



WEEKEND READING

Shedding the light on what's happening - our world - our finances - our times

Is Spring here?

The weather on the coast has been dreadful. Hat-sized day time highs, (for those unfamiliar with hat sizes, Google 'Fedora'), wind, driving rain and power outages. Typical November 'Wet Coast' weather... in April. Good time to hide indoors. The dog is going stir crazy and our horses look longingly at the green shoots in the fields. Investors have been similarly glum, hiding their wallets. They aren't seeing, or least aren't paying for, green shoots...yet.

US Recession Risk: Weekly Monitor National Bank Economics April 17, 2023

<https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=aa2d18c9-6725-41f7-86cc-d493b903cb59&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail>

I've regularly complained about Canada's fiscal position and do it again this week. The concerns are real. Let's keep it in perspective though.

'Canada enjoys foremost fiscal freedom (as per IMF)' Market View National Bank Apr 11, 2023

By Warren Lovely & Ethan Currie

We were treated to the IMF's latest World Economic Outlook (WEO) today. And while a sister publication, the Fiscal Monitor, arrives with a one day lag, the WEO nonetheless reveals how the IMF sees government financial health evolving across the globe. There's some interesting and encouraging news for Canadians, made all the more relevant by the fact that the federal government in Ottawa utilizes the IMF's international debt comparisons when setting/outlining its key 'fiscal anchors'.

So what does the IMF have to tell us? For starters, Canada’s general government sector (which is a concept that covers all levels of government plus social security) has a pronounced budgetary edge vs. G7 peers. There’s been more rapid fiscal repair here. Before fully ascribing fiscal traction to a couple of years of heady nominal GDP growth, consider that Canada’s general government sector has a comparatively modest structural imbalance (just -0.5% of potential GDP as of 2023). Unlike other large, advanced nations, the IMF sees Canada’s structural deficit being erased by 2028. As for the closely watched debt metrics, Canada’s edge is better than ever and expected to only grow over time. The IMF puts Canada’s general government net debt-to-GDP ratio at a relatively skinny 14% as of 2023. The G7 average? Well, it’s currently 95% and set to turn one hundred in short order. For those familiar with the IMF’s estimates on net debt, you’ll perhaps notice a non-trivial revision to Canada’s net debt load. That captures a move to market valuation for financial assets, boosting the country’s already large pool of financial assets. Not for nothing, financial assets are netted from gross debt to arrive at net debt. Lest we Canadians get too cavalier, we must acknowledge that our gross debt-to-GDP ratio isn’t nearly as impressive, which is something credit rating agencies tend to take note of.

Still, for investors placing any emphasis on how one nation’s finances stack up against key peers, the IMF’s fresh outlook shows Canada with the foremost fiscal freedom in the G7, particularly once you control for the nation’s large and growing stockpile of financial assets.

See the attached full report.

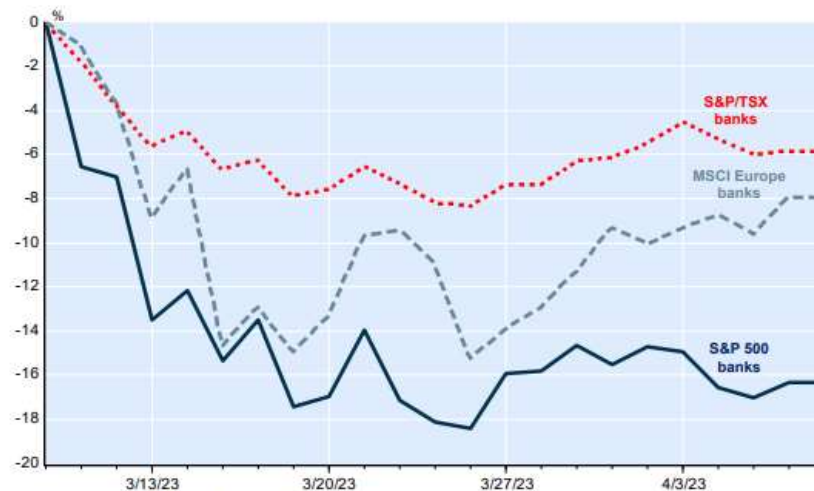
The above statement “There’s been more rapid fiscal repair here” should be preceded by, “A rebound in commodity prices, oil & gas in particular, meant...”. In short we got lucky.

