in the stocks in the Energy sector. The other sector exhibiting weakness was Health Care which is influenced by the volatile cannabis stocks. Hopes for an economic recovery if the situation is resolved in Iran led Material stocks, Mining stocks, to rise more than 6%. The top performing sector was the Telecom sector. The main reason it recovered was that the stocks had hit lows and the companies indicated they would reduce their capital expenditures which would improve their balance sheets. The banks generally reported strong results but pulled back as investors had already assumed the good results. The banks still rose more than 5% by the end of the month.

The graph on the next page presents the performance of the S&P 500 and the S&P TSX for year-to-date.

Year-to-Date Performance S&P 500 and TSX



TSX, S&P 500 source google.com/finance

Economic Indicators

Our economic indicators section is less in depth than in a typical month as nearly every economic statistic was impacted by situation in Iran or will be. It is like driving forward by looking in the rearview mirror.

1. Canadian GDP

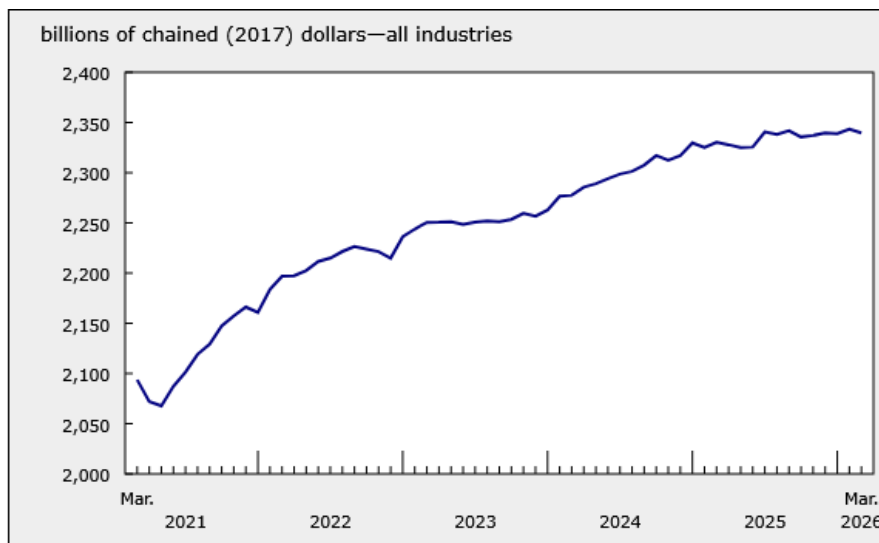
You may have heard or read that Canada is in a technical recession. I do not mean to belittle the impact of slower growth on the average person, but it is not all doom and gloom.

1. GDP per capita rose by 0.2% in the first quarter. This means the GDP per person improved, not declined. This is definitely good news. The decline in the population was greater than the decline in GDP which meant GDP per person rose.
2. The advance information received by Statistics Canada led them to forecast a 0.4% increase in the expenditures portion of GDP in April. If this is correct, then the growth in April would more than offset the declines experienced in the fourth quarter of 2025 and the first quarter of 2026 combined.

Now for the statistics that appear to present a less rosy picture. The headlines and political opposition point out that we are in a technical recession. A technical recession is when the economy contracts for 2 consecutive quarters. The decline has not been deep as the fourth quarter showed a 0.2% decline and the first quarter had a 0.1% decline. Often the economic releases get updated when new information is received and a 0.1% could be a rounding error. If you look at the graph at the end of this section, you barely notice the decline.

The flat economic growth was a balancing act across multiple sectors: a 2.9% surge in imports (largely driven by gold) was neutralized by an accumulation of business inventories, while decreased business, residential, and government capital investments were counterbalanced by a 0.4% rise in household spending on food and financial services. On the trade front, exports edged down 0.1% as US tariffs hampered automotive shipments, this drag was partially offset by strong crude oil and natural gas exports.

Higher global energy prices pushed corporate incomes up by 1.6% and boosted the GDP deflator by 1.1%. Employee compensation rose by 1.2% across all provinces. However, the household saving rate dipped to a two-year low of 3.5% as nominal spending outpaced a modest 0.6% increase in disposable income. This income squeeze was exacerbated by a 0.7% rise in household interest payments—the first increase since mid-2024—as the Bank of Canada held its policy rate steady, pausing a two-year trend of rate reductions.



Source: Statistics Canada

Just as expected

Originally, we were not going to put out a commentary this month as so much of the market movements were predicated on actions in the Middle East. Then we realized the markets seemed to be driven by expectations rather than facts.

Sometimes the markets price in hope. There is an investment axiom to buy on rumour and sell on news. In May there was a pause in the hostilities between the US and Iran. There were periodic missiles but not all out war. The US President says the US is not at war, so he does not need approval. As the month ended both sides indicated there was a proposed 60-day truce with the difficult items to be negotiated during the 60 days. The key feature is the Strait of Hormuz would open. Oil fell below \$100 per barrel. Gas at the local pumps fell nine cents in one night.

Here is where it gets interesting.

It was only a few weeks ago an expert on gasoline prices was on the news. He said if the Strait of Hormuz does not open soon the price of gasoline will continue to move higher. He forecast that the price would exceed \$2.50 per litre. At the time gasoline at the pump was \$1.93, a week later the price was below \$1.70 per litre. The strait is still not open. First the price of oil fell below \$100 per barrel which got passed on to the consumer. A second factor was we had just passed the May long weekends in Canada and the US. Typically prices rise into these weekends as there is more demand for gas on those weekends. Recently I read the dollar amount spent on gasoline is up over last year, but the volume of gasoline sold was down as people reduce discretionary trips. The expert knew that all these facts, excluding the price of oil so some of the decline could have been expected.

