June 2024

The Quarterly

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

"Don't try to buy at the bottom and sell at the top. It can't be done except by liars."

- Bernard Baruch

The Numbers:

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Index:		**2024 YTD:**
S&P/TSX:		4.75%
NASDAQ:		20.1%
Dow Jones:		4.36%
S&P500:		15.5%
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	4.60%	5.34%
5-Year Bond:	3.37%	4.12%
10-Year Bond:	3.42%	4.21%
30-Year Bond:	3.40%	4.44%

Economic Data:

- Global equities higher in the 1st half of 2024
- Commodities higher in the 1st half of 2024
- BITCOIN and Ether up roughly 50% during the 1st half of 2024, Solana ranking increases
- US Inflation moderates
- Political deadlock in parts of Europe

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	29.4	24
P/B: Price-to-Book	5.1	4.6
P/S: Price-to-Sales	3.0	2.6
Yield: Dividend Yield	1.3%	1.5%

2024 Calendar Year: June 30th, 2024

S&P/TSX Composite	4.75%
NASDAQ	20.1%
Dow Jones Industrials	4.36%
S&P 500	15.5%
Russel 2000 (Small Caps)	-2.6%
MSCI ACWI ex. USA	1.60%
Crude Oil Spot (WTI)	19.7%
Gold Bullion ($US/Troy Ounce)	9.38%
SOX Semiconductor Index	15.8%
VIX Volatility Index	-37.2%

Source: Canaccord Genuity Capital Markets & Thomson Reuters

Foreign Exchange - FX

As of July 16, 2024 1:00 PM	$5,000	Cdn		
Banks	**Rate**	**Buy USD**	**Cost**	**% Difference from Spot Rate**
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.3722	$3,644	$(11)	-0.3%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.4045	$3,560	$(95)	-2.7%
Raymond James	1.3799	$3,623	$(31)	-0.9%
Royal Bank	1.3968	$3,580	$(75)	-2.1%
Scotia	1.4042	$3,561	$(94)	-2.6%
TD	1.3928	$3,590	$(65)	-1.8%
Canadian Snowbird	1.3802	$3,623	$(32)	-0.9%

Cut the bull…then…get out of its way…

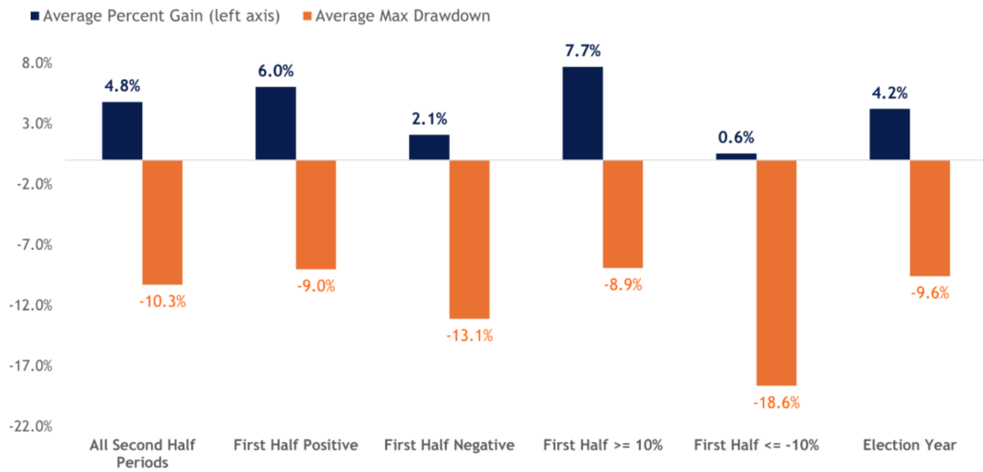
James Royal, Ph.D., recently compiled a list of the best performing stocks thus far in 2024. We certainly hope the name of the company that makes graphics processing units for the artificial intelligence industry is one that just rolls off your tongue by this point. The other names on Royal's list, quite frankly, are not ones we would expect you to know. With July officially marking the beginning of the second half of the year, we felt it would be helpful to share Royal's list with you while at the same time pointing out the Bernard Baruch quote festooned to the beginning of this edition of *The Quarterly*. Baruch was an American financial wizard who, after mopping the floor of the New York Stock Exchange with lesser investors, took his winnings to Washington where he started managing some *real* money. Baruch impressed President Woodrow Wilson so much that he was appointed the head of America's economic mobilization fund in World War I as chairman of the War Industries Board.

