Investing Wisely

A Newsletter from Mike Wise

November 2023

As is our tradition, my colleague Christine and I attended the Remembrance Day service at the Military Museums. Each year the crowd seems to get larger and larger, and it was particularly encouraging to see so many young people – unaccompanied teenagers as well as families – there. I guess the news of wars in Ukraine and Israel have brought home the very real possibility that Canada could be drawn into yet another foreign conflict. We parked at Central Memorial High School, and I was reminded that the school is named after the many Calgary high school students who served and died in the First and Second World Wars. Their names are inscribed on plaques in the foyer of the school.

Calgary Military Museums
Remembrance Day 2023

Yesterday was Grey Cup Day, and as usual the game itself did not disappoint. Montreal came from behind, and won the game with a touchdown with just 11 seconds left on the clock. Well done, Alouettes! Next year it will be the Stamps turn!

We're very excited to have received news that our Los Angeles family will be coming to Alberta for Christmas. Edgar's father remains ill in a hospice in Edmonton, so that will be the focus of their trip. Edgar's sister Maureen is planning to sell the family home and downsize to an apartment, so there is likely to be a fair amount of clearing-out of stuff involved while they are there. We'll likely travel to Edmonton for a couple of days at Christmas.

Where We Are

Table 1 shows how stocks, bonds and commodities are performing so far this year. The numbers shown are as of November 17.

Jack Way of Mulvihill Capital Management Inc. has written a great synopsis of what has transpired in the capital markets over the past 3 months:

After three months of corrective action in August, September and October that saw the S&P500 decline by 10%, the Index needed only one week of November to recoup over half of that loss. High interest rates and concerns about economic and earnings growth gave the bearish narrative the upper hand for those ninety-odd days, but as rates fell and third quarter earnings were solid, stocks have resumed an upward trajectory.

The so-called "Magnificent 7" continue to have an out-sized influence on the overall market. Just as a reminder that's Apple, Microsoft, Amazon, Tesla, Alphabet (Google), Meta (Facebook) and NVIDIA. The top 5 represent over 25% of the market weight of the S&P500, with Microsoft and Apple together exceeding 14½%.

PORTFOLIO STRATEGIES

11 Lenton Place SW
Calgary AB T3E 5C7
Tel: 403-616-3434
mikewise@wiseword.ca
www.wiseword.ca

Table 1
2023 Returns - Year to 17 November

	31 December Price	22 Sept Price	YTD Change
Equities			
TSX (CAD)	19384.92	20175.77	4.1%
S&P500 (USD)	3839.50	4514.02	17.6%
NASDAQ 100 (USD)	10466.48	14125.48	35.0%
Commodities			
Oil (WTI; USD)	$80.51	$75.84	-5.8%
Gold (Comex; USD)	$1830.10	$1983.50	8.4%
Fixed Income			
DEX Universe Bond Index (CAD) - Total Return	1054.5	1069.3	1.4%
Govt of Canada 10-Yr Bond Interest Rate	3.316%	3.714%	0.398%
Best 5-yr GIC Rate (rate as of Nov 20)	4.10%	5.00%	0.90%
High Interest Savings Account (rate as of Nov 20)		4.75%	
Exchange Rates			
USD/CAD	$0.7378	$0.7287	-$0.0091
EURO/CAD	$0.6894	$0.6680	$0.0214

New statistics continue to amaze me. Individually those two stocks on their own are larger than the Russell2000 Index of US Equities, and each of the country Indexes of the United Kingdom (FTSE100), France (CAC) and Germany (DAX). Such a concentration in so few stocks is great for those that own them in the good times, but as someone who has been around a long time and witnessed the rise and fall of the "Nifty Fifty" of the early 70's; Exxon and big-cap oils of the early 80's and many other examples of the "madness of crowds", I remain concerned. In defense of the "Magnificent 7", while their valuations aren't necessarily cheap, third quarter earnings for the group did beat estimates, and consensus earnings expectations for 2024 are at +12% while the rest of the 500 is at -4%.

Market internals improved dramatically during the recent rally, and seasonal strength will be with us into February, and as such are two more short-term pluses.

Most of my clients have a balanced portfolio. My Canadian Neutral Balanced Benchmark is up 4.74% so far in 2023.

Where We're Heading

The Canadian stock market continues to badly under-perform the US stock market. That's been

The Calgary Civic Symphony
Beethoven Symphony #9 "Ode to Joy"

a recurring theme over the past decade. It seems to be mainly a result of Mr. Market's (justified) infatuation with the growth story of Technology. As Mr. Way wrote in the previous section, the Tech growth story might not be over; the group's forecasted earnings growth for next year is much higher than the rest of the US market.

It seems that we need some exposure to Technology whether or not we fear that a recession is approaching.

The Canadian stock market has a heavy weighting in Financials and Resources. We're considered to be a "value" economy, while the US is considered to be a "growth" economy. That's not the end of the story. I recently attended an analyst's meeting in which a speaker noted that US Financials have out-performed Canadian Financials, and US Energy stocks have out-performed Canadian Energy stocks. Sobering news for a Canadian investor!

