Rickerby Wealth Management

# A Memo from the Trenches

August 2023

TD Wealth

# Memo from the Trenches

## Quotes:

**"It's tough to make predictions, especially about the future" – Yogi Berra**

## So, after 6 months of 2023….

One of the relentless challenges of being an active participant in the investment markets is trying to recognize my own propensity to confuse what I ***want*** from what I ***expect*.**

It seems that the consensus of investors is that we are waiting for what amounts to the most anticipated recession in recent memory and yet, it just isn't unfolding that way.

Let's review the business cycle. It starts with problems in supplying products, prices go up (inflation), interest rates increase because the demand for money to buy those products goes up and then the economy stalls as the cost of interest becomes punitive AND we are better rewarded for saving our money rather than spending it. Then economic activity declines (recession) and with that, interest rates follow. In fact, interest rates usually fall first anticipating this economic slowdown by a few months. In the meantime, unemployment goes up, profits decline, stock markets struggle, and we set up for the next cycle. And throughout this time, the "yield curve" – the difference between short-term interest rates and long-term rates - usually telegraphs to us the future changes in the economy.

Yet here we are with some powerful and conflicting data points and investment market responses. A significant jump in interest rates has stopped our inflation surge and though inflation rates are heading in the right direction, many economic data points are still on their merry way. New housing construction in Canada and the US is strong. Indeed, house prices in the lower mainland are basically unchanged – (although there has been a decline in Toronto real estate prices.) Who of my readers would have imagined that mortgage rates could go from below 2% to above 6% in a year and have no apparent impact on house prices? Not I for one.

Unemployment remains quite low in the US and Canada. Corporate profits have weakened but have been resilient and the sentiment remains "constructive" on future profits.

What do I want? What do I expect? Put bluntly I would like to see this period over and done with. Let's 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. Is that what I want… or what I expect? I guess it is what I want because I have client portfolios positioned for "defense" now and I am crossing my fingers for the opportunity to go on "offense"…. and I remain patiently waiting for that occasion.

For those interested in a little extra reading, a comment from Jamie McGeever on Reuters website from July 10th

https://www.reuters.com/markets/europe/elusive-us-recession-its-misleading-indicators-2023-07-10/?utm_source=Eloqua&utm_medium=email&utm_campaign=590162_NEWTDMNCCanadaTDNEWS&utm_content=MNCCA_TD_071123

# Another reminder…

This spike in interest rates does have some positives. The return on a one-year term deposit from TD that I can now offer is now 5.5%. (Note: I cannot promise this rate to be available in a regular TD Canada Trust retail branch). On Aug 1st there is a bond from BMO that matures June 30th, 2024, that offers a yield of 5.7% AND that more than half that return would be taxed as capital gains rather than interest.

High Interest saving accounts… Series A version is paying 4.55%

# RIF minimum withdrawals

This is a topic I have with clients from time to time. When to start RIF payments? This is an "insider" news article that discusses the fact that there are some internal industry and governmental policy makers reflecting on our current RIF withdrawal rules. Perhaps some changes in the future? We shall have to wait and see.

https://www.advisor.ca/tax/tax-news/finance-tables-report-reconsidering-rrif-minimum-withdrawal-rates/

# Inflation numbers.... WOW (in a good way)

In North America, US and Canadian inflation numbers are moderating exactly as we would hope to see. The June numbers for the US are now 3% and Canada's number came in at 2.8%. And finally, Europe is starting to see some inflation numbers that are encouraging although they appear to still be behind North America in their battle.

Today I was able to attend a seminar from one of TD Asset Management's more well-known portfolio managers, Damian Fernandes, and I put the question to him ".... where do short-term and long-term interest rates settle out in 1 to 3 years?" He suggested that his opinion and thesis is short-term rates settle at about 3% and that 5 to 10-year interest rates settle at about 4.0% - 4.5%. For context we are about 5% and 4.0% respectively now. He also mentioned that at the beginning of this year he would have handicapped the possibility of a recession at about 50% BUT, he would not reduce that chance to 35% as of today.

# US Model

July proved to be a very good month for the US model as value stocks seemed to fall into favor for the month. I would certainly like to see that momentum continue. Traditionally the US model has always been about high dividends from US stocks, from companies that you will know. It is a "value" approach. A defensive approach. A "no drama" approach. That said, the US Model has struggled over the last 6 to 12 months - having had a respectable 2022. The model posted a negative result in 2022 BUT, still managed to do better than most US benchmarks.

In the meantime, as you know from previous letters, 7 tech stocks in the US had been on a totally dominating run. (Microsoft, Amazon, Tesla etc.). Today, July 20th we are starting to see second quarter earnings reports being reported and today IBM and JNJ (which are in the model) had great results, resulting in material increases in share price. And though there have not been earnings reports today, Goldman Sachs and Amgen had a strong day as well.

Meanwhile, Tesla and Netflix had poor earnings reports resulting in meaningful declines in share price. And the other 5 high flying tech stocks took that as an opportunity to sell off in sympathy.

Is this a reversal of fortune for "value stocks" versus "growth stocks"? We shall see.

During the month we sold 3M and purchased JNJ. This did crystallize a loss for 3M but we have "booked" a lot of capital gains in the US model over the years and so I will use this opportunity for some tax planning for the future. We may well buy back 3M in the future. We cannot buy the share back for 30 days for tax reasons. The dividend yield on the US model is currently 4%.

## Fund Focus – the IA Clarington Floating Rate Income

This is a relatively recent addition to the funds I use. It is most often to be found in the TFSA "High Income" model. This group of investments in this model are focused on high interest income investment alternatives. This fund is invested in higher risk rated corporate bonds but ones that have very short periods until they mature and most importantly where the interest being paid is usually adjusted quarterly to current market interest rates (hence "floating rate"). Clearly an appropriate place to invest during a rising interest rate environment.

Here is a link for this interested in further research.

https://iaclarington.com/price-performance/funds/fixed-income?wc=9944

So that is it for July. Enjoy the summer. On occasion, please remind yourself to live for today. Eat, drink, and enjoy the company of friends and family during these glorious days.

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