MacNicol & Associates Asset Management Inc., 130 Bloor Street West, Suite 905, Toronto, Ontario, M5S 1N5

May 2019

The Monthly

With this commentary, we plan to communicate with you every month about our thoughts on the markets, some snap-shots of metrics, a section on behavioural investing and finally an update on MacNicol & Associates Asset Management (MAAM). We hope you enjoy this information, and it allows you to better understand what we see going on in the market place.

"Trade only when the market is clearly bullish or bearish"

- Jesse Livermore

The Numbers:

Index:	**Year-to-Date:**	
S&P/TSX:	13.3%	
NASDAQ:	15.1%	
Dow Jones:	9.7%	
S&P500:	12.7%	
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	1.68%	2.40%
5-Year Bond:	1.55%	2.18%
10-Year Bond:	1.66%	2.40%
30-Year Bond:	1.89%	2.83%

Economic Data:

- Chinese PMI short of expectations for April, many to suggest the rebound in Q1, 2019 was an anomaly
- The United States imposes $200 billion worth of tariffs on Chinese imports
- North American yield curve flattening puts investors on "recession watch"
- "Sell in May and go away" appears to be happening thus far in 2019
- Gold off the late April lows just barely crossing $1,300 per ounce
- Crude Oil off the late April highs sitting just above $60 per barrel

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	21.30	22.49
P/B: Price-to-Book	3.31	3.19
P/S: Price-to-Sales	2.10	2.09
Yield: Dividend Yield	1.95%	1.89%

Year-to-date Performance, by Sector: As at May 24th, 2019

S&P/TSX Composite	13.3%
NASDAQ	15.1%
Dow Jones Industrials	9.7%
S&P 500	12.7%
Russel 2000 (Small Caps)	12.3%
MSCI EAFE	7.8%
Crude Oil Spot (WTI)	29.3%
Gold Buillion ($US/Troy Ounce)	0.2%
SOX Semi-conductor Index	13.6%
VIX Volatility Index	-26.3%

Source: Canaccord Genuity Capital Markets & Thomson Reuters

Foreign Exchange - FX

We continue to survey all the Banks and some Custodians to compare Foreign Exchange Rates charged. As you can see in the chart below some of these Institutions are charging considerably more than previous months when we did our first comparison. We tried to include some other firms, but they do not post public rates online or require a membership fee. Let us know if we have left any organization off here and we will try to include in future publications.

As of May 24, 2019 4:00 PM	$5,000	Cdn		
Banks	Rate	Buy USD	Cost	% Difference from Spot Rate
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.3435	$3,722	$11	0.3%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.3538	$3,693	$(18)	-0.5%
Raymond James	1.3585	$3,681	$(30)	-0.8%
Royal Bank	1.3738	$3,640	$(71)	-2.0%
Scotia	1.3784	$3,627	$(83)	-2.3%
TD	1.3774	$3,630	$(81)	-2.2%
Spot Rate	1.3474	$3,711		

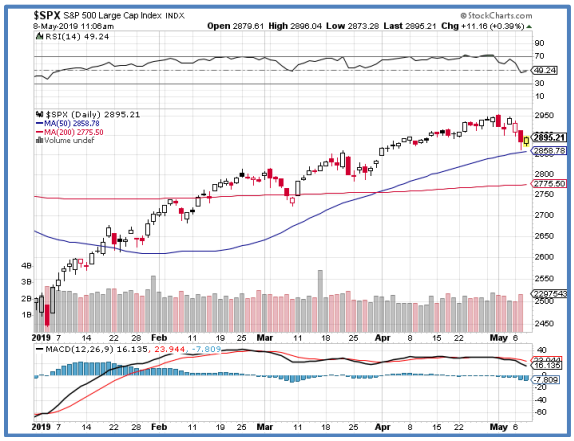
Trade only when the market is clearly bullish or bearish…so which is it?

Jesse Livermore famously said, "*Trade only when the market is clearly bullish or bearish*". I really wish it were that simple. Although markets have for the most part performed well in 2019 the arrival of May has dumped some cold water on the market's burning deserve to go higher. "*Sell in May and go away*" seems to be right on schedule in 2019. May's sell off would indicate that all is not exactly well with financial markets since they appear particularly prone to event risks such as the predictable tariff tweets from you-know-who along with ongoing uncertainty over global growth. Together, its made following Mr. Livermore's advice that much more difficult.

What's an investor to do?

