May 2022

The Monthly

With this commentary, we plan to communicate with you every month about our thoughts on the markets, some snapshots of metrics, a section on behavioral investing and finally an update on MacNicol & Associates Asset Management (MAAM). We hope you enjoy this information, and it allows you to better understand what we see going on in the marketplace.

"You miss 100% of the shots you don't take."

- Wayne Gretzky

The Numbers:

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Index:		**2022 YTD:**
S&P/TSX:		- 2.17%
NASDAQ:		- 21.2%
Dow Jones:		- 9.25%
S&P500:		- 13.3%
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	1.36%	1.07%
5-Year Bond:	2.84%	2.92%
10-Year Bond:	3.00%	2.96%
30-Year Bond:	3.00%	3.30%

Economic Data:

- Stocks global almost unanimously lower in April
- Oil and natural gas higher in April
- Gold flat, silver off 6.3% for the month
- Canada's inflation rate hits 3-decade high of 6.8% last month
- Bond markets pricing in tighter central bank policy rates
- US labor market continues tightening while producer prices exhibit moderate gains

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	20	28
P/B: Price-to-Book	4.4	4.2
P/S: Price-to-Sales	2.5	2.9
Yield: Dividend Yield	1.6%	1.4%

2022 Year to Date Performance, by Sector: May 2nd, 2022

S&P/TSX Composite	-2.17%
NASDAQ	-21.2%
Dow Jones Industrials	-9.25%
S&P 500	-13.3%
Russel 2000 (Small Caps)	-12%
MSCI ACWI ex-USA	-12.3%
Crude Oil Spot (WTI)	45.6%
Gold Bullion ($US/Troy Ounce)	3.8%
SOX Semi-conductor Index	-11.3%
VIX Volatility Index	32.2%

Source: Canaccord Genuity Capital Markets & Thomson Reuters

Foreign Exchange – FX

As of May 19, 12:00 pm	$ 5,000	Cdn		
Banks	Rate	**Buy USD**	**Cost**	**% Difference from Spot Rate**
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.2812	$ 3,903	$ 1	0.0%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.2944	$ 3,863	$ (39)	-1.0%
Raymond James	1.2975	$ 3,854	$ (48)	-1.2%
Royal Bank	1.3077	$ 3,824	$ (78)	-2.0%
Scotia	1.3157	$ 3,800	$ (101)	-2.7%
TD	1.3181	$ 3,793	$ (108)	-2.9%
Canadian Snowbird	1.3006	$ 3,844	$ (57)	-1.5%
Spot Rate	1.2815	$ 3,902	$ -	0.0%

Shoot…that didn't work…

Two Wednesdays ago, I was in my office juggling calls, calculations and compliance. It was a pretty normal day in that sense with one notable exception. US Fed Chair Jerome Powell was expected to increase the Fed funds rate by 50 basis points, the first-rate hike of that size in several years. Powell is the man who famously said that he wasn't even *thinking about thinking about* inflation barely 24-months ago (on July 20th) and that the economy would require accommodative monetary policy for an extended period of time. A transition from monetary accommodation to monetary restraint was considered big news, but the even bigger news was the rumor that future rate hikes could be even bigger. Networks such as CNBC and Bloomberg brought out heavy hitting guests like Harvard super economist Ken Rogoff and American hedge fund titan Paul Tudor Jones for their views. Others "celebrity" guests followed but their messages were largely the same.

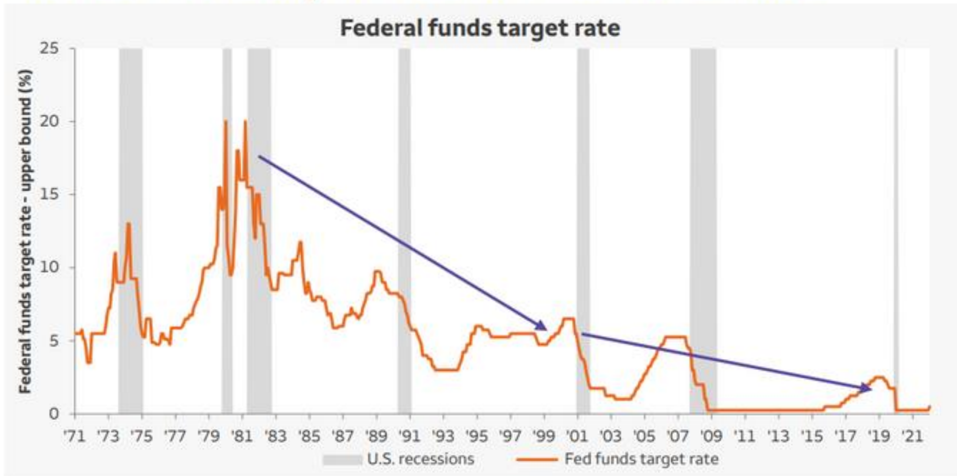
Run for the hills!!!

