Hilberry Group
Wealth Management

Aug 4, 2023

How Hot is It? Ask the Bears.

‘Bear cools off in a Burbank pool during heat wave’ - CNN

Two points.

1. This one is smarter than the average bears and..
2. There are still bears in Burbank California?

https://edition.cnn.com/2023/07/30/us/bear-pool-burbank-california-trnd/index.html?

The financial heat has been on stock market bears recently. A US Fed Govt Credit rating downgrade appeared to offer them some relief.

NBF Market Review Aug 2, 2023 – extract

“Global markets roiled by surprise U.S. credit rating downgrade Rating agency Fitch on Tuesday downgraded the U.S. government’s credit rating one notch from AAA to AA+, a surprise move that reverberated through the global markets. Global equities and oil prices tumbled as investors fled riskier assets. In a statement Fitch said, “The rating downgrade of the United States reflects the expected fiscal deterioration over the next three years, a high and growing general government debt burden, and the erosion of governance relative to ‘AA’ and ‘AAA’ rated peers over the last two decades.” Fitch’s downgrade drew an angry response from the White House which called it "arbitrary and based on outdated data" as it came two months after a bipartisan debt ceiling agreement averted a U.S. default. Fitch is the second major credit rating agency to strip the U.S. of its triple-A rating after Standard in Poor’s downgrade in 2011.

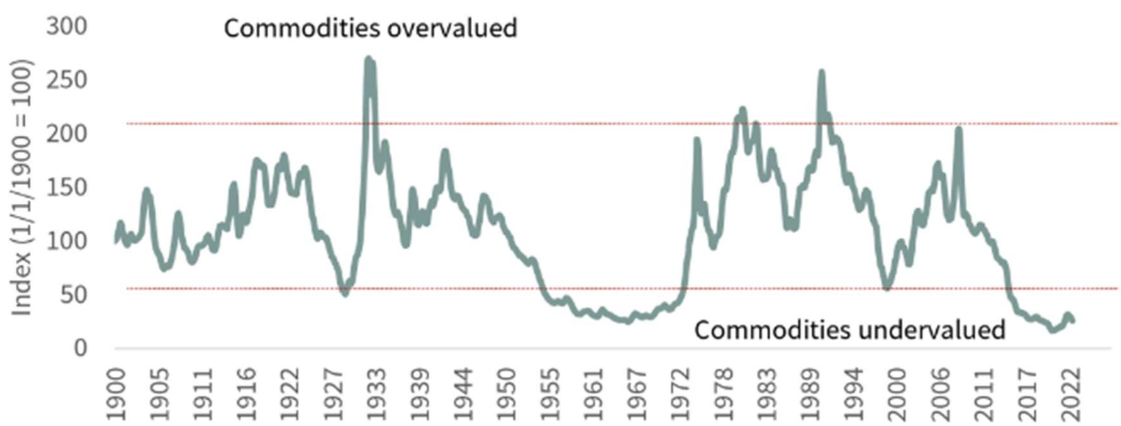
U.S. Treasury yields and the U.S. dollar rose on Wednesday, shrugging off Fitch's downgrade, after stronger than expected private employment data pointed to ongoing resilience in the labour market…"

The rating downgrade was met with 'outrage' from the US Administration who described the move as 'arbitrary'. Uhm. Yes, that's how rating agencies are supposed to behave. After a single day sell-off markets moved on. So much for the Crash. The downgrade raised howls from gold bugs and 'fiat currency' bears. Will the US Dollar lose it's status as reserve currency.

The US Reserve Currency & Commodities – GoRozen – July 24, 2023

We've regularly featured US based Goehring & Rozencwajg (GoRozen) work on commodities and recommend clients bookmark their site. In this week's blog posting they examine commodities performance during periods of financial upheaval. GoRozen concludes commodities have been wealth-preservers. They also examine the US dollar's reserve status, explaining why they see that status finally changing.

Chart 8 Commodities vs. Dow Jones Industrial Average



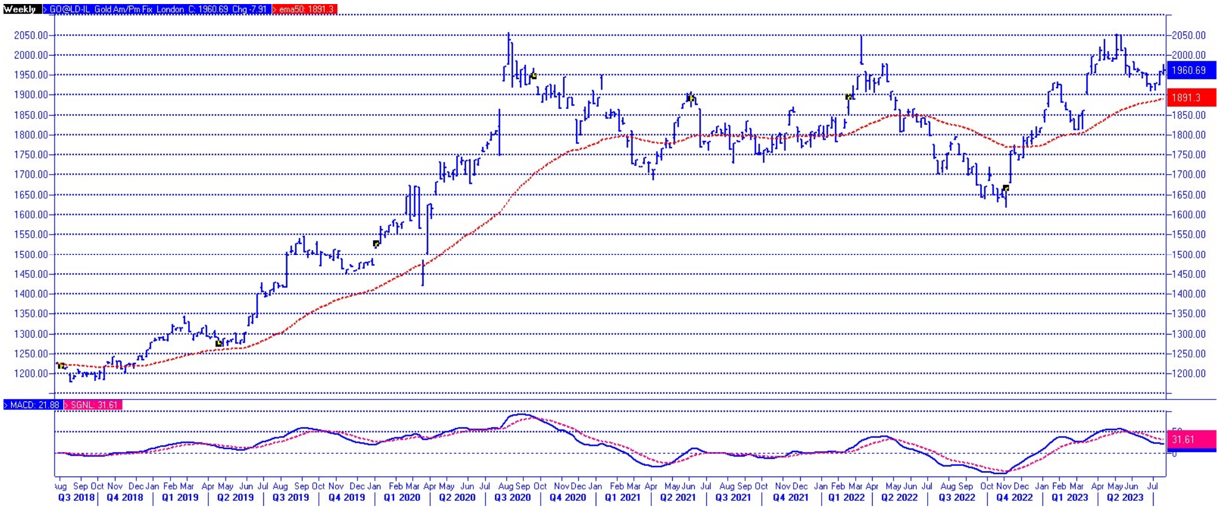
Source: Bloomberg and G&R Models.

