Joshua Brown, Portfolio Manger

Markets Made Simple

Wealth Management
Dominion Securities

FOURTH QUARTER REPORT – DECEMBER 31ST, 2020

Billionaire investor, Paul Tudor Jones - "I have four kids in their 20s. And, it's like a horse at the beginning of a race. They're so ready to get to see their friends, to get to restaurants, to vacation. They're just ready to get out and go crazy, like I think everyone else in the world."

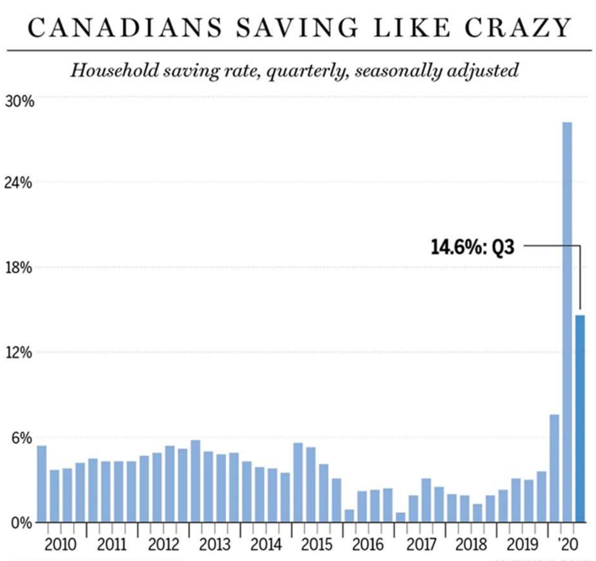
2021, READY TO ROAR?

Like everyone, I have been unable to do many of the things this year that I love. Traveling to the far corners of the world, enjoying live music and sports, spending time with family, and trying new things.

There is so much I can't wait to do. Visit New York again for the best pizza I have ever had. Prince Street Pizza, in Soho, Manhattan. A line-up stretches out the door during all hours of the day. Customers wait in the snow, rain and hot sun for their signature Spicy Spring Slice. It is simple, made of only sauce, mozzarella and pepperoni, yet amazing. I craved it so much after trying it I made another trip to New York, staying there for only a few hours. Basically getting off the plane, going to Prince Street for their pizza, walking around the city, and then getting back on the plane to go home.

This year my life has dramatically changed. With limitations on what we can do, I read a lot more, did a lot of local exploring and travelling, and worked on perfecting my cooking. My expenses have changed as my lifestyle has changed. I spent less, and my bank account steadily grew. Not all Canadians are in the same boat. Some industries, such as the hospitality and tourism industry have been hit the hardest by the pandemic and many are struggling to make ends meet.

However, as most of us have stayed home, the overall savings rate in Canada and the US has surged to record highs. For those that have been struggling, governments around the world have stepped in by providing record financial support to those that need it. This has helped fill the economic gap left from shutting down the economy. Canadians and Americans are saving like never before, as seen below.



The Spanish Influenza and The Roaring 20's

100 years ago the world emerged from the Spanish Influenza. A third of the world's population was infected from 1918-1920, with an estimated 100 million people killed. Cities had lockdowns, schools and churches closed, masks were mandatory, and people only left their house when absolutely necessary.

Not surprisingly, businesses did not do well. Sales collapsed, dropping by 40-70% and pushing the economy into a recession.[1]

When the pandemic subsided in 1920, those who survived had a different outlook on life. Life was precious. It was time to live lift to the fullest. This led to tremendous pent up demand.

Spending erupted following the Spanish Influenza. People bought new cars, bigger houses, and filled their new homes with refrigerators and radios. Consumers took on credit. A decade of tremendous economic growth followed. The 1920's became known as the Roaring 20's because of the strong economic growth that decade. With our new outlook on life, new spending habits, and pent-up demand, a decade of strong economic growth led to strong stock markets returns. The economy grew by 42% in the decade of the 1920's, Gross Domestic Product (GDP) doubled per person, and from 1921 to 1929 the DOW Jones rose by over 500%.

Pent Up Demand Today

Billionaire investor, Paul Tudor Jones, recently said:

"I have four kids in their 20s. And, it's like a horse at the beginning of a race. They're so ready to get to see their friends, to get to restaurants, to vacation. They're just ready to get out and go crazy, like I think everyone else in the world."[2]

With record high saving rates, cash in the bank, and pent-up demand from being stuck at home, consumers are flush with cash…and ready to spend.

Time to Invest? What Are We Doing?

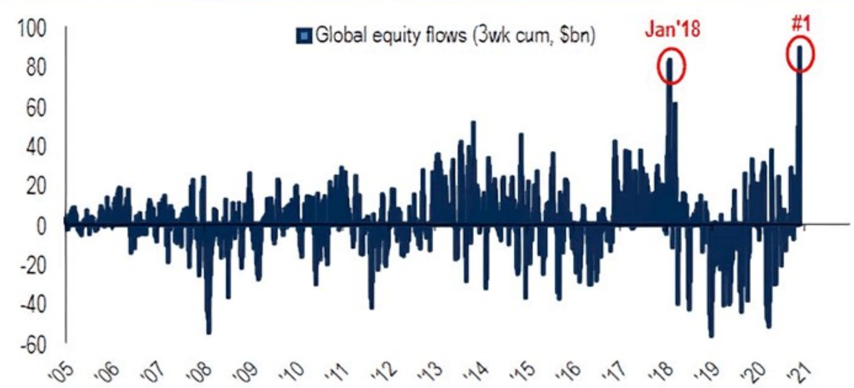
In March, the market had extreme pessimism. As I highlighted in my newsletter at the end of March, this was a generational opportunity. It was Boxing Day shopping in March and malls were empty. Imagine being able to walk into any store and being able to buy whatever you wanted, at blowout prices. The stock market was having a giant sale. We went shopping and were rewarded with amazing bargains.

