May 2021

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.

"Fear incites human action far more urgently than does the impressive weight of historical evidence."

- Charles MacKay, Author of *Extraordinary Delusions, and the Madness of Crowds*

The Numbers:

Index:	**2020 Calendar Year:**	
S&P/TSX:	9.6%	
NASDAQ:	8.3%	
Dow Jones:	10.7%	
S&P500:	11.3%	
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	0.10%	0.03%
5-Year Bond:	0.89%	0.78%
10-Year Bond:	1.51%	1.60%
30-Year Bond:	2.12%	2.32%

Economic Data:

* US Job Growth in April underwhelms
* India endures hellacious battle with COVID, economy remains intact for now, Reserve Bank of India takes "all hands-on deck"
* Canada losses 207,000 jobs in April, unemployment rate rises
* Canadian IVEY PMI down to 61 in April from March's very high 73 on a resumption of targeted lockdowns
* Industrial Copper, Iron Ore, Lead and Steel up in April
* Crude oil up about $5 to $64 per barrel
* Gold up $82 in April to $1792 per ounce

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	44.5	27.8
P/B: Price-to-Book	4.5	3.6
P/S: Price-to-Sales	3.0	2.0
Yield: Dividend Yield	1.4%	2.2%

2020 Calendar Year Performance, by Sector: Apr. 31st, 2021

S&P/TSX Composite	9.6%
NASDAQ	8.3%
Dow Jones Industrials	10.7%
S&P 500	11.3%
Russel 2000 (Small Caps)	14.8%
MSCI EAFE	5.6%
Crude Oil Spot (WTI)	34.7%
Gold Bullion ($US/Troy Ounce)	-6.7%
SOX Semi-conductor Index	6.1%
VIX Volatility Index	-45%

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 14, 2021 9:00 AM	$5,000	Cdn		
Banks	Rate	Buy USD	Cost	% Difference from Spot Rate
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.2125	$4,124	$(1)	0.0%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.2251	$4,081	$(44)	-1.1%
Raymond James	1.2280	$4,072	$(53)	-1.3%
Royal Bank	1.2389	$4,036	$(89)	-2.2%
Scotia	1.2531	$3,990	$(135)	-3.4%
TD	1.2480	$4,006	$(119)	-3.0%
Canadian Snowbird	1.2393	$4,035	$(91)	-2.2%

The $300 Mother's Day dinner I had to make myself…

Mothers have one of the most crucial jobs in the world, so it is important to acknowledge the work they do at least once per year and at best every chance you get. How you do it is up to you. Flowers, a card, breakfast in bed, a nice dinner (a new house if you are a Toronto Raptor's Basketball player: classy Pascal) …or perhaps some combination of each of these. For the 2021 edition of Mother's Day, I opted for a card and a nice steak dinner. The card was easily sourced and funded, and the dinner, well let's just say it was easily sourced. You see, I happen to live down the street from a Butcher shop that is well known in the east end for offering carnivores some of the finest cuts of meat they can sink their teeth into. The Mother's in my life appreciate a nice steak every now and again, so I thought I would "splurge" a bit. After all Moms are worth it!

The day I didn't really need caffeine…

I obviously work for an established and well capitalized asset management firm. But I was raised by a Canada Revenue Agency auditor and a Banker, so tracking my own personal bottom line is something I have been doing since 1987. Still, when it comes to celebrating those important to me, I tend to open the spigot a bit wider. The thing is, after leaving the Butcher Shop, I was left with the feeling that the spigot was cranked open and left on for days. No need for my customary mid-afternoon jolt of espresso on May 9th. Four pieces of admittedly succulent sirloin, a few jumbo shrimp (the King of all oxymorons) a bottle of steak-aficionado seasoning and some dessert came to within pennies of $300. Just let that marinate for a moment: $300 for *one* dinner, that *I* had to cook *myself* and which disappeared in just under an hour. It was certainly delicious, but I felt like my wallet had been tenderized, with a beef hammer. If anyone deserves to be spoiled, it's Mom.

