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

December 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 marketplace.

"When stability becomes a habit, maturity and clarity follow"

- B.K.S Lyengar

The Numbers:

Index:		**Year-to-Date:**	
S&P/TSX:		19.0%	
NASDAQ:		30.6%	
Dow Jones:		20.3%	
S&P500:		25.3%	
Interest Rates:	**Canada**		**USA**
90-Day T-Bill:	1.65%		1.58%
5-Year Bond:	1.56%		1.59%
10-Year Bond:	1.53%		1.77%
30-Year Bond:	1.62%		2.23%

Economic Data:

- Bank of Canada holds key rate at 1.75% as growth in Canada slowed in the 3rd quarter to 1.3%.
- S&P500 reaches 3,153 on November 27th, 2019
- WTI Crude up $3 in November to $56 per barrel
- Copper at 2-year cycle low now below $2.60
- Gold fell by $60 in November to $1,480
- November US ISM sharply lower at 48.1
- Bank of Australia keeps lending rate at 0.75%
- Bank of Montreal takes (another) charge related to severance packages for fired workers, this time as many as 2,300 positions could be at risk

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	22.8	19.4
P/B: Price-to-Book	3.5	2.9
P/S: Price-to-Sales	2.2	1.9
Yield: Dividend Yield	1.85%	1.90%

Year-to-date Performance, by Sector: December 1st, 2019

S&P/TSX Composite	19.0%
NASDAQ	30.6%
Dow Jones Industrials	20.3%
S&P 500	25.3%
Russel 2000 (Small Caps)	20.5%
MSCI EAFE	14.8%
Crude Oil Spot (WTI)	28.5%
Gold Bullion ($US/Troy Ounce)	14.1%
SOX Semi-conductor Index	47%
VIX Volatility Index	- 43.6%

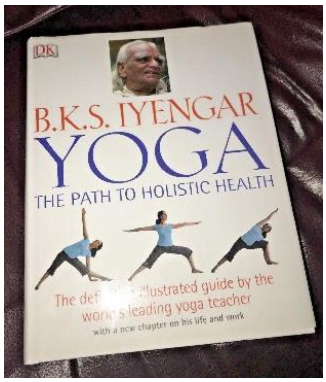
Source: Canaccord Genuity Capital Markets & Thomson Reuters

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 Dec 12, 2019 9:30 AM	**$5,000**	**Cdn**		
Banks	**Rate**	**Buy USD**	**Cost**	**% Difference from Spot Rate**
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.3187	$3,792	$-	0.0%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.3316	$3,755	$(37)	-1.0%
Raymond James	1.3327	$3,752	$(40)	-1.1%
Royal Bank	1.3461	$3,714	$(77)	-2.1%
Scotia	1.3518	$3,699	$(93)	-2.5%
TD	1.3523	$3,697	$(94)	-2.5%
Spot Rate	**1.3187**	**$3,792**		

A bit of stability in your portfolio, a world of clarity in your finances



Earlier in the week a friend of mine in the institutional sales space texted me the following question:

"Hey.."
"Do you know which US REIT's are the most stable?"

My friend wanted to learn more about real estate to provide his clients with better information when it came to their investment options. Institutional sales can be a tough, competitive business where you only "eat-what-you-kill" so it is important to have a competitive edge. With real estate being one of my favorite investment topics and this particular friend having been gracious with his own time in the past I was eager to help. But rather than simply *telling* him the answer I

thought I would *show* him how I derived it myself. The exercise, like a yoga workout, ended up benefitting me over and above the simple act of returning a favor.

