

September 2019

The Monthly

With this commentary, we plan to communicate with you every month about our thoughts on the markets, some snapshots 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.

“The best thing a human can do is help another human being know more”

- Charlie Munger

The Numbers:

<u>Index:</u>	<u>Year-to-Date:</u>	
S&P/TSX:	14.8%	
NASDAQ:	20.0%	
Dow Jones:	13.2%	
S&P500:	16.7%	
<u>Interest Rates:</u>	<u>Canada</u>	<u>USA</u>
90-Day T-Bill:	1.63%	1.97%
5-Year Bond:	1.15%	1.31%
10-Year Bond:	1.13%	1.45%
30-Year Bond:	1.41%	1.96%
<u>Economic Data:</u>		
<ul style="list-style-type: none"> • US ISM rolls over for the 1st time in 3-years • Bank of Canada holds key rate at 1.75% • US 10-year note at 1.45% • WTI Crude at \$56 per barrel • Canadian trade deficit widens to \$1.12 billion • Small caps moderate on a preference for quality • Copper at 2-year cycle low now below \$2.60 • Gold at \$1559 per ounce • Toronto home sales jump 13.4% in August on a 3.6% rise in prices • Argentina implements capital controls 		

<u>Valuation Measures: S&P 500 Index</u>		
<u>Valuation Measure</u>	<u>Latest</u>	<u>1-year ago</u>
P/E: Price-to-Earnings	22.14	22.25
P/B: Price-to-Book	3.43	3.45
P/S: Price-to-Sales	2.18	2.20
Yield: Dividend Yield	1.89%	1.94%
<u>Year-to-date Performance, by Sector:</u> August 30 th , 2019		
S&P/TSX Composite	14.8%	
NASDAQ	20.0%	
Dow Jones Industrials	13.2%	
S&P 500	16.7%	
Russel 2000 (Small Caps)	10.8%	
MSCI EAFE	7.1%	
Crude Oil Spot (WTI)	21.9%	
Gold Buillion (\$US/Troy Ounce)	19.4%	
SOX Semi-conductor Index	12.9%	
VIX Volatility Index	-23.7%	
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 September 5, 2019	2:00	\$	5,000	Cdn		
<u>Banks</u>		<u>Rate</u>		<u>Buy USD</u>	<u>Cost</u>	<u>% Difference from Spot Rate</u>
CIBC		No Public Rate Posted Online				???
Interactive Brokers		1.3239		\$ 3,777	\$ 0	0.0%
Laurentian Bank		No Public Rate Posted Online				???
National Bank		1.3367		\$ 3,741	\$ (36)	-1.0%
Raymond James		1.3350		\$ 3,745	\$ (32)	-0.8%
Royal Bank		1.3502		\$ 3,703	\$ (74)	-2.0%
Scotia		1.3536		\$ 3,694	\$ (83)	-2.3%
TD		1.3577		\$ 3,683	\$ (94)	-2.6%
Spot Rate		1.3238		\$ 3777		

Re-birth at REO...

I was married on August the 8th, 2009 to a girl so pretty (and smart) that I sometimes cannot even believe it happened. Our honeymoon took place on a small island north of Tahiti called Bora Bora. Bora Bora is not only a preposterously beautiful place to visit, it is an adventure where one can develop a *broader* understanding of the world in which one lives. Fast forward to this past May and our 10th wedding anniversary was upon us. My wife and I wanted something Bora Bora beautiful, but geared towards helping us develop a *deeper* understanding of ourselves. After extensive research through-out much of June, it was decided that we would travel to Boston Bar British Columbia to visit the **REO Rafting and Yoga Resort**. Following a short flight to Vancouver International, my wife and I rented a Jeep and set off on our drive through BCs beautiful interior. Yes, arriving in Bora Bora a decade prior was an experience on to itself, but make no mistake, BCs interior is a drive like few others. Full advantage of BCs beauty and great weather was taken by unclipping our Jeep's top and storing it in the trunk. Assuming you are not originally from the greater Chilliwack area, you will probably want to back up your rental's GPS system with your own. For me personally, the WAZE app, which you can download for free is about as good as it gets. Oh and please, make sure you upgrade to a Jeep the last leg of our journey to the REO site isn't exactly paved and there are signs everywhere reminding you that BC is bear country.

