December 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.

"This mountain, I thought, was like education: the higher you climbed, the further you could see"

- Christiaan Neethling Barnard

The Numbers:

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Index:		**2021 YTD:**
S&P/TSX:		18.5%
NASDAQ:		20.6%
Dow Jones:		12.7%
S&P500:		21.6%
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	0.04%	0.06%
5-Year Bond:	1.43%	1.24%
10-Year Bond:	1.53%	1.45%
30-Year Bond:	1.80%	1.76%

Economic Data:

- US Non-farm payroll report badly misses consensus estimates
- Crude sharply lower in November to $66
- Globally stocks were mainly lower in November
- Broad commodity indices down double digits in November
- Gold & Silver largely flat in November
- Inflation materially higher in Canada and the United States even when excluding food and energy prices

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	35	34
P/B: Price-to-Book	4.8	3.5
P/S: Price-to-Sales	3.3	2.3
Yield: Dividend Yield	1.3%	1.9%

2021 Calendar Year Performance, by Sector: Nov 30th, 2021

S&P/TSX Composite	18.5%
NASDAQ	20.6%
Dow Jones Industrials	12.7%
S&P 500	21.6%
Russel 2000 (Small Caps)	11.3%
MSCI EAFE	3.5%
Crude Oil Spot (WTI)	37.1%
Gold Bullion ($US/Troy Ounce)	-6.2%
SOX Semi-conductor Index	39.8%
VIX Volatility Index	5.8%

Source: Canaccord Genuity Capital Markets & Thomson Reuters

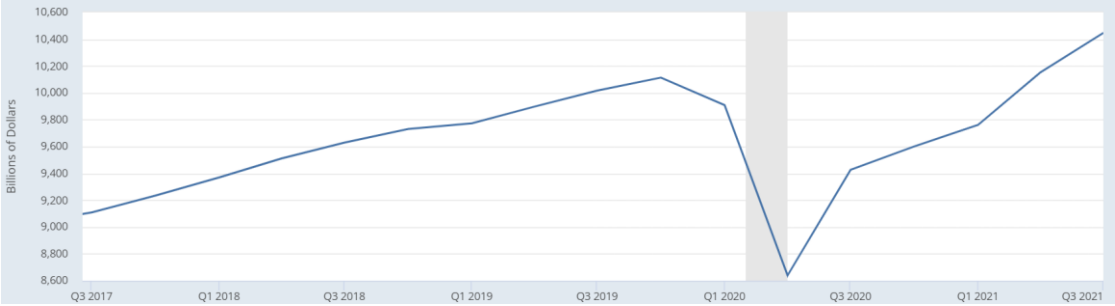
Foreign Exchange - FX

As of Dec 9, 2021 11:00 AM	$ 5,000	Cdn		
Banks	Rate	**Buy USD**	**Cost**	**% Difference from Spot Rate**
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.2708	$ 3,935	$ (0)	0.0%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.2831	$ 3,897	$ (38)	-1.0%
Raymond James	1.2850	$ 3,891	$ (44)	-1.1%
Royal Bank	1.2940	$ 3,864	$ (71)	-1.8%
Scotia	1.3037	$ 3,835	$ (100)	-2.6%
TD	1.3058	$ 3,829	$ (106)	-2.8%
Canadian Snowbird	1.2843	$ 3,893	$ (42)	-1.1%
Spot Rate	1.2707	$ 3,935	$ -	0.0%

"Small o…"

Omicron is the 15th letter of the Greek alphabet and the latest variant of COVID 19. Initial reports of omicron hit the press right around the US Thanksgiving which meant the world's largest capital market was closed at the same time as a market headwind was beginning to spread. The ensuing market tumult was unpleasant but not much more than that. Still Omicron's virulence and ability to outsmart vaccines are two major question marks at this time. Officials with the World Health Organization, drug company executives and prominent economists differ in their views on how dangerous the new variant is and what it might do to the economic recovery. But investment banks reckon that Omicron will – at the very least – shave off a good chunk of next year's GDP forecast. Indeed, cuts to GDP forecasts are already beginning to make their way around Bay and Wall Street but we can't help but feel this is more of an attempt to preserve vanity rather than investment capital.