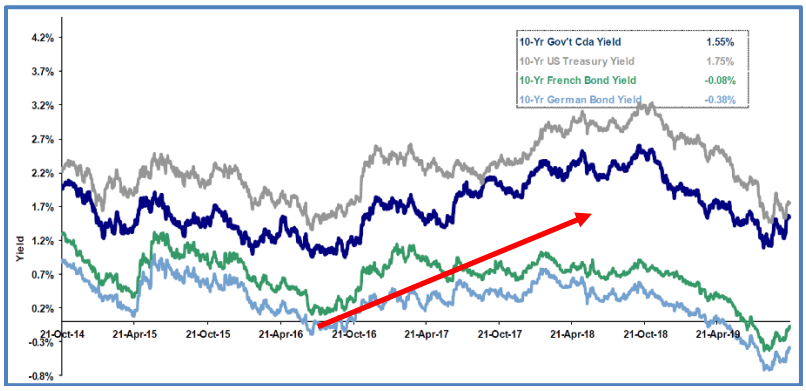
Using S&P Capital IQ's impressive securities database I was able to create a spreadsheet that followed all US REIT's and showcased several salient ones no real estate decision should be made without. If the spreadsheet is difficult on the eyes, then I apologize profusely. Please allow me to walk you through what all the cells mean: fund managers are great at that.

Capital IQ Equity Screening Report > U.S. REITs Screen

Ticker	Security Name	Company Name	Dividend Yield [Latest] (%)	Day Close Price / 52 Week High (%) [Latest]	Day Close Price / 3 Year High (%) [Latest]
NYSE:BEE PRBCL	PFD SER B	Strategic Hotels & Resorts LLC	-	-	-
NYSE:BMR PRACL	PFD 7.375% A	BioMed Realty Trust Inc.	-	-	-
NYSE:DTLA.PR	PFD SER A 7.625%	Brookfield DTLA Fund Office Trust Investor Inc.	-	-	-
NYSE:LHO PRECL	PFD SER E SBI	LaSalle Hotel Properties	-	-	-
NYSE:NRF PRA	PFD A 8.75%	NorthStar Realty Finance Corp.	-	-	-
NYSE:PRMI	Common Stock	Priam Properties Inc.	-	-	-
NYSE:TRNO	Common Stock	Terreno Realty Corporation	1.9	99.3	99.3
NYSE:ARE	Common Stock	Alexandria Real Estate Equities, Inc.	2.52	99.2	99.2
NYSE:GMRE	Common Stock	Global Medical REIT Inc.	6.01	99.2	99.2
NYSE:GMRE.PRA	7.50% CUM PFD A	Global Medical REIT Inc.	6.01	99.2	99.2
NYSE:SAFE	Common Stock	Safehold Inc.	1.67	99.2	99.2
NYSE:LPT	Common Shares	Liberty Property Trust	2.68	99.1	99.1
NYSE:DEA	Common Stock	Easterly Government Properties, Inc.	4.56	98.8	98.8
NYSE:GRP.U	Stapled Units	Granite Real Estate Investment Trust	4.12	98.7	98.7
NYSE:STOR	Common Stock	STORE Capital Corporation	3.48	98.7	98.7
NYSE:FR	Common Stock	First Industrial Realty Trust, Inc.	2.2	98.2	98.2
NYSE:FR PRKCL	PFD K 7.25%	First Industrial Realty Trust, Inc.	2.2	98.2	98.2
NYSE:PLD	New Common Stock	Prologis, Inc.	2.33	98.2	98.2
NYSE:VICI	Common Stock	VICI Properties Inc.	4.89	98.2	98.2
NYSE:EGP	Common Shares	EastGroup Properties, Inc.	2.26	97.9	97.9
NYSE:AMH	Class A Common Shares	American Homes 4 Rent	0.767	97.5	97.5
NYSE:AMH.PRF	CM RED PFD SHS F	American Homes 4 Rent	0.767	97.5	97.5
NYSE:AMH.PRG	5.875% CUM PFD G	American Homes 4 Rent	0.767	97.5	97.5
NYSE:AMH.PRH	6.25% CUM PFD H	American Homes 4 Rent	0.767	97.5	97.5
NYSE:BXP	Common Stock	Boston Properties, Inc.	2.78	97.4	97.4
NYSE:BXP.PRB	DEP 1/100 PF B	Boston Properties, Inc.	2.78	97.4	97.4
NYSE:CUZ	Common Stock	Cousins Properties Incorporated	2.92	97.3	97.3
NYSE:LSI	Common Stock	Life Storage, Inc.	3.65	97.3	97.3
NYSE:ELS	Common Shares	Equity LifeStyle Properties, Inc.	1.97	97.0	97.0
NYSE:DEI	Common Shares	Douglas Emmett, Inc.	2.41	96.9	96.9
NYSE:EPRT	Common Stock	Essential Properties Realty Trust, Inc.	3.35	96.8	96.8
NYSE:MAA	Common Shares	Mid-America Apartment Communities, Inc.	2.84	96.6	96.6
NYSE:DRE	Common Shares	Duke Realty Corporation	2.7	96.5	96.5
NYSE:AIV	Class A Common Stock	Apartment Investment and Management Company	2.92	96.4	96.4
NYSE:STAG	Common Stock	STAG Industrial, Inc.	4.69	96.2	96.2
NYSE:RHP	Common Stock	Ryman Hospitality Properties, Inc.	4.11	96.1	96.1
NYSE:RVI	Common Shares	Retail Value Inc.	5.49	96.0	96.0