Interest Rates

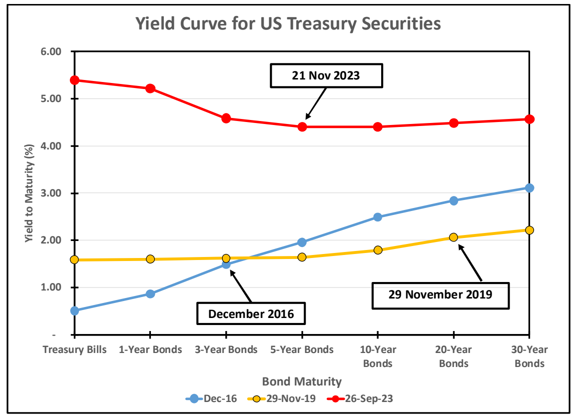
It appears that the Bank of Canada and the US Federal Reserve have ceased raising interest rates – their term is "paused" – pending further information on the health of the economy and the path of inflation.

Official inflation has fallen substantially over the course of 2023, likely mirroring the decline of energy prices. This morning's news report said that the Consumer Price Index in Canada fell from 3.8% in September to 3.1% last month. Energy costs are down this year, but groceries and services were both strongly up. Mortgage costs have pretty well doubled; bad news for those who had to renew their mortgages this year!

The pundits are now projecting that the Bank of Canada will begin lowering rates in the 2nd quarter of 2024, while the Fed will begin their cycle of lowering rates in the 3rd quarter, in time for the US election.

The interest rate yield curve is the single best predictor of future economic activity and recessions. Recession typically starts 12-18 months after the interest rate charged by 90-day Treasury Bills becomes higher than the rate charged by 10-year US Government Bonds. Chart 1 shows 3 curves: a strong positively-sloped yield curve at the end of 2016; the curve just before the outbreak of Covid in November 2019, and the current negative-sloped yield curve for US Treasuries. The 10yr/3mo curve turned negative in October 2022, or 13 months ago. As of November 21, the 10-year yield is 4.5407%, while the 3-month yield is 5.388%.

Chart 1
US Treasuries Yield Curve as of 21 Nov2023
Source: Barron's



Stock Market

I've frequently commented that Mr. Market is manic-depressive. The market over-reacts to even the slightest news, both good or bad, as investors and speculators try to gain an advantage over others. The news that central bankers have paused their rate hikes has caused Mr. Market to go into hyper-optimistic mode. Even the normally-staid "Flinty-eyed Bankers" who populate the bond market have got into the act. The bankers are speculating that interest rates are about to plummet back to pre-

An Old Barn in Southern Alberta

Cool Parrot

Covid levels, thereby giving an unprecedented chance for capital gains in the bond market (remember: bond prices rise when bond yields fall).

I wrote in the previous section that I thought that rates would begin to fall sometime next year, but my assessment is that they might go down by a ¼% or so, not fall all the way back towards zero! I think a reasonable expectation for bond returns next year will be the coupon return, or 4-5%; maybe a bit more.

The Flinty-eyed Bankers and Mr. Market seem to be predicting an apocalypse for the economy. While employment is softening, the labour market remains tight. Inflation is going down, following the decline in oil prices, but high prices in the grocery store are here to stay and employees will still be seeking higher wages as they try to recover from last year's bump in prices of food and everything else.

Tyler Mordy of Forstrong Asset Management makes the case that 2024 will be the start of a long-term cycle in which capital spending will be one of the engines of growth, as companies invest in real, tangible things such as investments in energy efficiency and productivity enhancers, as opposed to financial engineering tools like share buybacks and leveraged takeovers. I've talked about this before, mainly in the context of the continuing need for fossil fuels way beyond the magic 2050 deadline, and the investment mandate of the Mackenzie Global Environmental All-cap Fund.

Mr. Mordy thinks that "*many investment classes that struggled with chronically weak demand and dismal pricing power in the era of low inflation, are primed for a long period of outperformance: sectors with pricing power (banks, industrials, healthcare), select resource-exporting emerging market equities and international value stocks which trade on far lower multiples and far higher dividend yields. Investors shouldn't shut the front door on those exposures.*"

Canada

The Liberal government in Ottawa has just released its Fall Economic Statement. Although our prime minister keeps saying that his government is fiscally responsible, the Statement piled on an additional $20B of increased spending without reducing anything by a single penny. This year's deficit is expected to reach the $40B mark.

