

MARKET UPDATE

Q3 | January 1 to September 30, 2021

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Equities

To date, it's been a topsy-turvy year. At the beginning of 2021, the hot stocks were technology (Tesla), crypto-currency and small-caps. The Russell 2000 Small-Cap Index led the way with an almost 11% return in the first quarter (Q1 on the right) as investors chased after all the "flavour-of-the-day" names.

By the end of the second quarter (Q2 on the right), cyclicals and resource names were in favour, with the TSX 300 Composite Index up the most on the back of a declining US dollar and greater inflation fears. The Nasdaq Composite Index also rose because bond yields fell, thus favouring the mega-cap technology companies.

In the third quarter, the Delta variant of Covid19 slowed growth in many

Benchmark Total Returns (dividends re-invested) in Canadian Dollars (Jan. 1, 2021, to Sept. 30, 2021)

	Q1 RETURN	Q2 RETURN	Q3 RETURN	YEAR-TO-DATE RETURN
<i>Equities</i>				
Canada (TSX Composite Index)	8.06%	9.55%	-0.10%	17.51%
U.S. (S&P 500 Index)	4.54%	7.12%	3.51%	15.17%
World (MSCI Global Index)	3.45%	6.46%	2.82%	12.73%
NASDAQ Technology Index (CCMP)	1.38%	8.24%	2.34%	11.96%
Small-Cap (Russell 2000 Index)	10.97%	2.92%	-2.20%	11.69%
Europe (Euro600 Index)	2.64%	6.25%	1.05%	9.94%
Emerging Markets (MXEF)	0.68%	3.70%	-5.74%	-1.36%
<i>Fixed Income</i>				
Canada Mid-Term Corporate Bond Index	-3.76%	1.47%	-0.01%	-2.30%
Canada Long-Term Corporate Bond Index	-8.59%	2.92%	-1.49%	-7.16%
Canadian Real Return Bond Index	-7.62%	3.09%	-0.63%	-5.16%
Canadian Rate Reset Preferred Share Index	12.12%	5.68%	3.68%	21.48%
US Long-Term Corporate Bond Index	-9.79%	5.07%	1.14%	-3.58%
US Preferred Share Index	0.42%	1.23%	1.77%	3.42%

Data Courtesy of Bloomberg L.P.

global economies, the Federal Reserve talked about tapering its bond buying early to offset inflation and interest rates rose again. As a result, stock buying rotated into value names.

During the month of September, however, stocks fell with most major indices down between 2% and 5%. Talk began of “Stagflation”, a stagnant economy with rising inflation.

In a September 29th article from *Bloomberg Opinion* by Mark Gilbert, he wrote, “Thanks to the pandemic, global warming, stuck ships and other headaches, the world is suffering shortages of everything. Shortages make prices rise, making interest rates rise from the primordial ooze in which they’ve wallowed for the past year.”

Bonds

The easiest way to see how interest rates and bond prices have changed is to look at the 10-year US T-bond yield graph for 2021.



Data Courtesy of Bloomberg L.P.

From the chart above, the 10-year yield fell in March as the Covid19 Delta variant shut down economies. The yield reached a low by the end of July when inflation hawks disputed that inflation was not as transitory as the Federal Reserve predicted.

By September, yields rose as talk that the tapering of bond purchases through the Fed’s Quantitative Easing (QE) program may begin earlier than 2022.

In a September 29th story from *The Globe & Mail*, according to Goldman Sachs strategist Ryan Hammond, “U.S. inflation-adjusted bond yields have jumped this month and this makes the current environment a dangerous one for equity investors.”

Mr. Hammond estimates that, “The intra-month move higher in 10-year Treasury yields is a 1.4 standard deviation event. Historically, S&P 500 returns have been below average when yields move between one and two standard deviations and turn negative when the two standard deviation threshold is met. A rapid climb in inflation-adjusted yields is particularly ominous for technology and growth stocks.”

Kenneth Rogoff, a former chief economist of the International Monetary Fund and a professor of economics and public policy at Harvard University,

is equally concerned about stagflation, something we haven’t seen since the 1970s.

“The global economy suffered a massive supply shock in the 1970s, as Middle East countries massively hiked the price of oil that they charged the rest of the world. Today, protectionism and a retreat from global supply chains constitute an equally consequential negative supply shock.”

While the odds of stagflation appear remote because of deflationary pressures caused by lower technology prices and the aging populations in modern societies, it’s still important to understand that inflation can kill a lot of retirements.