Company and ticker symbol	Performance in 2024
Super Micro Computer (SMCI)	188.2%
Nvidia (NVDA)	149.5%
Vistra (VST)	123.2%
Constellation Energy (CEG)	71.3%
General Electric (GE)	55.9%
Eli Lilly (LLY)	55.3%
Micron (MU)	54.1%
NRG Energy (NRG)	50.6%
CrowdStrike (CRWD)	50.1%
Arista Networks (ANET)	48.8%

We will come back to Baruch in a moment. For the time being let's take a moment to absorb Royal's list. Absorb because returns [well] into the double digits are uncommon in stocks, never mind triple digits. And it is returns such as these that keep stock indices – especially those weighted by market capitalization – going up. For example, the MSCI World Index closed off the quarter with its 5th consecutive weekly gain as we began working on this commentary for you. Earlier this year, Japan's NIKKEI 225 index finally reached a new all-time high [of 42,200] and in so doing eclipsed a level last reached in late 1989. And that graphics processing unit company? Well, its own valuation hit 2.5x the GDP…of Poland.

Indeed, the first half of 2024 offers many different investment stories to many different investors. But by far the main story we believe equity investors need to concentrate on is the one being told by the granddaddy of them all the S&P500, which was up by 15.5% in the first half. We thought it would be helpful to share with you some of the things we have observed when it comes to US stocks and what they could mean for US equity investors during the second half of the year. We will also point out what we believe many investors could potentially be missing. For now, let's begin with the question on every investor's mind: **are stocks overvalued**? So, the way you need to think about this is as follows: the average ratio of price-to-earnings for the S&P500 since 1950 has been about 14x forward earnings. Next, you need to say to yourself the ratio of price-to-earnings for shares of the ten *biggest* stocks in the entire S&P500 is about 31x forward earnings. For your information, I have included Finviz's typically excellent "heat map" of the S&P500 below so that you can simply just look to see which companies are the biggest of the big, if you can see the stock ticker symbol without squinting its big.

Then, you need to say to yourself the ratio of price-to-earnings for shares of the remaining 490 companies in the S&P500 is *18x* forward earnings. While technically overvalued, 18x is hardly excessively overvalued and fundamentally more sensible than 31x. Therefore, observation #1 is that *stocks* are not overvalued, *some* stocks are overvalued. So, to Baruch's quote: is now the right **time** to get into stocks? To help us here, study the table of investment returns below [Source: LPL Financial Group.]



