MACNICOL & ASSOCIATES ASSET MANAGEMENT INC.

February 2024

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.

"By the time I became chairman and there was more of a feeling of urgency, there was a willingness to accept more forceful measures to try to deal with the inflation."

- Paul Volcker, 12th Chairman of the US Federal Reserve

The Numbers:

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Index:		**2024 YTD:**
S&P/TSX:		0.77%
NASDAQ:		2.33%
Dow Jones:		2.20%
S&P500:		2.86%
Interest Rates:	**Canada**	**USA**
90-Day T-Bill:	5.00%	5.39%
5-Year Bond:	3.67%	4.28%
10-Year Bond:	3.59%	4.28%
30-Year Bond:	3.43%	4.44%

Economic Data:

- Canada's Consumer Price Index rose 3.4% on a year-over-year basis in December
- The U.S. economy added 353,000 jobs in January, much better than expected
- The FED and BOC held interest rates in place at their January policy meetings
- Global equities started up in 2024 except in China which continues to struggle despite recent stimulus from the gov't
- Magnificent 7 (ex. Tesla) earnings have been extremely bullish over the last month

Valuation Measures: S&P 500 Index

Valuation Measure	**Latest**	**1-year ago**
P/E: Price-to-Earnings	27	23
P/B: Price-to-Book	4.7	3.8
P/S: Price-to-Sales	2.7	2.3
Yield: Dividend Yield	1.4%	1.7%

2023 Calendar Year by Sector: **Jan 31st, 2024**

S&P/TSX Composite	0.77%
NASDAQ	2.33%
Dow Jones Industrials	2.20%
S&P 500	2.86%
Russel 2000 (Small Caps)	0.28%
MSCI ACWI ex. USA	1.60%
Crude Oil Spot (WTI)	3.14%
Gold Bullion ($US/Troy Ounce)	-0.97%
SOX Semiconductor Index	8.44%
VIX Volatility Index	-4.21%

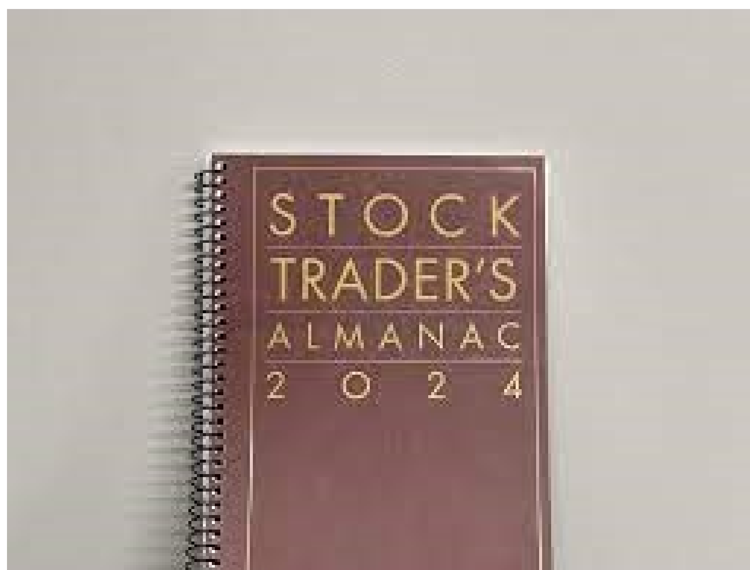
Source: Canaccord Genuity Capital Markets & Thomson Reuters