Officially REO specializes in rafting the crystal clean waters of the Nahatlach River (a tributary of the Fraser) and yoga classes overlooking pristine surroundings. Unofficially, REO gets you your soul back. REO puts back into you what years of Toronto, or New York or LA life take out and while I cannot truly pin point exactly what made my stay at REO was so impactful, the result was dramatic. REO was not just a "re-charge" of the "wash, rinse repeat" variety so many of us here in Toronto are accustomed to. REO was a *re-birth*. A re-birth replete with new words, such as "glamping", and new experiences, such as having to take bear spray with you on hikes. Most clients obviously know what a bear is, but what the heck is "glamping"?

I'm glad you asked...

Glamping is a form of camping involving accommodation and facilities that are more luxurious than those associated with traditional camping. Don't get me wrong, REO owners Bryan and Karen did not provide us with Dom Perignon champagne and Kaluga Black caviar. But we did not have to erect our own tents, hunt our own food or bathe ourselves in the Nahatlatch River (though we did anyways). Along with REOs west coast charm, great food and plentiful activities the grandeur of Canada's staggering and awesome beauty allowed years of Bay Street life to drain from my body rejuvenating my soul. Though the Nahatlatch river and adjacent Lake Francis would easily qualify as national treasures I suppose that if you want to be reborn you must first accept that traditional methods of personal replenishment are no longer as effective as they once were.



[If the thought of waves crashing into those exotic over-water bungalows in Bora Bora sounds appealing to you, it should be. Bora Bora really is that stunning. At the same time, glamping in one of REOs tents with the sound of the Nahatlatch river behind you will undoubtedly make you cherish this great nation of ours just a little bit more.]

Speaking of efficacy, the on-going trade talks between the US and China have dragged on and domestic economic indicators are beginning to join global ones in their decline. We referenced the slowdown in the US manufacturing sector on the front page of *The Monthly* noting that Institute of Supply Management's index turned lower for the first time in 3-years. Our hope is that malaise in manufacturing does not infect the services segment of the economy, far too many jobs are on the line there. Unfortunately, Beijing and Washington have not been able to agree to the terms for a September trade talk following a series of escalations and continued rhetoric that only stopped when President Trump hallucinated about a phone call between Chinese officials and his "top trade people". In an unfortunate twist, President Trump had to turn his attention to Hurricane Dorian, temporarily taking a pause from trade related twitter tweets. As *The Monthly* hits your inbox Dorian is starring at West Palm Beach Florida, a community only 100 miles away. Starring but not really much else. Like Dorian, trade talks between the US and China are severe but going nowhere, and that is causing markets like the S&P 500 to do the same.



[The S&P500 dealt with the Christmas “crunch” of 2018 quite well but the performance of the index since then has been a lot less impressive.]

When viewed on a 1-year basis the S&P 500 index has barely moved. An American appeal to set boundaries around the next round of talks seems, to us, more contrived than it does sincere. The Chinese for their part called on a delay of new tariffs, another stumbling point causing investors to sigh with the trade war no closer to resolution that several months ago. The last three run ups in the S&P500 were summarily dismissed with investors not wanting to be left holding the bag if things got worse. We believe investors are unlikely to drive stocks to new highs until a conclusive resolution to trade talks is consummated. The President for his part moved ahead with new duties on Chinese goods on Sunday, seemingly unaware of the consequences of his actions (and storm categories) yet again...stock futures dove predictably lower and most markets spent the day in the red. A re-birth of productive trade talks it would appear is still a very long way off and we believe it is *the* overhang that continues to loom over markets. At the same time, we do not believe a category 5 market implosion is in the cards either. Things like the ongoing slowdown in Europe or the calamity in Argentina (see "*Oh Cristina*" later on in this edition of *The Monthly*) are minor irritants rather than imminent threats to MacNicol clients: we hold wafer thin exposures to both. But we wish Americans and Chinese would accept the fact that traditional methods of replenishing their trade relationship are not working. Chinese foreign ministry spokesman Geng Shuang seems to agree. Shuang said:

"The most important thing at present is to create the necessary conditions for continuing trade talks".