[I know this is hard to read…but at least I did not include the *entire* spreadsheet which went on for 3 more pages!]

The US REIT's that I dropped into my spreadsheet included some variables I could adjust in order to get back to my friend with the original answer to his question. As it turned out, the exercise also allowed me to test a little thesis of my own. For now, however, focus your attention on the right most column I highlighted in lime green. This column is the one that compares a US REIT's most recent trading price to its 3-year high, and, after doubling checking that the 3-year high wasn't yesterday, I was confident in using this data series as my barometer for "stability". I chose the 3-year high because of the chart below:



[Mortgage markets are pretty sensitive to movement in the 10-year bond.]

October 2016 to October 2018 was primarily a period of rising interest rates, a period that gave me a decent taste of what mortgage markets were doing and in turn what real estate was probably also doing. Along with helping my friend, I wanted to figure out whether the following equation was actually true:

Rising Mortgage Rates = Falling Real Estate Prices

Rising interest rates are not exactly a tailwind for real estate, but my own personal thesis has always been that conservatively underwritten properties in great locations should be fairly stable because of a situation in which institutional investment capital effectively "floods" the market with capital, allowing real estate investors to access capital at a lower cost than that imbued by the mortgage market. As you can see in the data, many REIT's continue to trade near their 3-year highs, certainly a sign of stability if you ask me. Something that I feel compliments stability is the stream of monthly income that many real estate product types are associated with and in that sense quality real estate is a lot like quality yoga: good in both the short and long-term. Coming back to my friend's original question of which US REIT's were the most "stable", I was pleased to report that by a wide margin, the answer is conservatively underwritten residential REIT's with a focus on growth markets. The exact same strategy we have been investing into our MacNicol 360 Degree Realty Income Fund since the beginning. Driven by favorable demographics and ongoing supply/demand imbalances, residential real estate is poised to continue adding value to client portfolios is a reliable way. Mature investors know the importance of stability in a portfolio and mature fund managers know the importance of helping a friend with questions.

Real estate investing is a lot like yoga and paraphrasing Yoga Master Lyengar guides us to the conclusion that yoga, the relationships we have with our friends and the investments we make for our clients are all basically the same: all require dedication and all pay dividends well off into the future.

The MacNicol Investment Team

Modern Monetary Theory: borrowing your way to prosperity

I worked with a fellow who was married to an incredibly successful interior designer. This gentleman's wife had her own show, numerous magazine spreads, a book, a list of famous past clients not to mention the income that a successful business can bring. Though he continued to work with me, quite well I might add, work for this fellow was less of a requirement and more of a hobby. Making ends meet was more of an expression for him than a reality. Fortunately, he also happened to be a very nice person and one who knew and accepted that his enviable financial situation would expose him to jokes like:

"*Hey Francis, what's it like to have unlimited financial resources and famous connections to Toronto's elite*?"