Canada’s banks were targeted by the Putting Pundits lately. We took that on last week. NBF updates that view.

Monthly Equity Monitor April – NBF Apr 11, 2023

S&P/TSX: Banking sector outperforms

S&P500, S&P/TSX and MSCI Europe banks equity performance since March 8, 2023 (as of April 6, 2023)

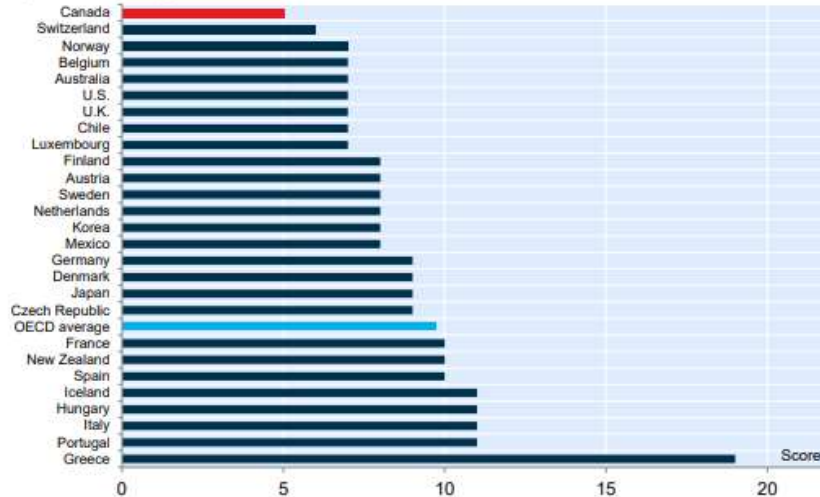


NBF Economics and Strategy (data via Refinitiv)



Canada: OECD's least risky banking system

NBF ranking based on S&P assessment of banking industry risk: Institutional framework, competitive dynamics and systemwide funding, selected OECD countries*



* Very low risk = 1, low risk = 2, intermediate risk = 3, high risk = 5, very high risk = 7, extremely high risk = 10
 NBF Economics and Strategy (data via S&P)

See the attached full report.

Some pundits worry China is gearing up for conflict.

China may cut oil products export quotas in second batch for 2023

Source: Reuters



Kyle Bass
 @jkylebass

One of the four speeches Xi gave at the 'Two Sessions' meetings regarding preparing for war focused on the statement: "we must hold the rice bowl firmly in our hands". Xi has been telegraphing his war preparation moves openly as he travels the globe in an attempt to secure approximately 12 million daily barrels of crude, 16Bs of LNG, and the 40% of China's food supply that they import each and every day. **If you take the time to put it all on a whiteboard, it's clear as day that WAR is coming.** #China #Taiwan

Source: Twitter

Staying with Energy...

Natural Gas Infrastructure: Winning the transition-security tug of war. NBF April 13, 2023

<https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=e350b636-a452-4bcf-80de-1b791231c93f&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail>