The MAAM investment team feels that caution is warranted. We are not in possession of smoking gun evidence that the market was poised to sell off or is poised to sell off even more. In fact, we feel pretty good about our more conservative stance here in 2019 but we do think times-they-are-a-changing. Many investors clearly under estimate the power of President Trump's Twitter account, the ability of the Chinese to deal with it. When we reference President Trump's Twitter account it isn't so much the case that his erratic comments can easily shave off hundreds of points of stock market valuations in a matter of minutes. Rather, we would surmise that it's the longer-term implications on sector allocation that investors should focus on. For example, our firm invests in technology names, but we do so primarily through privately held firms in our Alternative Asset program. Still we are shareholders of Microsoft because we believe that technology is an important contributor to portfolio growth, especially in a low growth low inflation environment. On the other hand, we probably wouldn't invest in semi-conductor stocks any time soon nor in firms materially involved in the hardware space since these sorts of companies are more likely to experience sustained periods of stress in a longer running trade tiff. So point number one for investors is to take a closer look at portfolio level sector allocations: we would surmise that painting this market with broad brush strokes could hurt your bottom line.

When it comes to the Chinese and their ability to deal with a US led trade war (or the communication strategy thereon) we would suggest neither one is particularly robust and again caution investors when it comes to "blindly" taking on global portfolio exposure even though it has heretofore been sold as something "good" for you. When Chinese authorities implemented a media ban on President Trump's Twitter comments they probably felt it was a good idea to shelter their citizens from the crazed ideologies of populist Western Dictator. We wish we could have been in the boardroom where that decision was consummated to intercede with a dollop of data and common sense. Statistica.com reports that as of the end of 2018 there were 257 million smart phones in the United States, which is a lot. But the problem is, Statista.com *also* reported that there were 713 million smart phones in China as of the same period. Oh yeah and the Global Times reports that every day (day not year) 8,000 Chinese citizens land in the United States while 6,000 Americans do the same in China. In a highly interconnected and digital world such a ridiculously pointless ban by the Chinese did more harm than good because it exposed them as not only fearful of the Americans when it comes to trade but guilty of being deceitful to their own people. Fear is one thing, lies are another but both undermine China's global market domination ambitions. Predictably, investors voted with their wallets with Asian equities swan diving harder than a seasoned Yoga Master and certainly harder than American equities. The MAAM investment team obviously does not know exactly what is happening in China's economy, but as of right now, we would suggest the first quarter rebound in 2019 Chinese economic activity is likely an anomaly. So much for much for clarity.



[US equities sold off on the Trump tariff tweet but look better than their Asian counterparts over in China]

[FXI is an ETF of Chinese Large Cap stocks, and one that's been beaten down badly. We doubt Asian equities hold up as well as North American ones. The Chinese certainly have more smart phones that the Americans do but when it comes to trade, the Asians truly are Trumped by the Yankess]

[26,686 Retweets. 103,765 Likes. 257 million American smart phones. 713 million Chinese smart phones. Thousands of business and leisure travelers daily. Good luck with subsequent media bans Beijing]

President Trump's twitter tweet on tariffs was probably the worst kept secret in China. It caused a lot of market uncertainty which undoubtably ruffled many investment feathers and it caused a lot of people to obsess over the advice provided by Jesse Livermore at the start of this article.

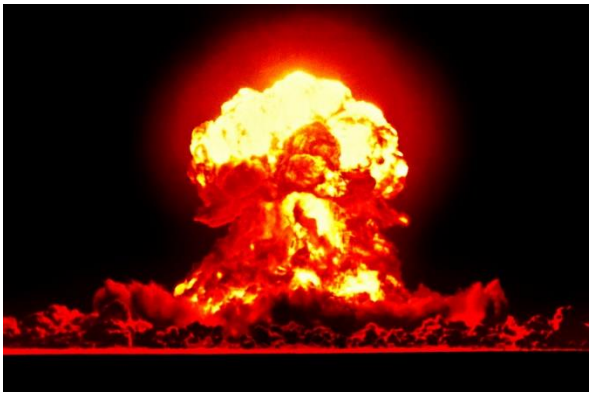
Except us that is…

We have been over weighting cash in most client portfolios and the ubiquitous presence of alternative assets has certainly helped our clients endure the market malaise. Yet a patient clairvoyance really had nothing to do with either. At MacNicol & Associates Asset Management we manage money for real people like you, and we feel no way about taking a slow and steady approach when we have a high degree of conviction in our beliefs.