But if anyone deserves to be labelled with spoiling financial markets, particularly our ability to notice the approach of the harbinger of inflation, it's the worlds major central banks.

One of the most common topics of discussion here at MacNicol & Associates Asset Management this year has been inflation. We are increasingly concerned by it, and increasingly perplexed by how unconcerned many central banks are. Unlike our central bank colleagues, our position on inflation has shifted from thinking about inflation to worrying about inflation as recently as this past March. If times have shifted and inflation truly is a problem, then such a shift has major implications for interest rates, currencies, asset prices and portfolio positioning. Out of an abundance of caution we began the process of adjusting client portfolios earlier in 2021 and we think being proactive will pay off in the third and four quarter.

In a recent report by the International Monetary Fund, the IMF concluded that how financial asset prices are impacted by inflation depends largely on the *reason* for the increase in rates.

[The IMF was founded in 1944 and currently has 190 member countries that it can lend up to a trillion dollars to.]

When interest rates go up because of robust growth, especially in the developed world, economies globally tend to experience stronger capital inflows and higher rates. On the other hand, when inflation, especially in the developed world, causes interest rates to "jolt" higher, the net impact is generally viewed as disadvantageous to financial assets. Unexpected changes to a monetary policy narrative alone – especially a change to a more Hawkish tone mostly by the US Fed – are bad for asset prices globally and especially bad in emerging markets. But Canadians can see and feel the impact of US monetary policy too. The Bank of Canada seems comparatively parsimonious compared to its US counterpart. And look what that's done to the difference between yields on our respective nation's treasury securities. Small wonder the Loonie is now well over $0.80.

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Although we view the likelihood of the US Fed suddenly becoming Hawkish on inflation as low, we think the risk of the US Fed having to "catch up" to inflation as possible. For now, the Fed is dovish. In Jerome Powell's latest press conference, the question about whether the Fed was behind the curve or in danger of becoming behind the curve was answered by Mr. Powell explaining what the economy was unable to do for quite some time. Since inflation had run so persistently *below* the Fed's 2% target there was little risk in allowing inflation to temporarily run above the Fed's 2% target. Mr. Powell went on to suggest that the Fed would need to see substantial progress in the recovery and in inflation itself before considering whether to raise rates. Isn't nearly $300 Canadian dollars for a few slabs of USDA prime sirloin substantial enough?

[Jerome Powell is not thinking about raising interest rates, in fact, he's not even thinking about thinking about raising interest rates.]

Mr. Powell's comments are as always, very lucid and well thought out. Yet, at the same time, they suggest he is unaware of the world around him. The US dollar index, a more global view of the US dollar against a basket of its main trading partners, hasn't looked good since after COVID landed. It is as though the Fed resented the US dollars status as the global reserve currency and attempted to ignore the flight-to-quality in 2020.

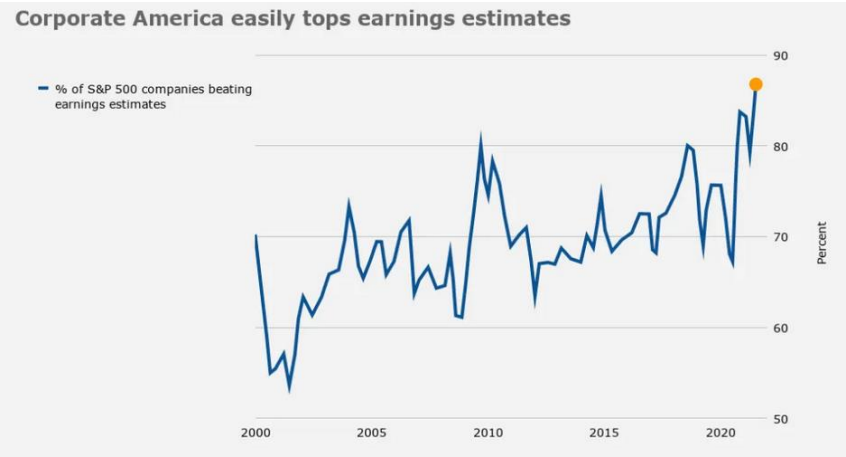
[I have no idea what currencies do daily, but the recent skid in the US dollar index has been on is hard not to notice. Source: CNBC.]

