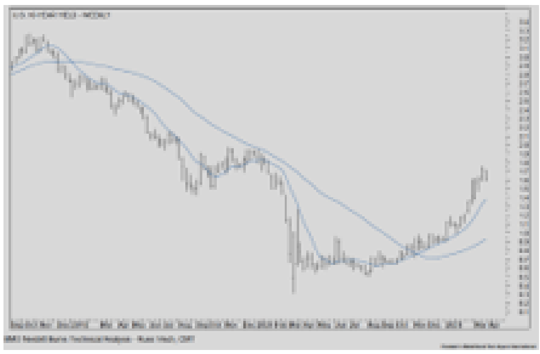
Portfolio Management
Monthly update

March 2021

Bond Yields Rising on Reopening

Weekly Chart U.S. 10-year yield
Source: Thomson Reuters as of Mar 24, 2021



Highlights

- **Easy money for a long time, but structural limits to inflation**
- **Rotation to reopening stocks continues. The pullback from extended levels giving buying opportunity**
- **Broader based earnings growth taking hold. Earnings will matter again**
- **•Industrials have lagged and strong growth is expected**

Easy Money, the Stock Market & Inflation

Some are concerned that the big jump in the US 10-year bond yield to 1.7% could derail stock markets. Brian Belski makes the following points in his March 19 strategy comments:

A move to 2% 10-year Treasury Yields is now massively consensus – just like a bear market correction due to a "blue wave" was supposed to happen, let alone calls for the next great depression that were dominating headlines a year ago this week. **Take-Away: Consensus is usually wrong.**

When examining S&P 500 performance into and out of historically low interest rate troughs, current trends are only slighter hotter than the prior two episodes. **Take-Away: We have seen this movie before.** The bottom for US 10-year yields was .82% in the July 2016 trough & peaked at 1.65% 15 months later with stocks much higher. While stocks may sell off because rising rates, prior trends suggest that the S&P 500 will finish the year at higher levels, should rates continue to rise. Take-Away: ***Rates typically go up because the outlook is improving – that's a good thing***.

Fed Reserve Chairman Powell recent statements were very adamant about maintaining stimulus and low rates. He won't increase rates or reduce quantitative easing until inflation is above 2% & expected to rise, employment is full, and the economy is running much closer to capacity. Easy money is here to stay. There are still long-term barriers to runaway inflation and rising interest rates: the aging population in the Western world, excess production capacity globally, especially in China and most importantly a massive debt overhang. Imagine the carnage a 2% increase in mortgage rates would do to real estate prices for example.

COVID update: Europe has been struggling getting vaccines to the public. They have a shortage of vaccines despite production capacity. Their usual bureaucratic dithering and fighting on price has hurt. Market Watch noted on March 22 that the Astra Zeneca Vaccine showed strong results in a US trial & the Europeans will start using it again.

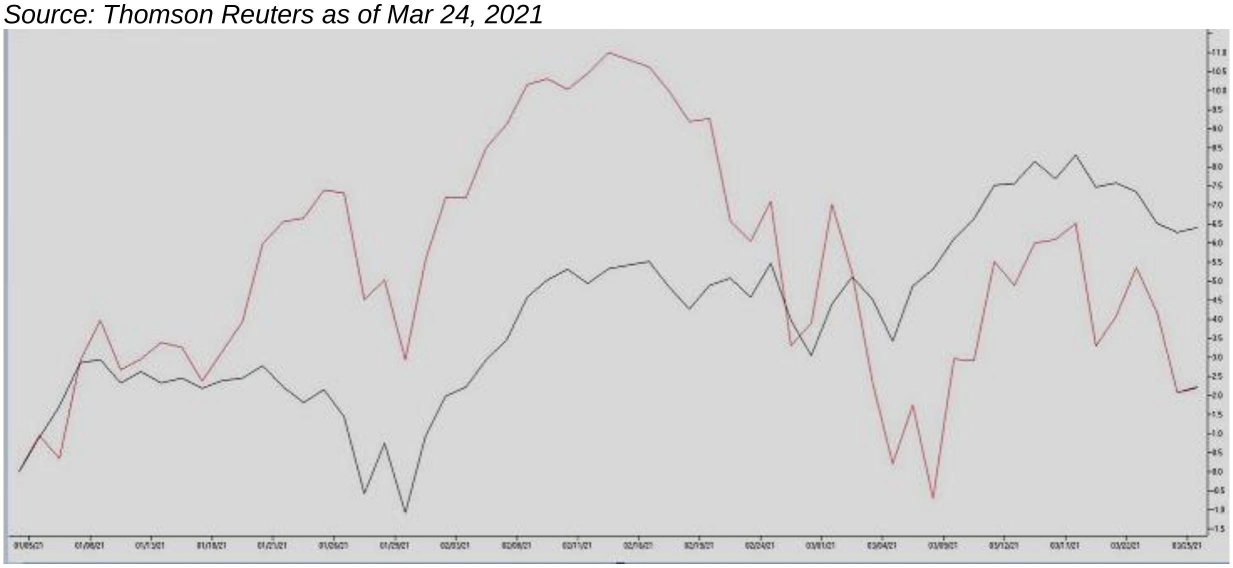
JP Morgan noted in their Mar 21 Asia Dashboard that China has reported no Covid cases in a month, domestic travel restrictions have been lifted and vaccinations are progressing well. The US has vaccinated 15% of it's population vs 12% last week and estimates all eligible should be inoculated by July. Canada lags badly with little domestic pharma production since Trudeau's anti-business policies encouraged them to leave a few years ago.

