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The Krygier Report

An exclusive newsletter from Mark J. Krygier, Vice President & Portfolio Manager | February 2021 www.krygierwealthmanagement.ca

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Got your tissue box ready?

Retail investor mania, financial institutions in turmoil, and stock valuations at sky-high prices... No, I am not referring to the latest headlines, but rather to those of an earlier era. Bear with me once again, while I take a stroll down my personal memory lane, to January 2000, as I am getting a nasty feeling of déjà vu that is worth sharing. In January of 2000, the Toronto Stock market was coming off a stellar year of performance, thanks primarily to (may it rest in peace) Nortel Networks, Canada's tech darling of the late '90s, whose shares were up in price over 200% in 1999. Investors who bought "the index" in Canada (unknowingly) held almost 30% exposure to Nortel due to its incredible share price rise, together with that of Bell Canada (BCE) which, at the time, held a large ownership stake in Nortel, resulting in a massive increase of its share price as well. What was that about putting all of your eggs in one basket? In the U.S., it was the high-tech laden NASDAQ which was up massively in 1999, due to concentrated holdings in a few large companies, such as high-tech darlings Microsoft, Cisco, as well as (may they rest in peace) Lucent, Netscape and AOL. The so-called "dot-com" hype led companies to "go public" left, right and center, in order to take advantage of the "FOMO" generated hysteria and speculative need to buy stocks at all costs.

I distinctly remember the phone call I received in January of 2000 from a young client, a medical professional with little investment acumen, who wanted to buy shares in the upcoming 724 Solutions IPO – the last technology stock in Canada to have an "IPO" (Initial Public Offering) of its shares before the "tech-wreck", based on the insistence of a relative in New York who told her she just had to "get in". Unsurprisingly, the popular mantra amongst such "investors" was "this time is different", as, after-all, the age of the internet was just getting started and its potential was limitless. I recall the gambling mentality of that era, when the idea of holding a broadly diversified portfolio of stocks in "blue-chip" companies was frowned upon as "so yesterday" - as why aim for 6-9% annual returns over lengthy periods of time, when you could make 30 or 40% in a month or two? The postscript? After hitting "all-time" highs in March 2000 (sound familiar…) at around the 5000 level, the NASDAQ index and most high-tech stocks plummeted as much as 80%. Those that survived the carnage – well-financed behemoths like Microsoft, et al. – and even the NASDAQ itself – took 12-15 years (**NOT** a typo) just to get back to the levels reached in March 2000. The broader U.S. stock market benchmark – the S&P 500 index - posted a return of 0%, per annum (**NOT** a typo), from 2000-2010 in US$ dollars. For Canadians holding investments in the U.S. markets, the proverbial "salt in the (investment) wound" was the Canadian dollar rising in the ensuing years – even rising above $US1 for a short period – leaving a Canadian dollar investment return in the S&P500 with a negative -5.0% return, per annum, from 2000-2010. Turning to today's markets, with the NASDAQ over 13,000, near its recent all-time highs, while the U.S. dollar has recently been turning downwards versus even our lowly Petro-Loonie…hmmm…that has me wondering…

Preceding the 2000 tech-market crash was the Long-Term Capital (LTC) collapse of 1998. LTC had been the world's largest and most successful hedge fund, run by "the" very brightest and "the" most academically decorated (including Nobel Prize winners for economics), which, in spite of their track record and credentials, required a bailout to the tune of $US3.6 billion (the equivalent of $US5.7 billion today) – to avoid a disastrous domino-effect on the world financial system. LTC had literally placed thousands of bets on all sorts of investment instruments, which all came crashing down at the same time, "fueled" by the leverage that bellowed the financial inferno. Long-Term was the largest financial disaster to hit financial markets to date, and its bailout set the tone for future bailouts of Wall Street giants deemed "Too Big to Fail." Fast forward to the present time when once again news about hedge funds in trouble is dominating the headlines…

In May 2020, following the initial Covid-19 economic closures, a new phenomenon arose. Americans who had no sports to watch, no casinos to visit, and no racetracks in which to place bets – turned to "investing". "DIY" investing began just prior to the 2000 tech market collapse, and after the DIY success on the "way up" turned into "should've, would've, could've," on the way down, it lost its popularity as a "past-time". A very bored but tech-savvy crowd, forced by Covid to sit around their computers day in and day out, besides on-line shopping, turned to the markets with their lure of easy money. The popular "Robinhood" app for DIY investors presents itself as a video game, and offers "options" and "margin" to novice investors as they sign up. In reality, it could be described as a gambling app rather than an investing one. In 2021, such retail DIY investing has literally come head-to-head with institutional "giants" – hedge funds which aggressively "short" ("sell high" to "buy low") stocks of companies facing financial collapse. The latest retail "game" is to "invest" in such losing companies en mass, with the goal of pressuring hedge funds to buy back shares they had sold, to cover their losses, known as "short covering", thereby forcing prices higher in a "Ponzi-like" scheme, while hoping not to be the last "sucker" at the top. This strategy is not investing. The pack of retail "mice" turning on institutional "elephants" is a bizarre phenomenon, even forcing some of these institutions into bankruptcies. One can't help but wonder if bailouts are far behind – as leverage always accentuates their losses (at $2.75 billion and counting). Combined with today's super valuations of many high-tech stocks, a record number of fad-like IPOs, and record levels of margin borrowing for investing - it seems we have seen this show before and we know its ending.

Bottom line

It is crucial to recognize that when investing becomes a game, and valuations of investments become irrelevant**,** one has to be very careful not to chase the crowd. Everyone is an expert – until common sense rules again. In the aftermath of 2000, valuation once again mattered and investing in good quality once again carried the day. Avoid the mistake of those that chase the latest path to "easy money", as historically that path ends in tears and a box of tissues as the solace.

Global benchmarks

As at January 31, 2021 (Canadian $ Returns – except where noted)

Asset class	YTD	1 year	3 years
S&P/TSX Composite T/R (Canada)	-0.3%	3.5%	6.1%
S&P 500 TR - US$	-1.0%	17.2%	11.7%
NASDAQ Composite - US$	1.4%	42.8%	20.8%
MSCI Europe Index Price Return	-1.1%	0.7%	-0.2%
MSCI Emerging Markets	3.3%	20.8%	3.2%
China S.E Shanghai A Price Return	2.2%	21.5%	0.6%
MSCI World Index Price Return	-0.7%	9.7%	7.7%

Asset class	YTD	1 year	3 years
30-year U.S. T-Bond - US$	-4.1%	4.9%	10.3%
10-year U.S. T-Bond - US$	-1.4%	5.0%	7.0%
Long GOC Bond (2051)	-5.9%	-0.2%	8.1%
10-year GOC Bond	-1.3%	5.2%	6.1%
5-year GOC Bond	-0.1%	4.8%	4.2%
3-month CDN T-bill	0.0%	0.6%	1.2%
US$/CDN$ (1.2777)	0.4%	-3.5%	1.2%

Source: RBC Capital Markets Quantitative Research

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