Foreign Exchange - FX

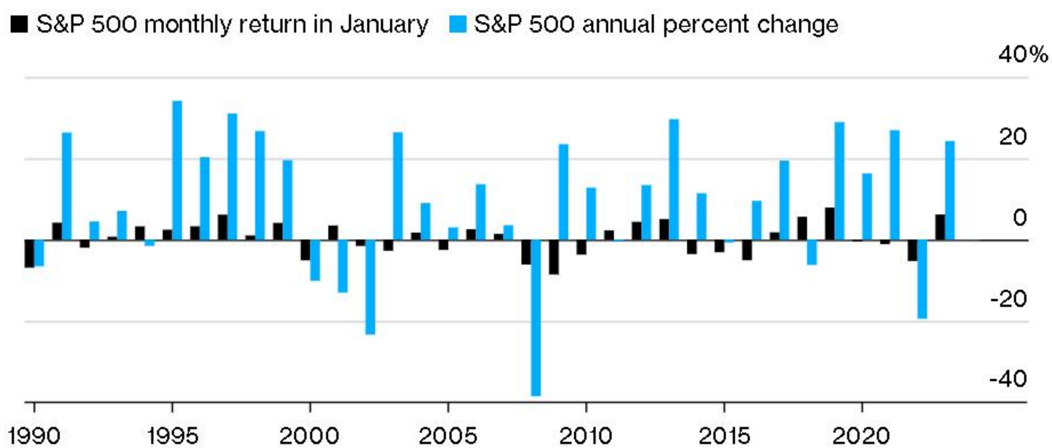
As of FEBRUARY 20, 2024 10:30 AM EST	$5,000	Cdn		
Banks	**Rate**	**Buy USD**	**Cost**	**% Difference from Spot Rate**
CIBC	No Public Rate Posted Online			
Interactive Brokers	1.3589	$3,679	$(18)	-0.5%
Laurentian Bank	No Public Rate Posted Online			
National Bank	1.3840	$3,613	$(85)	-2.3%
Raymond James	1.3612	$3,673	$(24)	-0.7%
Royal Bank	1.3799	$3,623	$(74)	-2.0%
Scotia	1.3853	$3,609	$(88)	-2.4%
TD	1.3884	$3,601	$(96)	-2.7%
Canadian Snowbird	1.3532	$3,695	$(2)	-0.1%

The November-December *affect*…

I am not big on folklore; most Portfolio Managers I would imagine probably aren't. In our line of work, stories can get you far, skepticism even further than that. Wall Street folklore suggests that if stock prices rise in January, they will likely finish the rest of the year on a positive note too. Referred to as the **January Effect**, this basic yet frankly good barometer of how stock prices can perform following a strong start to the year has not only a solid track record but a worldwide following. I studied the January Effect in greater detail about two weeks ago and looking into it was easy. Shortly before embarking on his own trip to Miami, David was kind enough to hand me the latest edition of the **Stock Trader's Almanac**. Like any almanac, the one for Stock Traders is more about record keeping (facts) and less about inferences, though the interferences one can make in this case are pretty good. The 80-year-old gauge on expected stock prices has been right roughly 70% of the time. If stocks do well in January there is more than a two-out-of-three chance that they do well for the year. The question I have, and which I invite you to ponder, is whether January did this all on its own, or, whether the momentum stocks built up in November and December affected the veracity or predictive power of January's numbers?



The MacNicol Investment Team was cautiously optimistic on stocks since mid-November. Inflation began to look like it was on a path to levels more consistent with neutral (versus Hawkish) monetary policy and more and more central bankers became inclined to suggest that their work was done and that no further increases in interest rates were needed to contain inflation. Along the way, be it the media or financial market participants themselves, the implications of the word hold[1] were extended to imply the word cut[2]. Stocks of course rallied quite strongly on the lack of any explicit warnings from the Fed and other central banks that the word hold actually meant hold, and that strength spilled over into the new year…