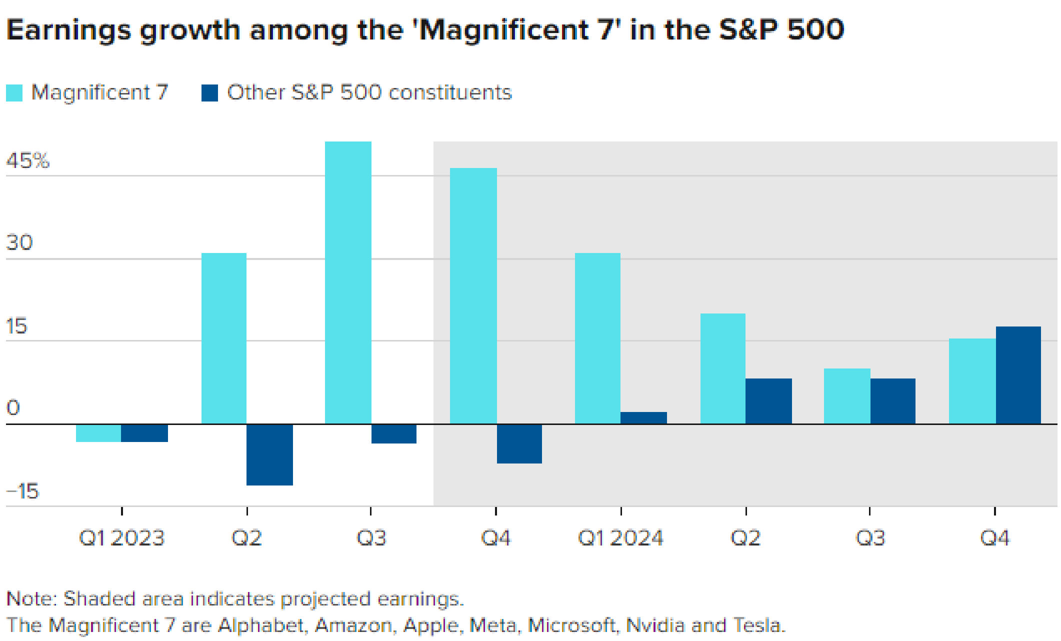
Though tempting to delay making an investment following a strong first half [again the S&P500 was up 15.5%] the data presented by LPL almost diametrically opposed sitting on the sidelines. On average, the second half of the year tends to be positive for the S&P500 no matter the first half's performance with the index registering a positive return of 4.8%. If the first half of the year is positive, second half returns were even higher clocking in at 6%. Since the first half of 2024 was not negative, we skip the S&P500's historical second half of the year performance and jump to circumstances where the S&P500 was positive during the first half by over 10%. In cases of double digit first half performance, the S&P500 averaged 7.7% during the second half. Finally, election years tend to be positive for the S&P500 with the index registering a 4.2% rate of return during the second half regardless of first half performance. And just in case you are still uncertain: the S&P500 has never lost money for investors during the second half of the year in cases where first half performance was more than 10%. At this juncture, we remind you that this year's first half performance for the index was **almost 15%**. Therefore, observation #2 is that although history doesn't repeat itself, it often rhymes [Twain] and in situations where the S&P500 registers a double digit first half return…the rhyming is catchy.

But what about a steep correction?

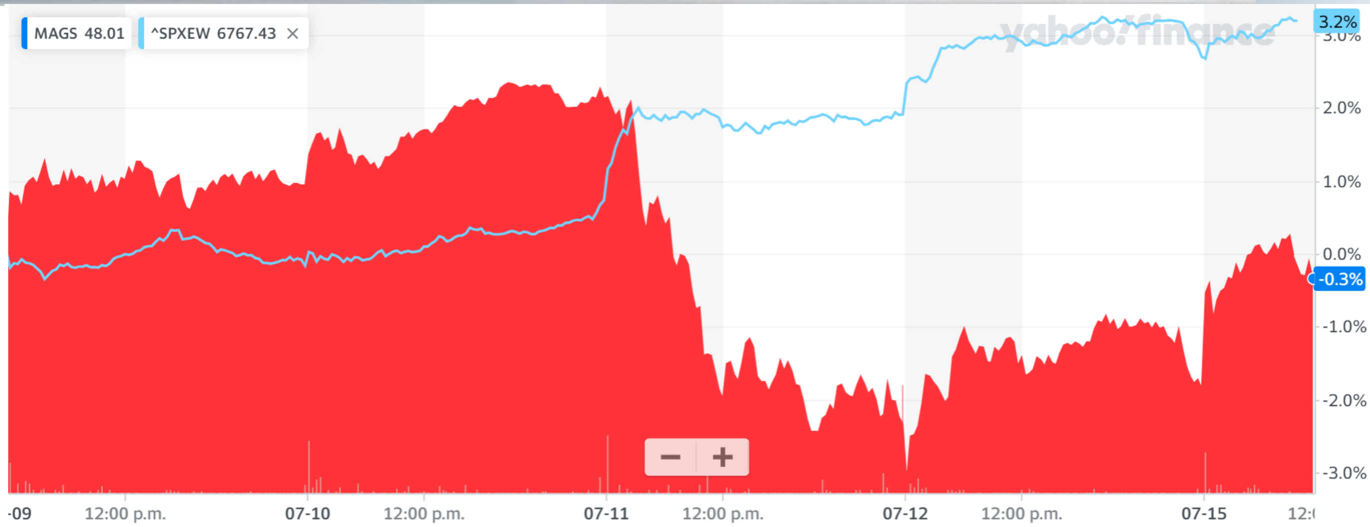
The simple reality of equities is that they can be volatile and LPLs analysis speaks directly to this point: in all post WW2 second half periods, the average maximum drawdown for the S&P500 was just over 10%. Drawdowns in years when the first half was positive or positive by more than 10% were less severe than in years when the first half was not as strong, registering declines from the peak of roughly 9% each. US Election years saw drawdowns average 9.6%. Observation #3 is that as an equity investor, you should bank on a period of weakness at some point during the second half of 2024 with our own investors here at MacNicol & Associates Asset Management likely sparred most of the carnage due to our more conservative approach to investing in general, and our flexibility to combined public and private market investments within client portfolios. In other words: there will be a minor correction, your friends and business partners will feel it more than you will and lastly, the historical precedent for a recovery is statistically very strong so get whatever "dry powder" [i.e. cash] you have laying around ready for action later in the year.