Quantifying Omicron is difficult to do and requires some judgement rather than a calculator. Assigning numerical probabilities to something really only works when the input data you have is clean and free from corruption. As a result, we believe that it would be helpful to consider an array of possible Omicron scenarios ranging from no impact whatsoever to more dire scenarios about the end of the world as we know it. Omicron's rapid spread through countries, like South Africa, probably means that we cannot place Omicron in the "nonevent" pile. But the good news is that preliminary data and expert medical opinions do *not* point to a sharp deterioration in vaccine efficacy when it comes to Omicron and severe hospitalizations are still dominated by the Delta variant. So, whereas a benign scenario now seems overly optimistic, a situation in which the global economy grinds to a screeching halt may be overly pessimistic. Delta provides us with the best proxy we have as to what Omicron may do to in the future. Consumer spending declined but remained positive in most areas of the services sector even as the Delta variant made its way around the world.



[The Delta variant slowed the growth of personal consumption expenditures on services, but people were still spending.]

Delta did impact global supply chains but only to the extent that it irritated existing shortages arising from spillovers in Southeast Asia. With increased rates of vaccination and a generally more "COVID smart" world today than a year ago, the incremental adverse impact of Omicron on global supply chains is likely to be moderate at the very worst. A more challenging piece of the Omicron puzzle is the impact it may have on labor force normalization. One issue we shinned some light on previously is that of the rising number of people that are transitioning into the segment of the labor force known as the *long-term* unemployed. It is far too early to say whether Omicron will exacerbate this problem but hiring is very likely to slow appreciably in industries such as leisure and hospitality despite a robust overall demand for workers.

[November's non-farm payroll report wasn't even close to consensus estimates but the economy does have things for people to do.]

Omicron is known as "*small* o" in Greek, but it is far from a small problem for health care professionals and investors alike. In our minds though, it is too early to conclude whether this latest COVID variant will have a small impact on financial markets or one that is more capitalized. The MacNicol Investment Team believes that Omicron will reduce the strength of the ongoing economic recovery but not derail it completely. Delayed re-openings and temporary closures along with some potential new barriers to the supply of goods will likely impact consumption but not result in outright financial market chaos. Regardless of how small the impact from Omicron may be, our team will operate in a vigilant manner to ensure your capital is safe guarded.

The MacNicol Investment Team

***Off* duty Portfolio Managers…**

I am the fellow in my family who fields questions about financial markets and the economy. I really don't mind answering my family's questions but occasionally it can be a bit annoying. No one becomes a Portfolio Manager unless they have a genuine interest in financial markets, but everyone needs a break every now and again, and for yours truly long weekends in the summer along with holidays are such times. But don't worry, I never begrudgingly bellow out a response when the family wants my opinion. In fact, I take it in stride, avoid highlighting the actual problem and check in with a big friend of mine weekly to ensure my response has a reasonable and adequate basis. Now when members of my immediate family who don't even know what a Central Bank is ask me what I think about what *"Mr. Powell"* said, I know the problem is not in fact what Mr. Powell *said*. Instead, the actual problem is the media's attempt to coax Mr. Powell into acknowledging that my family and others like it should take cover. For more on how I separate issues into big problems and little ones, I defer back to my big friend: the bond market.

At roughly four times the size of the stock market the bond market is a much bigger barometer of pressure in the financial system. And right now, the pressure is on Mr. *Jerome* Powell, who Chairs the US Federal Reserve (America's Central Bank also known as "The Fed") to come clean with why he is beginning to sound an awful lot like Alan Greenspan's predecessor Paul Volcker.