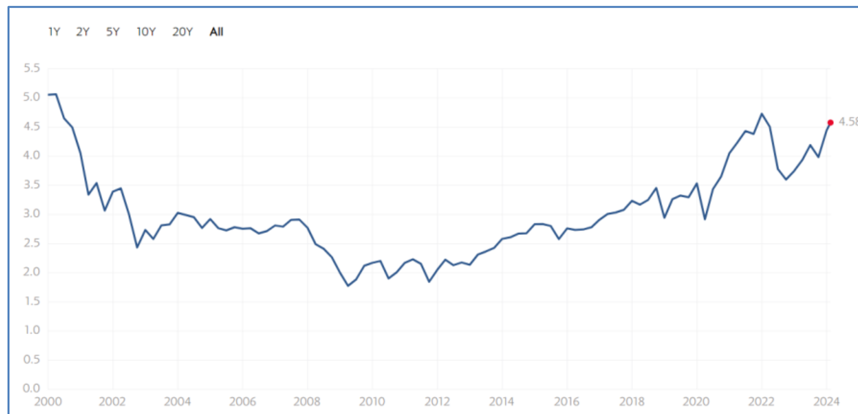


January's performance was in some ways impacted by momentum built up in prior months and also by money spent in prior months too. Government spending, whilst not only unsustainable in the long term, can make reducing interest rates in amounts more difficult to affect. Inflationary pressures tend to be more prevalent in economies with low unemployment and job creation, and that's precisely the sort of environment we see today. The Bureau of Labor Statistics noted that the US unemployment rate was 3.7% for the third month in a row in January and that the number of unemployed people was little changed at 6.1 million. The unemployment rate has been lower before [January and April of 2023] yet the 3.7% print remains well below long-term averages. We also learned that total nonfarm payroll employment rose by 353,000 in January, which was even better than the gain of 333,000 in December and **much better** than the overall average of 255,000 per month for the 2023 calendar year. In January, job gains occurred in professional and business services, health care and retail trade. This is all good news if you are a Politician but a potentially dicey subject if you happen to be a central banker waiting for a window in which to cut rates or worse, an investor with an investment strategy predicated exclusively on near term rate cuts. Maybe that's why one by one, more and more Fed officials have begun to use a different word in their various speeches and interviews and that word is patience. Patience is sort of a funny word because it suggests that interest rate cuts might not happen at the moment many investors feel they might. Patience also has a connection to valuations. At nearly 4.6 times its own book value, the S&P500 is approaching valuations last seen during the fourth quarter of 1999, and the first two quarters of 2000. That was almost 24 years ago…

[1] One of the ways Merriam Webster defines the transitive verb "hold" as follows: *to prevent from some action*.

[2] One of the ways Merriam Webster defines the transitive verb “cut” as follows: *to reduce in amount.*

S&P 500 Price-to-book ratio…



Stocks could indeed climb higher, remember the January Effect has a track record most consistent than that of many investors. However, one cannot help but get the sense that if investors have a correction coming their way in 2024 it will occur from a now more expensive and precarious recipe. Whenever we are confounded by a head on collision involving bullish and bearish data, the MacNicol Investment Team often turns to technical analysis. Recall that technical analysis attempts to answer the question of what not why. Technicians don’t care why stocks are going higher (or lower) they care about what various technical attributes of the market have to say about the likely future progress of markets. Technically, the S&P 500 is in unchartered territory but some indicators continue to support the likelihood of gains during late February and March. Again, stocks had a very strong run late last year, and last year in general. The only blemish concerning 2023 occurred from July 1st to October 1st, when – if anything – concerns as to overall market liquidity dragged performance lower. But what that achieved was a situation where less loved areas of the market had the opportunity to play catch up once the trajectory of monetary policy became clear. With a lot of the opacity cleared, we felt more comfortable about our ability to grasp the expected return potential for companies that lacked the sort of poetic beauty of the “Magnificent” (Malevolent) 7. These companies include financial services stocks, particularly those with effective cost cutting/margin expansion potential such as Capital One and Allied Financial and even brokerages such as Charles Schwab. Canadian stalwarts like Royal Bank and TD are currently under review and “on our radar” but not yet at a position where we feel confident about their future earnings growth. Another area of interest to our Team is transportation stocks such as Canadian Pacific Railway and Union Pacific, who may benefit from an increase in freight volumes later in the year and the associated uptick in earnings per share growth. Interest sensitive stocks such as pipelines, telephone companies and utilities are something we referenced last year. While we feel that more near term labor market data in the United States diminishes the likelihood of large and frequent cuts to US interest rates, the Canadian monetary policy environment seems one that is easier for us to feel bullish about. With that said, valuations to have an impact on our views of the telecommunication space, with shares in companies like Verizon trading at noticeable cheaper multiples than Canadian counterparts. Copper and oil also seem poised to recover with the prospects of increased demand in the back half of the year. Whether stocks finish higher or lower this year is at this point anyone’s guess. The MacNicol Investment Team is comforted by our measurable amount of portfolio insurance and by the work we do in-house in things like sector allocation and the careful selection of individual stocks. Still, we believe that although stocks could go higher from here, the 2024 edition of the January Effect will be defined by the things that January was affected by rather than the things January effected itself.