Indeed, most guests delivered bleak views on why stocks and bonds were bad ideas. The guests were different as were their stories, but the messages were all mostly the same: inflation had become rampant, and the Fed would have to apply the monetary brakes more abruptly at precisely the same time as the economy was beginning to lose momentum anyway. Central banks tend to trail inflation almost by definition and though this isn't something I've investigated with a great deal of academic rigor; it is something I've just sort of observe with my own eyes. When have you ever heard a central bank governor say that inflation is a problem, apart from when it is literally slapping the consumers and businesses in your neighborhood right in the face? One group well represented in my neighborhood are the Police, and they are a perfect group to use to explain central bank policy. Cops are there to fight crime when it becomes rampant. Any police officer will tell you that crime is bad, and that criminality should be stopped. The trouble is, communities with zero crime don't really need the police, do they? Now I reckon that most central bankers might tell you that inflation is bad while the propensity or inclination to engage in inflationary policies is worse yet stand willfully idle until it becomes rampant.

[Well, it's rampant.]

So, what do you do when the very thing you are mandated to control has gotten out of hand? Simple: panic. Thus, in a stroke of Federal Reserve policy "genius" the decision was made to dial up monetary tightening to levels not seen in years while promising even more twisting in the future. These actions and the new narrative that follows it have severely roiled markets in recent weeks, and the overall impact has a simple name: tapper tantrum. Essentially financial markets are resenting higher rates as the pretense for combating inflation because that pretense could stymie economic growth and trigger a drop in corporate profits, which financial markets just hate. The dilemma is compounded by investors inability to tolerate anything but an orderly and symmetrical approach to inflation, which is frankly impossible now.

The Fed's tendency to overshoot on interest rates



Sources: Bloomberg and Wells Fargo Investment Institute. Monthly data from March 1, 1971 to March 31, 2022. For illustrative purposes only. Fed = Federal Reserve.

So, is it possible that the Fed over does it on rates and destroys the economy in the name of simply bruising inflation? Well known Oaktree Capital head Howard Marks feels recession fears are potentially misunderstood. Marks recently presented to the Wharton School of Business and mapped out a way for investors to think about risk. Risk, Marks said, is *counter* intuitive. Marks went on to site an experiment conducted by the town of Drachten, Holland where all traffic signals were removed from local roads. Imagine doing that in Toronto. With roads devoid of any guidance, you might assume local auto repair shops saw a surge in collisions, yet this simply was not the case. In fact, accidents went down, not up. Marks noted that the lack of signals caused drivers to drive more cautiously (perhaps we should try that in Toronto) and create a safer driving environment out of what was thought to be a riskier one. Marks then referenced Jill Fredson, an expert on the terrifying subject of avalanches. Fredson showed that despite advances in mountaineering technology, the number of avalanche fatalities does not decline.

"I have safer gear; therefore, I can do riskier things."

Central bank policy rates have topped out at progressively lower levels during recent tightening cycles. In 2000, Alan Greenspan hiked the federal-funds rate to 6.5%; in 2006 Ben Bernanke was only able to boost it to 5.25%; and by 2018 Jerome Powell perked up the rate to just 2.5%. Despite better tools (data) today's central bankers are engaged in a never-ending contest of constant pursuit, near captures, and repeated escapes.

Rampant inflation can place central banks in the crosshairs of the public. Inflation is apolitical and more broadly understood than other economic problems: it affects everybody whilst unemployment impacts those who want jobs. And maybe this is why financial markets are feeling so glum.

The recent market rout has likely passed for the time being. But if you had any expectations for 2022 to be some, stable easy-going year in the markets, we unfortunately have bad news. Now more than ever is the time to get real about your investments and your expectations.