Market Summary

After a 2% to 5% drop in global stock markets in September, we enter October with lots of questions. Among them are:

- Is unemployment rising or falling?
- Is inflation transitory?
- Is more bad news coming from China?
- Will corporate profits continue to rise at the 20%-25% rate that analysts have forecast?
- Is the stock market undergoing a small correction or are there greater storm clouds on the horizon?

The Latest Unemployment numbers out of the United States

The U.S. Labor Department reported that job creation for August was a huge disappointment, with the economy adding just 235,000 positions. Analysts' expectations for non-farm payroll growth was 720,000.

The labor force participation rate was unchanged at 61.7%, still well below the 63.3% in February 2020, the month before the pandemic declaration. Meantime, wages continued to accelerate, rising 4.3% on a year-over-year basis and 0.6% on a monthly basis.

Then the numbers for September came out and they were exactly the opposite. Initial filings for unemployment benefits totaled a seasonally adjusted 326,000 for the week ended Oct. 2, below the 345,000 Dow Jones estimate and a drop from the previous week's 364,000.

The numbers came at a time when most pandemic-related programs that extended unemployment benefits are winding down, and amid hopes that declining Covid cases will spark a round of more aggressive hiring heading into the fall.

Usually, when jobless claims are below 300,000, the U.S. economy does well, including the stock market. We'll have to see how things evolve in the coming months to determine the direction of the economy and whether or not we see continued expansion or contraction.

Rising Interest Rates Equal Falling Markets

The old axiom is "Never Fight the Fed". When rates rise, markets tend to fall and vice versa.

The last time the U.S. Federal Reserve raised rates by 0.25% was in the fall of 2018. Between October 1st and December 26th that year, the S&P 500 Index fell 15%. The FAANG stocks (Facebook, Apple, Amazon, Netflix and Google) fell an average 25%.

If rates rise, tech stocks are vulnerable because they need cheap borrowing costs to offset their high cash burn rates. And if earnings disappoint in conjunction with a rate increase, we could face a Price-Earnings multiple contraction and get a deeper correction than anticipated.

Meantime, non-tech stocks have already fallen. If the tech names fall, we'll have a complete stock market correction across the board.

Market Breadth is Deteriorating

According to data from *Bloomberg L.P.*, about 15% of S&P 500 stocks are more than 20% below their 52-week highs, but much larger swaths of the midcap and small-cap universe are down 20% or more. The latter groups are less tech-focused and more susceptible to an economic slowdown. Below are the percentage of stocks that are 20% or more below their 52-week highs:

- | | |
|-----------------|-----|
| → S&P 500 | 15% |
| → S&P Midcap | 30% |
| → S&P Small Cap | 48% |

What about the Evergrande situation in China?

After expanding rapidly for years and snapping up assets as China's economy boomed, Evergrande and its \$300 USD billion debt-load could lead to a contagion that may spread to markets beyond China.

In a *CNBC* interview, Mark Williams, chief Asia economist at *Capital Economics* said, "Evergrande's collapse would be the biggest test that China's financial system has faced in years. A banking failure triggered by the collapse of major property developers was the single most likely scenario that could lead to a hard landing in China. And the fact that financial markets aren't currently signaling alarm doesn't mean they won't."

A *Reuters* news report noted that, "Banks have responded to Evergrande's deteriorating cash flow. Some, including HSBC and Standard Chartered, have declined to extend new loans to buyers of two uncompleted Evergrande residential projects."

Currently, the Chinese government is trying to create a ring-fence around Evergrande to avoid potential contagion. This means it will probably let the company

go under, hurting its owners, executives and investors but that it will provide assistance (bail-outs) to suppliers and others doing business with Evergrande.

As a result, these actions could slow growth in the Chinese economy and stall global economic growth, another negative to stock markets worldwide.

That said, late October / early November is the time of year when I like to buy stocks. That's when markets are often weakest and the fourth quarter tends to be the best of the four in terms of corporate profitability. The next upward climb in the stock markets will rest on earnings growth and the direction of interest rates.

For investors, it's important to take profits on stocks that have doubled in the last year as they are most exposed to a correction. Also, be diversified, as it is a very risky time to have a lot of correlated stocks in your portfolio. And if you have cash to buy, focus on the ones that make up the lowest percentage weighting in your portfolio. They have the best chance of either maintaining their prices or going higher.