In the short-term, the stock market is like a pendulum. It swings from one extreme to the other, ***from fear to greed***. In March it swung to the extreme in fear. By understanding the true value of an investment and having a long-term outlook, there were incredible opportunities for investors. We took advantage of them in March, significantly adding to our equity exposure.

Now, at the end of 2020 the pendulum has swung again. This time in the opposite direction, going from fear to greed. Investors who were pessimistic, are now optimistic. In November, a record amount of global inflows into stocks occurred. The last time there were inflows like this, was in January 2018. I highlighted in my newsletter at the time, that it was time to be cautious. The markets then sold off by 10%, followed by another 20% selloff at the end of 2018.

[1] https://www.stlouisfed.org/~/media/files/pdfs/community-development/research-reports/pandemic_flu_report.pdf
[2] https://www.barrons.com/articles/bucket-list-travel-is-being-booked-in-record-numbers-for-2021-and-beyond-01605963174

Chart 2: Record 3-week inflow to global stocks

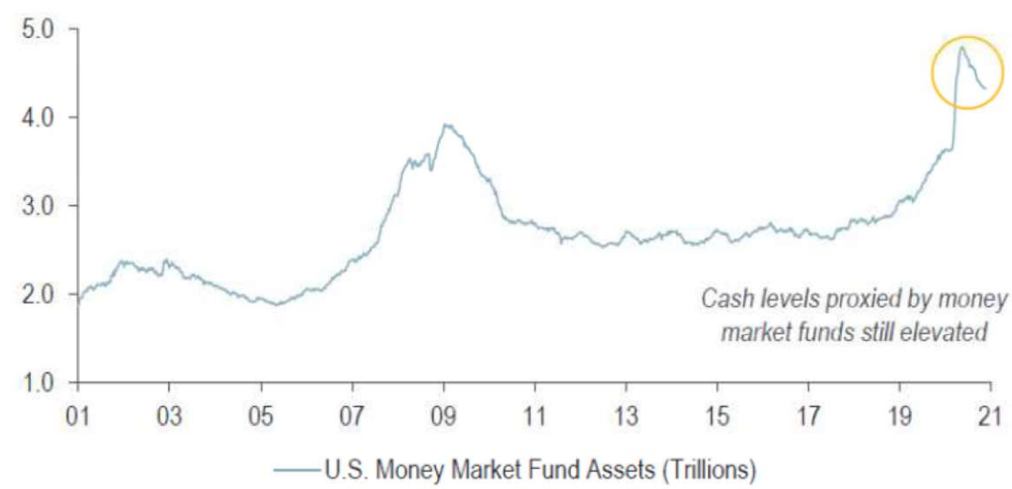


Source: BofA Global Investment Strategy, EPFR Global

We are expecting to see more market volatility this year. This coincides with whenever investors get too fearful or greedy. The more emotional investors get, the more volatility you can expect. It happened in 2018, it happened in March 2020, and we are seeing those same extreme emotions again.

As always, we are ready. This is how we add additional value for our clients. Buying when investments sell off more than they should, and trimming them when they get ahead of themselves.

As I have highlighted in the past, we are still in a very low interest rate environment. Just like in 2009, after the market sell-off, investors were sitting on large cash balances. With low interest, they could either choose to leave their funds in savings accounts paying them next to nothing, or have the money invested in the market with much higher yields. Investors had few alternative options for their cash, so money continued to flow into the markets after 2009. In the chart below you can see the elevated cash levels back in 2009, and how cash flowed back in the markets over the following years. This lead to the longest bull market ever in the S&P500 and returning over 400% return for investors. There were bumps in the markets along the way, but sell-offs were met with buying from investors who were sitting on cash.



We are in a similar environment today. Cash balances more elevated now, than back in 2009! We expect there to be bumps along the way, but with the record amounts of monetary and fiscal stimulus, interest rates close to zero, funds will continue to find their way back into the markets.

Now, more than ever, proper portfolio positioning is key. Future returns are dictated by your current positioning. As I highlighted last quarter, investors have flocked into different technology stocks, pushing their valuations to very high levels. Paying a high price for an investment today, means your future expected return will be lower. It is similar to paying $20 for a cup of Starbucks coffee. It would be difficult to find someone to buy it from you at a higher price. Consequently, paying a low price for an investment, means your future returns can be expected to be higher than normal. If you were able to buy the same cup of Starbucks coffee for $0.10, it would be easy to find someone that would pay significantly more for that. We have already started to witness a rotation out of some of the technology companies, back into the segments of the market we have been buying with the best value. Over the quarter we have seen significant outperformance in these companies, which has benefited our equity holdings.

Our equity exposure is in high quality companies with strong balance sheets, pay attractive yields and are at great valuations. We are well positioned as the economy returns to normal, and we will stand to take advantage of the volatility along the way.

With low interest rates, investor cash balances will continue to flow into the markets. We will be taking advantage of market weakness when we see it.

If you have any questions on your portfolio, or the markets, please don't hesitate to reach out to me.

TFSA's –the contribution limit for 2021 is $6000. If you have been eligible to contribute since 2009, your cumulative contribution room is now $75,500. For a couple, that is $151,000. TFSA's are a great tax planning tool, and should be utilized.

RRSP – the RRSP deadline to make a contribution for 2020, is March 1st, 2021.

As always, we hope you and your loved ones are keeping safe.

-Kind regards,

Joshua Brown, BBA, CFA
Portfolio Manager

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