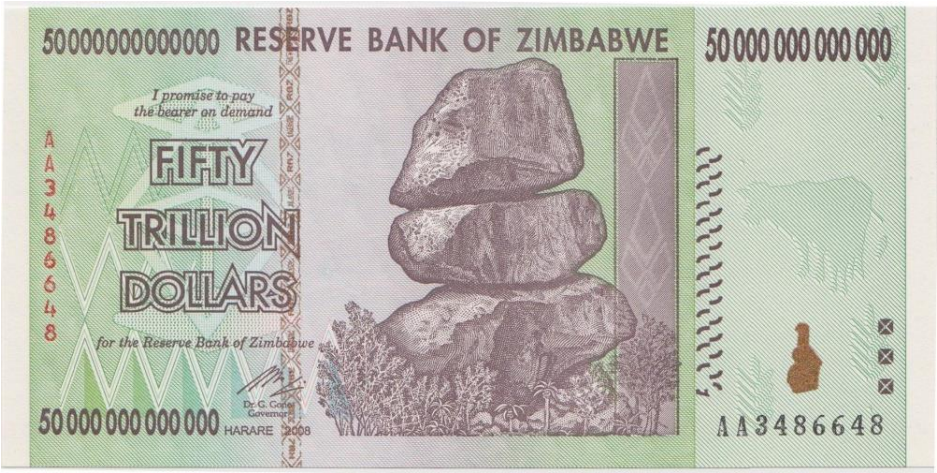
"*I wish I knew*" was Francis' usual response. It was great that Francis did not let his wife's success fuel unrealistic desires about the lifestyle he led, nor did it appear to alter Francis' lovely Mediterranean personality. But while Francis and his wife seem to be doing quite well for themselves, the rest of us have to make do with choices regarding our lifestyles. Either that or, borrow.

[Gosh this is getting heavy; I wonder whether that Ferrari and Rolex were worth it at my age.]

High levels of debt are viewed as irresponsible, but they are not necessarily a bad thing. If household incomes are rising fast enough to offset burgeoning debt obligations, then families should be okay. By the same token, if the projects that governments invest in increase productivity and create new jobs, then borrowing to fund them should also be okay. The only real risk in both situations is inflation. Households that live beyond their means can become vulnerable to inflation. Prices may not necessarily go higher, but if a family's ability to afford the things they need collapses due to debt then the lifestyle desired might simply be out of stock. Still, not everyone who borrows money is reckless. Before someone gets handed an Ivey League diploma, they typically have to take on some serious debt to afford tuition not to mention be bright enough to pass the admissions test. Before a new business sells a single product or service, it often has to borrow to pay for salaries, rent and the procurement of all of the other inputs that go into a business. Before you get handed the keys to your first new home, you will have had to qualify for a mortgage or at the very least be on extremely good terms with Francis' wife apparently. Borrowing then is completely normal, but can it go too far? Under Modern Monetary Theory, governments can make all of their necessary payments and yet never face a solvency problem when faced with a bill they are required to pay thanks to the magic of deficits. Through deficits, governments can function a lot like our Yale graduate, organic beef entrepreneur and first-time homeowner in Aurora, Ontario…but they have to be smart about it. And maybe that's why government deficits are something that many feel should be eliminated. Perhaps they signal a nation that is poorly run or vulnerable to economic setbacks. The truth is deficits, even large ones, can be sustainable and the antidote for economic setbacks rather than the setbacks themselves. The caveat though is that the capital spent when governments choose to run deficits must be deployed to things that add value to the economy.

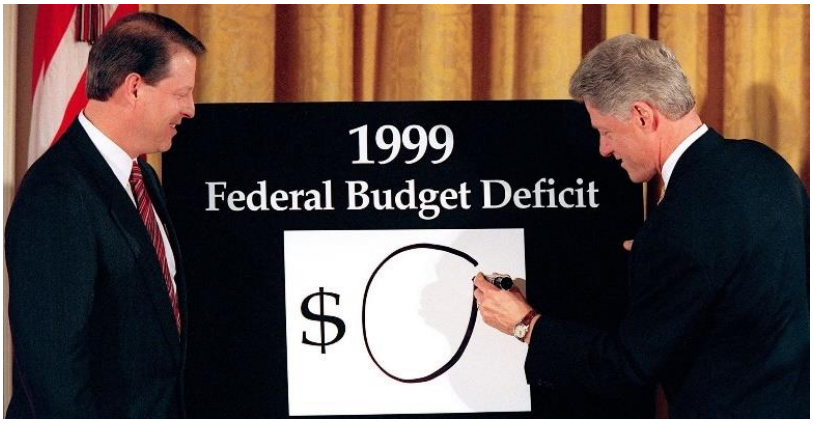
["Mr. Speaker, Canada's financial position is *rock solid*…it's just that we are about $14 Billion short this year"]