Land of the rising cryptocurrency:
how sentiment for some fiat currencies is creating a heatwave after the "cryptowinter"

We sure like to talk about cryptocurrencies here at MacNicol don't we? As you know, our forays into the world of digital currencies have been tangential, indirect and less frequent than the articles we use to opine on about in the space. We have never owned a single Bitcoin, Ether, or any other digital currency. Instead, we have opted to participate in the space peripherally with others taking more of the risk themselves. The small handful of financings we did participate in functioned to create the underlying machinery that mass produced a product or security that in a long about way was tied to Bitcoin or Ether. But don't think of us as being wishy washy or unsophisticated. Often, it is better to be a live chicken than a dead hero.

A heroic rise poised for a spectacular failure?

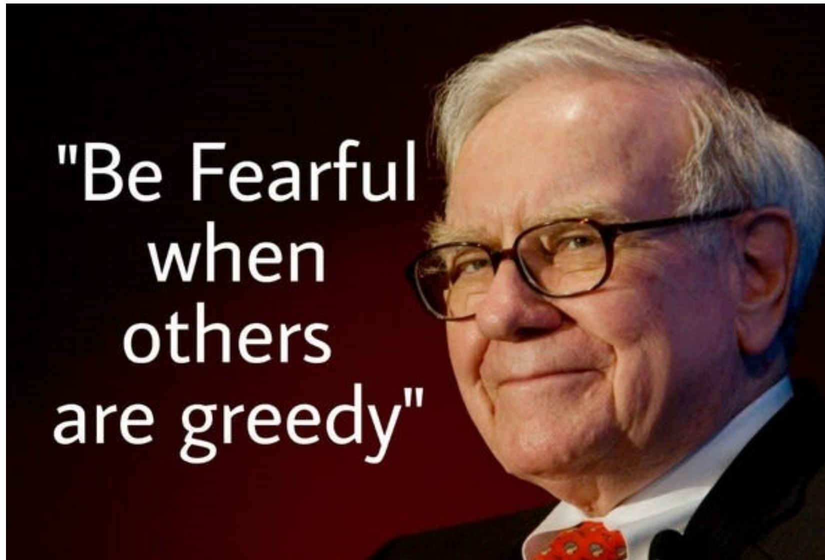
We have indeed been talking crypto of late and our last missive stated that regulation was good for the space because regulation was articulation: clear credibility made more investors likely to invest in the space because more consumers and business would use digital currencies in everyday commerce. Yet many of you have (correctly) pointed out Bitcoin's heroic rise out of the ashes of the "cryptowinter" and asked us for our thoughts on the matter. The king of all digital currencies certainly looks royal following an extremely robust pop thus far in February. Bitcoin's recent boom builds on earlier ascension in October and November of last year. The "crypto winter" is definitely over, but with Bitcoin now commanding over $70,000 Canadian dollars what might we say to one of those people who openly scoffs at the idea of decentralized currencies yet secretly had a digital wallet loaded with the stuff some place no one can see? Well, I suppose we would say the following: whatever your perceptions are about Bitcoin and other cryptos, they should be exactly the inverse of your perceptions about fiat currencies in general and the Japanese yen in particular. You see the biggest currency pair trades in the world is Yen/BTC. Japan's recent economic challenges, mainly: a) a recession that began last year, b) continued Yen printing by the Bank of Japan and c) the dawning of a new wave of inflation have made the Yen exposure risky. Fiat currencies like the Yen, but also the US Dollar, the CAD, the Euro and others are not backed by physical assets. While the US Federal Reserve and Bank of Canada raised rates forcefully in 2022 and 2023 to tame inflation, the Bank of Japan kept interest rates at zero and continued flooding the market with Yen. Japan's core rate of inflation, which excludes more ornery components like food and fuel rose more than 3% last year representing the biggest gain since 1982.

Suffice it to say, even if I was asked to lead the Bank of Japan (right now) I would probably say no thank-you…

[Bank of Japan Governor Kazuo Ueda is under the sword to lessen weakness in the Japanese Yen, which won't be easy. An interest rate spread between Japan and the United States, sluggish domestic demand and inflation mean Ueda has his work cut out for him. The bane of Ueda's existence though is your chance to potentially cash in on a lucrative move in Bitcoin and other digital currencies.]

