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

February 2020

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.

"The unprepared mind cannot see the outstretched hand of opportunity"

- Alexandre Fleming, Nobel Laureate who discovered penicillin

The Numbers:

Index:		**Year-to-Date:**
S&P/TSX:		1.85%
NASDAQ:		3.35%
Dow Jones:		- 0.49%
S&P500:		0.56%
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	1.64%	1.57%
5-Year Bond:	1.39%	1.45%
10-Year Bond:	1.38%	1.64%
30-Year Bond:	1.51%	2.12%

Economic Data:

- Canadian economy grows by 0.1% in November as Bank of Canada holds at most recent policy meeting along with (downward) revisions to its forecast
- US Fed also on hold while acknowledging the uncertainly of Coronavirus
- S&P500 sells off slightly in late January before recovering in early February on a lift in earnings reports mainly in the technology space
- Crude Oil lower in late January to $51/bbl
- Copper sells off after having reached $2.80/pound
- Gold tests $1,600 per ounce in early January

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	25.0	23.8
P/B: Price-to-Book	2.8	3.2
P/S: Price-to-Sales	2.4	2.1
Yield: Dividend Yield	1.75%	1.84%

Year-to-date Performance, by Sector: February 4th, 2020

S&P/TSX Composite	1.85%
S&P/TSX Venture	- 0.51%
NASDAQ	3.35%
Dow Jones Industrials	- 0.49%
S&P 500	0.56%
MSCI ACWI ETF	-3.16%
Crude Oil Spot (WTI)	-17.95%
Gold Bullion ($US/Troy Ounce)	3.52%
VIX Volatility Index	5.38%

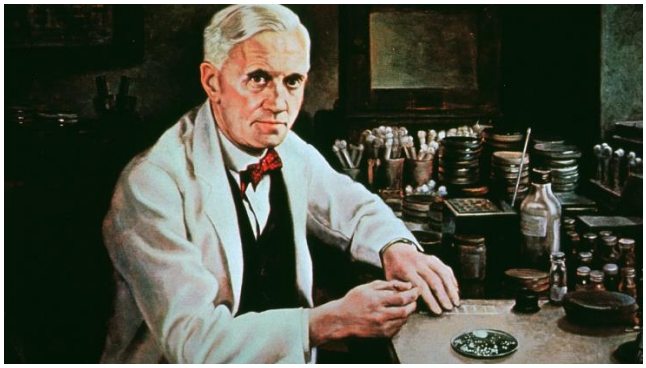
Source: Canaccord Genuity Capital Markets & Thomson Reuters

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.

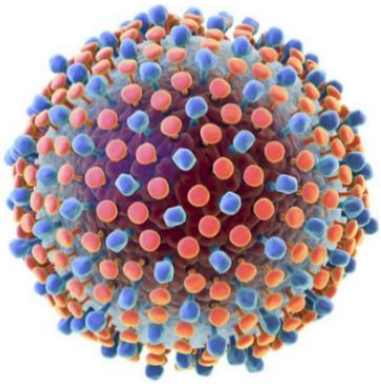
As of Feb 10, 2019 3:36 PM	**$5,000**	**CDN**		
Banks	Rate	Buy USD	Cost	% Difference from Spot Rate
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.3318	$3,754	$(4)	-0.1%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.3446	$3,719	$(39)	-1.1%
Raymond James	1.3460	$3,715	$(43)	-1.2%
Royal Bank	1.3586	$3,680	$(78)	-2.1%
Scotia	1.3644	$3,665	$(93)	-2.5%
TD	1.3654	$3,662	$(96)	-2.6%
Spot Rate	1.3305	$3,758	$-	0.0%

Concerned about a viral outbreak?
Don't be…as long as Phase 1 of the US/China deal doesn't get infected



I earned a Science Degree from the University of Toronto in the late 1990's. Among the more challenging courses I took in those days was human immunology. Human immunology gave me the opportunity to learn how the body fought off bacteria and viruses, and whole host of other interesting things I never even knew. For instance, did you know that viruses and bacteria are completely different? Believe it or not, viruses - strange as this might sound - are not technically *living* at all. A virus is a biological agent that reproduces inside of living host like a cell. When a virus infects a host cell it commandeers its victim into procuring thousands of copies of itself which go on to infect other cells and procure disease. Viruses are also deceptive since they can employ genetic "trickery" to evade capture. Evade? Despite the fact that viruses are not living, they do have genes, which means they have the ability to mutate inside of whatever agent they happen to hijack. As you can see, treating (or capturing) a virus can be very difficult.

