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The Krygier Report: SPECIAL EDITION

An exclusive newsletter from Mark J. Krygier, Vice President & Portfolio Manager | March 2020 www.krygierwealthmanagement.ca

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Pandemic of Panic – Part II

In an unprecedented move, and at the behest and encouragement of a few clients, I am writing my third "Special Edition" Newsletter in two months and the second in a month. Rest assured this one will not be as verbose as the last one.

Not to sound apologetic, but "should've, would've, could've" is likely the feeling we all have about holding any investments other than cash, gold and bonds – and when I say "we all have," it is because I personally hold every single security that I hold for my clients. Interestingly, unlike many of our clients, I don't actually look at my own portfolio on a regular basis – in truth, it's usually once a year after the December statements come out, and even then it's only to mark the change year-over-year. I highly recommend this approach as a means of alleviating stress about one's portfolio. Why? Because two out of every three years the markets have historically been positive, which means every time I look at my personal statements I have a 66.66% chance of seeing positive returns! Statistically, as I mentioned in the previous Special Edition newsletter, the more often one checks one's statements (or one's accounts via on-line access) the more likely one is to see negative returns. Why is this important? Simply because one has to have the "end-goal" in mind at all times and literally "battle" to maintain a positive attitude. Life is way too short to focus on negativity, and there are far too many things that can distract us into a depressive state, without having to add to that emotion by "checking" too often.

Okay, so what about the markets? Today is a tough one to stomach, BUT this type of drop is not unprecedented, neither in the depth of the drop nor in the broad range of the sectors impacted. Like famed portfolio manager Warren Buffett said in an interview yesterday, 1987 and 2008 were far worse markets – and we survived those ones. While I was not investing in 1987, I was there for the 2000 tech wreck (a mere 4 years into my career) which was really only a disaster for the technology sector, and 2008, and I agree with Mr. Buffett that 2008 was a much worse market environment. What made 2008 so bad was that it was the financial sector at risk of collapse and without finance there is literally no business and no economy. Unlike that time period, the markets today are fixated on two main issues – coronavirus and oil prices. Regarding coronavirus, not to minimize the health risk, but let's be clear, from all the medical information I have read and heard, while it may be highly infectious, it seems not to be airborne and is a fatal risk almost exclusively for the very elderly and those with already compromised respiratory systems. For the broader populace, the impact – even if one contracts the disease which is unlikely – is no more than a mild flu, which we have all experienced from time to time. That means that while it may take some time, it should be contained and then most areas should get back to normal economic activity, other than a few select areas like travel and leisure which will likely take longer to recover. As for oil prices collapsing – that is a political battle between Russia and Saudi Arabia, and their respective oligarchs. Those in Western Canada are certainly feeling the pain of lower prices, but that has unfortunately been a reoccurring theme since 2008, so it's just an exacerbation of the same issue.

Where do the markets go from here? Obviously, we can only know if we "hit the bottom" after-the-fact, but some things are clear. Firstly, to determine if the selling or buying pressure is overdone, I rely upon an objective standard known as the daily Relative Strength Indicator or "RSI". An RSI score over 70 indicates something is "overbought" and a score below 30 is "oversold". Based on this measurement, the Toronto TSX stock market reached a crescendo of selling with a 15.9 RSI, versus 20.7 on December 24th, 2018 which was the last day of that brief downturn. The U.S. S&P 500 hit a low RSI score of 26, versus 17.98 on December 24th, 2018. It makes sense the U.S. markets hit a lower mark in 2018 as it was a concern over U.S. interest rates rising that caused the downturn. Conversely, with the oil price drop it makes sense the Canadian market is more "oversold" today. Secondly, a market technician I follow regularly noted yesterday that the Put/Call Ratio is rising strongly and is approaching another extreme level "very similar to the December 2018 market bottom." He concludes this means that investors are extremely fearful and buying too many put options (i.e. taking defensive measures) to hedge the downside risk of the stock market, which is a contra-indicator of market risk. Portfolio Manager Doug Kass commented earlier this week that "the differential between the S&P 500 dividend yield and the 10-year U.S. Treasury bond yield is greater than at any time in over a decade." Put together, those are pretty good indicators we are close to the bottom if not there already.

So what are we doing with our portfolios? Again, "should've, would've, could've", means anything other than cash, bonds or gold has not been a positive experience today or over the past 3 weeks. However, back to reality, firstly, for over two years we have limited our exposure to the Canadian energy sector, and we gradually reduced our exposure to the Canadian banks as they are leveraged to a slowing economy including the Canadian energy sector via loans (you might say we have a very "nonCanadian" Canadian portfolio). Secondly, we had been adding to our bond holdings for clients with the investment agenda of balanced portfolios, and within the bonds we had already been reducing our exposure to more aggressive bonds and adding to higher quality bonds. Thirdly, in both our U.S. and Canadian portfolios we added and then increased our exposure to gold earlier this year, albeit still a small portion of the portfolios. Fourthly, since mid-January we have been repositioning our stock holdings by selling stocks in the companies we believed were most likely to suffer on a longer-term basis from the Coronavirus. For instance, stocks like Air Canada (travel) and Disney (leisure) were already sold. In their place we added stocks we have been eyeing for some time but did not yet buy because the prices were too high. We have specifically been adding to our portfolios stocks of companies with stable businesses, mostly stable-dividend payers, unless the high growth rate of a particular business is sustainable to justify not paying a dividend. Finally, while we all talk about buying "low", when prices are in fact low, there seem to be very few buyers. For those with cash to invest, while we cannot know what tomorrow brings, it is certainly cheaper to buy today than it was yesterday or the week before.

Bottom line – as technical analyst Walter Deemer said, "When the time comes to buy you won't want to." This is certainly not the first time the markets have been volatile, nor the last. We will continue to invest in good companies which can withstand the sometimes vicious cycles of economic activity and we will be around to "tell the tale" of the 2020 market pullback in a future newsletter many years in the future.

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