The MacNicol Investment Team

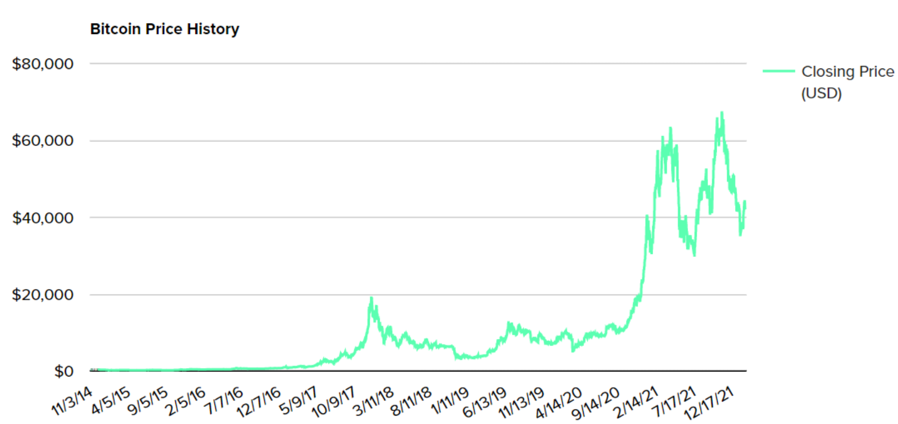
Bitcoin beat down…

One classic philosophical thought experiment metaphysics students are challenged with is whether a tree falling in a forest with no one around to hear it makes any noise. Since digital cryptocurrencies don't really exist, did the group's plunge in late April trigger any sounds? Cryptocurrencies fell badly in April, and we think the real "noise" around this space is veteran investors saying, "I told you so", and it's hard not to hear them. Bitcoin or BTC the cryptocurrency equivalent of a giant sequoia ended April at USD $38,300 and that's a big $7,700 below where it began the month. Ethereum, or ETH the world's other major cryptocurrency, also fell sharply in April. The April losses for BTC and ETH of -16.24% and -15.46% respectively were bad and the admonishment received by younger investors from their elders was like getting a really bad splinter. And this leads to another interesting thought experiment, is it a good time to buy cryptocurrencies? We think so, here's why…

The US Securities and Exchange Commission (SEC) announced that it will almost double the size of its cryptocurrency enforcement division, adding another 20 positions to the Crypto Assets and Cyber Unit while also renaming the group the "Cyber Unit" (I swear…it sounds like sci-fiction but it's true). The total number of staff will rise from 30 to 50, increasing the agency's ability to prosecute securities law violations related to new crypto products. Interest in crypto currency markets has always been high in certain groups, but more broad-based usage in some US States and Latin America has meant fewer people doubt the legitimacy of transacting in something other than a fiat currency.

Unfortunately, this has also meant that smaller investors have become subject to abuses and cyber-related threats, and "scams" create lots of noise.

One scam going around these days is the "rug pull" where scammers solicit investment, promise big returns, and simply abscond with the money — as happened recently when an unknown developer launched a crypto token inspired by the wildly popular Netflix show "Squid Game", in which players risk their lives to dig themselves out of extreme financial debt. The digital currency began trading on the PancakeSwap platform on October 26 at a penny per token, according to crypto-pricing website CoinMarketCap. Not long after the "Squidcoin" hit the market, CoinMarketCap issued a warning to investors that something was not quite right. Someone tore down the Squidcoin website and promotors of the cryptocurrency were long gone. That is why we feel the SEC will be better equipped to protect investors and consumers alike, which will enhance the appeal of recently discount BTC and ETH. BTCs built-in scarcity also has great appeal. Crypto technology is also becoming adopted at a much higher rate than the internet was 25 years ago. And processing power expands daily which impacts "mining" the process by which transactions are validated digitally on the BTC network and added to the blockchain ledger. It is done by solving complex cryptographic hash puzzles to verify blocks of transactions that are updated on the decentralized blockchain ledger. Lastly, halving is *having* an impact too. It's complicated and algorithmic in nature, but halving is a step in the BTC mining process that results in the reward for mining Bitcoin transactions getting cut in half. Halving influences the rate at which new coins enter circulation, which can impact the value of existing BTC holdings. Historically, halvings have correlated with boom-and-bust cycles.



Source: CoinDesk

Recent setbacks in crypto pricing are bust to proponents but a potential boom to more intrepid investors. Volatility is nothing new to BTC and other cryptocurrencies, the question is whether they are new to you.