THE WORST WAY TO INVEST

By Annie Bertrand CIM

“The investor’s chief problem - and even his worst enemy - is likely to be himself.”

— BENJAMIN GRAHAM, ECONOMIST

When I started my career in the securities industry at the end of the 1990s, I hired a portfolio manager (PM) at the firm where I worked to manage my investments. Since it was my first experience investing in markets, I was happy to have a professional guide me.

The PM and I sat down to establish an Investment Policy Statement (IPS). The asset mix was determined to be an equal weighting between fixed income and equities. It appeared to be a good, rational plan.

Then, human nature took over. I was reading and hearing about the increase in value of technology stocks. Even though I had part of my portfolio invested in that sector, I went through a phase called, “Fear of Missing Out”, or FOMO.

I feared that I would miss out on a once-in-a-lifetime opportunity if I didn’t invest more money in that sector. Technology was the future. The Nasdaq index rose almost every day. I was convinced that I couldn’t lose money.

I called my portfolio manager to discuss adding more tech stocks to my holdings. She reminded me of my long-term investment plan. Bonds were an important defensive component of my portfolio even if they were not attractive at that time and my equity allocation was on target.

She also pointed out that the valuation of tech stocks was extremely high relative to market averages. She concluded that it didn’t make sense to add more funds to that sector. After our discussion, I agreed with her and left my portfolio intact. When Nasdaq took

its plunge in March 2000, I was glad for her rational thinking. I lost some money but it could have been much worse.

Today, with equity markets behaving similarly to Year 2000, it’s not surprising that investors are in a FOMO mood. It’s important not to be overconfident that markets will continue to rise. In these conditions, temptation is high to concentrate funds in a sector that has had amazing short-term growth and to let go of the “plain-vanilla” investments like bonds.

The moral of the story is this: Acknowledge your feelings but don’t act on them. You need to focus on your long-term goals and the reasons for your original target asset allocation.

At Liberty, we build portfolios like a hockey team. Depending on your risk tolerance and investment horizon, your portfolio should have a defensive section (bonds) and an offensive section (equities). Each piece is essential to reach your financial objectives.

We create a plan and are rigorous in implementing it. Currently, the bond portion may not be an attractive investment. However, it may become favorable again if a large stock market correction occurs and bond prices rise as investors run to the safety of bonds.

The equity portion of investor portfolios has had the wind in its sail for a while but it may be influenced negatively when central banks start raising interest rates again.

And, like a hockey game, view your investment time horizon accordingly. You and your advisor should use defensive and offensive strategies depending on the economic and financial situation in each period with the goal to be the winner when the siren goes off at the end of the game.

INVESTING FOR MILLENNIALS: FOCUS ON REAL RETURNS

By Victoria Zhang

When the market is volatile and fear is in the air, many new investors often buy Guaranteed Investment Certificates, or GICs. That's because a GIC works like a savings account - your principal is guaranteed and you earn interest on the investment.

While a safe instrument for return of capital, GICs cannot protect you against rising inflation. With inflation, the purchasing power of the GIC upon maturity will be eroded, particularly for those with a longer term.

For clients with fixed income mandates, Liberty has recently increased its exposure to inflation-protected bonds from an average weight of 5% to 10%. The reason behind this is straightforward. We care about *real returns*, not *nominal returns*.

The *nominal return* is the return made on an investment without factoring in expenses such as inflation and taxes.

The *real return* is money generated by an investment after subtracting taxes and inflation. The inflation rate is measured by the Consumer Price Index (CPI). The relation between the nominal return R_n , real return R_r , and the inflation rate (I) can be displayed by the following equation:

$$1 + R_n = (1 + R_r)(1 + I).$$

For example, if there is a bond with a high yield of 30%, a \$1,000 investment will return a total of \$1,300 by the end of the year. However, imagine that inflation over this period is 40%. This bond, therefore, has a real return of negative 7%, which isn't very appealing. Over time, inflation can, indeed, eat into your returns and decrease your purchasing power.

How to stay ahead of the inflation curve

Is there a way to beat inflation? Yes, an inflation-protected product can provide you with a higher return after inflation.

There are different types of inflation-protected products such as Exchange Traded Funds (ETFs) and inflation-protected bonds. Even though both products are considered to have low risk and can help to hedge against unexpectedly high inflation, ETFs have two drawbacks:

- They tend to invest in a basket of inflation-protected bonds but don't have a maturity date. Therefore, there are no opportunities for capital gains.
- ETFs also have a higher cost structure, as they charge management fees along with the trading commissions.