https://blog.gorozen.com/blog/the-us-reserve-currency-and-commodities

When GoRozen talks commodities, we listen. They're thoughts on gold run contrary to our historical views. We've tended to avoid pure commodity plays (IE owning the stuff directly), focusing on companies that provide the material instead. Our thinking is if a commodity will be in demand, the real money will be made by the producers. The issue with gold miners is a lack of consistent cash-flow, low to no dividends and volatile 'event driven' earnings. Things must get really bad for gold miners to make consistent money. While there's always something to worry about, constantly counting on disaster hasn't rewarded.

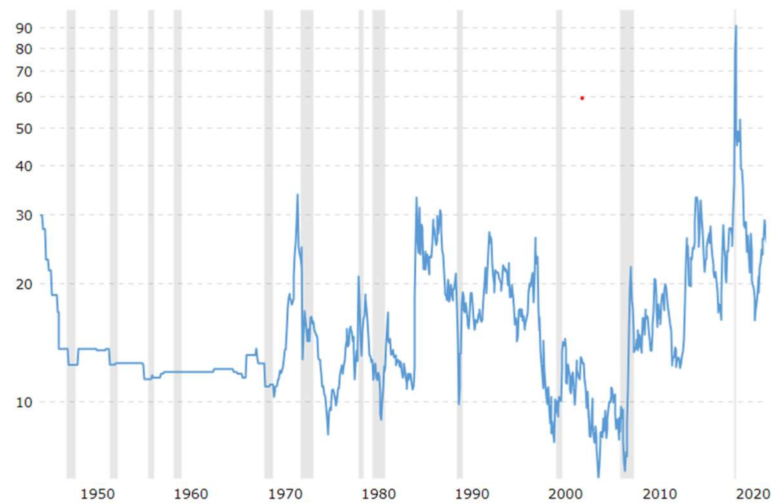
GoRozen's notes on potential changes to the US Reserve Currency status are worth pondering. Changes to the US Reserve Currency status has been a regular feature of gold-bug punditry and disaster-mavens for my 30-year career, so I've tended to ignore it. Maybe that's about to change? The price of gold in US dollars has been flat since late 2020.

Gold London Fix per oz $USD – weekly 2018-2023



Source: Refinitiv, Hilberry, NBF July 24, 2023

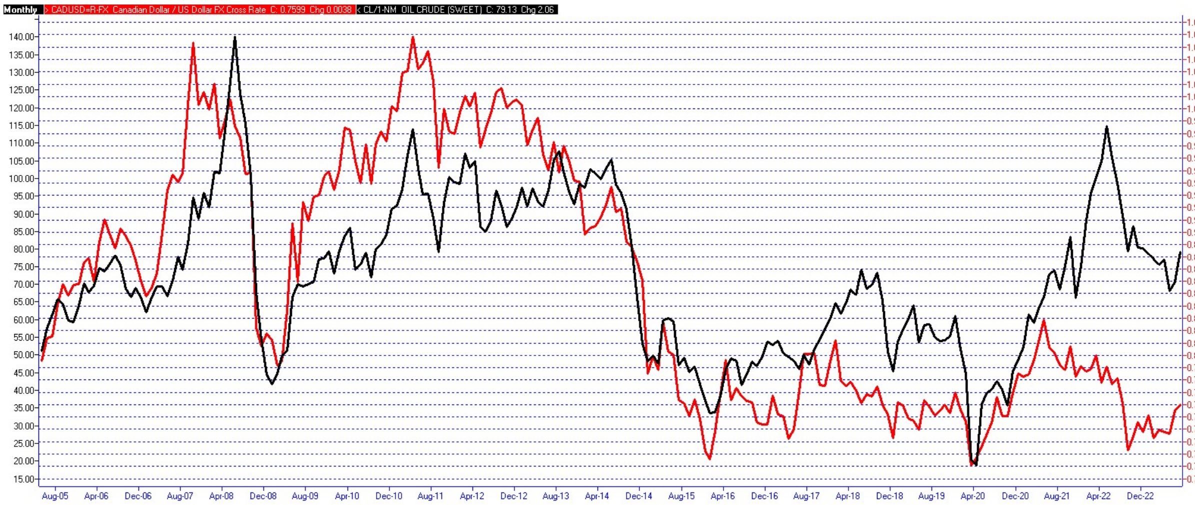
The Gold-to-Oil Ratio compares barrels of oil (West Texas Intermediate or WTI) acquired per ounce of gold. The long-term average is 16 barrels per ounce. This relationship matters to oil producing nations ruled by despots, anxious to move funds outside the US banking system. Guns for gold etc. The ratio hit extreme highs in 2020 90 barrels per 1 oz of gold during the COVID that saw gold rise while oil plummeted). Note how gold peaked in Q3 2020, roughly 3-4 months prior to Mr. Putin's invasion of Ukraine. Was Russian money taking a walk? Today the ratio is 30, roughly twice the long-term average. Is oil cheap or gold expensive? Take your pick.



Source: Macrotrends – July 24, 2023 https://www.macrotrends.net/1380/gold-to-oil-ratio-historical-chart

The Canadian dollar has shown a positive correlation to crude oil prices. WTI up, Loonie up. This correlation remains but has been muted since late 2020, perhaps reflecting changes in Canada's government policies towards the commodity. This could change. Maybe.