Just don't be passive about it…

Take the escalator down and the stairs back up. Broader market momentum has of course been highly concentrated in the Magnificent 7 or the Terrific 10 or the whatever-the-media-calls-the-market-leaders this week. And there is of course a very good reason for this: the biggest stocks in the S&P500 have quite simply produced the best earnings growth to date…but could that be about to change?



LPL and Bloomberg figure that earnings growth for the 493 companies that are not part of the Magnificent 7 could begin normalizing later in the year. Observations #4 and #5 then as follows: an active approach to equity selection is [highly] recommended at this point given the valuation gap referenced earlier [i.e. 31x versus 18x] and given the wider pool of potentially attractively priced candidates below the Magnificent 7. If you only had seven stocks to pick from, well then you only have seven stocks to pick from. With a pool of over 490 stocks from which to pick from, active approaches to equity selection are more likely to unearth gems that offer the potential for earnings expansion at a price that would make your eyes water.



[In this chart we compare the performance of the Roundhill Magnificent 7 ETF versus the equally weight version of the S&P500 ETF. The year-to-date version of this chart is no comparison: the Magnificent 7 leads the way by a mile. However, in recent sessions, you have begun to observe more downside pricing in "MAGS" and more upside movement in "SPXEW". While still early in our opinion, the advice to be active and selective during the second half of 2024 stands as does the advice to remind yourself that strong corporate profit, the denominator in the Price-to-Earnings ratio only "feels" strong when the multiple you are paying for that growth is fair.]

Another aspect of the current market environment has been the underperformance of small cap stocks. Of course, much is this makes sense when one considers that smaller companies are less likely to manage persistent pricing pressures, inflation, higher rates and a global economy transitioning to a more moderate pace of growth.

Andrew Adams, technical analyst with Saut Strategy, points out the above chart to us each week. The chart [of the Russell 2000 small cap ETF] is essentially being backed into a corner out of which Andrew surmises it will "explode". But explode in which direction, higher or lower? For insight into what might be the most likely move investors need to account for the fact that thus far in 2024 many of the year's best performing stocks have been the same mega cap growth stocks that are featured on James Royal's list. Indeed, that move has been driven by the requisite bump in earnings, however gigantic technology companies aren't the only ones making money these days. For context, BMO Capital Markets suggests that earnings by smaller companies trail their larger peers by fewer than 3%, hardly a wide gap. Considerably wider though is the valuation gap that exists between shares in the biggest and smallest companies. It therefore pays to be active, and looking for growth where you can still find it at a decent price. If there is one caveat that merits mention here it is rising US treasury yields. Higher yields can pose a problem to many companies, but they can be more problematic the further down the capitalization spectrum you go, and that is especially true for start-up or quasi start-up companies who still are seeking financing solutions from the tier of the US financial system that brought us names like Silicon Valley Bank and Signature.