Economic growth forecasts are rising: Ned Davis' Mar 18 research upgraded global GDP growth estimates for 2021 to 6.1 from 5.8%, largely due to improving US GDP growth, which they now forecast at 6.5-7%. Expectations for the U.S., China, India & Germany have been rising, while growth projections for France, Italy & Brazil are lower. On March 19 BMONB Economics also bumped up their 2021 real GDP growth estimate to 6.5%-7.0% from 4.6% driven by US stimulus & success in the vaccine roll out. **There will likely be a consumption boom in restaurants, travel etc.**

Sector rotation has been dramatic. High growth technology and the stay at home stocks have struggled, while re-opening stocks and those which benefit from high rates have boomed. The TSX in finally doing well, with its heavy weight in cyclicals and financials.

Nasdaq vs TSX

Source: Thomson Reuters as of Mar 24, 2021



The steeper yield curve pushed up US banks 24% & Canadian 14%. Canadian Insurance companies such as Great West Life and Sun Life offer strong yields and reasonable growth. We would look for somewhat of a pullback from these big moves before buying more.

Big pullbacks in technology and other stay at home stocks offer some interesting buy points once they have based a little longer. We bought Costco & Visa recently on a pullback. Buyers should stick with the best companies, such as Nvidia, Microsoft and Alphabet. Those more adventurous could look at companies like Teledoc, Pinterest and Draft Kings. Be careful of excessive valuations however, since rising rates and a broader choice of sectors with earnings growth limit the prices the market will pay.

We have been buying Fidelity Canadian Opportunities fund and XEI Canadian high yield ETF to take advantage of improving prospects for Canada, which benefits from the expected improvement in global trade more than the U.S. The downtrodden energy stocks have had a great move, and although they need a pullback, they have more room to rise. Fossil fuel use has many years yet.

The big push for alternative energy is a long-term growth engine for copper, especially given the limited spending to increase production in the last few years. Stocks like Ivanhoe and Freeport have done very well and are buys on pullbacks.

Belski's recent strategy update notes that the key to 2021 market positioning is a transition to normal as earnings growth becomes much less concentrated. Q4 earnings were better than expected & 2021 growth will likely blow past expectations. Companies have adapted to lower volumes, so supply chain issues will cause problems, but productivity growth should be massive. Companies are utilizing technology better to reduce labour requirements and will only bring the best people back as needed, reducing costs. Wage growth will likely be subdued as well.

President Biden's $2 Trillion clean energy & infrastructure spending initiative should boost industrials. Belski particularly likes them & some of his Canadian industrial picks are Air Canada, Boyd Group, CNR & CP, Finning, Toromont, Thomson Reuters and Waste Connections. In the U.S. we recently purchased Borg Warner, which has lagged Linamar & Magna. Other Interesting U.S. industrials are Boeing, Eaton, 3M, Sherwin Williams, & Union Pacific Rail.

Regards,

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