Therefore, investing in inflation-protected bonds such as Treasury Inflation-Protected Securities (TIPS) in the US and Government of Canada Real Return bonds (RRBs) are a better choice.

With conventional bonds, the nominal dollar value of the future cash flow is determined at the time of purchase while the purchasing power at maturity depends on the inflation during this period.

Inflation-Protected Bonds, meantime, are bonds where the principal is indexed to inflation and will increase in value during inflationary periods, especially when stagflation occurs.

Stagflation refers to an economy with rising prices (inflation) accompanied by slow economic growth and a high unemployment rate. It is one of the biggest risks that every investor faces but that's why inflation-protected bonds exist.

Investing in inflation-protected bonds helps us minimize the impact of the volatile market during this time and earn some "real returns". During these markets, we believe they are much better investments than GICs.

ARE REAL ESTATE INVESTMENT TRUSTS WORTH OWNING?

By Brett Girard CPA, CA, CFA

Historically, Real Estate Investment Trusts (REITs) have been major holdings in many retirees' portfolios. Attracted to the higher-than-average yield, older investors often rely on the frequent distributions to subsidize their retirement spending.

Given the ultra-low interest rate environment these past few years, other investors have also become interested in REITs as a mechanism to increase portfolio yield. Let's examine the merits of these investment decisions.

Canada's largest REITs

For the purposes of this article, we present data on Canada's five largest publicly traded REITs. These REITs are diversified by tenant and provide a broad overview of the market.

Largest REITs by Market Cap			
COMPANY	TICKER	CAD\$ BILLIONS	TENANTS - FOCUS
Canadian Apartment REIT	CAR.UN	\$10.2	Residential – Multi Family
RioCan REIT	REI.UN	\$6.9	Commercial – Retail
Granite REIT	GRT.UN	\$5.9	Industrial – Logistics/ Warehouse
Allied Properties REIT	AP.UN	\$5.1	Commercial – Office
Choice Properties REIT	CHP.UN	\$4.7	Commercial – Retail
Total		\$32.8	

Data courtesy of Morningstar.ca

Dividend performance

In Canada, REITs have become synonymous with yield. This could be a function of the dividend distribution schedule whereby REITs pay dividends monthly, as opposed to most other payors that distribute funds on a quarterly, semi-annually, or annual basis. The increased frequency of dividends may give the illusion of more yield, but this would be obfuscating the truth.

COMPANY	DIVIDEND YIELD	3-YEAR DIVIDEND GROWTH RATE
Canadian Apartment REIT	2.34%	2.9%
RioCan REIT	4.42%	-12.6%
Granite REIT	3.33%	3.3%
Allied Properties REIT	4.19%	2.9%
Choice Properties REIT	5.15%	0.0%
AVERAGE	3.89%	-0.7%

Data courtesy of Morningstar.ca

Based on the table above, the average current dividend yield is 3.89%. While this is materially better than the Bank of Canada's 1 year T-Bill rate of 0.26%, it is almost on par with the dividend yield of the Big 5 Canadian banks (3.82%).

As an investor, the inherent safety of Canada's banks, in part from government regulation, but also from size (\$578.1B Market Cap vs. the 5 largest REITs' \$32.8 market cap) should favour the banks.

Further, government regulation has prevented the banks from raising dividends since COVID-19 began. With the expectation of this directive being lifted, bank dividend yields are poised to rise higher than current REIT yields.

More concerning to those in, or approaching retirement, should be the negative dividend growth over the last three years of -0.7% per annum. With consumer prices rising, investors should be able to rely on dividends to grow on a real basis (inflation adjusted) and preserve purchasing power.