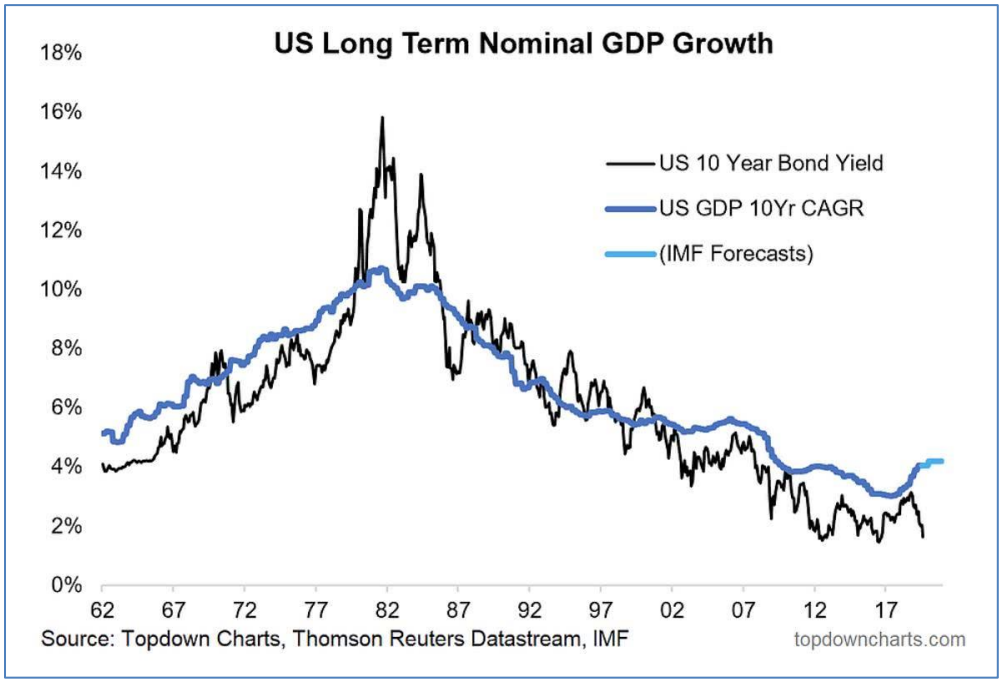
Mr. Powell is a centrist (neither Hawk nor Dove). And as a centrist, Mr. Powell's narrative on inflation has been and should continue to be that it is transitory. But his messaging of late hasn't been all that convincing and the bond market is failing to obey his lead to higher interest rates. People who believe central banks physically print money are getting mixed message as well, and accumulating debt at ever higher rates.

["Transitory was so 2020".]

Mr. Powell told the U.S. House Financial Services Committee that the spiteful qualifier "transitory" should be removed as a descriptor of inflation. Last month, we mentioned that the Fed has pledged to go on a bond buying diet reducing its monthly binge by $15 billion per month but by no means ending the hedonism prematurely. If all goes according to plan, the Fed will add a further $420 billion in bonds to its balance sheet which currently sits at $8.6 Trillion and begin raising the target for its trend setting federal funds rate. I suppose the real surprise was that anyone was surprised at all – apart from members of my family obviously. Senior members of the Fed have been calling for a more sobering approach to bond buying for a little while.

[Richard Clarida is Vice Chair of the Fed. Clarida is centrist as well, but he would not consider a repeat of 2021 as "policy success".]

Politicians got in on the action as well. Congressional leaders lobbed questions about soaring prices at Mr. Powell with constituents in most states expressing grave concerns about a repeat of 2021 next year. Our Investment Team, beyond all else, notes that the gap between GDP growth rates and yields on 10-year treasuries has broaden out to extreme levels. Ordinarily increases in nominal GDP and long-term interest rates track each other rather closely, but this is not happening today.



These days, GDP growth rates are pulling away from yields on the US 10-year note all while inflation is well above target. The growth is a result of massive and successive rounds of fiscal injections, starting with the Cares Act in 2020 and continuing with the American Rescue Plan, but not necessarily a healthy and robust economy. Central Bankers might *say* they intend to raise interest rates several times in 2022 but we will believe it when we see it. For now, we are skeptical about traditional approaches to fixed income and the less long yields move up, the more the Fed would have to lift short-term rates to rein in inflation. The Fed has been in this situation before. Back in the early 2000s the Fed raised rates several times between 2004 and 2006 however long-term yields failed to take their que which led to the housing bubble and global financial crisis.

It will take more to raise interest rates and close the chapter on accommodative monetary policy than interviews with the media or a bunch of politicians. And it will take many more financial questions during off hours to make me dislike my family or profession. But it will take much more to solve the enigma that now faces fixed income investors, which is that the very instrument the Fed began using as a solution to a problem (the federal funds) has now become part of the problem.