The Reuters news agency summarized some of the key points that are most relevant to us as Canadian taxpayers:

- invest an additional C$15 billion in new loan funding, starting in 2025-26, for the Apartment Construction Loan Program, for a total of more than C$40 billion in loan funding. This investment will support more than 30,000 additional new homes, bringing the contribution to more than 101,000 new homes supported by 2031-32.
- invest an additional C$1 billion over three years, starting in 2025-26, for the Affordable Housing Fund. This investment will support non-profit, co-op, and public housing providers to build more than 7,000 new homes by 2028.
- help remove barriers to internal labor mobility, including by leveraging federal transfers, and other funding, to encourage provinces and territories to cut the red tape that impedes the

movement of workers, particularly in construction, health care and child care

- deny income tax deductions for expenses incurred to earn short-term rental income, including interest expenses, in provinces and municipalities that have prohibited short-term rentals. It will also deny income tax deductions when short-term rental operators are not compliant with the applicable provincial or municipal licensing, permitting, or registration requirements.
- propose to spend C$50 million over three years, starting in 2024-25, to support municipal enforcement of restrictions on short-term rentals.
- introduce a new Canadian Mortgage Charter, which outlines how financial institutions are to work to provide tailored relief and ensure payments are reasonable for borrowers.
- begin buying up to C$30 billion of Canada Mortgage Bonds, starting as early as February 2024
- the Canadian Radio-television and Telecommunications Commission will conduct a prompt investigation of international mobile roaming charges, and will provide an update and concrete next steps in 2024.
- work with the Canadian Transportation Agency to ensure that airlines seat all children under the age of 14 next to their accompanying adult at no extra cost

Brian Lilley of the *Toronto Sun* commented that the "new housing" initiatives might help low-income families, but does nothing for middle-class families, for whom home ownership is now an impossible dream.

Changing gears slightly, the litany of federal government incompetence, if not corruption, makes a story that is even more interesting than the nonsense going on south of the border. You might not know of much of this if you get your news from CBC, CTV, Global or the print newspapers.

One item that just came to light yesterday concerns Mr. Trudeau's famous battery plant in Windsor. We, the taxpayers, handed over a $15B subsidy to

Fall Colours

Stellantis et al for construction, with Mr. Trudeau particularly stressing all those high-tech jobs in the Green Economy. Well, it turns out that the construction phase is likely to employ around 2500 workers, of whom 1600 will be imported as temporary foreign workers from South Korea. The companies claim that they need those foreign workers because they all have the specialized training required. No "teach a man how to fish …" for this crew!

There is a committee hearing going on that is trying to determine how the ArriveCan app ended up costing $54M, and how a couple of guys, working in their parents' basement, could score a cool $9M while not actually doing anything beyond sub-contracting the app development to others. (The guy in charge, Chief Information Officer Minh Doan, apparently did such a great job on ArriveCan that he has since been promoted to Chief Technology Officer of the entire federal civil service!)

Another hearing concerns the $1B Green Technology Fund that the Liberals set up a few years ago. It first gained minor attention because it gave its Board of Directors big bonuses despite not handing out any grants to anyone. That's not quite true; it turns out that the Chair of the Board set up her own private

Kelowna Flight Center

company, for which she is CEO and everything else, and then awarded her company a $200K grant from the Fund. Her company then gave her, as CEO, payment of $120K for the good work. One of the Board members is a lawyer for a major law firm, and he wrote a legal opinion that there was nothing wrong with the transaction.

There are a number of other hearings as well, which I won't go into. Even the SNC Lavalin affair is still hanging around. One committee is examining why the CBC refuses to call Hamas a terrorist group, even though the federal government has given it that designation. Meanwhile, the trial of Tamara Lich and Chris Barber continues in a courtroom in Ottawa. They have been charged with mischief in relation to the Freedom Convoy. Lots going on in our nation's capital!

United States

There is less than a year to go before the 2024 presidential election. The election campaign does affect the US stock market. Typically, the stock market is flat to down early in the year, but begins to rise as November approaches and the result becomes clearer.

The pundits are predicting that this year will be the most acrimonious campaign since before the Civil War.

President Trump is of course the lightning rod. It appears virtually certain that he will be the Republican candidate despite his bombastic personality and frenzied Democrat efforts to keep him off the ballot.

Polls that compare him to President Biden place him in the lead in both the popular vote as well as the electoral college vote.

I don't think that President Biden will be the Democrat candidate. He is too unpopular, and his lack of mental ability is just too painfully obvious. It would be a disservice to his country for him to run as a candidate, when there are other potential candidates on the Democrat side.

Who do I think will be the candidate? Hard to say, but I'd put Michelle Obama at the top of possibilities, with Gavin Newsom and Kamala Harris behind. There won't be any primaries (Ms Obama hates campaigning) and it will all be sorted out behind the curtains at the Democratic National Convention.

Meanwhile, the Republicans in the House of Representatives continue their investigation of Hunter Biden and his business dealings with various foreign governments while President Biden was Vice-President. They are circling around the Biden family like vultures, and it is only a matter of time before they bring impeachment proceedings against President Biden. Of course, the Democrat-controlled Senate won't pass any impeachment charge, so to a certain extent it is all theatre. And President Biden has the power to pardon his son and other family members if they are formally charged with a crime.

Best Wishes for a Very

Merry Christmas,

and a Happy, Healthy

and Prosperous

New Year!