[Chinese Foreign Ministry spokesman Geng Shuang would never sigh at a press conference. But we feel sorry for the guy and think he could benefit from some replenishment himself. A full-time job that includes balancing the relationship his country has with its largest trading partner is bound to be taxing, especially considering President Trump’s basic lack of economics knowledge and introspection.]

The MacNicol team believes that a re-birth in trade talks will ignite a powerful re-birth in equity markets, but the former will entail some introspection and a lot of consensus building. Introspection is not the first one we would come up with when thinking about President Trump. Perhaps he could use a trip to REO. REOs staggeringly enjoyable activities and mind-altering beauty are truly the right environment for re-birth. In the case of President Donald Trump, we think that he would be much better off solving some of his own problems before tackling the issues plaguing the United States of America.



[This is a shot of the Nahatlatch river from REOs common area. A little bit up the river lies surreal Lake Francis. A strong command of superlatives is necessary when speaking about Lake Francis to friends and colleagues.]

I allowed myself to think differently about what a vacation *should* be and the results were dramatic. What I put into a vacation is what I got out of it. If you or someone you know thinks differently about your investments, a similarly dramatic result may occur.

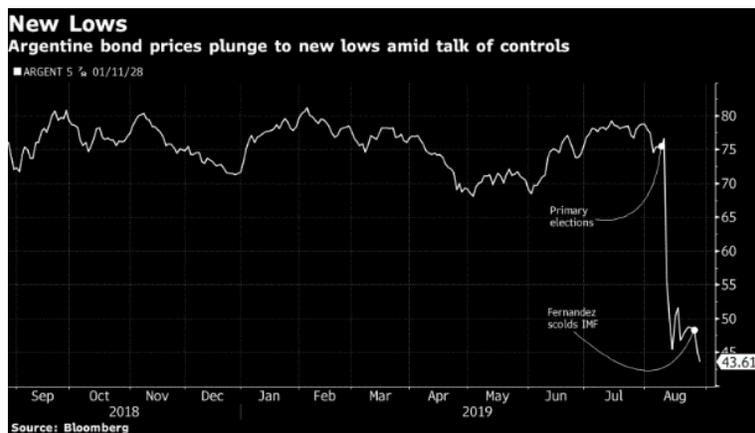
REO Rafting and Yoga Resort in Boston Bar BC was transformative because it provided the framework for me to address issues other vacations never could while clearing my mind of years at the apex of capitalism. It was an experience unlike any other and I will do it again. A face-to-face meeting with President Trump or President Xi is not in the cards for the MacNicol Investment team and that is why nothing will ever make us deviate from our time-tested investment process even though we approach financial markets with a new and reborn perspective.

The MacNicol Investment Team

“Oh Cristina...”



If there was a beauty contest for politicians, Argentina’s Christina Fernandez de Kirchner would win hands down. But that’s not the only thing Cristina would win at. Argentina’s ex President is winning quite a lot these days and is now one step closer to getting her old parking spot back at the Presidential palace in Olivos (Buenos Aires). “CFK” as she is known in political circles is running to be Argentina’s next Vice President – we assume that citizens under investigation for corruption are not permitted to run for the full Presidency – alongside partner Alberto Fernandez (no relation). The pair had quite the showing at Argentina’s primary elections. The duo just about ran incumbent Mauricio Macri out of town on their first attempt. Should the same result play out in the Argentinean national election in October, Macri will have to clean out his desk. In the mean time Argentineans have begun emptying their bank accounts, many older Argentineans have seen this soap opera before. Still, should Macri sustain a second such beating in October, there will not even be a need for a run off election. Yes, CFK would easily win a beauty contest and stands poised to win a political contest too, unfortunately, as it pertains to the “beauty” contest being waged in financial markets, CFKs brand of populism isn’t exactly comforting to investors...



[CFK has her political groove back...and that “groove” is costing the Argentinean financial system a lot of money. Bonds collapsed, the Argentinean Central Bank had to intervene and foreign currency reserves plummeted. “Welcome back home” Cristina.]



[I make nationalizing private pension plans and other assets look good. And when I fire the head of our central bank and tell the IMF to shove it...again...they will thank me for the pleasure.]

Currency traders and fixed income investors did not enjoy the feeling of having to seriously consider left wing Peronist populism. But with CFKs own “rebirth”, it seems highly probable that Argentina swings left. And that’s a huge problem when it comes to the impact on sovereign debt and the \$57 billion loan the country received from the IMF. CFK commented on the loan:

“The current economic program is not our program”. “It commits our country well beyond its own possibilities”.