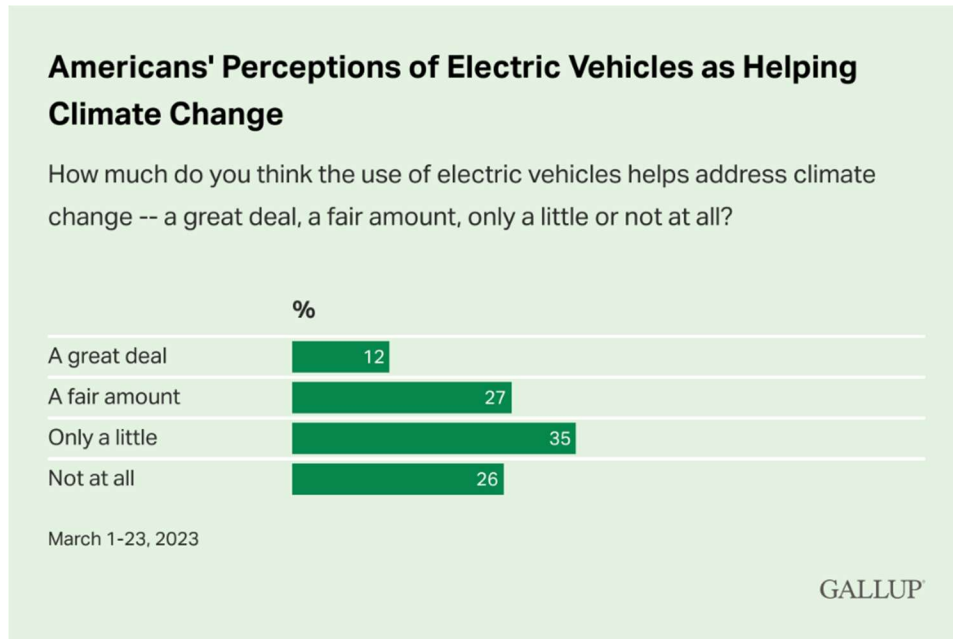


'Clean and Green but Not Very Lean: Our Analysis of the Federal Budget 2023' – Conference Board of Canada

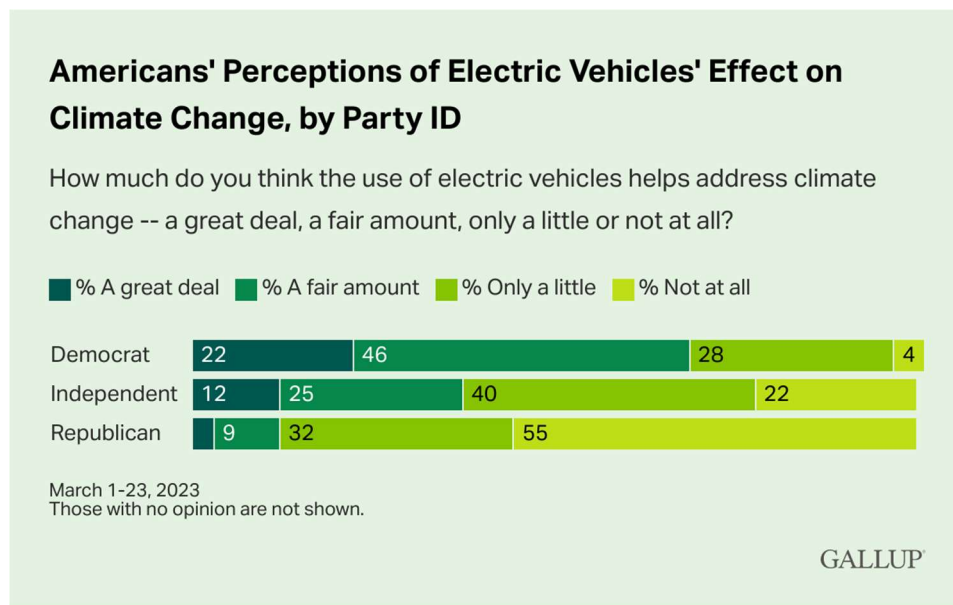
<https://www.conferenceboard.ca/insights/federal-budget-2023-analysis/>

Given the Canadian Federal Government's focus on energy transition, how do our neighbors to the south feel about it all?

'Most Americans Are Not Completely Sold on Electric Vehicles' Gallup Polls Apr 12, 2023



39% of Americans are convinced EV's are the answer. 61% not so much.



68% of Democratic party members favor EV. That party is forced to have EVs on their platform. Independents (37%) and GOP ((9%) don't care much. The public majority is unconvinced. Counter-intuitively, convincing the majority isn't key to winning US elections. 51% of votes cast wins. The 2022 mid-term elections saw 45.1% turn out = 22.6% of votes cast and even less of the population whole, wins. The 2020 US Presidential elections saw 66.9% turn-out (highest since 1936) = 34%+ wins. Previous elections required 26%+ or less to win. Convincing the base wins. Politicians are held in low esteem because most citizens, let alone most voters, don't receive policies they most want, most of the time.

<https://news.gallup.com/poll/474095/americans-not-completely-sold-electric-vehicles.aspx>