Investors therefore are left wondering whether the Fed is in a state of oblivion or just ignorant, and it's making the job of deciphering whether bad news is good news a kind of heads I win, tails you lose narrative when it comes to the interplay between US economic data and stock prices.

Stocks are a kinder, gentler placed when monetary policy is loose and rates are low: corporations can buy back shares in container ships like the one that clogged the Suez Canal and even last week's substantial US jobs miss is now seen as allaying fears of an "early" start to taper talk from the Fed. Looser policy is supportive of equities but detrimental to the dollar and despite our concern about valuations and our big concern about inflation, equity gains could extend through out the Summer maintaining the inverse correlation between most US stocks and the greenback. Then again, they might not…

[NO these aren't two of our Portfolio Managers…and NO we never put all of your eggs onto one Scooter.]

The one largest risk as we see it (apart from runaway inflation obviously) is the "no fear" mentality among investors. Though when it comes to corporate earnings it is hard not to brush off feelings of glee. According to Goldman Sachs, well over 80% of companies in the S&P500 index reported better than expected top line revenue growth.



[Earnings season was a good season but will beating expectations be so "easy" in an inflationary environment.]

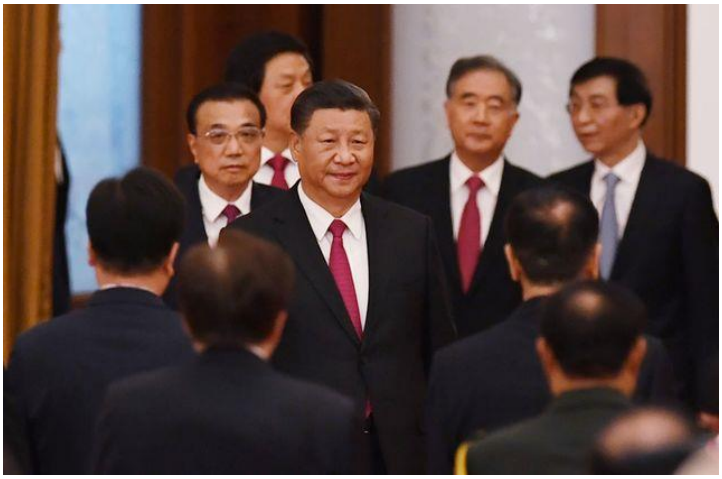
Weaker data such as the recent US payrolls miss undermines the recovery narrative and functions as an excuse for the Fed to keep their own monetary spigots open and in the process weigh further on the US dollar, bolster big-cap tech and put the Bank of Canada in a position where it might have to talk down the Loonie. Causing inflation, aiding and abetting inflation or willful omission of the signs of inflation; reasons to never put all your eggs in one basket [or Scooter].

I appreciate not just my Mother but all Mothers. But I do not appreciate having to pay $300 for a meal that I had to prepare myself. Financial markets certainly appreciate the support. Just like when you frequent the Butcher Shop a little too often, you reach a point where a little problem becomes a big problem. Could we be heading to a place where next year's Mother's Day dinner costs an even thousand dollars for more surf and turf? I know that sounds ridiculous. But think about how ridiculous this article would have sounded just 24 months ago. Perhaps it is time to tighten up those spigots I told you about earlier. They say it is best not to "fight the Fed"… don't worry we won't…but we will certainly attempt to position our investor portfolio for inflationary pressures…and that's our way of getting the Fed to help pick up the tab.

The MacNicol Investment Team

Distressed Autocrats…

China's economic rebound from the depths of COVID has been impressive. But things are beginning to look a bit distressed. The benefit of a command economy is that a lockdown is a lockdown. The drawback of a command economy is when the government tells lenders to make loans and they do.