Adding value to an economy primarily means increasing productivity since productivity is what increases economic capacity and thus leads to more output and more jobs. Spending on healthcare, infrastructure and education are pricey tabs the government is advised to run because they stimulate growth. At the same time, excessive deficits can invariably lead to situations where inflation runs rampant but not necessarily because the type of economic picture a nation wants is out-of-stock. The Weimar Republic of the 1920's, Zimbabwe in the late 1990's and more recently Venezuela all teach us that evidence of a large deficit or one that is poorly managed is inflation. Beyond any other definition, inflation is the simple idea that the money you have (or your ability to borrow more of it) loses its value.



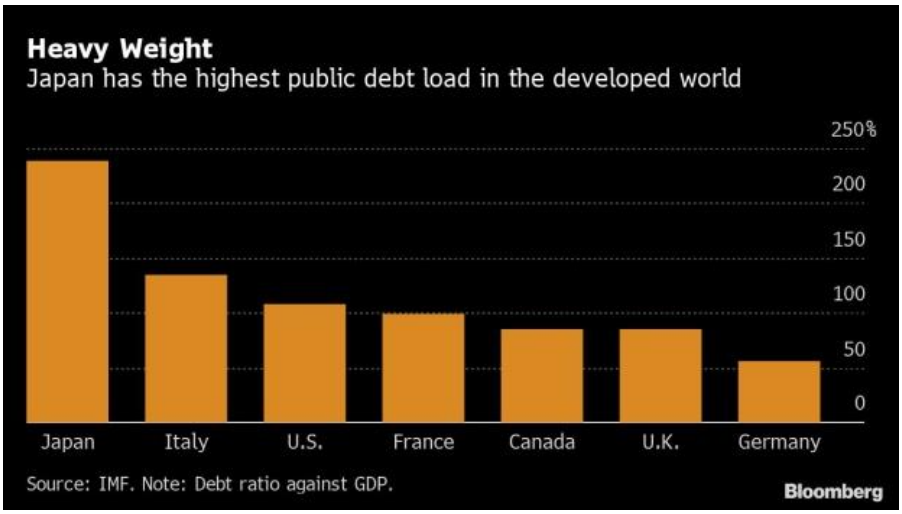
[A sharp increase in the price of goods is less a narrative about the worth of those goods than on the worth of the money used to acquire those goods. Objectively, Zimbabwe's currency had next to no intrinsic value and probably doesn't today. But subjectively, the people of Zimbabwe lacked the confidence in their currency's ability to retain value because they probably lacked confidence in the Leadership of Robert Mugabe. Zimbabwe's war with the Democratic Republic of Kongo and its culture of corruption led to hyperinflation which makes money less valuable than the paper it is printed on not to mention economic case studies that the folklore of Modern Monetary Theory.]

But deficits can also be too small…



["There you are Vice President Gore…zero"]

When a deficit is too small it fails to support the economy since demand can recede in an environment without the support that deficits create, and when that happens unemployment rises. You see one thing that tends to get overlooked in deficit discussions is the idea that if the government collects $0.90 of revenue in taxes and spends $1.00 of it there is now an additional $0.10 somewhere in the economy. A deficit to the government becomes a surplus to the people since red ink in Ottawa or Washington will eventually become black ink for Canadians and Americans alike. Whether deficits should be expanded to stimulate growth depends on what the capital is used for. Investments in hospitals, roads, transit, and education are things that come with hefty price tags, but which can bring us to a place where the goal of a desired lifestyle is back on the table. The MacNicol team feels that like other fiscal tools, deficits should be managed with precision and with the recognition that "If that doesn't work, we can always raise taxes" is never a good option. So how big of a deficit is too big?