Behavioral Investing

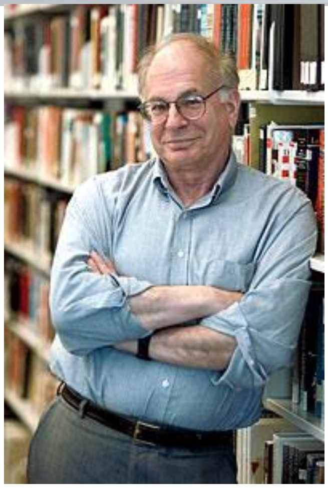
Loss Aversion…

Loss aversion is the tendency to *avoid* throwing in the towel on an investment that just hasn't gone according to plan. In general, people feel pain from losses **more** than they feel joy from gains of equal size. Loss aversion bias typically manifests itself in the financial choices people make and this is especially true among investors. Investors often need an extra incentive to take financial risks that might result in a loss, and often these incentives have to be sizable. A new car, a home renovation, topping up the kids' education fund or simply being viewed as the investment "wizard" in your social circle are all pecuniary and non-pecuniary examples of such incentives.

[Throwing in the towel in boxing stops the pain, but does throwing in the towel when it comes to an investment start the pain?]

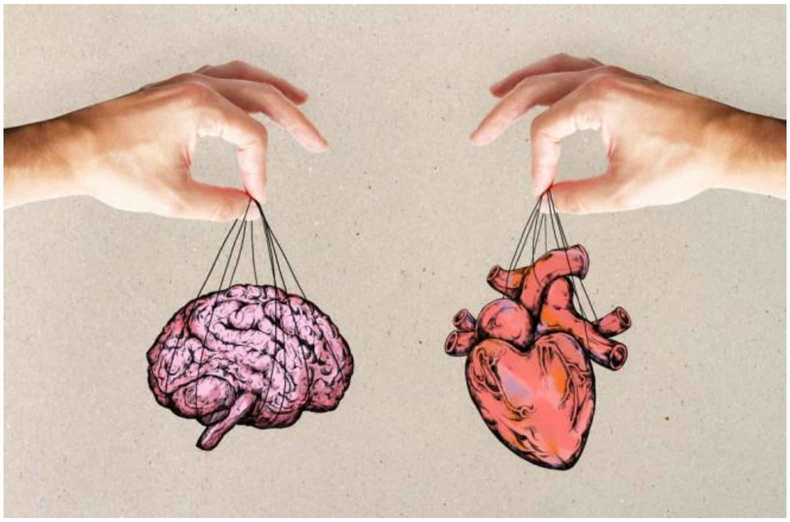
But if you are struggling to grasp the concept of loss aversion, you aren't alone. Each year, dozens of university students struggle with this same concept. Fortunately, Nobel Prize–winning economist Daniel Kahneman devised a clever little way to show how loss aversion plays out in a simple exercise. Kahneman told his students that if a flipped coin lands on tails, they would lose $10. Then he asked them how much they would need to win to make the coin flip worth the risk of losing $10. The answer was usually more than $20 or double the amount of the $10 loss. **Loss aversion** can result in investors avoiding risk, leading to overly conservative portfolios that do not deliver on return goals particularly in an inflationary environment. But it can also lure investors to sell during an overall market set back, which could compromise future gains when markets rebound. Conversely, loss aversion can lead clients to hold on to investments that have declined in value to avoid realizing a loss in their portfolio, even when selling is the prudent decision.

Loss aversion is a major reason why investors underperform the market on average. This disparity can largely be attributed to investors selling stocks out of fear of further losses and consequently missing out on market rebounds.



[Daniel Kahneman is a Professor at the Woodrow Wilson School of Public and International Affairs at Princeton University. Kahneman won the 2002 Nobel Prize in economics or having integrated insights from psychological research into economic science, especially concerning human judgment and decision-making under uncertainty.]

Loss aversion is grounded in the human impulse to avoid pain. If your fighter is losing, throw in the towel. But making financial decisions that are not emotionally charged decisions takes a team effort. By working with MacNicol & Associates Asset Management, we can help you set up rules-based objectives for buying, selling, and rebalancing your portfolio especially during difficult market conditions that require a more systematic approach. For example, agree that you won't sell holdings unless it falls by a certain percentage. We can also help media junkies go on a day trading “cleanse”. Such a financial “diet” will help your portfolio subsist on facts and not become influenced by short-term ups and downs in the market. Doing so will help your heart, your mind and your wallet.



[Loss aversion can tug at your heart strings; just be sure your brain doesn’t get bound by the same restrictions.]