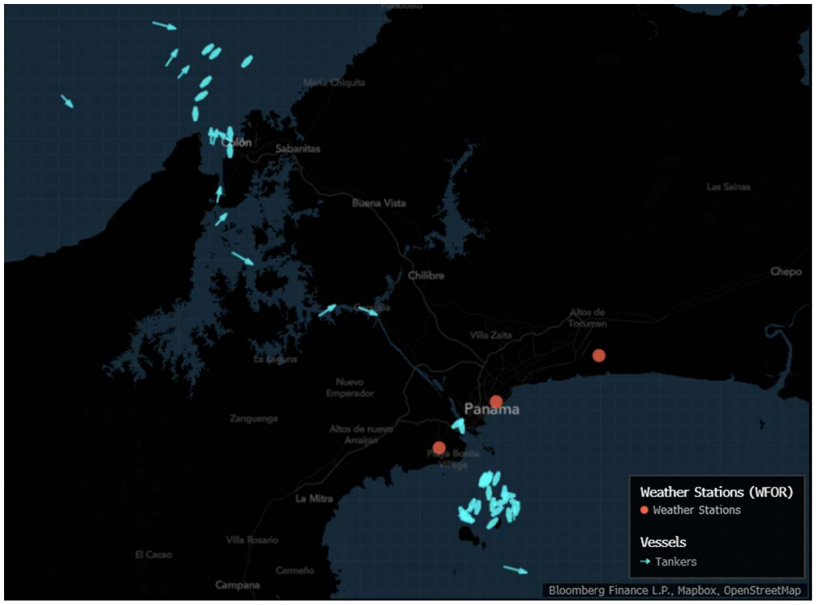
Loonie (red) vs WTE (black) monthly ranges 2005-2023



Climate change and shipping. Will the Panama Canal choke.

Excerpt from National Bank's Energy and FOREX Daily Note July 27, 2023

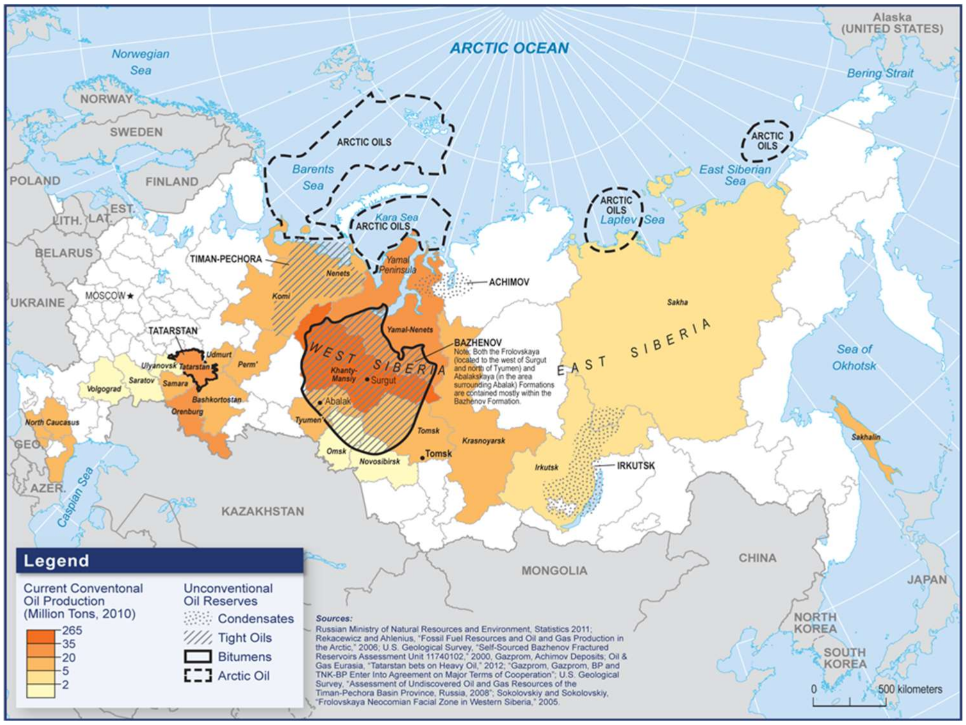
"We had some watercooler chat about the Panama Canal yesterday as drought and El Nina continue to challenge shipping logistics as the canal recently announcing that as of July 30th, the canal will reduce average daily crossings to 32 from 35/36 (Reuters here). Current water levels are 80 feet over sea level, whereas the minimum is 75 feet, so the probability remains high that the next 18 months under El Nina will see additional restrictions. This involves fewer and smaller vessels that are ultimately easier to manage at key transfer points. Overall, it seems like the Canal will continue to increasingly restrict daily crossings while also facing added complexity around how to layer on increased emissions regulations (increasing costs further). Frankly, we're far from experts on freight or canals or ships, but wonder if this will be an ongoing story around limiting some energy trade as time moves on – after all, there's still five more months before the rainy season can assist in boosting water levels too. Based on Bloomberg's tanker tracker, there's 8 that are anchored on the North side, while the South side has 16-20 – we'll see if these numbers drastically increase?"



Climate change and shipping continued. The Polar Silk Road?

Canada's North could see dramatic changes in importance.

The potential for Russian access to year-round open saltwater ports along their northern coastline could have profound implications. Russia may refocus from their long-held need for open water access via the Black Sea to their northern coastline. Should Russia continue its hostile policies, enraging the neighbors, Russian access to the Black Sea via the Dardanelles and Bosporus is a problem. Ukrainian military advances saw the Russian navy move their capital ships out of Sevastopol, Crimea. Russian oil assets are focused in the northern areas of central and eastern Siberia.



