3 Things Every Beginner Should Know About Canada's Stock Market

Description

For beginners, the stock market can seem intimidating. Investing in stocks has been glorified in movies and seems to dominate the news cycle these days. For the average saver who's simply looking for a way to get started, the volatility and breadth of the market can indeed be overwhelming.

I believe beginner investors need some context or perspective to get started on the right foot. Understanding the nature of Canada's stock market is a critical first step for your investment journey. With that in mind, here's an overview of the top three factors beginner investors should know before diving in.

Expected returns

The most important question for any investor is the one about expected returns. Figuring out stock market returns could help you decide whether it's worth putting your savings into stocks or whether you prefer real estate or gold. Realistic expectations can also help you create a plan to achieve your financial goals and set appropriate targets.

So, how much can you expect? Well, on average, the Canadian stock market has returned an average of 6% compounded annually. The **iShares S&P/TSX 60 Index,** which tracks the country's 60 largest stocks, has delivered 5.8% annually over the past 10 years and 6.5% since its inception in 1990. You can expect similar returns going forward.

At 6% compounded annually, any investment you make today could double within 12 years.

Stock market's biggest sectors

Understanding which sectors dominate the stock market is another critical factor. The biggest sectors tend to have the largest impact on stock market performance and Canada's economic growth over time.

At the moment, the Canadian stock market is dominated by energy and financial stocks. Banks such as

Royal Bank and **TD Bank** are the biggest corporations in the country. Insurance and asset managers like **Brookfield Asset Management** are nearly as large. Oil and gas giants such as **Enbridge** and **TC Energy** are the second-largest sector.

Financial firms account for nearly one-third of the **TSX 60's** (32%) overall value. Energy accounts for 14%, while materials (such as gold) account for 12.3%. Overall, Canada's economy is dependent on financial services and energy exports. However, technology is rapidly gaining momentum. Technology stocks such as **Shopify** are already the biggest drivers of stock market performance.

Focusing on emerging technologies and asset-light financial firms could be the best strategy for a beginner investor.

Valuation

The media and some investors seem concerned that the stock market is overvalued. However, media attention is usually focused on American stocks. Canadian stocks seem relatively better priced.

The TSX 60 index currently trades at 1.78 times book value per unit. It also trades at a price-to-earnings ratio of 13 and offers a 3.5% dividend yield. Compare that to the 1% to 2% yield you can expect from savings accounts across Canada or even the 0.5% return you can expect on government bonds.

Canada's stock market offers a dividend yield that's nearly comparable to rental yields in most Canadian cities. The gross rental yield in Toronto is 4.1% at the moment.

Given that you don't have to pay utilities or property tax for dividends, stocks seem like a better and easier bet.

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