So, what do we believe is the likely course for Bitcoin and other digital currencies going forward? Well from a regulatory perspective, better legal clarity regarding digital assets is of course a broad based, unanimously bullish trend. Whether you are based in Zurich, Warsaw, Toronto, Toledo, Madrid, Belfast or Bologna the trading and use of digital currencies is today faster and easier than ever. And knowing that someone is indeed finally watching is a source of comfort and confidence. As it pertains to fiat currencies generally, the answer to that question is mixed. Some fiat currencies are more liked than others. But as it pertains to the Yen, specifically, we think the answer there is very clear. The Yen tanked against the American dollar last year and it is down a further 6% this year. Bitcoin will certainly trade at a premium in the market for Japanese Yen unless Mr. Ueda and his staff are able to exit his country from uber easy monetary policy. Could Bitcoin some day be worth $100,000 Canadian dollars? We think the answer to that is yes.

Behavioral Investing: greed, fear and the old man who has walloped the stock market for decades…



Technical indicators of stock market activity are a useful mental health check of not only stocks in general but whether the way you, as an investor, might be feeling about them. With the S&P 500 officially through the psychologically important 5000-point level, I thought it might be constructive to point out, and interpret key technical levels for you, and then have you do your own self-assessment. If you agree with any of the data present here, it is possible that you are feeling just a little bit greedy – and therefore – potentially expecting too much from the market for the rest of the year. Remember that there is no one indicator, technical or sentimental, that should overwhelm your thinking about where the stocks sit at any point in time. Being lulled into a false sense of security about a single "magic" indicator is fraught with risk and sure to compound your stress rather than alleviate it.

Let's begin at the giant landfill site for bonds known as the "junk" bond market. Junk bonds are issued by companies with weak financials, poor revenues, or a shirking share of a particular market. As a result, compared to investment grade bonds, junk bonds carry a high risk of default, and you can use market-based information about how junk bonds are trading, to arrive at a view on overall risk appetite, and subsequently (by triangulating with the other sources of information) a conclusive on greed or fear. Junk bond yields, the return you get buy making an investment, dip when prices go up, and this is exactly the same for all bonds. If fixed income investors are starved for junk bonds yields will drop. Likewise, yields on junk bonds rise when investors are selling, and that figure can be compared to the yield on safer government bonds to arrive at a spread or risk gap. A wider spread between government bonds and junk bonds shows that caution is in the wind. For the past year, the yield spread between junk bonds and government bonds has been falling and we would suggest that this is definitely a sign of greed. More colloquially, that spread compression in yields indicates that – by and large – investors are engorging their portfolios with progressively riskier securities whist being seemingly unconcerned with the fact that government bonds are dramatically safer than junk bonds.

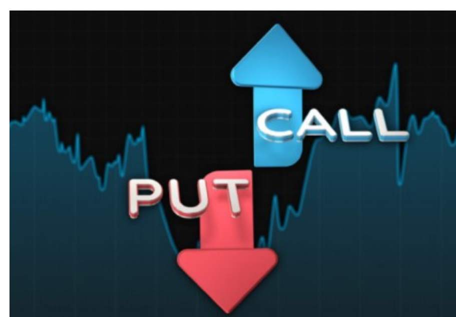
Next up is a basic comparison of stocks to bonds. Andrew Adams, a noted technical analyst we follow here at the firm, likes to compare the movement of the S&P 500 against the total US bond market. Two ETFs (SPX and USB) help make this analysis easier to visualize and the interpretation is quite simple. Stocks are thought to be riskier than bonds because they represent an investment in an asset instead of a lien *on* an asset.

But the expected returns associated with investing in stocks for the long term are greater. Note however that bonds can outperform stocks over short periods, and this is especially true in situations where demand for "safe haven" assets is high.

But that certainly isn't the case in the recent past. Stocks have made quick work of bonds since 2024 began, and from an asset allocation perspective greed is certainly in the air.

The CBOE Volatility Index, known as the "VIX" is a measurement we quite in each edition of this publication and for good reason. The VIX is a barometer of anticipated price movements in S&P 500 options over the next 30 days. In general, the VIX drops off when the broader stock market rallies and spikes higher whenever stocks plummet. Perhaps that analysis is overly simplistic, so the key is to look at the VIX over time. The VIX tends to be lower in bull markets and elevated when the bears are in control. Once again, we quote VIX on the very first page of each edition of this commentary and though the measure popped up slightly a week or two ago, readings below 15 are generally regarded as low to moderate. Taking into account both historical trends in the VIX as well as near term spikes, one can best frame this indicator as inconclusive, which is to say neither greedy nor fearful.