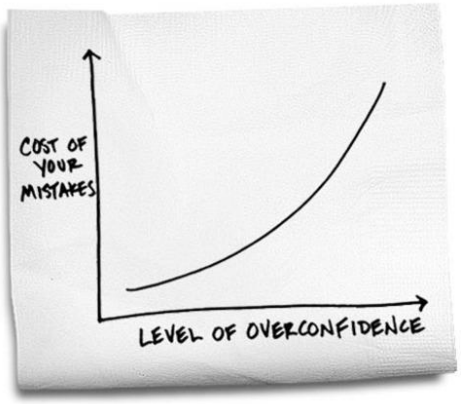
[The United States and Japan have similar levels of public debt but America's economy produced 4x more than Japan.]

When you look at Japan, you see a level of debt to GDP that towers over our own and those of our peers. How is Japan able to sustain a debt load of that size without paralyzing inflation and crushing interest rates?

As the Japanese have been able to demonstrate for several years now a debt load of nearly a quadrillion yen isn't a bad thing if you are smart about it. Long-term Japanese rates are essentially nil, and you'd be hard pressed to find an economist that feels Japan has an inflation problem. What's the secret? Well the Japanese still have plenty of scope for large public and public-private partnership investments in growth-enhancing infrastructure projects of transportation, information technology, life sciences and social welfare. This sort of scope takes the edge off a lot of fiscal red ink. But if you are still unconvinced that borrowing is bad consider this. After the 2nd world war, America's debt to GDP ratio rose to 121%. Yet economic historians do not speak of that period as a time when America risked burdening future generations with its debt problems. The next generation did not inherit the debts of the War Bond generation, they instead inherited the hospitals, roadways & airports and schools the government built in the wake of fighting World War II. What followed was not economic ruin but a golden age of capitalism and American prosperity. So, if the government considers a new spending bill, rather than asking what it will do to the deficit, the real question to be asked is what does this do for our future growth prospects and do we risk the threat of inflation? What do you do if inflation becomes a problem? The answer depends to a considerable extent on what is driving inflation. Inflation that is important is the result of aggregate spending and hard to believe. We have not experienced **demand pull** inflation [too much money chasing too few goods] for years. Rather, inflationary dialogues have tended to be dominated by **cost push** inflation which is the substantial increase of an important good or service that has no substitute. Having the Bank of Canada raise rates or Ottawa raise taxes does little to impact things like an oil price shock, healthcare costs or housing price increases.

