Why the TSX Might Correct in Q3 2021

Description

Will the **TSX** continue its show of resiliency in the third quarter of 2021? Canada's primary equities benchmark closed below 20,000 for two consecutive trading days after July 15, 2021. We're not sure if it's the start of a market correction leading to the poorest month of the stock market.

According to the Stock Trader's Almanac, a drop-off usually occurs in September. It's a worldwide phenomenon or a market anomaly if you want to call it. A case in point is the average decline of the **Dow Jones Industrial Average** and **S&P 500 Composite Index** every September since 1950.

However, some analysts say the negative effect isn't exclusive to the U.S. stock markets. It may be due to seasonal behavioral bias when investors profit-take after summer. Since selling pressure is high, the broad market declines. In September 2020, the TSX lost 3.15% overall and fell below 16,000 twice during the month.

Formidable Big Bank

The unexpected happened in May 2020 when **Shopify** displaced the **Royal Bank of Canada** (TSX:RY)(NYSE:RY) as the most valuable company on the TSX. Canada's largest lender held the throne for many years. Fast forward to September 2020, and the premier bank stock also lost 5.59% during the month.

Shopify did not escape the September Effect as it posted a larger loss (-8.63%) than RBC. However, the $179.93 billion bank showed its formidability once more and did not disappoint. It rewarded investors with a 6.52% total return in 2020. Thus far, in 2021, RBC is doing better with its 22.38% year-to-date gain.

At $125.54 per share, the dividend yield is a decent 3.44%. Currently, talks are loud that the Big Banks could raise dividends in Q4 2021. Investors wait in suspense if the Office of the Superintendent of Financial Institutions (OSFI) would lift restrictions on dividend increases in October.

RBC can afford to increase its dividend yield after booking the third-highest CET1 ratio (12.3%). At the close of Q2 fiscal 2021, it had $9.9 billion in excess capital. RBC CEO Dave McKay said, “It’s great to have the luxury to see accelerated organic growth to increase our dividend based on current core earnings and to return increasingly excess capital to our shareholders.”

Unaffected by the pandemic

Wholesale power generator **Capital Power** (TSX:CPX) did not feel the September Effect in 2020. Unlike the top two largest TSX companies, the utility stock gained 3.22% during the month. Thus far, in 2021, the year-to-date gain is 18.78%. This $4.72 billion company is as illustrious as RBC because it’s also a Dividend Aristocrat.

Management has raised the dividends for eight consecutive years. Besides the higher-than-average 5.08% dividend, the business model is low risk, if not recession-resistant. Capital Power’s cash flow is stable because its power purchase agreements (PPAs) are long-term.

Also, the COVID-19 pandemic had a negligible impact on the operating performance of Capital Power’s facilities. Currently, the company leans towards increasing gas and renewables generation technology. Management projects the adjusted EBITDA from renewable energy sources to be around 37% by 2025.

Monitor the TSX

The movement of the TSX in Q3 2021 is worth watching. It could defy the market anomaly in September or experience a market correction. However, there should be no worry for investors in RBC and Capital Power. Both stocks can overcome a downturn.

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1. Bank Stocks
2. Dividend Stocks
3. Investing

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2. TSX:CPX (Capital Power Corporation)
3. TSX:RY (Royal Bank of Canada)

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