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Letters from Leib

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Key Themes

We are only a few months into a series of medical, social, and economic crises that have disrupted supply chains, forced business closures, and crushed consumer demand. Even as Covid-19 lockdowns ease, uncertainty remains.

Sectors are opening at different rates and with different degrees of resiliency. Actions taken in response to the pandemic seem to have accelerated the pace of change, exacerbating weaknesses in companies that were already challenged by declining markets and excess debt and boosting others that were already well-positioned for the future. More than one analyst has suggested that we have covered five years of economic evolution in three months.

Monetary and fiscal policy responses to the impact of the virus on the economy were rapid and broad and, thus far, successful in forestalling a full-blown economic catastrophe. Markets fell dramatically in part because they had been pushed higher by the lack of alternatives created by low interest rates. The equally dramatic rebound has been driven in part by expectations for a quick recovery that may or may not be met.

Sooner or later there will be a financial reckoning for governments. This will likely involve a mix of higher taxes and service cutbacks. Both are likely to be opposed by older voters who are expecting more, rather than fewer, government services. Other scenarios involve governments holding interest rates down to shrink the debt as a percentage of the economy, or, alternatively, monetizing debt obligations through inflationary measures. The long-term implications of record deficits and money-printing policies are unknown.

Owners of surplus capital – that is business decision-makers and investors – have much to consider.

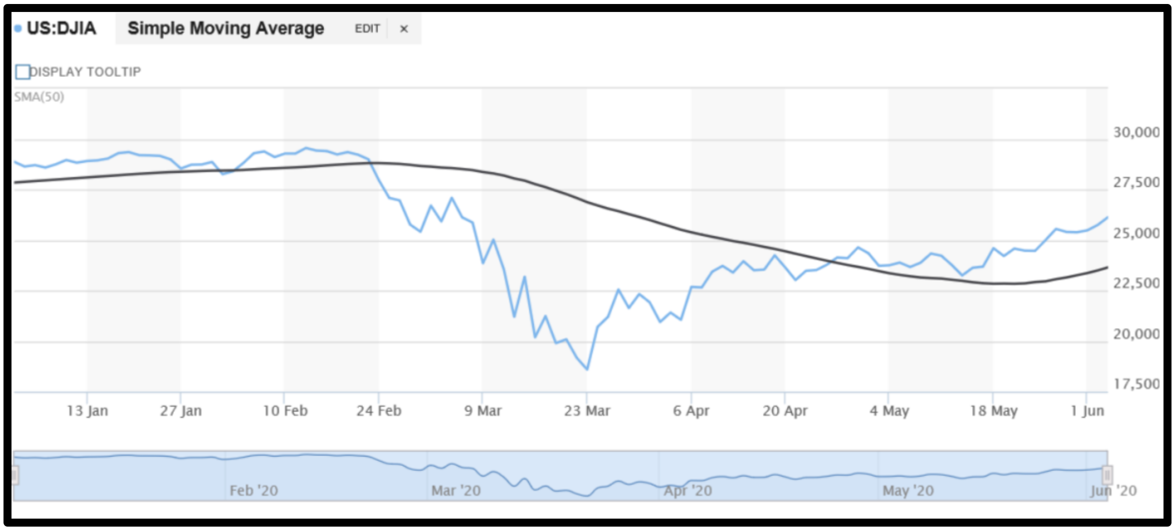
What should investors do at this point in the market cycle?

Today's rising markets reflect expectations of prolonged low interest rates and growth in certain sectors; at the same time investors seem to have little confidence in many traditional market indicators and often trade in reaction to headlines and rumors.

You have no doubt been reading about the great disconnect between the stock market indices and the economy. Stock markets are usually understood to reflect expectations of corporate profits six months out — right now six months out is a particularly uncertain time: Will there be a second wave of infections? What will happen when schools restart? There are upcoming American elections for president, and it is possible that control of the Senate will shift. There is a very good chance that we are not 'out of the woods', either medically or economically. Some businesses in some sectors will never return to their pre-Covid status.

However, the job of stock markets is not to predict the future but to allocate capital in the present in the context of alternatives. Volatile markets are not irrational markets. Different sectors have different rhythms and investors have different needs. Expectations of corporate profits and losses, low interest rates, and expansive money supply policies will continue to direct equity investments.

History has repeatedly shown the benefits of staying in the market and the wisdom of investing incrementally over time, particularly in periods of high volatility. We may not know when current crises will end, but we can have a high level of confidence that most industries will survive and that we will in time arrive on firmer ground. Investing in equities continues to be one of the best opportunities to protect, grow, and transfer wealth to the next generation.