Source: Carnegie Endowment

https://carnegieendowment.org/publications/interactive/russia-oil-map/

Existing Russian northern ports have been ice-locked, requiring heavy icebreaker support. Retreating sea ice could change many things

https://www.worldatlas.com/articles/the-arctic-ports-of-russia.html

While the narrative has been climate change equals open Artic waters, that's not what happened in 2021 and 2022.

'One year after the crisis, there is again early ice on Northern Sea Route' - The Barents Observer Nov 15, 2022

https://thebarentsobserver.com/en/2022/11/one-year-after-crisis-there-again-early-ice-northern-sea-routev

The North Sea and the Bering Strait between Russia and Alaska could make for uncomfortably close passages for hostile Russian shipping. Russia may decide to focus economic and military assets northwards. Murmansk, connected by rail to Moscow, would be a logical choice.

Good fences make good neighbors. Canada may need to focus on Arctic sovereignty. The Federal Government has issued policy papers emphasizing that commitment. Our newly accessible neighbors may need something more upfront and personal than paper.

Near Term direction for interest rates?

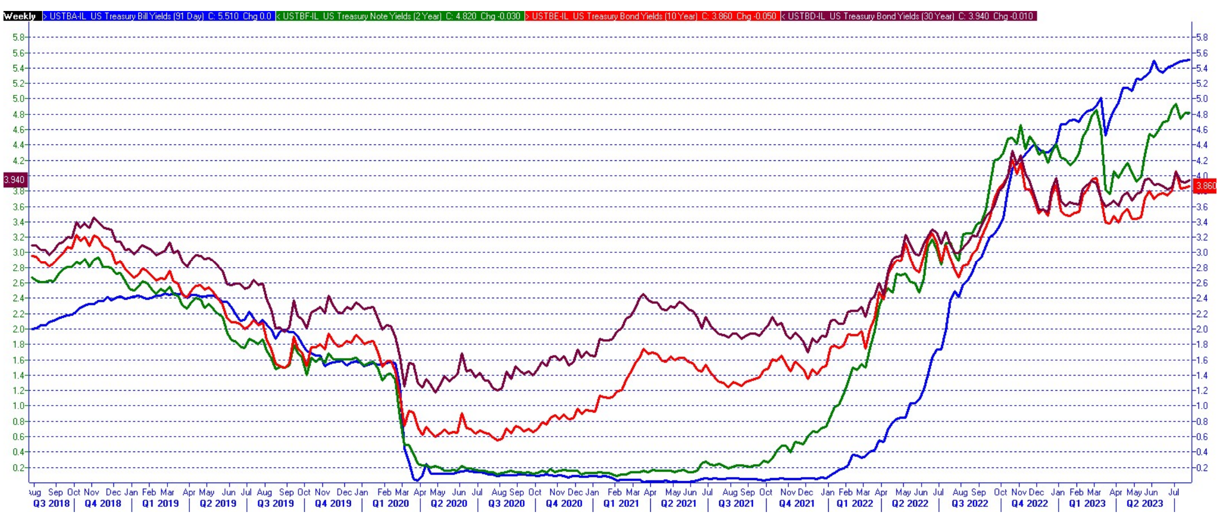
'The data dependent Fed keeps the terminal rate debate alive' **– National Bank Economics and Strategy July 26, 2023**

Bottom Line Once again, there was little doubt of today's decision as the FOMC has consistently and effectively guided markets throughout this hiking cycle. But while there wasn't uncertainty about this policy action, it was very much unclear if the Fed would be willing to tighten again this year given the encouraging data we've received in recent weeks (particularly on CPI inflation). Based on today's statement and Chair Powell's press conference, this will remain an open debate over the coming months as guidance was left open-ended, neither committing to another hike nor taking one off the table. While there may be no clear/definitive guidance contained here, we do expect the next Fed decision to result in a 'hold', just as policymakers opted for in June. With rates in more clearly restrictive territory today, the FOMC should want to proceed more slowly/cautiously. Indeed, Powell explicitly noted that risks are more finely balanced now, highlighting clearly positive real rates. While policymakers will surely frame September as a 'live' meeting, the true test in our view will be the early November decision. If incoming inflation/labour market data continues to soften then it's unlikely another hike this year will need to materialize. This is our base case outlook. Still, we don't want to fully dismiss the risk of an additional hike in the fall, consistent with the June dot plot. If data were to 're-heat' (which again we don't expect), we wouldn't doubt the Fed's resolve.

https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=de6ab13f-609b-4ec8-8d43-73ce48739298&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail

What does the US bond market think?