I told you human immunology was a doozy…



[Computerized images can give viruses an almost cartoonish appearance but Hepatitis-C, pictured above, is no laughing matter.]

Over 5,000 difference species of viruses have been discovered but their ability to mutate makes me question just how many of these things are fugitives in disguise. But there is no questioning the fact that the word virus alone can make people paranoid, and for good reason. Many viruses are a nuisance, but some can be deadly. HIV, the virus that causes AIDS, is perhaps the world's most well-known extremely dangerous virus while Influenza (the flu) is the most common. Viruses then are tricky little bastards that are all around us and garner loads of media attention whenever a highly publicized outbreak occurs. Fortunately, one area that seems resistant against infection is the stock market. The Dow Jones company compiled a list of several epidemics that have occurred over the past 40 years and the data shows that stocks have tended to offer investors reasonably good immunity against financial infection.

Epidemic	Month end	6-month % change of S&P	12-month % change of S&P
HIV/AIDS	June 1981	-0.20	-10.73
Pneumonic plague	September 1994	8.22	26.31
SARS	April 2003	14.59	20.76
Avian flu	June 2006	11.66	18.36
Dengue Fever	September 2006	6.36	14.29
Swine flu	April 2009	18.72	35.96
Cholera	November 2010	13.95	5.63
MERS	May 2013	10.74	17.96
Ebola	March 2014	5.34	10.44
Measles/Rubeola	December 2014	0.20	-0.73
Zika	January 2016	12.03	17.45
Measles/Rubeola	June 2019	9.82%	N/A

—Source: Dow Jones Market Data

But is the new Coronavirus that has infected thousands and killed hundreds an affliction that merits investment paranoia? Yes and no. If you accept the idea that the outbreak will damage global travel and badly harm consumption in China, then you will probably also accept the idea that holding Chinese stocks or bonds probably is not the best idea just now. Moreover, you might also want to avoid the stocks or bonds of companies that do a lot of business with China. After all China is somewhere in between the 3rd or 4th inning of its own economic slowdown.

[Industrial profits in China sank in December by 6.3% - better than the 9.9% plunge in October – but still not good. It is also not good that China's economy continues to rollover while it has agreed to a Phase 1 trade deal with the United States that obliges it to purchase an awful lot of US stuff.]

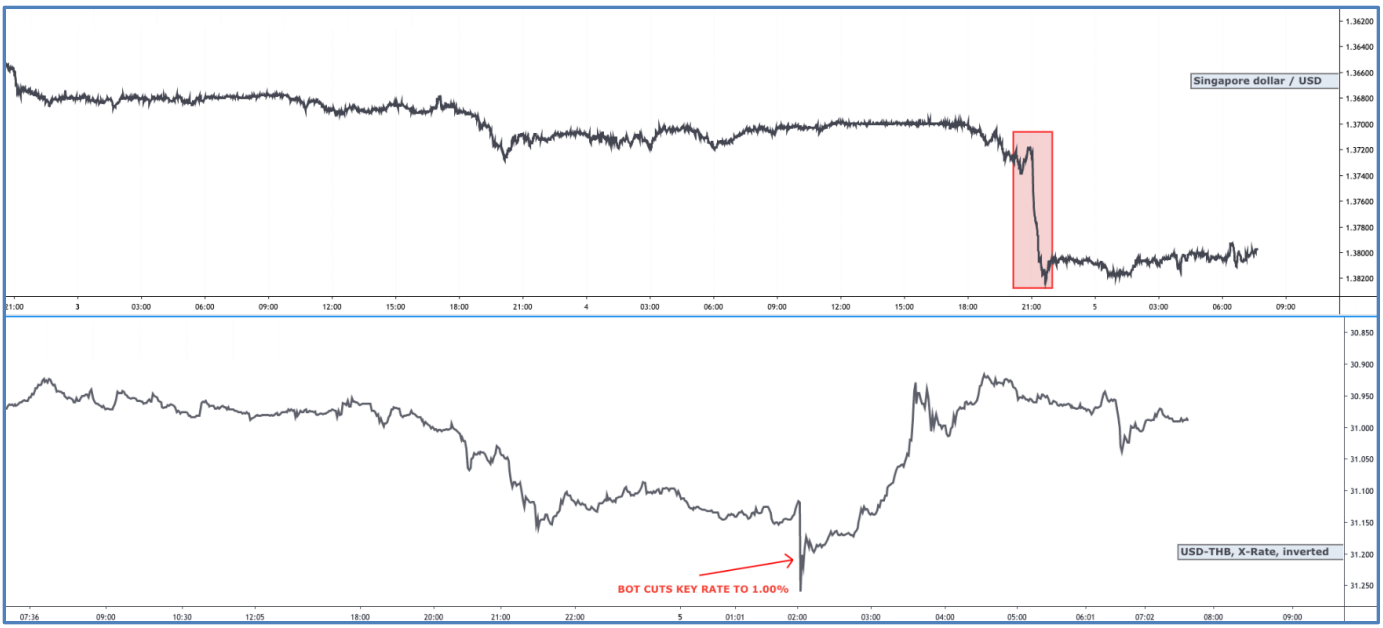
The Chinese themselves reigned in credit growth in mid-2018 to combat what was viewed at the time as rampant credit expansion, a shadow banking system, malinvestment and a real estate market that was a metaphorical house-of-cards. Perhaps the monetary brakes were applied too abruptly?