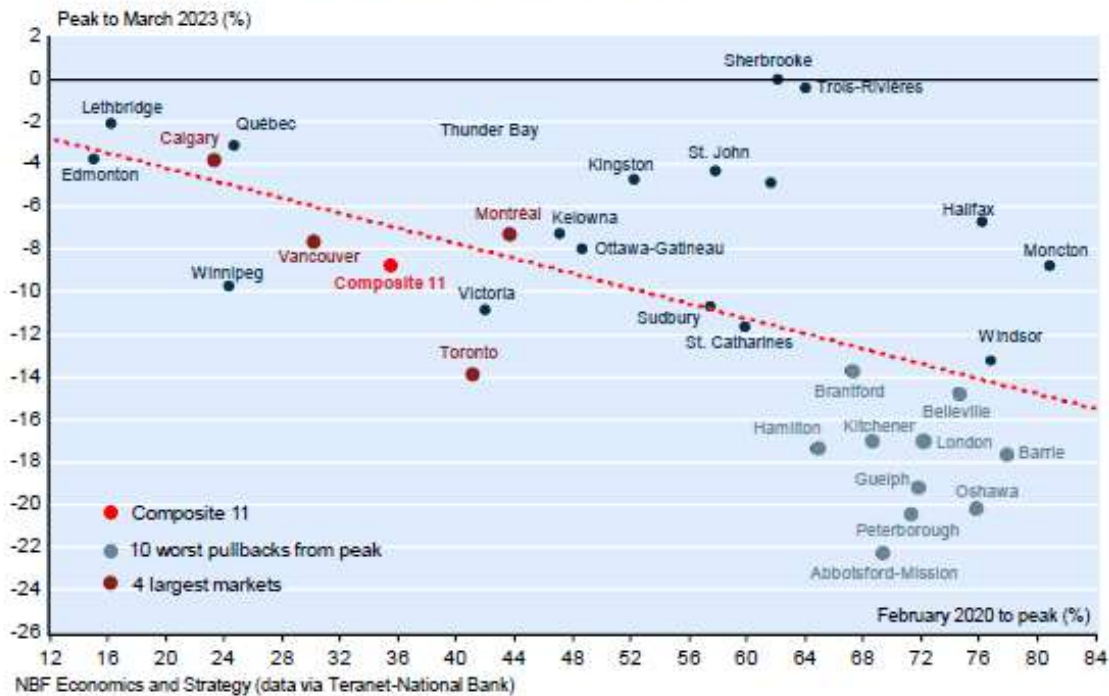
There were more doom and gloom headlines on Canadian house prices this week, noting a 'Record Decline' in March/2023. NBF puts it into perspective.

Canadian House Prices: Record Annual Price Decline in March

Teranet-National Bank Canadian House Price Index -April 20, 2023

Canada: Rapid declines after soaring increases

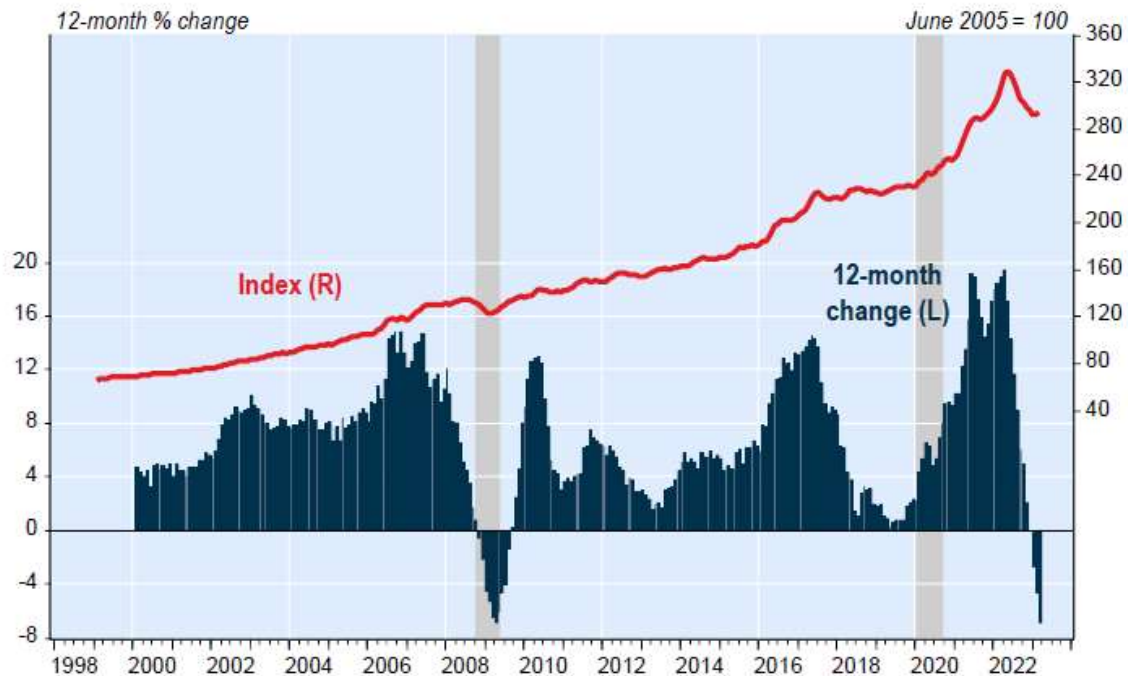
Price change from February 2020 to peak and from peak to March 2023



Abbotsford prices dropped 24%...from last year's highs. The Teranet entire Canadian House Price Index jumped +22% between March/2021 and March/2022. Flat – not 'crashing'.