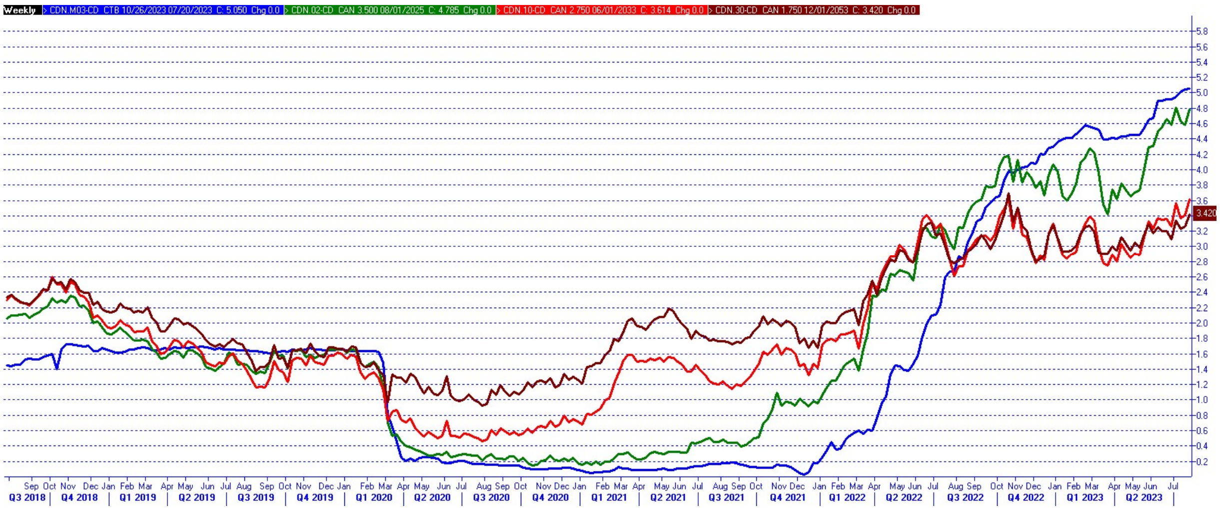
US Treasury Bond Yields: 90-day (blue), 2-yr (green), 10-yr (red), 30-yr (burgundy)



The 10 and 30's are saying not higher inflation (red & burgundy flat since Oct/2022).

How about Canada?

Fed Govt Canada Bond Yields: 90-day (blue), 2-yr (green), 10-yr (red), 30-yr (burgundy)

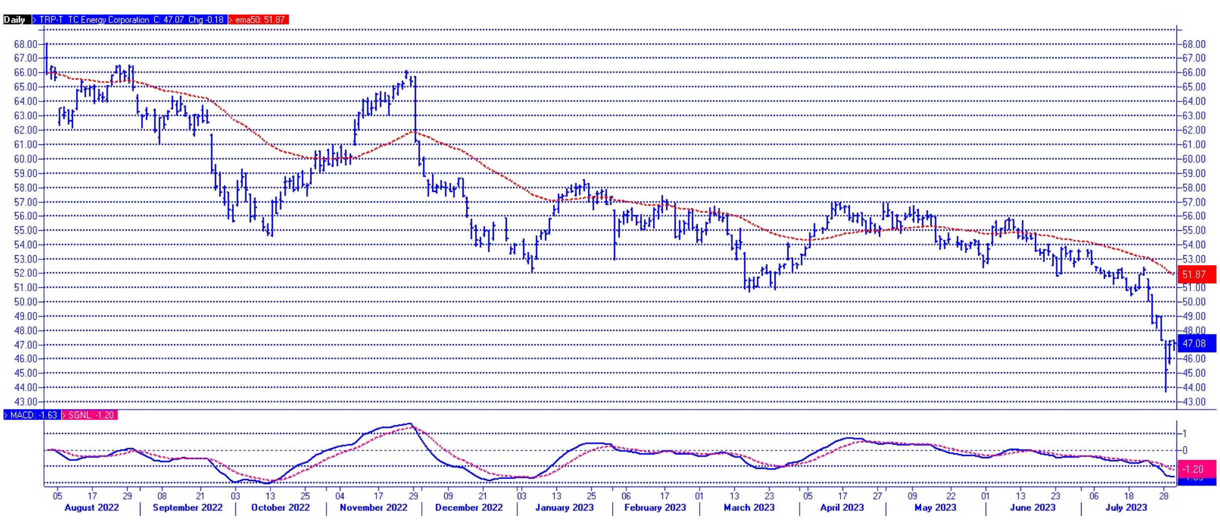


The Canadian bond market isn't so sure inflation is dead. While the yield structure is typically close to the US we note the CDN 10's and 30's are pushing the upper ends of the recent bands. Does the Canadian bond market see made-in-Canada inflation?

TC Energy Update

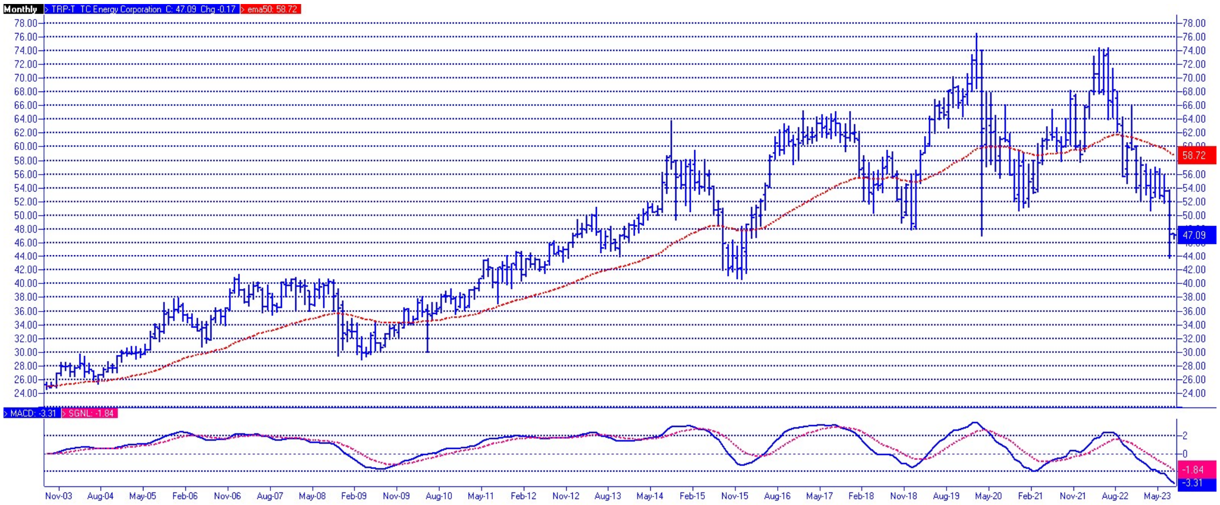
We hold TC Energy in our Canadian Dividend Income portfolio. The company's business is unspectacular and boring. The share price has been anything but. It's been a dog lately. From the June, 2022 highs of $74.44 TC's share price flopped 41% to a July/2023 low of $43.70.