The “program” CFK is speaking about is the one in which Macri agreed to tough fiscal commitments and austerity measure such as a primary fiscal surplus of 1% in 2020. Economic interventionism’s aim is to correct market failures to promote the welfare of the people. But investors don’t always like intervention. Nor do we. The MacNicol investment team has worked closely with our Hedge Fund partners in Greenwich, CT and Sao Paulo to get a better understanding of where we stand on the matter. Fortunately, our exposure is measured in basis points and not tens of millions of dollars. Attached on the following page is a summary of our exposure to Latin American debt on a country basis in our award winning **MacNicol Absolute Return Fund**, which functions as our primary emerging market investment vehicle.

Country	Long	Short	Net	Gross
Brazil	27.9 %	0.0 %	27.9 %	27.9 %
USA - Multinational	15.1 %	-4.3 %	10.8 %	19.4 %
Brazil - Multinational	15.9 %	0.0 %	15.9 %	15.9 %
Venezuela	8.3 %	0.0 %	8.3 %	8.3 %
China	8.2 %	0.0 %	8.2 %	8.2 %
France - Multinational	5.5 %	0.0 %	5.5 %	5.5 %
Mexico	4.3 %	0.0 %	4.3 %	4.3 %
Jamaica - Multinational	4.1 %	0.0 %	4.1 %	4.1 %
UAE	2.5 %	0.0 %	2.5 %	2.5 %
Australia - Multinational	2.1 %	0.0 %	2.1 %	2.1 %
Canada	1.9 %	0.0 %	1.9 %	1.9 %
Mexico - Multinational	1.4 %	0.0 %	1.4 %	1.4 %
Canada - Multinational	1.1 %	0.0 %	1.1 %	1.1 %
Argentina	0.8 %	0.0 %	0.8 %	0.8 %
Chile	0.7 %	0.0 %	0.7 %	0.7 %
USA	0.0 %	-0.7 %	-0.7 %	0.7 %
Spain - Multinational	0.6 %	0.0 %	0.6 %	0.6 %
All Other Countries (Gross < 50 bps)	0.3 %	0.0 %	0.3 %	0.3 %
Grand Total	100.5 %	-5.0 %	95.5 %	105.5 %

[As of July 2019, the MacNicol Absolute Return fund counted its exposure to Argentinean debt in tiny basis points rather than large percentages.]

Though we would gladly do dinner with CFK just about anywhere in Buenos Aires we doubt executives from the IMF would do the same. CFKs attitude towards the IMF is not recalcitrant just yet, but the implications of her return could influence the next tranche of the IMF's \$56 billion line of credit causing Argentina to dip into its currency reserves as investors do the same. It is just too bad that to many, ourselves included, the IMF imposed austerity measures are what is temporarily submerging Argentina in the first place and the predictable rise of populism following soon thereafter.

Contagion?

Contagion is present in the short term for sure, but we struggle to accept it as a broad-based existential risk. Mark-to-market risk in regions like Venezuela and hedging risk in Brazil (i.e. capital controls that prevent investors from yanking money out of Argentina could see investors shorting Brazil as the "next best thing") are on the table but not in a real way. Shorting Brazil may be the "next best thing" but it is also a far cry from the economic reality of a Brazil that appears to be performing reasonably well.

As far as the Argentinean bond we do own goes, the good news is that it is one of 3 provincials backed by royalties from the Oil & Gas sector. Revenues from oil and gas sales are channeled into a private trust which issues debt against those royalty streams. It's a technique of exposing the bondholders to more in the way of an international oil price and less in the way of CFKs political battle with the IMF. We spoke with a group in Greenwich CT and learned that throughout the entire history of Argentina, only 1 similar trust structure failed. That certainly makes us feel a lot better but our next update call is already in our calendar. Suffice it to say, fall should be an exciting time for Latin American debt managers. For our part, we are happy to hold a seat way up at the back and near the exit doors.

