Rickerby Wealth Management

A Memo from the Trenches

October 2023

TD Wealth

Markets

Remember August's newsletter: …

"What do I want? What do I expect? Put bluntly I would like to see this period over and done with. Let us get a short, modest recession quickly addressed and then get our interest rates moving lower and the start of the first inning of the next business cycle started.".

Well economic data in September reported that the Q2 GDP numbers in Canada were surprisingly negative … that the Canada economy shrunk over the second quarter … and might represent the pivot point I have been hoping / waiting for. Other data suggested that Asian economies are also slowing quickly, real estate prices in Toronto have been on the decline and labor markets are weakening, although from a uniquely strong position. We shall see. But my conclusions are that we are at the peak in interest rates in my view, or perhaps one more hike in rates.

Next question will be when they start to decline … and how quickly. It is a tricky question. We know it will happen, but when is the challenging question.

Let me give you a little extra data to reflect on.

An "inverted yield curve" is when short-term interest rates are higher than long-term interest rates. This event usually occurs when central banks push up short-term rates in an attempt to slow the economy as they fear inflation getting out of hand.

Using the 3 months return on US Treasury bills and comparing that to the return on 10 Year US bonds, the curve has been inverted for 11 months so far. Now, the AVERAGE time that yield curves are inverted is 12 months and so far, the longest period the yield curve has been inverted has been 19 months in the past (that was in 1973 and again in 1980). And invariably, about every time we have an inverted yield curve, we have an economic recession. Sometimes deep and hard, sometimes shallow, and barely noticeable.

As I have mentioned in the past, we have been living through the most anticipated recession in recent memory and yet… it just is not showing up, and candidly there are an increasing number of commentators that are moving from their position of a recession to that of a "soft landing". That is to say that the economy slows, inflations dips to an inflation target rate of below 3% and we DON'T slip into a recession in the US. Bottom line is it seems to me that we are likely to have this inverted yield curve for longer than the current record of 19 months. In other words, a longer period of indigestion then once hoped for.

Bottom line is that August and September have been quite negative months. Indeed, as of the end of September, the return from the TSX for the year is basically 0 %. The Dow Jones index is also effectively flat, but the seven tech stocks have assisted indexed such as the S&P 500 to a YTD return of about 10%. BUT the "magnificent 7" tech companies have sold off hard the last 2 months as well. Candidly I get slightly nauseated just looking at the chart of the technology indexes.

Incomes increasing? Yes.

In recent letters I have made mention of the fact that although this jump in rates was going to have negative implications for all asset classes and thus all portfolios in the short-term, it did suggest that at some point the INCOME from our holdings would start to increase. In previous newsletters I have pointed out that dividends on preferred shares have been increasing. In addition, a mortgage investment related company called TREZ Capital, (note: not all clients own Trez) have increased their dividends three times in the last 12 months.

In September I received notice that an income fund, widely held amongst clients called PIMCO Monthly Income fund, just increased their dividend distribution and the current yield at this time is 5.75% as a result. (See notes for details.) I suspect we can expect more announcements of increasing incomes from a long list of investment alternatives in the future.

PS: Another piece of good news is that many clients own TD preferred series K and TD announced, surprisingly, that they WOULD redeem those shares at $25 in October. Pleasant surprise. The shares rose from about $22 to $25 overnight. So now I will have cash for those clients to reinvest in this current world of 6% – 7.5% incomes from "safe" alternatives. Great news.

Changes to TFSA High Growth Model

We have been holdings a 7% cash weight in this model since January. We have now invested 5% in an Index share for Japan markets and 2% for South Korea. (PS: We also rebalanced ALL accounts to our "target" so you may notice some small trades as well). Japan has been in a unique position for many, many decades and that is that they have been TRYING to stoke inflation in their country, and finally it is showing up. In their country, uniquely, inflation moving up to 3% might stimulate their citizens to spend some of the money they have been hanging on to for so many years. At least that is the thesis.

Demographics question

Following up from last month. The largest city in 2050 is projected to be Mumbai at 42.4 million. Not a surprise but for 2100… and I suspect this will surprise readers, Lagos, Nigeria as eighty-eight million. Can you imagine what it would mean to live in a city that has more than double the entire population of Canada?

Speaking of which ... extra reading

Long-time readers will know that I have followed John Mauldin for about 15 years. He is the one writer that I will read every week. In the past I have also advanced to you, short reports from one of his colleagues whom I have grown to follow, Jared Dillan. I find that Jared is always a balanced observer of markets. I "get" what he is trying to say. And oftentimes nodding in agreement with him saying to myself "he is articulating exactly the sentiments I have.".

I would encourage folks to read this week's short article from Jared as once again, his insight frames my own long-term expectations of the future, a future where GDP growth for developed economies continues to moderate from previous cycles going back to the second world war. (Again, it's about demographics). And of course, it is up to me to try and establish how we invest if this thesis does unfold in the many years ahead.

https://www.mauldineconomics.com/the-10th-man/the-next-100-years

Cyber security: A reminder

The event of new Artificial Intelligence technology (A.I.) is providing increased opportunity for "the bad guys" to create and send increasingly sophisticated and increasingly more difficult to discern legitimate email communication with scam and fraud attempts.

I know that many clients worry and can be unsure of what is real. As my Dad always told me as a youngster, "…don't believe everything you read and only half of what you see". And in this day, that is true as never before. In fact, don't believe everything you see either.

Here is a simple process to help you.

If you EVER receive a communication that you are unsure of, then always go to a fresh, standalone web browser and YOU proactively contact the organization about the email or get the phone number of their website and call directly.

The bad guys still rely on you responding to their email or text that they have sent you. If you stop that path of communication, and initiate your own, new path then you massively mitigate the chance of making a mistake.

Until next month…

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