Teranet-National Bank National Composite House Price Index™



This year's house price flop retraces last year's panic buying. The trend for Canadian house prices are still waaaaay up. Note how the recent decline matches the 2008-09 on the chart. Yup, looks like a recession. It will end. Immigration will put a floor under house prices. Expansion follows. The Canadian banks will be fine. Invest accordingly.

<https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=d851de22-9608-4ee5-8328-40342bd04754&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail>

Will falling inflation mean lower building costs and house prices?

A client couple plans on building a house in the next 3-4 years. We've been predicting declining inflation, and interest rates (but not to previous lows). They asked, "Do you think building material costs will decline too?". The question is a good one. It address broader claims of populist politicians on both sides of the aisle, puffing about Price Gouging.

EXAMPLE: You're a housing developer. You are continually building new houses on previously acquired raw land for spec sale. You will sell to unknown buyers at unknown prices. You are taking a lot of risk up front. Roughly 1/3rd of that cost goes for land prep and foundation, 1/3rd for putting up the building to lock-up and 1/3rd for finishing. Concrete prices have soared (cement is energy-intensive). Lumber prices have soared from the sawmills. The lumber price, once landed in the retail lumber yard is set. Every transaction after-words will be something higher. While you Mr. Builder might have a supply of lumber in storage at lower cost, given wastage, that cost advantage will soon disappear. You can't pass on the savings. The longer permitting takes, the more risk you face.

Lumber prices at the sawmill spike. Supply increases. Sawmill prices then decline due to short-term over-supply. It takes time for that effect to show at the lumber yard. The price effect is modest. During the spike, lumber yards had to raise the cost of lumber and all their costs of equipment and employee wages. If the lumber yard doesn't raise their prices, they lose money. If you Mr. builder doesn't raise your house prices, you will lose money. Like the lumber yard, the builder had to increase all their costs. Prices are 'sticky'. After a lag, workers demand higher wages, meaning inflation is sticky too. Inflation erodes the previous invested land value. Land sellers need a higher price to break even. This same effect happens for groceries and other goods. Falling commodity prices rarely translate much to falling consumer prices. The Food stores are not gouging their customers, they're just running their business, dealing with risks. Politicians often try to deflect consumer anger towards the business community. US President Joe Biden blamed 'Big Oil' and OPEC for rising energy prices, despite the US being a net energy exporter. His energy policies weren't discussed. Canadian politico's blamed Loblaws for higher groceries, when their policies increased costs.

Historically productivity has driven costs down. In developed nations, a main driver of inflation has been the supply of money. Too many dollars chasing too few goods. Money supply is controlled by both monetary and fiscal policy. The 2019 onwards expansion in money supply and Government spending has resulted in inflation. This has been a problem.

<https://www.investopedia.com/articles/investing/050615/fiscal-vs-monetary-policy-pros-cons.asp>

Lately, increased regulatory and energy costs have added to the inflation pulse. Those latter two trends seems likely to continue. The Governments currently on offer appear unwilling to control spending, reduce regulatory hurdles, or reduce living costs. For a dive into Canadian fiscal spending see the Canadian Taxpayers Federation report.

<https://www.taxpayer.com/media/NYTC-Report-2023-CTF.pdf>

The bottom line is while we believe the recent spike in inflation approaching double digits will abate, we don't believe we'll see sub-2% for years. We don't think house building costs will decline much and we don't think house prices over all will decline sharply below the Teranet trend line. At best we see sideways for awhile. Sideways can be okay, permitting earnings and savings to catch up.

Q: If we're facing a higher inflation world, how to navigate it?

A: Own businesses that can pass along the inflationary pulses and increase their dividends accordingly to you. With luck, you'll maintain your purchasing power.