TC Energy (TRP-TSX-$47.09) daily ranges 12 months



The latest slump puts TC Energy's share price back to the Nov/2015 lows.

TC Energy (TRP-TSX-$47.09) monthly ranges 20 years



Note the flop in the middle of the chart. July-Oct/2014 the price averaged around $60. In Nov-Dec/2015 the price bottomed out around $40.50. While correlation isn't causation, the current Liberal Govt was elected with a majority on Nov 5/2015. Since Nov/2015 the stock price has seen wide swings. From the Nov/2015 low around $41s, the stock soared to over $61 in July/2016, moved moderately higher to $65.18 Nov/2017, then slumped to lows of $47.90 in Dec/2018. The price spiked again to $76.50 in Feb/2020, ranged between $62 and 72 until Dec/2022 when investors began losing confidence again.

The share price swings have been much wider than earnings results would imply.

2013-2023 earnings climbed 90%.

Earnings 'visibility' has been high. Annual earnings per share have typically been within pennies of analyst consensus opinion. Revenue revisions have been small.

2013-2023 the dividend climbed 102%

From 2023, consensus opinion sees TC Energy's $C revenues and earnings climbing close to 27% by 2027. The dividend looks solid. On today's price around $47.00 the $3.72 annual dividend is priced to bear a 7.9% cash yield. The dividend is predicted to grow.

We checked TC Energy's bond yields. If the company is facing a long downslope into oblivion surely bond investors would be very uncomfortable. TC Energy's current yields would reflect it. TC Energy's 9-year bonds are priced around par, implying investors think they're going to get their money back. The yields are around 5.4%. Bell Canada's 2035 maturities are priced to pay 5.5%. The bond market doesn't appear worried about TC Energy's 10-year prospects.

The company has been, is and probably will continue to be boringly stable, yet share prices have been anything but.

2013 to 2014 the Price to Earnings ratio (P/E) averaged $24. Since 2015 the P/E lows have been falling meaning investors have been steadily less willing to pay for increasing earnings.

The 2023 P/E range has been around 12, implying an earning yield of 8.3%

Today's price-to-cash flow ratio at 6.5, implies a cash-flow yield of 15.4%. Going back to the company's 10-year yields of 5.4%, that is the company's current borrowing cost. With enough money, taking TC Energy private would 'cost' 5.4% in debt costs, serviced by 15.4% cash flow, leaving 10% cash flow to pay down debt. Asset sales, etc. could increase the cash flow.

Europe's experience confirms natural gas transmission is a needed industry. Canada has plenty to sell. Fundamentals say TC Energy has a solid business with high visibility. Yet investors aren't buying. What gives?

Is it an ESG thing? TC Energy's ESG Score is a B. TD Bank has an ESG Score of B+.

The wide price swings track investor tension between actual results and the attempt to predict public consumption response to government climate change regulations (more below). This week TC Energy made some dramatic announcements surrounding their liquids pipeline assets. NBF reviewed and upgraded their opinion.

'Just what the spin doctor ordered…upgrading to Outperform' **NBF July 28, 2023**

TC Energy Corp.

Just what the spin doctor ordered...upgrading to Outperform

	STOCK RATING	TARGET	EST. TOTAL RETURN
TRP (TSX; NYSE) C$47.30; US$35.79	Outperform (Was Sector Perform)	C$54.00 (Was C$53.00)	22.0%

Q2/23 results + Liquids Pipelines spinoff

Announces intent to spin off Liquids Pipelines business...

On the heels of its recently announced $5.2 bln divestiture of a 40% stake in the Columbia Gas, TRP announced plans to spin off its Liquids segment on a tax-free basis into a pure play, publicly traded Liquids Pipeline Company with TC Energy retaining the natural gas pipelines and storage and power assets (expected closing in H2/24). Inside, we highlight key pro forma financial metrics for both entities on a 2026e basis (i.e., full Southeast Gateway contributions), corroborating TRP's guidance of achieving <5x D/EBITDA while sustaining 3-5% dividend growth with a 2026e AFFO payout ratio of ~75%.

See the full report at this link:

https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=8260184f-b4ae-4ff7-88e8-325b39490bf9&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail

With our comments on predicting energy consumption trends in mind…

'When it comes to EV charging infrastructure, how does your province rank?' – CBC Aug 1, 2023

CBC ran an article this week assessing the state of Canada's EV charging infrastructure given that… *"By 2035, 100 per cent of new cars and light trucks sold in Canada must be zero-emissions vehicles, under federal rules. Experts say the number of charging stations will need to increase exponentially to meet that mandate".*

The article compares how many charging stations are in various jurisdictions, claiming that 444,000 stations are needed in Canada. We tallied ~3,100 that are current operational in Canada – although verifying these numbers proved difficult (and seemed low). Regardless, current Govt regulations mean Canadians have only 11.4-years regulatory permission to buy an ICE engine and will need to build 441,000 new charging stations (at least) to get the infrastructure up to snuff. Here is the data table in the article focusing on Canada. We note The Yukon has the highest North American per-capita charging station infrastructure at 36 charging stations per EV (3 cheers for Whitehorse!). That's what happens when you install 17 stations to service the 47 EV's operating in the Yukon. Our guess is most are in Whitehorse.