Sinking profits, big bills…

As part of the Phase 1 trade deal with the United States, the Chinese have agreed to buy an awful lot of American stuff. Stuff that that falls into four main buckets: agricultural products, energy, manufactured goods and services. During year 1 of the deal, the Chinese are obliged to purchase more than $15 Billion of farm agricultural products, nearly $20 Billion of energy, over $35 Billion of manufactured goods and over $10 Billion of services from the Americans. Making these obligations could be difficult if the Chinese do not improve the performance of their economy internally, which is what makes the timing of Coronavirus so bad. Achieving such staggering trade goals will be difficult, which could once again frustrate relations with the Americans. Recent injections of liquidity on the part of Chinese and other Asian central banks [though good for stocks in the region] inoculate the same money used to pay for most of the American stuff mentioned above. Let's also not lose site of the fact that stocks in Shanghai for example peaked in 2015 and have not yet returned to those peak levels and it does not appear that they will do so any time soon.

[The Chinese injected the equivalent of USD $72 Billion into their financial system on February 4th and USD $172 Billion on February 3rd. While the coronavirus is China's latest infection a viral form of populism known as protectionism may prove to be more damaging longer-term.]

Adjacent central banks in Asian were also on the move. In Thailand, policy makers cut rates for the 3rd time in 5 meetings to account for the threat to travel and tourism that Coronavirus poses as it waylays attempts to re-ignite growth.



[Coronavirus and a general economic malaise have caused challenges for currencies in Singapore and Thailand.]

The world is in a challenging economic predicament indeed: too much accommodation weakens the currencies while too little accommodation raises the risk that Asian economic weakness is here to stay. Corporations like Ford, Apple and Starbucks are shutting down Chinese operations and letting capacity idle until the Coronavirus is contained.

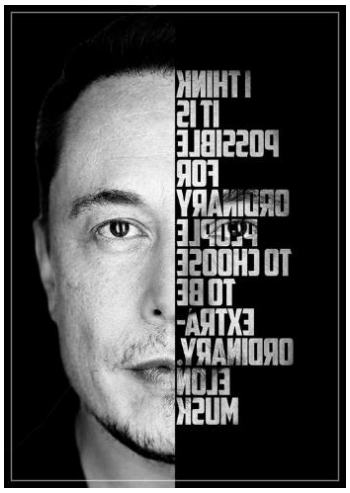
So, should you be concerned?

The Coronavirus dominates global headlines and media attention. As Portfolio Managers we believe that the historical precedent of decent stock market performance during viral outbreaks needs to be balanced by a narrow focus on geographic allocation and company-specific risk factors. Rather than asking whether it is "good" to be in stocks or not, one might wish to take a more clinical approach by asking *which* stocks to own and which to avoid.

The remedy for sluggishness in Asia and the Coronavirus might just be worse than the sluggishness and Coronavirus themselves. Phase 1 of the US/China trade deal was a big step for investors and thought it is too early to assess whether the Coronavirus impacts the deal, but we aren't taking any chances and nor should you. But rather than allowing financial hypochondria to overwhelm you personally and financially, speak to us first we will be happy to prepare your mind for the outstretched hands of opportunity.

