3 Reasons the TSX Index Is Headed for Trouble This Fall

Description

The **S&P/TSX Composite Index** was down 165 points in early afternoon trading on August 31. Canada's economy shrank at the fastest pace on record in the second quarter. The COVID-19 pandemic had a major negative impact on consumer spending, business investment, imports, and exports. Canada's gross domestic product (GDP) fell 11.5% in Q2 2020, representing a pace of contraction of 38.7%.

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Today, I want to explore three reasons why the **TSX Index** is headed for trouble as we look ahead to the fall.

TSX: Jobless benefits weighing on overall economy

Canada's unemployment rate has fallen from the high of 13% it hit earlier this summer. However, the jobless rate is still hovering around the 10% mark. The federal government stepped in this spring to provide financial relief in the face of the COVID-19 pandemic. This included social programs like the Canada Emergency Response Benefit (CERB).

Trudeau's government has opted to let the CERB expire this fall. However, his government restructured employment insurance (EI) and introduced several new benefits to ensure that the expiration of the CERB would not cause a financial shock. This unstable environment could drive down investor sentiment for the TSX in the weeks ahead.

Canadian businesses are in crisis

Manulife Financial (TSX:MFC)(NYSE:MFC) Investment Management head Frances Donald warned that the rebound for Canada's economy is at risk, pointing to the dire situation when it came to Canadian employment. However, businesses are also facing critical challenges.

Key sectors like travel and hospitality are reeling from low activity in the spring and summer. On the plus side, Canada has provided more fiscal support which may provide it "a little more time" compared to the United States.

A slew of business failures will undoubtedly impact the TSX in the fall. Manulife remains one of my top dividend stocks in this environment. Its shares have climbed 8.9% month over month as of early afternoon trading on August 31. The stock last possesses a favourable price-to-earnings ratio of 9.9 and a price-to-book value of 0.8. Better yet, Manulife offers a quarterly dividend of $0.28 per share. This represents a strong 5.6% yield.

Could an avalanche of delinquencies crash the TSX Index?

New social programs were not the only measure introduced by the federal government, however. Financial institutions were pressured to make concessions to their client base in order to provide relief. The most impactful of these programs were mortgage deferrals at major lenders.

Royal Bank of Canada, Canada's largest financial institution, approved roughly 500,000 payment deferrals to customers in the third quarter. Its peers have reported a similarly high ratio of deferrals. Similar to the expiry of CERB, some analysts are anxious that the winding down of deferrals will put millions of Canadians in a dangerous financial bind.

Royal Bank CEO David McKay warned that the "real test of recovery" will occur when these programs wind down. There are therefore big risks for the TSX Index as we head into the fall. Investors may want to target more dependable dividend stocks, or pile into gold as a hedge.

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