One individual less prone to taking a wait-and-see approach was Chinese Vice Premier Liu He. Premier He quickly leapt into action and arranged for some 1-on-1 face time with US Treasury Secretary Steve Mnuchin and US Trade Boss Robert Lighthizer

[Liu He is at the centre of the US-China trade talks, figuratively and literally. As shown in this piece from *The Guardian* investors should probably get use to Mr. He's face, they're going to be seeing it an awful lot in the coming weeks. Much is at stake when it comes to US-China trade talks however the signal that Premier He is motivated to talk-this-out is probably a good sign]

While the MAAM investment team ultimately does not know whether the Chinese intend to make concessions or to push back. We do believe some sort of "showdown" between Trump himself and Chinese President Xi Jinping is in the cards. For one thing it will allow Trump to "sell" his savvy deal prowess to the American people ahead of a 2020 election if he emerges with a solution that truly benefits Americans or stick-to-his-guns if things get ugly. Some kind of Chinese retaliation is inevitable. But here's the thing, the April Chinese PMI report missed badly, and as we just mentioned many are starting to seriously consider the idea that the rebound in Chinese economic activity was more of an anomaly and less of a resumption of dominance. Perhaps the Chinese economy really is a house of cards…time will tell.



[This is what $1.13 trillion in US treasuries looks like when ignited by the Chinese]

The Chinese do have a nuclear solution to all the drama though and it is not a reduction in US energy or agricultural purchases. The Chinese could unload their massive $1.13 trillion mountain of US treasury securities. A reduction in the accumulation (or sale) of US Treasuries is a radical option but let's face it…it could happen. Radical but highly counter productive: a global economic meltdown would almost certainly ensue. The paring of US treasury purchases has been talked about before, it is what former US Secretary of Defense Donald Rumsfeld might call as a "known, unknown". Known or unknown the simple fact that certain Chinese academics openly discussed the topic was enough to cause a small sell off in the US Dollar index.

How President Trump and President Xi respond in their meeting will be important and likely the defining global economic event of 2019. This trade war is a dangerous blend of economic logic and political aspirations and that's really why it is so truly difficult to know whether the market is bullish or bearish.

[Jesse Livermore is widely regarded as the world's greatest trader. A feat he accomplished predominantly by shorting markets. How would "The Boy Plunger" trade today's markets? Who knows. But barring (another) shot from left field the next few weeks will almost certainly continue to be dominated by President Trump's twitter account and the Chinese response to it. Ladies and gentlemen please fasten your safety belts, it's going to be a bumpy ride]

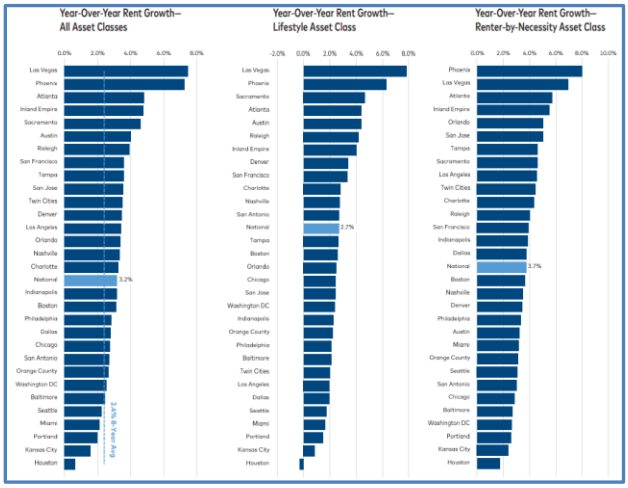
Unfortunately, President Trump's Twitter account will continue to be a New York Times best seller and a must read for anyone with even a cursory interest in the markets. Responses from the Chinese will garner nearly as much attention. Thankfully the MAAM investment team does not view managing your wealth as a game nor do we need to make split second decisions. We began this edition of *The Monthly* with a quote from famed trade Jesse Livermore: "*Trade only when the market is bullish or bearish*" and if you were hoping for a clear-cut answer from us as to which it is, well, we are sorry to disappoint you. Sometimes the "do nothing" approach is an approach in-and-of-itself. We're not saying we aren't doing anything…believe us…100s of hours each week go into looking after your money. But the Chinese will never concede on issues of principle and Trump is already campaigning for the future by warning Beijing that he will serve to make matters worse in his second mandate in 2020 should the Chinese opt to "wait things out". Livermore's advice to trade only when presented with clarity may require clairvoyance, which we don't have. We'll stick to our time-tested investment process until that should change.