Do dividends work? Show us the money!

Hilberry Dividend Growth Model (live account net of fees)

-From Dec 31, 2018 to Dec 31, 2022 Market Value increase +50.7%

2022 cash income increase +49.5%

2018-2022 deposits/withdrawals: \$0

A combination of corporations hiking their dividends and our portfolio allocation decisions saw a 49.5% increase in cash income. Clients noting the close correlation between rising income and rising prices often assume the latter is increasing the former. They have it backwards. Dividends are declared 'per share' and are not a function of stock prices.

Each stock sold, is bought. Sellers (owners) set the price. Buyers ask 'At what price are you willing to sell?'. Shareholders (the business owners) who have received a 50% increase in their cash income are less motivated to sell those shares to a buyer. They are likely to demand an increase price before they agree to sell. At least 50% higher would make sense. If they don't get that 50% increase, they could continue to hold and get paid.

That was then, this is now. What about 2023 onwards?

- 2023 projected cash income: **+66% over 2018 values**

The total market value of our portfolio has been stagnant since March/2022. Jan-Oct/2022 saw the S&P500 decline 27%. Rising dividends appear to have discouraged other investors selling the stocks we continued to own. Our portfolio income is now 66% higher than 2018. An investor purchasing our portfolio Dec 31, 2018 got paid each year and is now receiving 6.12% cash income yield on their 2018 money. Inflation has been running around that same rate lately. At worst we're seeing income purchasing power maintained. I expect the longer-term correlation between rising income and rising prices to continue. My hunch is by April/2024 we'll be glad we waited. Meanwhile we get paid to wait. But I might be wrong.

DISCLAIMER: 'Projected Income' assumes dividends and interest payments are maintained at the date of the projection (no cuts or hikes). FOREX rates on US dividends will affect the Canadian equivalent results. Dividends are not guaranteed and may be altered or eliminated without notice. Loss of capital is possible. The portfolio returns quoted are from a live NBF account (my own). I personally hold similar positions for myself, my immediate family and for client accounts over which I have trading authority. Readers may assume we have transacted in the securities within our portfolios within the past 60-days. Individual account results may vary. Fees, deposit and withdrawals affect total income. Past results do not predict future performance.

'One Big Web: A Few Ways the World Works' – Morgan Housel Apr 19, 2023



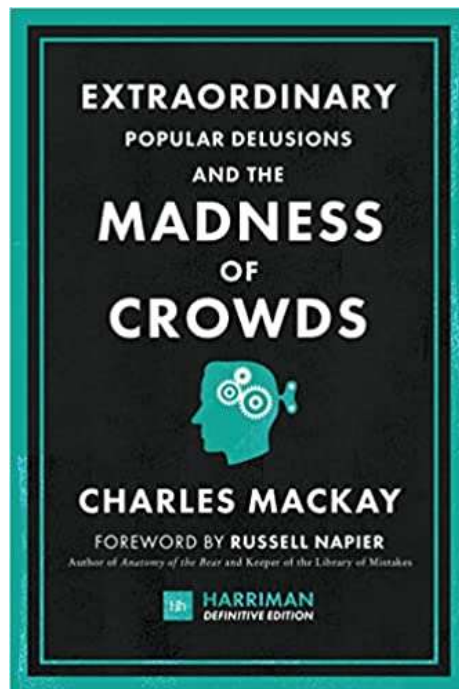
Joseph Tussman, a UC Berkeley philosophy professor, wrote in the 1960s that, “What the pupil must learn, if he learns anything, is that the world will do most of the work for you, provided you cooperate with it by identifying how it really works and aligning with those realities.”

What could be more obvious than that? Figure out how the world works and align with those realities.

<https://collabfund.com/blog/one-big-web-a-few-ways-the-world-works/>

If you figure out how the world works, CALL US FIRST!

In the meantime keep copy of ‘**Extraordinary Popular Delusions and the Madness of Crowds**’ by Charles MacKay on your bedside reading table.



<https://www.amazon.ca/Extraordinary-Popular-Delusions-Harriman-Definitive/dp/0857197428>

Have a Great Weekend

Steve & Anna Hilberry



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FOR THE RECORD Apr 21, 2023

DOW INDUSTRIALS:	33,765
S&P 500:	4,127
S&P/TSX COMP:	20665
WTI:	\$77.74
LOONIE IN \$USD:	\$0.7380 \$US

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