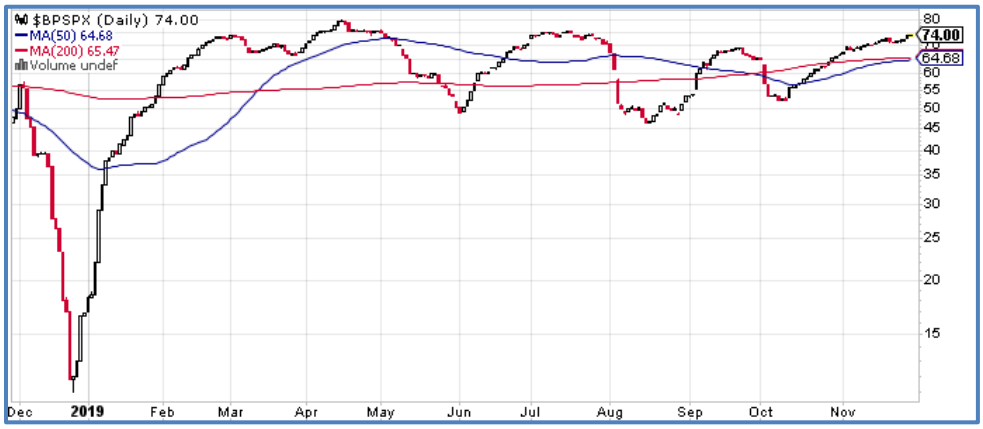
The MacNicol Investment Team

Overconfidence: neither sexy nor lucrative…



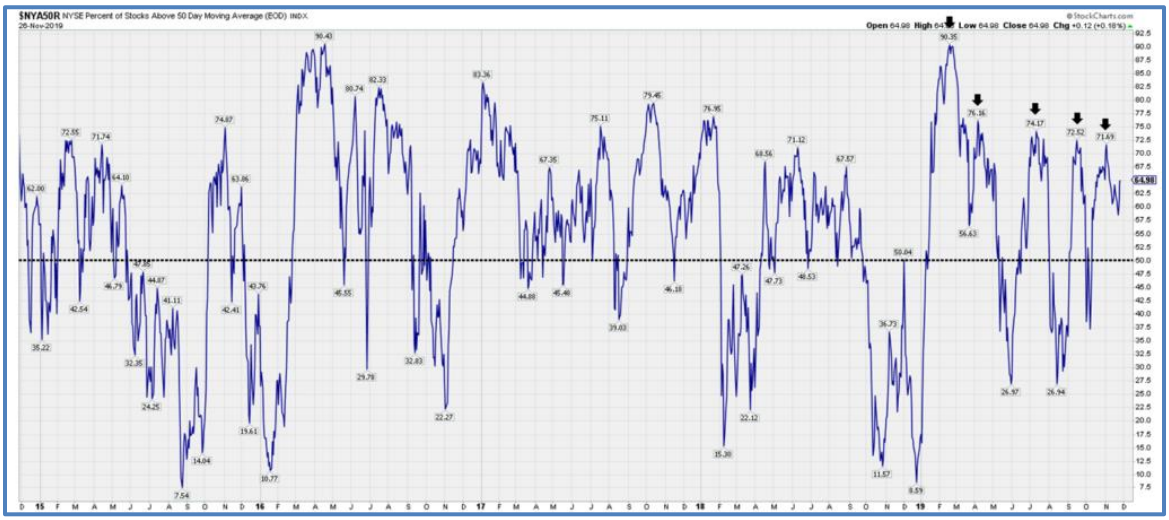
Most would describe me as a highly sociable person bordering on gregarious [for a Portfolio Manager]. I think it takes a certain degree of self confidence to succeed in social settings. Not that I always succeed in social settings, I think what I am trying to say is I embrace them. But there is a fine line between confidence and arrogance that can get blurred on Bay and Wall Street. A sad but enduring stereotype people in my line of work suffer from is that finance people sometimes are arrogant jerks. I assure you I am not arrogant. As far as the jerk part goes, in all honesty, that's a function of how much caffeine I have managed to ingest in any given morning.

But when it comes to investing, the line between confidence and arrogance can be blurry too. Blurry and costly. When our group studied the Bullish Percent Index for the S&P 500 to assess investor optimism, we came away from the exercise feeling a bit anti-social.



[The Bullish Percent Index shows investors feeling gregarious themselves these days. Hopefully this "good will" won't get the better of them]

Antisocial but in a way that still allowed us to advocate for the one special interest group we care about most: our investors. Corroborating the need to pen this missive was this next chart of the percent of stocks listed on the New York Stock Exchange that were trading above their 50-day moving average. Sure, the NSYE has "perked up" in the past few days, but if you take a step back and look at the peaks in 50-day moving average activity by the NYSE thus far in 2019, you get a sense that the index itself is re-setting lower each time and therefore that fewer and fewer stocks are exhibiting bullish price action.



[The real value of this chart isn't the blue line

Objectively, stock markets have done pretty well in 2019. So, it becomes easy [not to mention subjective] to assume that the plethora of profits will continue into 2020. To be clear, we are not suggesting that stocks cannot move higher, we are simply saying that right now, we stand at a point where a) the pace of corporate profit growth has slowed and b) the fundamental underpinnings of the economy seem, at the very best, soft. To us, this really is not the sort of environment that goads us to throw caution in the wind. And that in essence is how working with MacNicol & Associates can help you be more social. We not only offer complimentary, unbiased views of your existing portfolio, we show you how our time-tested, and objective investment process works over time. That way, you can feel confident knowing you have someone on your side.

At MacNicol & Associates Asset Management, we view investments as the vehicles needed to take our clients to their financial goals. They aren't our children, spouses or friends. Investments can be held, sold off or avoided entirely and they never warrant our blind faith or unconditional love.

Firm News

Dave MacNicol attended the Capitalize For Kids Conference in October. The Conference brought together top advisors from around the world to share market insights and actionable ideas. Not only was it a very informative event, it also helped to raise funds for cutting edge research and crucial mental health services for Canada's youth. Since 2014, the event has raised over $8 million for kids' mental health. It was a very worthwhile experience!

MacNicol & Associates Asset Management Inc.