2022	Fast Charging Stalls	# of Evs	Stalls/EVs per 100 Cars
Yukon	17	47	36.17
Newfoundland and Labrador	33	154	21.43
Saskatchewan	109	543	20.07
New Brunswick	86	464	18.53
Manitoba	76	875	8.69
Prince Edward Island	18	240	7.50
Nova Scotia	34	633	5.37
Alberta	205	4,073	5.03
Ontario	1,100	35,974	3.06
British Columbia	924	48,263	1.91
Quebec	499	62,071	0.80
Total Canada	3,101	153,337	2.02

2035	Goal	ICE Fleet 2022	Stalls/EVs per 100 Cars
Total Canada	444,000	26,000,000	1.71

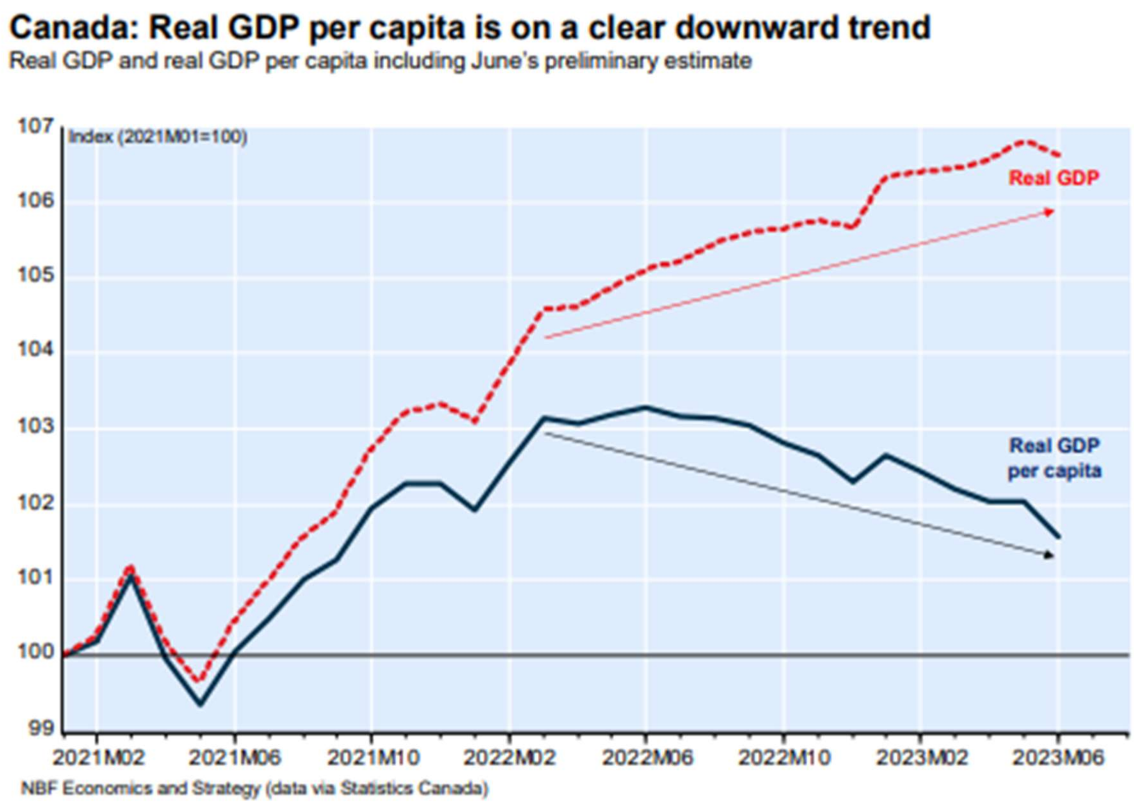
Source: Source: Transport Canada, Statistics Canada, U.S. Department of Energy (Graeme Bruce/CBC)

Full article link:

https://www.cbc.ca/news/canada/ev-infrastructure-canada-us-comparison-1.6923582

Weekly Economic Watch

This week's Economic Watch looks at Canadian GDP adjusted for inflation (real) and for population (per capita). The headline's say GDP is growing. Adjusted for Canada's booming population, not so much.



https://www.nbc.ca/content/dam/bnc/taux-analyses/analyse-eco/weekly-economic-watch.pdf

