ROYDS REPORT

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SOUNDBITES IN THIS NEWSLETTER

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China's Re-Opening

According to Invesco's Global Market Strategist on Apr 20, 2020, about 99% of workers at large companies and 77% of workers in small or medium sized companies in China had returned to work. In one week the important Purchasing Managers Index (PMI) that fell to 35 in March was back up to 52. Anything above 50 indicates that the purchasing managers expect to be ordering more supplies for their companies than in the last year. So that shows business expects a fast restart to their businesses. Traffic congestion and coal use have bounced back strongly in China. Let's hope the rest of the world can have such a strong start to our recovery.

Oil – Remember June 2008, when you had to mortgage your home to fill up your gas tank, because oil was selling for over $165/barrel? If you had bought barrels of West Texas Crude (WTC) oil "on paper" in Jan 2020 at over $50/barrel for delivery Apr 21, hoping to sell the oil for more money them, before you had to take physical possession, you might have been one of the traders panicking on Apr 20. The price of oil was at the lowest point in 23 years, because no refineries needed oil. So, you couldn't sell your oil, AND you couldn't arrange for it to go into storage to sell later either, because there was no storage room left in Oklahoma (the delivery point). **Oil traders were paying people up to $40/barrel to take WTC oil off their hands**. That's a first. Oil was selling for a substantially negative price. It points out how severe the oil glut is in the world with demand being down, while so many people aren't commuting to work and so much of industry is idled. This is at the same time as Russia and Saudi Arabia are flooding the market with oil at cheap prices. It points out how risky commodity trading can be, and the oil industry in general. Some of our fund managers have remarked on how historically cheap the oil companies are, and that they are sure that many of the companies which survive this period of the oil war and COVID will be worth lots more years from now. They have also said that it would be like trying to catch a falling knife to buy them now. Maybe later they will pick up a "bargain", when it's clear which companies will survive, and that an oil company in North America can make money again. Even then, our investment style doesn't really lend itself to gambling with commodity stocks. So, most of our fund managers never hold commodities and say they can find lots of better things to buy. We all may need to look at oil differently going forward. I've read projections that peak oil demand may happen as early as 2025, and that after that the world will start using less, as alternative energy sources become more and more important.

Markets in General

As I write this, markets have recovered a lot from the bottom. Per the chart below, the main American, the main Canadian and the global small/mid size stock index fell between 34% and 40 from their peak on Feb 19 or 20 to the bottom of the market to date, Mar 23, 2020. The market is down way, way less now.

	Drop from High	Current Amt Below Peak	YTD Drop
S&P 500	34%	15%	12%
TSX Composite	37.5%	19%	15%
Russell 2000	40%	27%	23%

Two points on this. First, our managers almost all fell less than their respective indices and better yet have been recovering faster. <u>Last week the US market recovered about 1.7%, but our most used US funds recovered 4-6%.</u> That's what active management and the GARP (Growth At a Reasonable Price) style can do, and has done in past downturns. Secondly, the recovery in the US market, and to a lesser extent the Canadian market, is a skewed. Much of the recovery has been concentrated in the FAANG stocks (Facebook, Apple, Amazon, Netflix and Google) and Shopify (now Canada's second most valuable stock, just behind RBC).

Bloomberg Economics estimated on Apr 27, 2020 that the global economy would end up being down 6% this year, 6.4% in the US, only 4% in Japan and 8.1% in Europe. If stimulus from governments is insufficient, output could drop more. China is still expected to expand production over 2019, but at a much slower rate than in past recent years. This economic contraction is terrible, and it could be worse, but maybe it's not as much as some anticipated.

April Relief? – As we have been looking at portfolios in April, we've seen some nice progress in recovery back closer to Jan 1 portfolio values. Analysts are divided on whether this means that investors thought the market had been overly punished, especially given the $10 Trillion plus that governments around the world are using to relieve the impact of the pandemic, or whether this is just a bear rally/ dead cat bounce, that will be short-lived. Some think that when second quarter earnings reports come out in July, markets will realize they were too optimistic, and the market will go back down to where it was around Mar 23. No one knows who is right. Even if the bears are right, and the market does re-test the bottom (that is, it goes back to its low), it doesn't change what we have to do now. We need to stay the course. If we risk getting out of the market, with the idea that we would buy back in when the market goes down, we are risking missing the upside, if the market doesn't go back to its low. And, if we don't time it just right, for when to get back in the market, we could miss a lot of the recovery. **Since Feb 19, 2020, the general high of the market, we have seen 7 of the 30 largest one-day market gains of the last 30 yrs**. Anyone who panicked, and got out of the market, missed those, including the biggest one day gain in history. (We're glad to say that none of our clients panicked and sold out.) So, just **don't be**

surprised if the market goes back down again, before it starts the sustained, but not straight-line, climb back to previous higher levels.