Another expert on the oil market and oil related equities pointed out that even if the strait is reopened the price of oil will remain elevated.

One reason for the price of Oil to remain at \$80 per barrel or more is that it will take months to clear the backlog of ships. At the moment, there are approximately 2,000 ships parked in the Persian Gulf. Let's assume that peace really breaks out and the strait can be reopened. This does not mean that every ship can leave in one afternoon and refill oil storage around the world. Prior to the closure a typical day had between 100 and 140 ships pass through each day. At 100 ships per day, it would take a month to clear the backlog, The math is a little too easy.

The strait has been mined which narrows the route ships can travel, this will severely limit the number of ships passing through each day. One branch of the US government estimates it could take up to six months to ensure all the mines have been removed. Some ships are loaded and ready to sail while others need to load their cargos. Once the ship is ready to go, they need to get insurance. What rate will the insurance companies charge? How many would be comfortable providing insurance at the beginning of a truce when we have seen many deals undone. No insurance means no one will risk the passage. Just like the knives sold on TV, wait there's more. Currently the ships only have skeleton crews to maintain the equipment. To fully

crew the ships will require 20,000 sailors. It will take some time to fly them in from around the world. A further delay to the return to normal.

The reasons for prices to remain elevated even if there is a truce include: the strait is mined, the need to fly in the crews for the ship, they must get insurance, and some must get loaded. It looks like it will be a while.

However, and there is always a however, the price of oil declined by more than \$9 on the hope there might be an agreement between the US and Iran. No deal but the hope of a deal.

Now you see why the price might not decline as fast as people might expect. But.....

The market trades based on expectations. When Trump announced he was close to a deal with Iran the price of oil declined. You just read all the reasons oil prices should remain elevated even if the strait reopens, yet even before it reopens optimism caused prices to decline. Just wait and see when there is a deal, If there are only 3 balls and there are 4 players they will bid up the price. If 2 of them expect more balls to be delivered next week they might not bid on the 3 balls and the price would sag, despite there still being only 3 balls and 4 players. The balls will trade closer to the price they expect to pay next week, Countries are concerned about running out of fuel but if you believe there will be a delivery in a month you know your inventories will be low but that you will not run out. Once you eliminate the risk premium the price will decline even if there is still a shortage. Oil futures prices forecast \$72 per barrel in December 2026.

That was expected. Sometimes investors price in good news and when it happens the stock does not go up as they had anticipated the good news. I had a conversation with an investor who questioned why the Canadian bank stocks should not keep going up as the earnings were up double digits from the prior year and most of the banks raised their dividends, often an indicator of continued earnings growth. The problem was the earnings growth was expected so some of the bank share prices declined as analysts did not like the source of the earnings growth,

While I was compiling the information for this commentary Bitcoin continued to decline. I normally do not comment on crypto currencies as I have no way of establishing a value. Someone who is more knowledgeable on the topic explained, after the fact, why Bitcoin had begun to crack. He indicated that when the US 10-year bond yield rises above 4.43% then historically Bitcoin falls. Right on cue rates rose and Bitcoin fell. I did not ask how low rates have to go to reignite the rally. Back to our discussion of expectations. A company famous for holding Bitcoin and using preferred shares to add leverage to increase its crypto currency holdings. The company, Strategy, formerly Microstrategy, has a reputation for not selling any Bitcoin. It had been 3.5 years since they sold any. They sold 3.2 Bitcoin so they would have the cash to cover the dividends on their preferred shares. That is 3.2 bitcoin, not 320 or 3.2 thousand. To put this in perspective Strategy has MORE than 843.5 THOUSAND Bitcoin. The crypto currency denizens were all a buzz. I am not sure about the cause and the effect, but Strategy stock fell 9% on the news while Bitcoin fell 6%. The sale of 3.2 coins should have had zero impact on the price of Bitcoin but it did. When someone with a reputation for not selling any coin, sells, does it mean something else?

Summary

“Buy on cannons, sell on the sound of trumpets.” Lord Rothschild

This month we looked at the fact investors expectations are more important than the facts. The primary focus in the reflection section was the direction of the price of oil if, and when, the Strait of Hormuz reopens. We listed many factors that will delay shipments from the Strait but even the thought of opening the strait caused oil prices to fall \$9 in a day. Many experts warn that it will take a significant amount of time to bring global oil inventories back to the pre-war level. What analysts missed is that once people believe oil will soon be plentiful there is no need to pay a premium for short term deliveries. The current price of oil is \$96 but the futures price for December is \$72. The \$72 price still reflects the uncertainty so the real price in December, assuming the strait opens, will be lower, maybe even close to the mid sixty-dollar level experience before the war. A second instance was a company that had a reputation as one that would never sell its holdings of Bitcoin. When they sold 3.2 bitcoin of their over 843 THOUSAND Bitcoin both Bitcoin and the stock collapse. There was a change in perception. There was the hope of a deal but no deal and yet the price of oil collapsed.

The markets continue to gyrate. We continue to focus on dividend paying stocks with the potential for capital appreciation. In addition to the traditional dividend paying stocks our client portfolios are diversified with holdings in the Energy and Gold sectors. We, and our clients, find comfort in the steady stream of income that you get when you invest in dividend paying stocks, such as the Canadian banks.

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