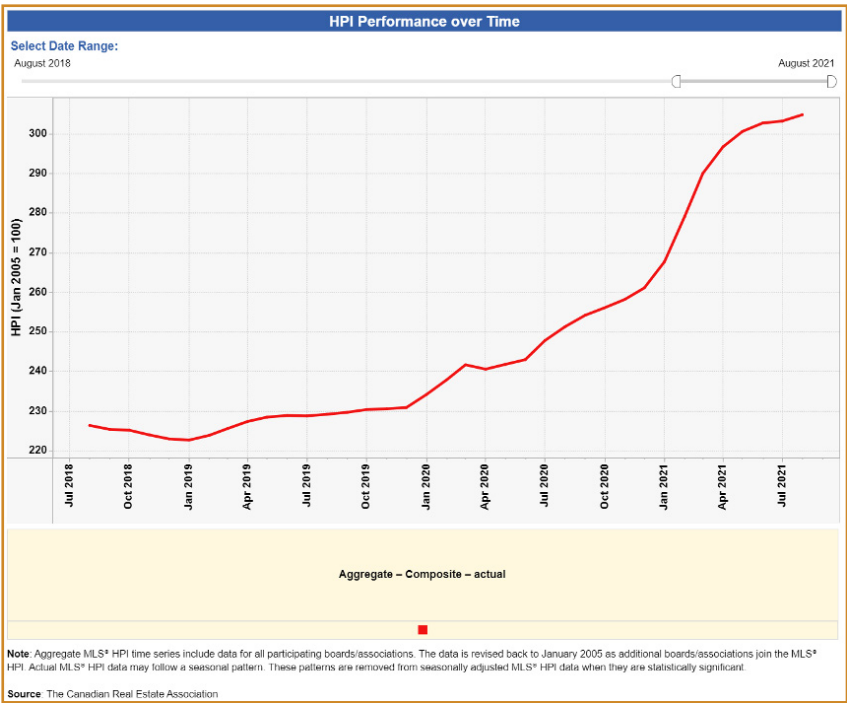
That is not possible with a negative dividend growth rate. Even with RioCan REIT removed as an outlier, the dividend growth rate since 2018 has only increased by 2.3% a year. The bottom line is, an investment in REITs, known for their dividends, actually impairs purchasing power.

Price performance

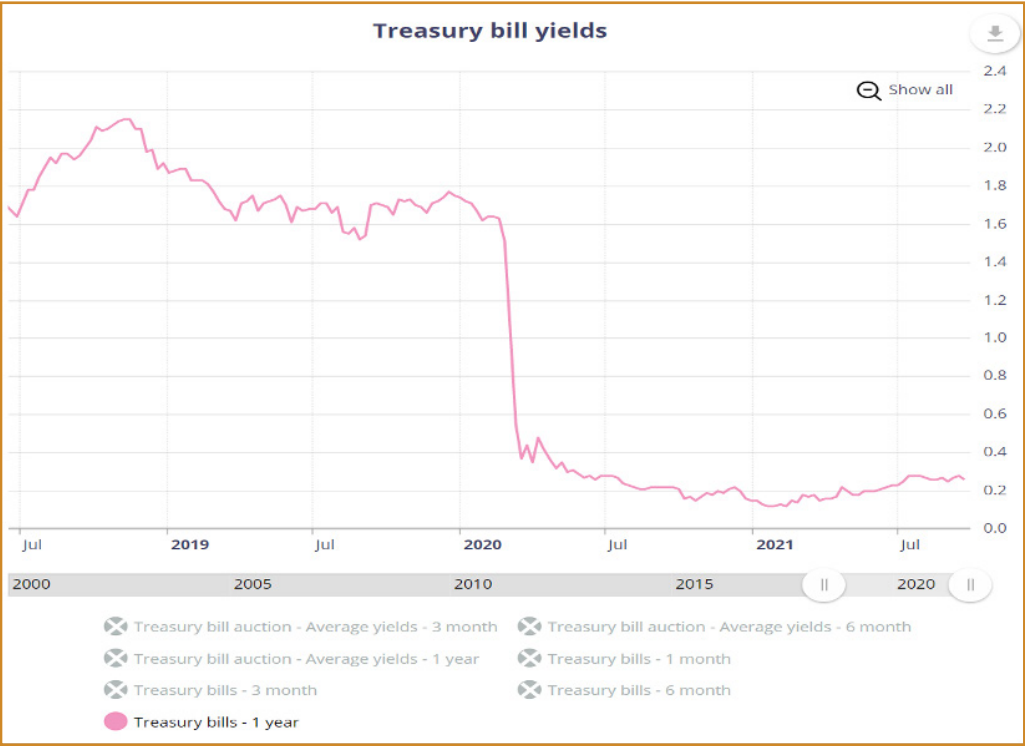
Dividends aside, REITs must also be evaluated for their capital appreciation. Over the last three years, per the chart below, the 1-year Bank of Canada T-Bill rate has fallen precipitously, most notably through early 2020 as the COVID-19 virus spread.

Since REITs are leveraged, this decrease in rates would have made borrowing progressively cheaper for them over the period. Provided borrowed funds could be reinvested at higher rates of return, this should have been a tailwind for the REITs, but it wasn't.