It's also important to realize that our fund managers don't hold the same basket of stocks as the market. Our managers don't have airlines, energy companies, restaurant chains, hotels, cruise lines etc and are severely, if not totally, devoid of banks, especially Canadian banks. Our fund managers are continuing to hold or adding companies which are essential, well capitalized (so not likely to run out of money before the economy is back on its feet) and are selling for cheap prices. A couple of managers have even found companies they could buy for less than the cost of the net cash or liquid assets the company has. Most of our managers relish volatile markets like we have been experiencing, because it gives them a chance to buy companies that others are willing to sell cheaply. In the end it usually allows our Growth At A Reasonable Price style to outperform the general market.

If you are afraid that your portfolio might never recover, have a look at **what the most common stocks are that are held in the funds we use**. It's hard to imagine that the world won't need these companies and that these companies won't make money and increase in value in the future:

- **Microsoft** – this company grew its cloud computing business by 770% in March 2020 thanks to the pandemic. It moved to a subscription model for selling much of its software, which is a more profitable way that selling it outright, like in the past.
- **Nestle** – produces not only coffee, chocolate, Delissio, Stouffer, Perrier, Purina, and Haagen Dazs, but 2000 other brands
- **Johsnon & Johnson** – makes Band-Aid, Benedryl, Aveeno, Lactaid, Tylenol, Visine, Reactine, Nicorette, Neutragena, Listerine, medical devices and pharmaceuticals including a potential COVID19 drug in trial
- **TJX** – operates discount stores that often do better than other retailers in hard financial times with stores like Winners, Homesense, Marshalls, TJ Maxx and others
- **Roche** – manufactures a whole range of pharmaceuticals and diagnostic products, including COVID19 test machines
- **Becton, Dickinson** – a global medication, diagnostic too, dental supply and surgical equipment manufacturer
- **UnitedHealth Group** – the largest health insurance company in the US that cut premiums for its subscribers but is still making more money than ever since it doesn't have to pay for elective surgery, dental hygiene etc
- **Mastercard and Visa** – both growing their businesses in emerging markets, where people only use credit cards 1/19th as much as Canadians so far. Global sales are down right now, but more people are getting used to using plastic instead of cash, which could carry over after COVID passes. And charge cards will benefit when pent up demand is unleashed.
- **Sherwin Williams** – a paint and industrial coating company
- **Taiwan Semiconductor** – the largest independent semi-conductor company whose products are used in just about every kind of high end electronic equipment
- **Diageo** – global leader in alcoholic beverages with over 200 brands
- **Unilever** – some of its many brands are Axe, Degree, Dove, St Ives, TreSemme, Vaseline, Q-Tips, Knorr, Lipton, Hellmans, Liptons, Ben & Jerry's and Breyer's
- **Alphabet (parent company of Google)** – besides the search engine we all know (and love), Google has a cloud computing division, Google Maps, a translation service, Gmail, Google Calendar, owns YouTube, is the leader in selling on-line advertising and has its fingers in many other pies

- **CME** – the Chicago Mercantile Exchange, the commodities and options trading centre for North America which should be doing great business during recent markets since market trading activity is quintuple normal
- **Nike** – sportswear and shoes
- **Moody's** – one of two leading bond credit rating agencies. It's able to raise it's prices by 8% every year
- **Apple** – computers, phones, iPads, watches, Apple TV, Apple Music etc
- F**acebook** – Facebook, Instagram, WhatsApp and more than 70 other companies
- **Stryker, Roper Technologies, Danaher, Thermo Fischer Scientific** – all companies in the medical field producing diabetic supplies, pharmaceutical testing equipment, hospital beds, artificial hips, drugs etc.
- **Pepsi** – Lays, Gatorade, Doritos, Tropicana, Lipton Teas, Quaker Oats, Mountain Dew etc.