The MacNicol Investment Team

The Smartest guy in the room…



…sure ain't me.

But I am no slouch either – according to some anyway. For example, the other day, my nephew who [full disclosure] happens to be an automotive aficionado called the house and asked me to explain to him what a parabola was. I was more than willing to oblige. When the mathematical definition of a parabola [a symmetrical open plane curve formed by the intersection of a cone with a plane parallel to its side] elicited dead silence I offered an explanation I figured a teenaged boy might better appreciate [the path of a projectile under the influence of gravity] and it worked. My sister, always wanting to stay on top of her son's education called the house 48-hours later and asked that I explain what a parabola was to her too. Naturally I was also glad to help. But this time I used an example that I thought would resonate with her:

Tesla stock…

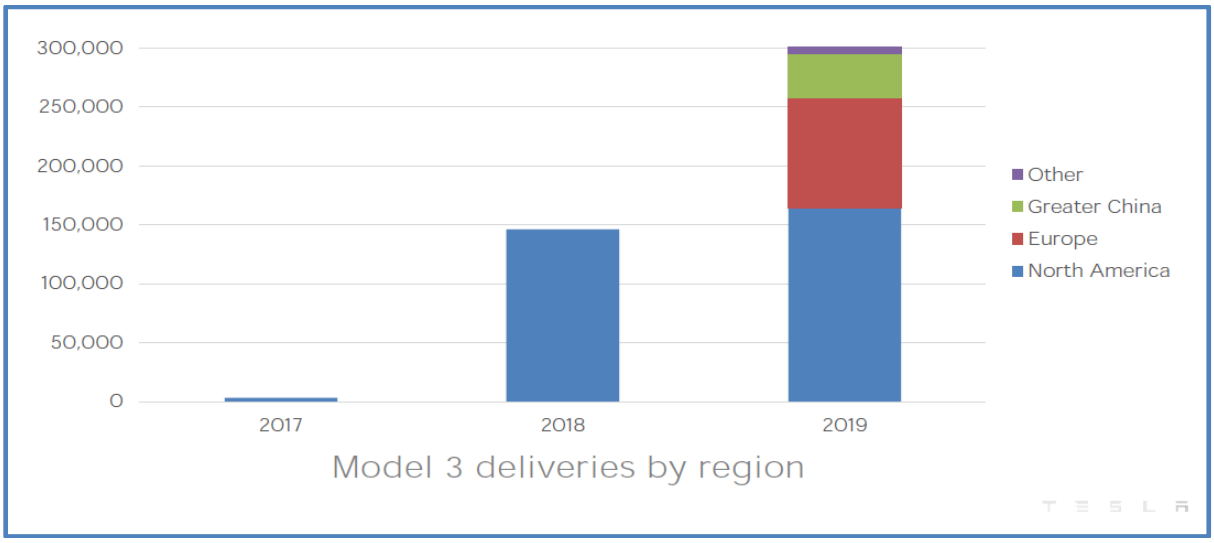
[Tesla stock drives home the concept of a parabola perfectly.]

Telsa stock has surged ever since its January 29th, 2020 earnings report. The company is on pace to deliver as many vehicles as they promised they would in 2019. The company saw more vehicles roll out of dealerships and into driveways than in the previous two years combined: may-be Tesla vehicles are being purchased by more than just fans of Elon Musk or fringe buyers. But does that make Tesla a good investment? Tesla's financial position has improved in recent years but not in the way one would hope. Tesla effectively reported no year-over-year revenue growth and operating income that's badly in need of a re-charge. Though the fourth quarter saw a slight bump up in *adjusted* profit, much of the rise came in the form of regulatory credit sales. *Net* profit for the company fell in the 4th quarter. Fans of the vehicles and the stock will doubtlessly tell you that the company was profitable on a non-GAAP basis, and if you take out the $890 million in stock-based compensation, the company was indeed profitable to the tune of $36 million. But doesn't $890 million in stock-based compensation sound like a lot? It does to us. This extremely large cost of running the business results in ongoing dilution of value for existing shareholders. Shareholders who we feel might be placing a bit too much stock in the company's Model Y compact vehicle. But why then does Tesla refuse to release any numbers on pre-orders on the Model Y.

