Crowder Wealth Management Group's Quarterly Comment

Wealth Management
Dominion Securities

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One of the realities every investment professional faces is that there's always a risk of being wrong. Nobody needs to point out that generally every investment recommendation or strategy carries with it certain degree of uncertainty. Considering that, when dealing with investors life savings puts the importance of risk control into the perspective that it deserves. There's simply no room for high risk speculating in a long-term wealth management strategy.

You can appreciate that our position as wealth advisors is to help our clients build and retain their wealth. Naturally, that would suggest that careful thought and analysis should be the cornerstone of any recommendation. It follows that that path would call for following conservative and time-proven principles.

Case in point, we've been getting a lot of inquiries about Cannabis stocks. While I hesitate a little even to discuss the topic, it's a good example to illustrate some of thoughts that should go into investment decision-making. Suffice it to say, at this point we view Cannabis stocks as "un-investable", despite their popularity and success so far. The bottom line is that there are far too many unknowns to make a prudent decision about them. There is no crystal ball; only analytical tools. In this case the fundamentals are highly unreliable, making any analytical conclusions highly uncertain and risky.

Cannabis stocks generally have all the makings of an asset bubble. In the first paragraph I mentioned that every investment professional faces the risk of being wrong. Perhaps, here too, we are wrong. So far, that's certainly been the case, yet we still would not recommend them.

Asset bubbles have been a frequent – and painful – experience throughout history. We can't make this point more strongly. They have happened over and over and over. Generally, they're characteristics and pattern are alarmingly similar, yet they do get repeated. It's an interesting behavior pattern of human nature.

Bubbles are generally driven by a combination of access to easy money and leverage, some sort of new technology or concept, regulatory changes, but most commonly: widespread investor speculation.

Here's a few examples of past bubbles (there have been many others as well):

When the railroad industry was in its infancy in the late 1800's, an investment bubble was created. When all was said and done, roughly one third of all railroads went bankrupt resulting in huge losses for investors. Yet the industry went on to be the backbone of a nation.

Similarly with the automotive industry. We don't have the exact numbers, but in the early stages we believe that there were a hundred plus automotive manufacturers. At one point we were down to something like 7. Yet, we all know the lifestyle changes that automobiles brought with them.

More recently, many of us lived through the internet bubble that eventually burst in the early 2000's. Remember Nortel? Even a successful company like Microsoft took 16 years before its share price moved back to where it had peaked at that time. In the end, the infrastructure and the resulting internet has dramatically changed business and our personal lives.

Last year, Bitcoin was all the rage and rose over 1,400% in 2017. It is now down 65% from that level. The euphoria seems to have dissipated…..

All of these bubbles had those common characteristics, but widespread speculation without regard for fundamentals and economic realities was what drove asset prices to excessive levels.

To quote Warren Buffett: *"People start being interested in something because it's going up, not because they understand it or anything else"*. They want in because they see neighbors who are dumber than they are getting rich, and want to get in on the action. If it's not wanting to get a piece of the action, then it's the fear of missing out that drives investors. Either way, it's an emotional decision, rather than one based on rational thought.

This spiking of share prices tells a story that is forgotten, yet often repeated throughout history. It's a story of unbridled greed for what the future might hold. The worst part is that it also feeds on itself; the higher prices move, the more interest it generates and reinforces. This positive feedback loop helps explain how prices can reach over-extended levels. Feedback loops and other behavioral mistakes are critical components in every bubble in history.

At this point there's no way to know for sure if the Cannabis stocks are a bubble waiting to burst, but valuations seem to be quite extended using any typical fundamentals. For sure, we're witnessing the birth of an industry that's looking very similar to the births of these other industries. There's almost no doubt that some of these companies will be successful. After all, industries aren't born every day. What's concerning to us is theses valuations, plus how difficult it is to assess how the industry will unfold, and how it might look 5 or 10 years from now. Presently, for things to continue on the current path, and for the current fundamentals to work, one has to make some very aggressive estimations and projections.

In the long run, stock prices tend to move in tandem with fundamentals. Over the short run human behavior driven by emotions can dominate over everything else and drive prices well beyond (or below) reasonable explanation. In the area of Cannabis stocks, we're prepared to be wrong in order to be prudent. They may very well have an extended run, but currently the fundamentals don't support that.

To repeat messages from previous quarters, we believe that there is a strong argument for owning stocks, as fundamentals remain favorable, while valuations could generally be described as "fair". Interest rates are creeping higher at this point, but fixed income securities are still not that attractive with interest rates still close to historic lows, combined with the negative prospect of rising rates.

As always, thank you for the opportunity to work together. Should you have any questions or concerns, please don't hesitate to contact me at 1-800-265-5911, 519-675-2512 or any other members of the Crowder Wealth Management Team.

Final Thought:

> *"The four most dangerous words in investing are: 'this time it's different.'"*
>
> \- Sir John Templeton

Sincerely,

Wayne Crowder, B.Sc.(Agr), CFA.
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Crowder Wealth Management Group

Index	**YTD**	**1 Year**	**5 Year**
S&P/TSX Composite Total Return Index	1.4%	5.9%	7.8%
S&P 500 Total Return Index ($CAD)	13.4%	22.0%	19.2%
S&P 500 Total Return Index ($USD)	10.6%	17.9%	13.9%
MSCI World Price Index ($CAD)	6.5%	13.0%	12.1%
Broad Composite Cdn. Bond Index	-0.3%	1.7%	3.3%

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