Assuming you are motivated to invest and tenacious at carefully reviewing individual companies rather than following the heard, you might like to consider some specific sectors such as energy and materials. You might also like to consider taking a gander at financials, yes financials. Last month's edition of *The Monthly* featured an article that fell short of being a TD Bank "hit piece" even if it really wasn't. However, financials offer investors two things that we like: attractive earnings prospects and decent valuations. Observation #6 then is the relative valuation gap and strong dividend growth prospects that the banks offer investors.

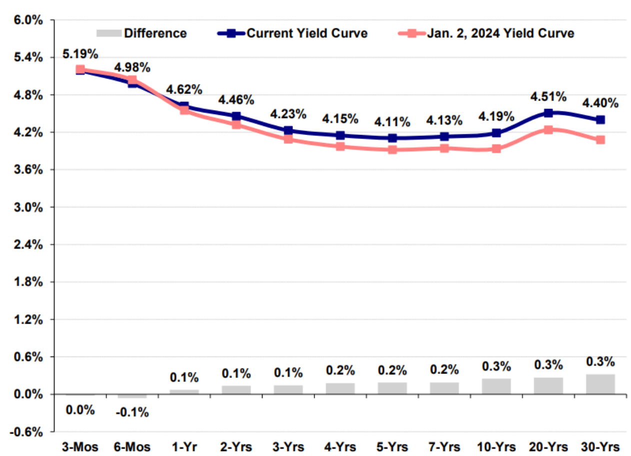
We hope that our observations [and data] encourage you to get up off the sidelines and take the proverbial Bull by the horns. A bull market is out there somewhere and whether you have us work for you or with you we are pleased by the opportunity. If there is anything that investors are missing these days it's that for whatever reason, investing just isn't a priority for a lot of people and that's just too bad. Whether it's heading up to the cottage or out with friends, we get it: investing is not top of mind for everyone. But do spend some time thinking about your financial future.

The enormous market [that no one is talking about] …

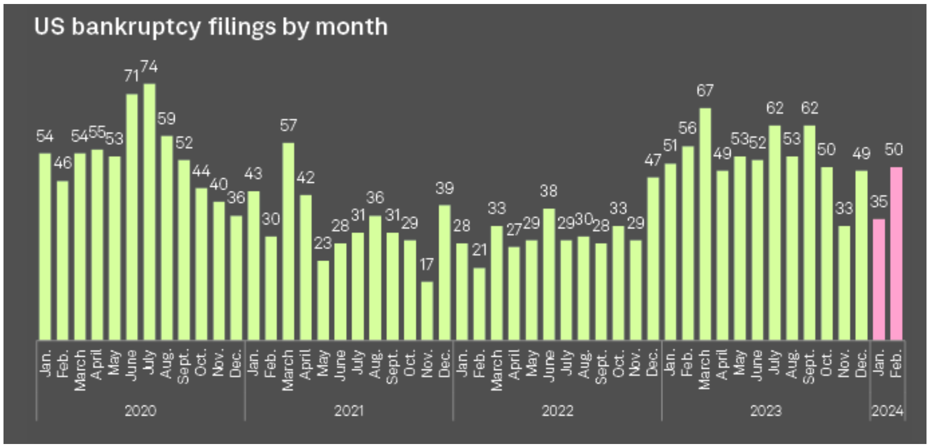
We made a very brief reference to rates in the previous article as they do in general impact financial markets. One rate, *the* rate, that tends to impact stocks the most, is the yield on the US 10-year note. While most investor attention is fixated on the Magnificent 7 [or not on investing whatsoever] one part of financial markets that we believe isn't quite getting enough attention is bonds. Naturally, following one of the quickest periods of monetary tightening, you would expect returns on fixed income securities to be bad, and given their term-structure, the further dated notes should have done the worst. A painful case in point is the US 30-year which fell by nearly 50% since this time in 2022. Strong nominal GDP growth can have a devasting impact on bond prices. They say you buy stocks to hedge against inflation and bonds to hedge against deflation. In the United States, a lack of activity, growth or progress in retail sales, a cessation of the upwards trajectory of global PMIs and most importantly of all early signs of labor market weakness suggest that the US economy's best days could be behind them. As far as how this augers for fixed income policy, we believe it bores holes into the narrative that the world no longer needs long-term bonds. But do take note, all bonds, nor all bond market term structures are created equal. We mentioned the outright gnarly campaign of the US 30-year over the last few years. Real estate investors know the US 30-year best as it is the note that provides the US mortgage market with its pricing ques. However, the MacNicol Investment Team feels confident that the short end of the term structure is easier to decipher rates are biased to the downside. But we feel the real money will be made by those investors intrepid enough to get the long end right, and that means maturities more than 10 years. For practical purposes, the iShares 20+ Year Treasury Bond ETF is our preferred method of studying longer dated bonds.