The Dow Jones: One third down (February 21 to March 23rd; 21 trading days)
and one third up (March 23rd to April 20th ; 20 trading days)

Protect capital: Portfolios should always be monitored for changes in the economy that are likely to impact the prospects of particular investments. Take a hard and critical look at your portfolios – is it time to part ways or trim back holdings in past favourites and previous winners? It is good practice to evaluate your investments relative to each other and to other choices. This is an opportunity to upgrade portfolios by replacing good with better to ensure your investments remain relevant to the unfolding economy and consistent with your goals.

Add Long Term Value: Keep and add to positions in blue chip companies in financial, manufacturing, and utility sectors for stable, long term growth and dividend income. Shares in many of the world's great companies are currently offering above average yields. These will be especially valuable for investors in the low interest rate environment most analysts expect to see for some time.

Add Growth: Leaders and innovators in e-commerce, providers of digital and cloud services, artificial intelligence, machine learning, and robotics are experiencing rapid growth and are well-positioned for future. Responses to the Covid-19 crisis gave new relevance and credibility to these sectors. Businesses that have been resisting internet, AI, and cloud strategies are now embracing change; so should investors. There is a second reason to add growth stocks to your portfolios: many observers believe that we are entering a prolonged era of slow economic growth with increased employment instability, longer life spans, the prospect of higher taxes, and low real returns. Older investors need a component of growth in their portfolios to maintain purchasing power. We are also seeing a record number of new accounts opened by young people who see the pull back in the markets as an opportunity to build strong financial foundations.

Commodities, International Investing, and Deep Contrarian Plays: Best values are often found in sectors where concerns are the greatest and the outcomes least predictable. It is said that the cure for low commodity prices is low commodity prices; many great Canadian commodity companies are trading at bargain prices. Similarly, many of the world's leading companies are headquartered in Europe and trading at excellent values, partly due to currency differentials. We also believe in the long-term future of many Chinese e-commerce and technology companies. Some of these are among the world's most dynamic and innovative companies in their sectors, successfully selling to global youth markets. Of course, opportunities that offer above average growth potential do come with additional risk.

The Work of Stock Markets

As investors in public securities, we should be aware of what the markets are and what they are not. Stock markets function to allocate capital among alternatives and they have changed a lot in recent decades. Since 1996 the number of publicly listed companies in the United States has dropped by over half. Small speculative 'penny stock' opportunities that once allowed ordinary investors to participate in start ups have been almost entirely replaced by private venture capital. Market swings are magnified by the concentration of investment capital in institutional hands, ETFs (created in the 1990s), and by automated trading. Changes in the indexes also reflect shifts in the economy, including a decade of low interest rates and re-weightings of the indexes, with some industrial and commodity companies replaced by consumer staples and technology giants. In short, it is not your grandparent's stock market.

In Conclusion

I believe that investing involves more than just buying and selling stocks and bonds. I enjoy engaging with clients to discuss portfolios and financial needs, and then working with you to develop strategies and an overall financial plan that responds to your circumstances within the larger investment environment.

Social protests are rocking the world. We follow social and political events, and as thinking, caring people we are concerned about the fate of others, our families, and our world. Recent months have given many of us time for reflection. The choices we make as investors are meaningful – we can invest in our values as well as in value stocks.

You are hearing more about ESG investing. Although these words mean different things to different people, ESG stands for environment, social responsibility, and good governance. Increasingly shareholders, employees, and customers are calling on businesses to play a leadership role in effecting positive change. A young generation of investors believe that ESG factors should be a consideration in their decision-making.

As individuals we can make a positive difference in many ways, by reaching out to members of our community in need by rolling up our sleeves and by offering moral and philanthropic support.

Change may be scary, but it can also bring wonderful opportunities.

Stay safe.

Sincerely,

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A Quick Look Back

As COVID concerns rose, markets declined: slowly at first and then with increasing velocity as investors reacted to both the medical crisis and the shut down of global economies. Professional money managers were forced to liquidate holdings and corporations suspended stock buybacks, some out of prudent management, others to qualify for government support. Collapsing oil prices – although largely unrelated to the pandemic – increased uncertainty. Although the timing, speed and depth of decline were the result of the pandemic, it is worth remembering that the February highs were the culmination of many months of government policies that had left income-seeking investors of all kinds and sizes, ranging from institutional pension funds to individual households, with few alternatives. Many analysts were already warning that those high levels were disproportionately concentrated in a handful of stocks and unsustainable. What began as a health crisis accelerated into an economic crisis. Initially, no asset class was spared. As governments rushed to put a wide spectrum of fiscal, monetary, and public health policies in place, markets bottomed out. Although no one could be sure at the time, the low was reached on March 23rd, the day the American Fed announced that it would buy illiquid bonds. Stock markets slowly stabilized as various government interventions in the economy took hold and measures to control the spread of the virus began to show their effectiveness.

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