The MacNicol Investment Team

Investment Hypochondria…

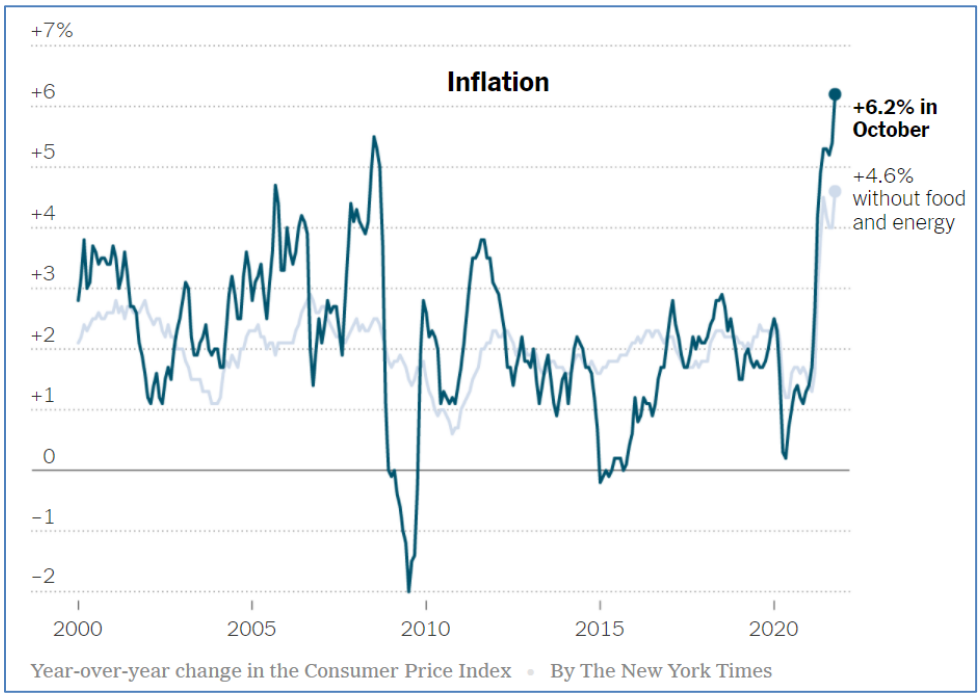
People with hypochondria have an unfounded fear of serious medical conditions or fear they are at risk of becoming seriously ill when no predisposition exists. Hypochondriacs may misinterpret normal body functions as signs of illness even after medical tests confirm that all is well under the hood. Perhaps more unfortunate is the fact that people with hypochondriasis can remain preoccupied with the idea that they are sick for extended periods of time. Their persistent health worries can interfere with their relationships, careers and life.

People with *investment* hypochondria often cannot control how they feel about financial markets. They behave in an irrational way by constantly worrying that financial markets are ill and poised for a catastrophic decline at any moment. Unfortunately, this results in chronic under investment, which can be a real problem. In an inflationary environment, constantly delaying an investment decision can be detrimental to your long-term financial health. If you consider an inflation rate of just 3%, the money you have today will have lost 30% of its purchasing power in just one decade should you defer making an investment decision for that long.

[Politicians playing the blame game, that's how you know inflation is an issue.]

Regardless of your political ideology, recent readings on inflation were very hard to downplay. The Consumer Price Index (CPI) in Canada rose by 4.7% on a year-over-year basis to October, the largest gain since February 2003.

Excluding energy, Canadian CPI rose 3.3% year over year, matching the increase in September. Prices in all eight major components of CPI measured by Stats Canada rose on a year-over-year basis in October. America's inflation figures were even more eye watering: US consumer prices jumped 6.2% in October, the biggest inflation surge in more than 30 years.



[Even if you don't eat or drive, your life just got a whole lot more expensive.]

Worrying about the next variant, the next monetary foible or the next financial crisis are completely acceptable reactions for investors to have. But such feelings should never derail a long-term investment plan that will help you tackle inflation in the coming years. At MacNicol & Associates Asset Management, we have built our entire business on prudently applying a time-test, disciplined process that serves your greater financial good.

Cognitive Behavioral Therapy (CBT), behavioral stress management and psychotropic medications are all used to combat hypochondria. An independent approach and objective financial advice are what we use to combat the fear of worrying about what might be brewing in every nook and cranny of the market. By helping you take the "sting" away from worrying about the market's little problems, we can focus your attention on things like inflation, which we feel are far more important when it comes to overall financial health.

Just give us a call: (416) 367-3040 or send us a note to info@macnicolasset.com

The MacNicol Investment Team

Firm Wide News

As the year winds down, we would like to thank everyone who has contributed to making 2021 a year to remember. We appreciate your support and interest in MacNicol & Associates. Here's to 2022 and all that it will bring.

Here's hoping everyone has a Merry Christmas, Happy Hanukkah and a Happy New Year!

The MacNicol Team