Hmmm…

Tesla was fully charged up when it came time to talk about pre-order figures for the Model 3 in 2016 and their new "techno" truck just this past November but they remain silent about the Model Y, a car intended for the masses. The MacNicol Investment Team patiently awaits Tesla's 10-K report, which is due out in a less than a month for greater insight/confirmation into what might very well be the company's bread-and-butter car, but for now, all we know is this: the company's quarterly revenue [under US GAAP] was up just 2% compared to the previous year ended 12/31/2018. Net income actually fell in the fourth quarter to $105 million and represented a 25% decline compared to the fourth year ending 12/31/2018. The *trend* in the company's net income is also losing its charge and tapering off as the number of cars the company delivers rises. The more cars Musk delivers, the more money shareholders lose.

[Tesla's Model 3 is the white car on the right. A slight uptick in North American sales coupled with decent sales in Europe helped Model 3 sales more than double on a year over year basis, but what about the blue SUV on the left and the snazzy red sedan in the middle?]



[Tesla's Model 3 is a success…perhaps too much so.]

Model 3 sales doubled for sure, but the sales in the company's other two key products, the Model X and Model S fell by 1/3rd. The smaller pop in revenues versus number of vehicles delivered was the result of a higher concentration of the cheaper Model 3 rolling off the line at progressively lower prices. For instance, today, Model 3s can be bought for around $60,000 here in Toronto which is down from a year ago when most Model 3's would set you back deep into the $70,000's. With more competition in the electric vehicle space, less Provinces and States willing to pony up environmental credits and millennials simply choosing to drive less, we feel Tesla's price compression could continue in 2020. Despite all the above, the near-term trend in Tesla's share price is unclear at best. On the one hand, the shares could easily test $1,000 with some analysts forecasting the company's shares hitting an electrifying $1,700.

So, what do we suspect is driving Tesla's most recent run surge?

SQUEEZE…

A short squeeze [lack of supply of a stock as short sellers who borrowed the stock to sell it in the hopes of buying it back at a lower price rush to buy-back their borrowed stock] can certainly explain much of Tesla's recent run up. Volume indicators support this. Ordinarily, Tesla trades at a respectable though somewhat underwhelming 10 million shares per day. In the past few trading sessions however, nearly 40 million shares of Tesla changed hands daily.

At MacNicol & Associates we are serious about safe harbour investing and while we enjoy the novelty of seeing Tesla's electric cars growing in popularity, we continue to be deeply skeptical about the company's underlying fundamentals and would frankly prefer something a little *less* "electric". With that sad, it is hard not to want to cheer for Tesla's brilliant [and rich] CEO Elon Musk. Musk's estimated net worth of $40 billion (and counting) shows what you can do when you choose to be extraordinary, we just hope that choice does not come at the expense of extraordinary losses for investors who didn't see it coming.

The MacNicol Investment Team

From vehicles to viruses: investing in a Bipolar World

The best way to describe bipolar disorder to someone not familiar with mental health issues is a situation in which an individual can suffer turbulence as they fluctuate between a series of highs (defined by mania) and a series of lows (defined by depression) over a short period of time. In this edition of *The Monthly* we tried to present you with two articles that will hopefully prompt you to ask whether your own views of the market are congruent with our own. Violent mood swings – in life and in how you feel about your investments – can often lead to poor decisions made in great hast.

[Episodes of mood swings can occur rarely or often in people who suffer from bipolar disorder. Episodes of malinvestment can occur rarely or often in people who worry about their investments too much.]

Investments made in great hast can make you feel as those you have checked off one more item on your "to do" list, but should something as important as saving for your future not be given more attention? At MacNicol & Associates we have over 18 years of experience working with families just like yours. We take the time to explain our views on investing in plain language. We also have a robust, time-tested process that helps take the emotion out of investing.

Call us today for more information on what Safe Harbour investing can mean to you, we just might be the dose of good medicine you asked for, and in the process, we can help you "…*see the outstretched hand of opportunity".*

The MacNicol Investment Team

Firm News

MacNicol & Associates Asset Management has been helping families find a safe harbour for their futures since 2001. If you know someone who currently deals with a bank or mutual fund company please feel free to direct them to our website at www.macnicolasset.com or have them contact us at 1-866-367-3040.

We offer complimentary no obligation portfolio reviews.

MacNicol & Associates Asset Management Inc.