Your portfolio holds some of these companies and many other great businesses that will survive the COVID shutdown and should resume making money, if they're not still doing so during COVID. The next time you're worried about your portfolio, ask yourself if you think any of these companies are in trouble or whether you'd like to share in their profits going forward.

Investing Rationally, Everything Else is Gambling – There's a great newsletter on the public part of Edgepointwealth.com's website, that talks about why they added certain stocks to their funds, and which talks about how the impact of a company being shut down even for many months has less impact on a company's value than people think. It describes how to unemotionally determine valuations, which is exactly what we pay our managers to figure out. This newsletter is also a great way to get insight into how professional value fund managers think and into the research that has to be done to value a company, which is generally beyond the capability of individual investors. If you go to that website, click on the Insight heading along the top and on the menu that drops down, click on Simply-Put. Then choose the article "Second-Level Thinking In Periods Of Market Extremes.

We'll give you one example of why it's so much harder to figure out which companies' profits are safe, and why extensive analysis and research is needed. A company that's involved in waste management might seem pretty recession and pandemic proof. Every community needs garbage disposal and recycling/dump management. And such companies have contracts with cities and counties that don't stop paying just because of a pandemic or recession. Indeed, some of our fund managers did like this industry before the pandemic. However, during the pandemic, people started doing more on-line shopping and getting a lot more deliveries in cardboard boxes. This had implications that one might not have expected. This increase in cardboard boxes has caused a 60% reduction in the price per ton of recycled paper. Waste management rely on selling the cardboard to offset the cost of picking it up. This is really hurting their bottom line. It is however helping the makers of toilet paper save on one of their raw materials. Who knew?

Time on Your Hands Because You're Home from Work?– A friend of ours said he'd seen every movie on Netflix and that he's running out of ways to spend his time at home. If you have a bit of spare time during these self-quarantining times, why not work on your budget. If you think you need a better emergency reserve for the next time a financial shock of some sort happens, then you might need to reassess how you spend your money and how much you allocate to your future. So in the future you can build a bigger emergency reserve. Or, if you are nearing retirement it's a good time to add up what you actually spend according to your banking and credit card records. In order to know if you have enough money to retire on, you need to have a firm idea about how much income you need to sustain your desired lifestyle in retirement. You have time now to look at your pattern of spending, what your real needs are and figure out what income you'll need in retirement.

I hear that a lot of people are re-evaluating how they have been living and spending. Some say more people will resist wearing ties, belts, colouring their hair, dressing up for work, going into an office to work, or striving to put on a show of perfection. How people used to spend their money may change. People may look at wants versus needs differently. This is a good time to see what you really have to spend and **to look at what you actually need to be happ**y.

If you are all of a sudden not working, this is also a good time to plan for how you'll handle retirement emotionally, when you get there. Are you happy without your normal routine, co-workers and the work itself? Once you're tired of watching or playing things on your computer and TV, and you've tidied all your cupboards, are your bored? What are you missing about work? If you were to retire, what would you need in your life, that you aren't getting during COVID19, to keep you happy. It is the social interaction, the schedule, the sense of accomplishment, the challenge, the identity your get from your work or something else that you miss (aside from the paycheque)? Before you retire, you need to find activities that will provide you with the same satisfactions in retirement that you get from work. Whether it's hobbies, friends, volunteering or something else, you need to get it in place you retire.

New Way of Seeing the World – Jeff Rubin, the former chief strategist at CIBC World Markets has an upcoming book from which an excerpt was published in the Apr 25, 2020 Globe & Mail. There were a few memorable lines from it that we wanted to share. "Outsourcing is how yesterday's global economy worked." "What only yesterday were universally recognized accomplishments of globalization have suddenly become its greatest failures." "As the much-beleaguered middle class of North American might note, past pandemics from the Black Plague to the Spanish flu all boosted wages in decades that followed. Of course, in those cases, it was the decimation of the population that made the supply of labour scarce and its price dear." So what Trump didn't accomplish with his 30% import tariffs, the pandemic may have accomplished – the death/decline of globalization. And maybe going forward some of the lower paid of our essential workers will be better compensated, so there's not such a disparity between top and bottom wages in Canada.