The MAAM Investment Team

Is real estate *slowing*? Don't bet the house on it…

[As it turns out the so-called demise of the housing sector appears to have been exaggerated. Hey it happens. We were advising investors to hang in their all along. Higher interest rates do not always mean higher capitalization rates. In fact, higher interest rates do not always mean higher interest rates either]

We are deep into the late stages of the current real estate cycle, but quality real estate holdings should continue to form a deep part of any allocation to alternative investments. While the many in the media and some investors fretted about how rising rates would demolish property values, we took a closer look at the product types within real estate that made the most sense to us. Our investigation started with properties that form the backbone of the economy while excluding "trophy assets" like glamorous casinos, pricey resorts and overly one-dimensional boutique hotels. Of all the product types in real estate multifamily residential continues to dominate our desire for properties that are in demand today and have a clear path towards sustained demand in the years to come. Strong demand continues to define multifamily with the growth in prime renter-aged individuals expected to continue and growth in the number of people turning 20 forecasting to increase through to at least 2020. Job growth remains healthy for those with skills or in value creating areas. Additional student debt load restricts access to the market place for first time home buyers at the bottom end. While at the top end, many retirees are downsizing and moving into rentals for quality-of-life and logistical reasons. Apartments are a gem and proof that concerns about real estate liquidity (both on the public and private side) are over blown. Rent growth remains healthy at a national level and even temporary market softness in a few pocket markets was firmed up as part of the lease up of new units.



[Yardi's Matrix is a leading real estate data base that provides investors with a lot of information. Perhaps most importantly, Yardi's data shows that the renter-by-necessity crowd is helping to keep rent growth is materially above the pace of inflation, and to those with savings that's very important]

Residential real estate is something that portfolio managers a like and clients can understand. As a portfolio manager, residential real estate offers cash flows that are easy to model. For clients, residential real estate offers an investment they can understand.

But what about liquidity?

[The liquidity spigot is an important one for investors to consider. But don't be tricked into thinking private equity real estate investments are devoid of liquidity. Real estate liquidity has more to do with the real estate itself rather than the investment vehicle it is housed in].

Liquidity has more to do with the property itself rather than what type of vehicle it is packaged into for investors. Your principal residence in Toronto or Mississauga has much greater liquidity than your Muskoka cottage does because of the underlying demand and stuffing it into an LLC or a REIT or a Fund really wouldn't change much. The MAAM investment team seeks real estate investments that are in demand and that have a high rate of occupancy, location matters. Such properties are found in great locations and allow investors to reap gains from a refinancing or sale. It seems builders are following the same logic. We have rarely veered far from this simple formula and it has served us well. When looking at real estate always think like the property owner not a Lawyer. Liquidity through rental distributions and sales comes to public and private equity real estate opportunities a like.

The MAAM Investment Team

Sophisticated cerebral power and the spurious correlations that can result

Unlike other creatures, humans have the ability to think into the future. Other animals, the Goldfish for instance, live mainly in the moment and respond to life mostly on a moment-by-moment basis. The ability of humans to imagine or dream allows us to behave in ways today that may have a desired result later such as saving money for retirement. In a best-case scenario, self-awareness is essential for planning, improving ourselves, and avoiding future threats. In a worst-case scenario, self-awareness is often a recipe for anxiety, poor judgement and lousy investment choices. Take the recent flattening of the yield curve and the notion that equity market volatility will rise in the future...because of the flattening of the yield curve. The MAAM investment team loves investors, but even we sometimes wish more of them had the attention span of a Goldfish.

[Do you know someone with the attention spam of a…well you get the idea…chances are they too believe that a flattening yield curve is the *cause* of the latest bout of market volatility. To us such thinking is fish food]

The trouble with believing that a flattening yield curve will *cause* equity market volatility down the road is that it ignores a basic principal of economics (the business cycle) and a subtle nuance of financial markets (the hunt for yield actually lowers volatility as oppose to elevating it). The yield curve usually starts flattening as the economy matures into the mid-to-later stage of the business cycle. Later phases of the business cycle aren't especially interesting and so investors are typically unable to enjoy lucrative capital gain opportunities on risk assets like stocks and instead begin hunting for yield. Now when the hunt for yield shifts into full swing, volatility is compressed (not expanded or accentuated). Want proof?

You don't have to look to far:

In 2017 the stock market took off like a scalded cat, yet volatility was nowhere to be seen. During the smooth ride that was 2017 the only volatility confronting Bay Street portfolio managers concerned Toronto's weather or local sports teams (and in that sense not much has changed).

The MAAM investment team has been working with investors for years. It is what we do and what we love doing. If you or someone you know is psychologically predisposed to think about their investments a certain way, that's okay. We offer complimentary portfolio consultations in an open, judgement free environment. Working with us might help you gain a better understand of cause and affect, and in the process achieve a better allocation of capital in your portfolio. Check us out on the web at www.macnicolasset.com or call us toll free at 1-866-367-3040.

The MAAM Investment Team

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