[President Xi was said to have told President Biden recently that autocracy is superior to democracy. But is it sustainable?]

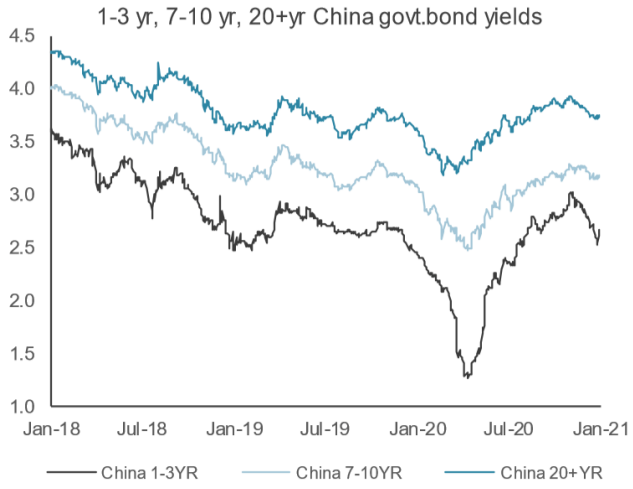
Sustainability and debt overhang don't go hand in hand…oh and let me tell you about a firm called Huarong.

[PricewaterhouseCoopers recons that Chinese Banks and Asset Managers hold about $1.5 trillion in distressed debt at the end of 2020, which is a lot, especially if the economic recovery does not continue to go exactly as commanded.]

China Huarong Asset Management said it will miss an April 30 deadline to file its 2020 earnings results as auditors need more time to prepare financials (this is already the 2nd postponement?) not exactly the sort of thing investors like to hear. Huarong, one of China's biggest distressed asset management firms, had first planned to release results on March 31 but delayed that announcement, which led to a suspension in trade of its shares and a selloff in its bonds. Huarong could release earnings as soon as next month but we'll believe them when we see them. The Hong Kong stock exchange requires companies to file earnings results by March 31 and publish their annual report by April 30. Huarong is one of four entities created in the 1990s to buy nonperforming loans from government-owned banks. Huarong expanded into banking, insurance, real estate, and other fields later and sustained injuries from failed investments and dubious leadership. Former chairman, Lai Xiaomin, was executed in January for bribery and corruption. Concerns that restructuring Huarong's debt could lead to a possible wash out in the world's second-biggest bond market are no joke and have weighed on yuan debt markets. The China Banking and Insurance Regulatory Commission, attempted to reassure the market that things weren't so bad, but the situation at Huarong certainly seems acute. Huarong, which is saddled with more than $40 billion in local and offshore debt, is the latest drama in a lengthy soap opera of sketchy and shadow banking practices. Given the size and condition of Huarong's balance sheet this situation will have to be handled carefully. Perhaps more importantly is global perception of how Beijing handles the mess at Huarong. After all, the government said to make loans. We cannot envision Beijing being eager to add a debt crisis at a state-linked debt manager to a growing list of problems that currently includes international ire over what's been formally declared genocide in Xinjiang, rumors that President Xi may give Taiwan the "Hong Kong treatment" and deteriorating relations with Washington.

Oh, and by the way, their economy is stalling out…

China's rebound from COVID last year has been impressive indeed but the rate of Chinese economic growth, is plateauing. The Citigroup Chinese Economic Surprise Index for example highlights that agents are less optimistic about the real Chinese economy than indicated by data releases. Chinese bond yields signal sluggishness in the recovery.



[The military got China out of its COVID mess 13 months ago but a massive debt overhang, hard line foreign policies and slowing economic momentum could prevent China from "commanding" its way to prosperity.]

Unlike previous economic challenges the latest one is not being driven by a cyclical downturn in a specific industry. It is being driven by the government. A government that orders lending, and then sanctions defaults while at the same time instituting rules against speculation in areas like real estate. China's "Three Red Lines" policy on certain debt ratios for 12 major property developers led to creative work arounds that might not fail today but instead fail more spectacularly tomorrow.

