Horizons Seasonal Rotation ETF (HAC)

Market Review

The S&P 500 started the first quarter of 2024 on a positive note, as investors were anticipating that the U.S. Federal Reserve (Fed) would start to cut its key federal funds rate in the near future, helping to support the stock market. The S&P 500 continued to rally for the remainder of the first quarter, despite the Fed pushing back on investors' beliefs that it would shift and become more dovish with looser monetary policy. In January, investors started to shift their focus from the technology sector to the cyclical sectors of the stock market. The industrials, materials and energy sectors outperformed the S&P 500, from January and continued to outperform the S&P 500 in the first quarter.

In Canada, the S&P/TSX 60 Index performed well in the first quarter as it benefitted from investors starting to shift their focus to the cyclical sectors of the stock market. In particular, the energy sector performed well as the economy remained stable with increasing demand for oil. In addition, geopolitical tensions with the Russia-Ukraine war and in the Middle East helped to support a higher oil price.

Quarter in Review

At the beginning of the quarter, HAC was substantially invested in equities, favouring broad market exposure in the U.S. and Canada. In late January, HAC started to initiate positions in the cyclical sectors including materials, industrial and energy, as the sectors started their strong seasonal periods or were about to start their strong seasonal periods in the near future. During the first quarter, HAC favoured the Canadian stock market over the U.S. stock market. The fund generally maintained its position in the cyclical sectors of the market in the second half of the quarter.

Outlook and Positioning

Historically, the second quarter of the year tends to start on a positive footing in April as the stock market tends to be positive on a seasonal basis. However, in early May, the stock market transitions into its six-month unfavourable period, which lasts from early May to late October. Starting in April and into May, investors tend to rotate out of some of the growth sectors and cyclical sectors of the stock market into defensive sectors, including the consumer staples, health care and utilities sectors. The defensive sectors have been underperforming the stock market in early 2024, but that could change if investors shift to a risk-off mode.

In addition, government bonds tend to start their strong seasonal period in May and could present a good diversification opportunity if the stock market becomes volatile. Also, the biotech sector starts its strong seasonal period in mid-June and could provide a good seasonal opportunity late in the second quarter.

The risk to the stock market in the second quarter will probably be higher-than-expected inflation. The Fed has maintained a tight monetary policy with restrictive rates in order to combat persistently high inflation, which in turn has put negative pressure on the stock market. If inflation remains high and the economy slows, this could present a challenging situation for the Fed, making it more difficult to cut its key federal funds rate.

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