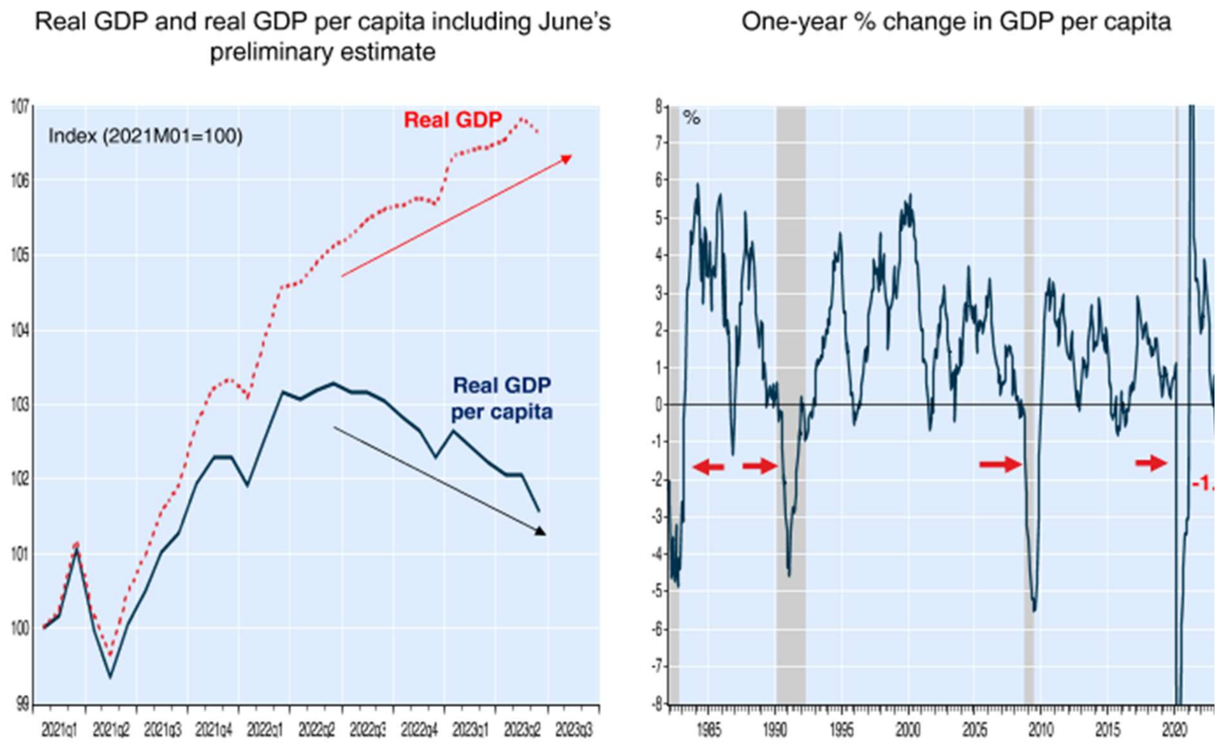
This week's Hot Chart's drills into the decline of Canadian GDP per capita, explaining why it matters.

'Hot Charts – Canada: GDP per capita is down 1.7% over a year. Is it a big deal?' NBF Economics July 31, 2023

Canada Watch

With last Friday's release of May GDP (+0.3%) and Statistics Canada's preliminary estimate of a 0.2% decline in June, annualized growth for the second quarter is on track to be 1.0% (see note for more details). While not stellar by historical standards, some may be pleased that the Canadian economy continues to grow despite the central bank's extremely aggressive monetary tightening. However, taking into account surging population growth, real GDP per capita is actually declining at an annualized rate of 2.1% in the second quarter, the fourth consecutive quarterly decline, a streak that coincides with the beginning of the central bank's monetary tightening. For the 12 months ending June 2023, it's down 1.7%, and one wonders how many times this has happened in the past. As today's Hot Charts shows, a decline of more than 1.5% has only occurred in recessions. In all of the episodes where GDP per capita was barely below the prior year, the central bank was already in easing mode, which contrasts with the current stance where Governor Macklem said the bank is ready to raise rates further. In our view, the BoC has prematurely lost patience on the inflation front by tightening further in June and July, while an already fragile economy has yet to feel the full impact of the increases applied since the tightening began. Against this backdrop, we remain cautious about the 12-month outlook (see [Monthly Economic Monitor](#)).

Canada: GDP per capita is down 1.7% over a year, is it a big deal?



NBF Economics and Strategy (data via Statistics Canada)

https://nbf.bluematrix.com/sellside/EmailDocViewer?encrypt=e71eb44b-7e1c-4e31-8396-9b707c7677a0&mime=pdf&co=nbf&id=steven.hilberry@nbc.ca&source=mail

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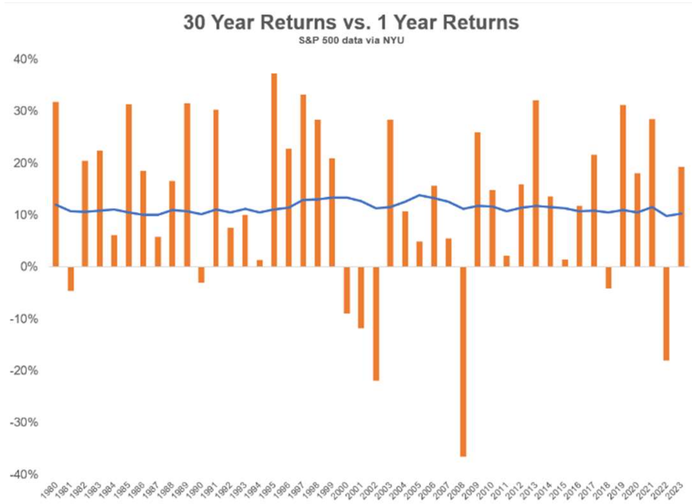
Matthieu Arseneau & Alexandra Ducharme

For more NBF commentaries see this link:

https://www.nbc.ca/about-us/news-media/financial-news/financial-analysis.html

And finally, a note on how to view your returns.

‘One Year Returns Don’t Matter’ – Ben Carlson July 30, 2023



https://awealthofcommonsense.com/2023/07/one-year-returns-dont-matter/

We think a new business cycle has started. While one year returns don’t matter, we think one year from now investors will be glad we continue to hold our dividend payers.

Have a Great Long Weekend

Steve & Anna Hilberry

FOR THE RECORD Aug 4, 2023

DOW INDUSTRIALS:	35,382
S&P 500:	4,523
S&P/TSX COMP:	20293
WTI:	$82.07
LOONIE IN $USD:	$0.7486 $US

NATIONAL BANK FINANCIAL
WEALTH MANAGEMENT

Aug 4, 2023

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