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The Krygier Report

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

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Money talks…

As Covid-19 goes into its 15th month of impacting North America, I can't help but wonder what will our future look like with what I believe has become a real crisis in leadership in most parts of the world. Certainly in Canada there seems to be a complete dearth of quality leadership at all levels of government, as all was left bare in the (mis)handling of the Covid crisis. While many parts of the world are in the midst of reopening their economies, including our American neighbours, in reducing the need for masks, allowing public gatherings and trying to get back to pre-Covid norms, in Canada the saga continues with no clear light at the end of the proverbial tunnel, other than to throw up yet more stumbling blocks to the many entrepreneurs that have been devastated by closures. To get some idea of how far off the main course we are historically, consider that the current Trudeau Liberals have racked up more debt in their few years in office than all of the prior 22 Prime Ministers before him – combined! And who is buying all of this Canadian government issued debt? The Canadian government itself via the Central Bank of Canada - $302 Billion or 84% of the $354 Billion in debt issued by the Government of Canada since 2020 alone! Incredulous, yet, despite his seemingly annual trip to the Ethics Committee to defend yet another conflict of interest accusation, with the general lack of leadership it is hard to imagine who will replace him. A very sad state of affairs indeed.

In the business world, leadership often takes on caricature-like dimensions. On the one hand, there is famed investor Warren Buffett, whose Berkshire Hathaway company has managed to outperform the stock market over several decades, with his folksy, whimsical, down-to-earth style. In contrast, you have Elon Musk, the CEO of electric car company Tesla, who has achieved "cult-like" status to the point where he is to appear on the long-standing comedy show "Saturday Night Live," in the latest rendition of Hollywood meeting Wall Street. While Buffett prides himself on focusing on the positive cash flow of the companies in which he invests, Tesla boasts about making cars that don't make money! In its most recent quarterly earnings report, Tesla declared a "net earnings gain" of about $USD 438 million. However, equity analyst Rajvindra Gill of Needham Investments points out that the declared "profit" included about $518 million in carbon credits (zero emission vehicle or "ZEV" credits). Being able to sell government "credits" gave Tesla an artificial profit which it could not achieve by selling its own products. Furthermore, what purchase did Musk make with some of Tesla's corporate money, which it raised recently when issuing more shares on the market? $USD1.5 Billion worth of Bitcoin – which Tesla trimmed for profit to add an additional $USD101 million profit in the recent quarter. Okay, let's do the math. Declared net profit on sales of 185,000 vehicles of $438 million. Strip out the selling of artificial tax credits ($518 million) and profits ($101 million) on a speculative investment in Bitcoin (where was the due diligence committee when that purchase was made?). That leaves a net loss of $USD181 million – for the quarter! Oh, and don't forget that Musk pocketed $299 Million as a "bonus" since Tesla's share price reached a certain level. Real profits and real cash flow or smoke and mirrors? Barnum and Bailey would have been proud!

I have been speaking and writing about a proverbial changing of the guard in the stock market for almost nine months. From a "big picture" view, technology stocks may be the exciting stories to watch, but investors have been better rewarded in recent months by looking to old fashioned commodity stocks once again. In a "never say never" deja vous, those areas which were left by many for dead have arisen with a vengeance. Rather than technology leading the market returns of late, it has been oil, copper, iron ore, potash, lumber, etc. which have led the brigades. However, I find many investors are quite skeptical and while they might nod their heads politely in the affirmative to such remarks, in their hearts they are still betting on technology to rule the stock market roost once again. So, in an effort to seek objective commentary on this subject, consider the following comments from several CEOs of some of the world's largest corporations – for whom knowing their company's "P&L" is a matter of these business leaders getting their bonuses or not!

- **Proctor & Gamble:** "The commodity cost challenges we face this year will, obviously, be larger next fiscal year."
- **Chipolte:** "We feel like there is going to be significant increases in inflation…we think everybody in the restaurant industry is going to have to pass these costs along to the consumer."
- **Honeywell:** "For us, inflation is taking hold. There is no doubt about it…I don't think things are going to abate."
- **Constellation Brands:** "We're expecting substantial inflation headwinds in the low to mid-single digit range."
- **PPG Industries:** "We experienced a significant acceleration of raw material and logistics cost inflation…"
- **Celanese:** "We're certainly feeling the inflationary factor…we've been able to push that through in our pricing."
- **Nestle:** "We now see broad-based inflation [in] various commodities, packaging materials and transportation costs."
- **Mattel:** "We are evaluating price adjustments for the recent increases in input costs."

Bottom line

Whether you like it or not, inflationary pressures are real, so, if you have not yet adapted your investing strategy, now is the time for action. If instead one thinks that chasing what looks exciting is the way to make money, and that the stock market is ineffective in figuring out what makes sense in the long-run, consider that year-to-date Tesla's share price is flat to slightly negative while Buffett's Berkshire Hathaway is up almost 18%. Fads are fun and exciting to follow, but serious investors follow the flow of money!

Global benchmarks
As at April 30, 2021 (Canadian $ Returns – except where noted)

Asset class	YTD	1 year	3 years
S&P/TSX Composite T/R (Canada)	10.6%	33.3%	10.4%
S&P 500 TR - US$	11.8%	46.0%	18.7%
NASDAQ Composite - US$	8.3%	57.1%	25.5%
MSCI Europe Index Price Return	4.0%	23.3%	2.0%
MSCI Emerging Markets	0.7%	28.4%	3.5%
China S.E Shanghai A Price Return	-3.4%	15.9%	1.6%
MSCI World Index Price Return	5.5%	26.2%	10.5%

Asset class	YTD	1 year	3 years
30-year U.S. T-Bond - US$	-13.3%	-20.0%	7.7%
10-year U.S. T-Bond - US$	-6.1%	-8.1%	5.8%
Long GOC Bond (2051)	-17.8%	-18.8%	3.5%
10-year GOC Bond	-6.9%	-7.7%	3.9%
5-year GOC Bond	-1.8%	-1.4%	3.5%
3-month CDN T-bill	0.0%	0.2%	1.1%
US$/CDN$ (1.2289)	-3.5%	-11.8%	-1.4%

Source: RBC Capital Markets Quantitative Research

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