Inflation or Deflation on its Way? – One would have thought that all the money the US is effectively printing for its bailout ($2 Trillion+) would cause inflation (or $10+ Trillion for the world). After all, more dollars would be chasing the same amount of goods and property in the world, so prices should go up as dollars compete for assets. On the other hand the steep decrease in the price of oil and the potential long-term decline in demand for it, as people work from home more, should keep the price of oil down from last year's levels and that is deflationary. And, the drop in interest rates is also deflationary. Stephen Poloz, the Bank of Canada Governor, says no one can predict if we are going to see inflation or deflation going forward. Inflation really helps borrowers, because they pay their debt off later in inflated dollars. Deflation leads to people deferring their spending because prices will be cheaper next month, and then cheaper again the month after. No one has learned how to solve deflation, a condition that Japan has been in for 20 yrs. (Source: Globe & Mail Apr 25, 2020)

Fixing Your Finances, Without Excuses - A horrendous number of people in North America (at least 27 Million) have lost their employment, at least temporarily, or have seen their businesses shut down virtually without warning. This is unprecedented in our lifetimes, and governments are busy announcing all sorts of safety nets to help affected individuals and businesses to survive financially. We're not talking about a comfortable ride, by any means. We're talking about scraping through, with a financial mess left to clean up afterwards, as the price to pay for containing COVID19. So, a lot of people will use up any emergency reserve they had and may build up debt as well, before their normal paycheques return. And the people, who never had an emergency reserve and had significant debt before the pandemic, will be in an even worse financial situation than before. I hope this crisis will help the latter people resolve to have some savings in place and not have credit card debt or any kind of heavy debt, before we run into another crisis or even a regular recession.

Back on January 7, 2020, the Globe & Mail published an article which was pretty blunt, and true, and which may help some people think differently about finding cash flow to pay down debt and to save. Here are the main points and advice from the article:

- If you think you don't have money to save or to pay down debt with, recognize that as an excuse. You do have the money. You've just decided to spend it on something else.
- If your cell bill came in $50 higher than usual, would you find the money to pay the bill? If the answer is yes, then in a regular month you could have afforded to put $50 down against your debt or into savings.
- It's not hopeless for you to be able to make improvements in your finances. Think of some other goal you achieved. How did you do it? Did you rely on certain personal strengths? Did you get coaching or use someone else's expertise to help you succeed? Were there things you had to stop doing or situations you needed to avoid to help you reach your goal? Can you apply those same strengths or techniques to help you reach your financial goals?
- If you have a partner, involve them. Not only are two heads better than one, but if you aren't both striving toward the same goal, it will be much harder to reach.
- It's not a matter of how much you make. It's a matter of how much you spend. Do whatever it takes to spend less than you make, and you will have money left to pay down debt or to save.
- Don't let friends influence you. They have their own priorities.
- Reassess what is necessary spending versus discretionary.
- Pay down your highest cost debt first. Ask your credit card company to work with you on reduced interest rates. They are more receptive to that now than they used to be.
- Especially if you have trouble controlling your spending or knowing where your money went, use a smartphone app or your bank's spending tracker. An example of a free phone app for Apple or Android is Spending Tracker which allows you to easily document and analyse your spending.
- Lastly, here's an old saying that contains a lot of truth. Watch your pennies and the dollars will take care of themselves.

And do your kids a favour. Teach them to pay themselves first, that is to put money aside from every allowance or paycheque for the future.

Planning Meetings – We continue to listen to fund managers and economists on conference calls and webinars and to read commentaries and analysis every day. We are doing our best to stay on top of what's happening in the markets and particularly in our investments. And we've been busy repositioning investments, that we don't think will catch all of the recovery, and helping clients buy into the market while it's down. Things are much calmer now than they've been since mid-Feb. So, we are back to scheduling planning meetings. Of course the meetings will be by phone, or possibly by videoconference, until social distancing and self isolating are over. So, if you're concerned about whether recent markets have affected your retirement plans, or you just want a regular planning and review meeting, feel free to call us for an appointment, rather than waiting for a call or e-mail from Sarah or Amber offering an appointment. You can call for an informal chat too. We're here for you.

The early 20th-century British explorer Sir Ernest Shackleton, famous for his leadership that saved his whole crew who unexpectedly over-wintered in Antarctica after ice crushed their ship, once said, "Optimism is true moral courage."

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