We like the iShares 20+ Year Treasury Bond ETF or “TLT” as it is known in the industry because it parcels off just maturities of sufficient length that they can unequivocally be described as long. And because the ETF is highly liquid, trading much more than comparable products from Vanguard and 100x of times more than Canadian fixed income ETFs such as XBB.TO. Long time TLT unitholders will know that taking a long position, in long bonds, has been anything but fun. But could the time for a long-term bond investment be now? Admittedly: NO. But as asset managers, we always must look well beyond our own horizon for the next investment opportunity for you. For what it’s worth: a case for the US 30-year is not one we shall table here.

US Yield Curve



We aren’t even entirely sure whether we’d make an investment in a US 10-year note at this juncture. What we are saying is that higher debt, way higher deficits, inflation and de-globalization have rapidly pushed bond yields higher. What’s more, we wish to point out that while the likelihood of a US hard landing forms no part of our base case scenario here at MacNicol & Associates Asset Management, the data would suggest that the very potential for a hard landing is perhaps under appreciated. The unit price chart of the TLT ETF [still] looks pretty bad to us however many of the data points we shared with you earlier along with things such as the lowest small business hiring plans since 2020, job openings to unemployed ratios being the lowest since August 2021, and the highest unemployment rate since January 2022 [still generationally low mind you] remind us that the world of long bonds at the very least is there watching over all of us. And when it comes to stress: the stress is there…



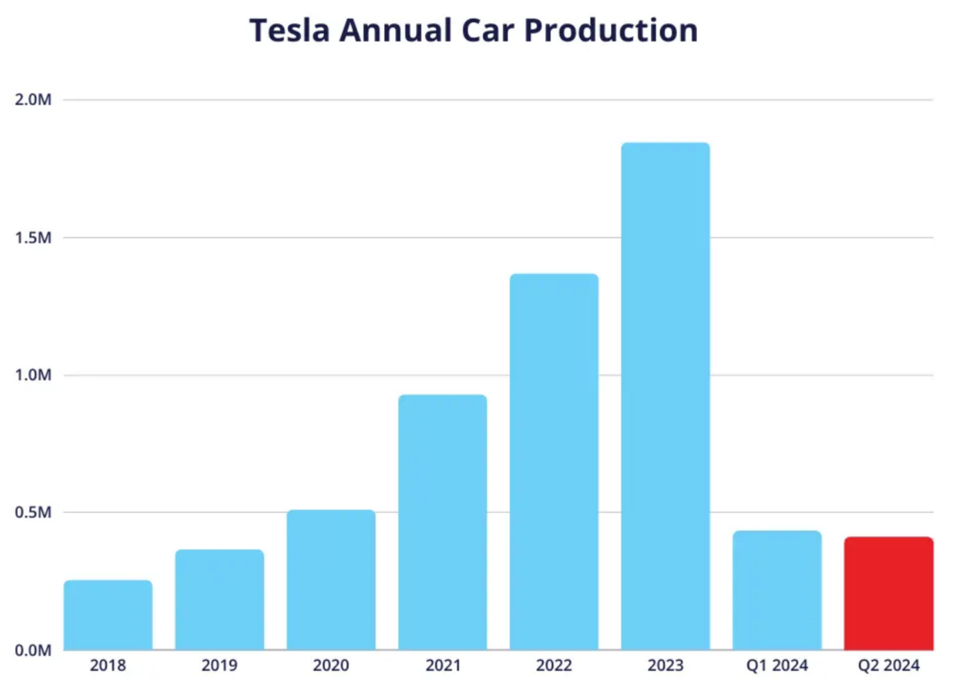
The chart at the bottom of page 8 [Source: Oleg Parashchak] tracks US bankruptcy filings by month. It is too early to draw conclusions about Parashchak's table however February of 2024 saw a notable uptick in filings that we feel may be under appreciated by investors. Prior to distributing *The Quarterly*, we checked for more current US bankruptcy filing data, but we were unable to reproduce anything material at this point. Suffice it to say, long bonds offer some of the things we like in an investment such as a fair price. But we also need a thesis that supports price appreciation or growth. Neither TLT nor long bonds in general have the sort of obvious buy signals that scream growth. However, some of the longer-term trends to consider are US government spending. The American government spent over $6 trillion during the 2023 calendar year. Statistically, the 4th quarter of a US Presidential cycle is the strongest for government spending however a big slowdown often occurs following the swearing in of a new President. Monetary policy will doubtlessly be easier in early 2025 and we believe that with tighter fiscal policy [i.e. cooling it down on the spending] US long bonds might just make an appearance at a portfolio near you. At the end of the day, long-term government bonds can be your friends if financial markets and the economy get ugly. That isn't now, and it might not even be close to now. What we can tell you now, however, is that no one is talking about long-term bonds, and so we figured we'd at the very least raise the issue.