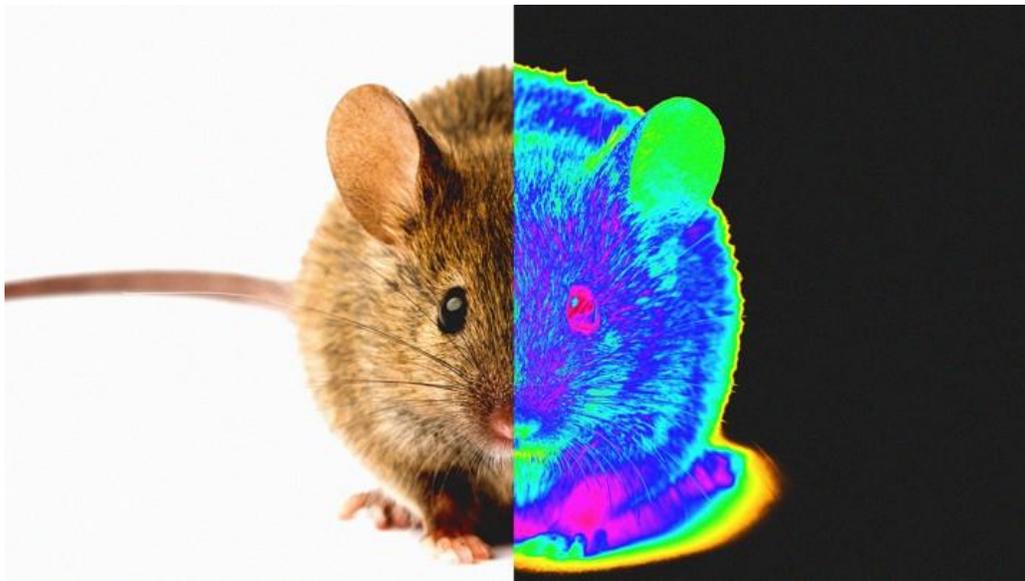


[As lines begin to form at Argentine banks, capital controls are back in fashion. Far from new for many Argentines, the latest round of capital controls simply kick off the latest chapter in the country's dubious financial history.]

To the MacNicol investment team, being asked what we think of CFK is an open-ended, abstract question. The definition of CFK is a populist Peronist who likes a good fight and spells trouble for foreign investors holding Argentinean assets. Longer-term, who knows, perhaps a deeply socialist agenda will prevail resulting in an Argentina that is reborn itself. Time will tell.

The MacNicol Investment Team

Neophobia



In "*Neophobia in wild and laboratory mice*", researchers Terry Meddock and Don Osborn both with the University of Miami's psychology department, found that wild mice were more reluctant to approach a new object introduced into their cage than domesticated lab mice. The new object in the Meddock and Osborn study happened to be a toy horse and as simplistic as the study might sound it offers a transformative lesson to investors. Laboratory mice were more open to a toy horse being inserted into their cage because the rodents had experienced more than their wild counterparts.

Investors can exhibit neophobia too, especially when propositioned with investments that are not what they are use to. That's why we take the time to hear about our clients needs first and then educate them about our process. Part of that process involves the inclusion of alternative investments directly in client portfolios. Though the MacNicol investment team is known for the successful application of alternative investments in client portfolios for over a decade, we still take the time to communicate to investors our ideas.



[Neophobia is not exclusive to mice.]

Neophobia is not fun when it comes to new foods or new investment ideas. But working with an investment manager that has been there can certainly help. We are confident that after you visit our website www.macnicolasset.com or meet us in-person you will realize that safe futures tomorrow begin with safe harbours today, even if we include something in your portfolio that you might not have seen before.

The MacNicol Investment Team

Firm News

MacNicol & Associates Asset Management turns 18!!! Congratulations to founders David and Diane MacNicol and a big thank you to our dear clients. Thank-you for the trust you place in our relationship and the referrals we receive from you, it means a great deal to us.

If you have made it to the end of *The Monthly* then I truly thank you for your attention. They say good things come to those who wait and here is one very, very good thing. The REOs website can be found here www.reorafting.com and when you call them at 1.800.736.7238 just make sure you tell them that a Yoga obsessed money manager in Toronto sent you.

The MacNicol Team recently concluded two days worth of corporate planning meetings in Northern Ontario. The focus of the meetings was to enhance our services offering to investors and partners through mutual accountabilities.

MacNicol & Associates Asset Management Inc.