Building on data from the options market, let's next take a look at the ratio of two specific kinds of options contracts to see whether they have anything to say.



I actually hold a specialized designation in derivatives but the gist of how they work is that options are contracts. The contracts give investors the right to buy or sell stocks at specified prices up to a specified date. Beyond that date, the options contracts themselves expire as worthless. Puts options are contracts to sell stock while calls options are contracts to buy stock.

Whenever the ratio of put buying to call buying grows, it is usually a sign investors are becoming anxious about stock prices, and worried that a possible correction might be near. A ratio above 1 is considered bearish and today's barely 0.8 ratio in the measurement confirms greed inasmuch as investors do not seem to be especially concerned about a crash in the stock market.

Whenever you look at the stock market, you always want to be mindful about whether the index you are looking at is capitalization weighted (i.e. are a small handful of gigantic companies "pushing" the index higher or are most stocks participating in the rally?). Amazon, Apple, Google and Nvidia are not the entire market. The market is made up of stock in thousands of companies and on any given day, investors are busily buying and selling them and so a good measurement of the amount, or volume, of shares on the NYSE that are rising compared to the number of shares that are falling is the McClellan Volume Summation Index. A low or even negative number is bearish, however, as it pertains to where the index stands today is that it would be in the greedy range but not extremely so.

Building on the McClellan Volume Summation Index is a measure of stock price vigor. Since a few big stocks such as the ones we reference above can exceed returns for the entire stock market it is important to also know how many stocks are doing well versus those that are struggling. This shows the number of stocks on the NYSE at 52-week highs compared to those at 52-week lows. When there are many more highs than lows, that's a bullish sign and signals greed and excluding the malaise of February 13th the number of stocks making new highs on the NSYE is very high and signals excessive greed.

Finally, it is always helpful to compare stock prices today to where they have been over the recent past. When the S&P 500 is above its moving or rolling average of the prior 120 trading days, that's a sign of positive momentum, and we talked about how momentum from late last year spilled into trading activity in 2024. At 5000 points, the S&P 500 is now (well) above its 120-day moving average of just over 4,550. This nearly 500-point gap is very big and a clear signal of extreme greed from the perspective of market momentum.

A S&P 500 index over 5000 points is what many market observers describe as unchartered territory. Yet, technicians can indeed use charts of various indications of market sentiment to map out a likely path forward. As an investor, the informational value in any one of these indicators is low and this is why it is crucial to draw out an investment strategy that incorporates many indicators against your own personal feelings. And remember, feelings should really have no bearing on your investment strategy, after all investing is a business decision. We began this article with a well-known investment quote from the great Warren Buffett. We are big fans of Warren Buffett but even bigger fans of the investors who trust us with their capital. If you ever feel like your own personal opinion on the market doesn't quite jive with the indicators we discussed here or elsewhere in our MacNicol publications, just give us at call or check us out online at www.macnicolasset.com.

The MacNicol Investment Team

Firm Wide News:

Members of the MacNicol Investment Team were in South Florida conducting onsite due diligence visits with real estate sponsors at 13th Floor Investments. Our team toured a residential single family home development in Fort Lauderdale, and we also toured a gigantic (700 unit) multifamily residential build in Delray Beach. Data, including video and images of the properties along with financial statements were retained by our team and we were pleased with the answers provided to our questions during the visits.

MacNicol & Associates Asset Management is issuing a final reminder that the 2023 RRSP contribution deadline actually falls on **February 29th of 2024**. The maximum deduction limit for 2023 RRSP room is $30,780 which would require earned income of approximately $170,000 in 2022, or the carrying forward of previous year's unused contribution room. Please reach out to us to ensure you are getting the maximum benefit from your RRSPs.

MAAM would also like to point out that with the transition to 2024 you are now able to add $7,000 to your TFSA (Tax Free Savings Account) plus any withdrawals made in the previous year.

Finally, for families with children under the age of 18, those individuals can also make a $2,500 contribution per child to a RESP (Registered Education Savings Plan) to maximize the 20% CESG Grant of up to $500 per child.