Behavioral Investing: recency bias

The irony of us not having commented on **recency bias** recently certainly is not lost on us. In any case, recency bias is closely related to another behavioral investment pitfall: the availability heuristic[1]. **Recency bias**, as you can probably guess, causes individuals to give *more* importance to recent events or information. In investing, this bias can lead to decisions based on the latest market trends rather than carefully studying historical patterns or looking for wide variations between traditionally longer-term relationships. We can think of no better example of recency bias in the real world than the likelihood of a bear attack in Northern Ontario. Unfortunately, earlier this summer, in a remote area of Wabakimi Provincial Park, which is located 970 kilometers Northwest ***of Huntsville, Ontario***, one person sustained non-life-threatening injuries and was sent to hospital for treatment of their injuries. Despite the fact that yes indeed Ontario does have bears, and despite the fact that annually there are literally thousands of bear/human interactions in this Province, lethal bear attacks are exceedingly rare.

1 The **availability heuristic** is another bias that plays a significant role in investing decisions. Availability heuristic causes investors to rely on readily available information, often recent or extremely clear examples, when making investment decisions. In the context of investing, this bias can lead to decisions based on the latest news or recent market performance, rather than considering historical data or long-term trends as we ourselves did in the first article.

Nonetheless, assuming you own a cottage, I challenge you to go for a walk, in the woods, at night, shortly after reading this article. You can take your gun or canister of bear spray, but the fact of the matter is you won't enjoy it. And so, recency bias is just that fear, specifically what we call "FOMO" or Fear of Missing Out. Short-term market moves caused by recency bias can derail long-term results because they make it more difficult for investors to stay focused and stay on track. If bears aren't your cup of tea, consider for a moment the movement in shares of Elon Musk's company: Tesla. Tesla's revenues to the end of the first quarter of this year were down by 9% with profits off by over 50%. We have no explanation as to why Tesla stock suddenly kicked into overdrive however, we assume it has something to do with the fact that sales beat [lowered] analyst estimates, and that Mr. Musk's artificial intelligence business is similarly picking up steam.



But the problem is this: we know some of you and others you know will assume that all is well in the world of EVs and that Tesla shares will continue to surge forward when that simply is not known at this point. Tesla remains well off-peak levels [November 2021] however it is nevertheless a company whose market valuation stands at a very noticeable $800 billion.

Whether it is reading a scary story about a bear attack one full day of driving away from wherever you have your cottage or assuming that one beat is enough to signal all clear for Tesla stock, recency bias can cause you to make decisions that don't always make sense. The MacNicol Investment Team can help you avoid recency bias when it comes to your investment decisions.

The MacNicol Investment Team

Firm Wide News:

Ken Reid officially received his Chartered Investment Manager certification last month.