[Against the backdrop of a strong recovery, China focused on tightening up liquidity and on reigning in moral hazard.]

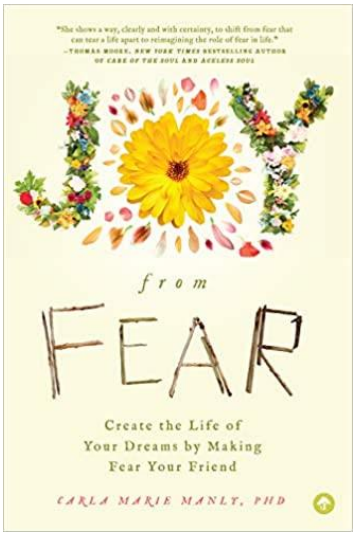
Traditionally, implicit guarantees from Beijing on State Own Enterprises caused a build of credit in China's financial system. The government now wants debt differentiated based on credit quality, an interesting time to choose to embark on a distressed debt cycle. Being forced into a distressed debt cycle is one thing, choosing to originate such a cycle from within is another. If China's economy recovery doesn't quickly resume its post COVID upward slope, the autocrats in Beijing will likely be under some considerable distress of their own.

The MacNicol Investment Team

Behavioural Investing

When too good is too bad

Carla Marie Manly, is a California-based clinical psychologist and author of *Joy from Fear*. Dr. Manly holds no formal training in economics or investing, but after having learned more about her work, I wonder whether investors would be better served reading *Joy* than the epic *Reminiscences of a Stock Operator*. When the NASDAQ stock market dipped during the past few trading sessions, many investors were spooked even though the index did a great job of clawing its way out of the depths of COVID. The odd thing is that the NASDAQs slight downward blip amounted to just a few basis points to an index that has done remarkably well over the past year. When you accomplish something amazing like earning a promotion, finishing a year-long passion project, or finally paying off your credit card you'd think a burst of happiness would be followed by relief. Maybe even a dash of relaxation. Right? Well according to Dr. Manly that's simply not the case for everyone. It's actually not unusual to feel more anxious following good news or hard-earned success than you do when you're putting out fires or working hard.



[Does the stock market going down make you anxious? Put down that Wall Street Journal and pick up a copy of Joy from Fear.]

Essentially what happens is that the feelings of elation and joy fade in the aftermath of a substantial achievement. This kind of cognitive dissonance results in one being vulnerable to anxious thoughts thus making anything other than a significant achievement a bit of a let down.

Stock markets don't always go up. Occasionally they go down, and once in a while they go down quite a lot. Working with a registered Portfolio Manager like MacNicol & Associates Asset Management can not only lead to good financial health through our carefully selected and thoughtfully combined portfolios of conventional and alternative assets, it can also lead to good mental health. If you're feeling uneasy about a dip in the stock market and worried it could be the start of something more than just a blip on the radar, give us a call. We're always glad to speak with clients and share our ideas about the financial markets with you. Sometimes just the discussion alone can make you feel a lot better about your finances even if there might be trouble ahead. Remember we adapt to market conditions and to your individual situation within it.

You should definitely read *Reminiscences of a Stock Operator*; it is an investment classic just as relevant today as when it was first written in 1923. But you should also read Dr. Manly's book *Joy from Fear*, if anything it just might be even more relevant after an extended run of market bullishness.

The MacNicol Investment Team

Firm News

Edward Biding is the newest member of the team, bringing over 20 years of experience in the finance industry. Experienced in operations, Edward is responsible for providing support to the Portfolio Managers and clients.

Edward started his career at a large Canadian bank and worked in several large and boutique investments firms on Bay Street. He is a graduate of Ryerson University. Edward currently lives in Toronto and on his spare time likes spending time with his large family; skiing and snowboarding in the winter; camping and fishing in the summer; and traveling to distant places with his wife.

MacNicol & Associates Asset Management Inc.