When examining residential home prices across Canada through the same period, as expressed by the



Canadian Real Estate Association's (CREA) Aggregate Composite MLS® Home Price Index (MLS® HPI), the capital appreciation is notable in the table on page 9.



Data courtesy of Morningstar.ca

The chart above details the average value of a Canadian home, showing an increase in the index from 226.3 to 304.7. This translates to 34.6%, or 10.4% annually. However, failing interest rates did not have the expected impact on the REIT sector. What should have been a boom time for REITs in terms of profitability and return did not occur. REITs returned just 5.8% per annum (see next page) and underperformed both residential real estate and the S&P TSX 60 (up about 9% over the same period).

Since most readers already have exposure to the residential real estate market through their principal residence and/or vacation property, adding incremental publicly traded real estate in an investment portfolio only increases correlation risk.

While property prices have benefited from lower interest rates, a reversal of that trend may have negative consequences.

Liberty's opinion on REITs is:

- Canada's largest REITs have failed, in aggregate, to grow dividends over the last three years. In the context of historically low interest rates and access to cheap capital, this is concerning. Should interest rates rise, REIT dividends may not grow at all.

- Canada's largest REITs have had varied price performance. This creates a challenge for investors looking to build a diversified basket of REIT holdings.
- COVID-19 and falling interest rates had an outsized impact on residential home prices. For most investors, this exposure should be sufficient. If these trends reverse, investors should aim for less, not more real estate exposure.

COMPANY	AVERAGE ANNUAL PRICE RETURN	3-YEAR PRICE RETURN
CAPREIT	8.2%	26.8%
RioCan REIT	-3.4%	-9.9%
Granite REIT	18.5%	66.3%
Allied Properties REIT	-1.8%	-5.3%
Choice Properties REIT	7.5%	24.1%
AVERAGE	5.8%	20.4%
vs.		
Aggregate Composite MLS® Home Price Index (MLS® HPI)	10.4%	34.6%

Data courtesy of Morningstar.ca

FUN WITH MATH: HOW THE PRICE-TO-SALES RATIO CAN HELP IDENTIFY OVERVALUED NAMES OR INDUSTRIES

By David Driscoll

Is the stock market undervalued, overvalued or just about where it should be? There are no clear answers to this question. However, there are some ways to determine where a market, an industry, or a stock may stand relative to the current state of the economy. One such analytical tool is the price-to-sales ratio.

The price-to-sales ratio (Price/Sales or P/S) is calculated by taking a company's market capitalization (the number of outstanding shares multiplied by the share price) and dividing it by the company's total sales or revenue over the past 12 months. The lower the P/S ratio, the more attractive the investment.

“While technology names had the greatest number on the list, we were surprised to find that REITs (Real Estate Investment Trusts) accounted for the second highest sector.

While there is no particular magic about 10 times sales being the unique true sign of overvaluation, it has gained fame from a statement that Scott McNealy, co-founder and CEO of Sun Microsystems, made to *Bloomberg L.P.* in 2002:

“Two years ago, we were selling at 10 times revenues when we traded at \$64. At 10 times revenues, to give you a 10-year payback, I have to pay you 100% of revenues for 10 straight years in dividends. That assumes:

- I can get that by my shareholders.
- I have zero cost of goods sold, which is very hard for a computer company.
- I have zero expenses, which is really hard with 39,000 employees.
- I pay no taxes, which is very hard.
- You pay no taxes on your dividends, which is kind of illegal.
- There is \$0 for Research & Development (R&D) for the next 10 years.
- I can maintain the current revenue run rate without R&D.

“Would any of you like to buy my stock at \$64? Do you realize how ridiculous those basic assumptions are? You don't need any transparency. You don't need any footnotes. What were you thinking?”

We recently looked at the TSX 300 Composite Index, the S&P 500 Index and the EuroStoxx Index to find companies trading at greater than 10 times sales. Here's what we found:

INDEX	NUMBER OF COMPANIES WITH A PRICE / SALES RATIO OVER 10	PERCENTAGE OF INDEX
S&P 500 Index	72	15%
Euro600 Index	80	13%
TSX 300 Composite Index	24	8%

Data Courtesy of Bloomberg L.P.

From the data in the box above, the S&P 500 Index had the greatest percentage of companies with price-to-sales ratios over 10. This implies that the U.S. market is the most expensive of these major indices.

While technology names had the greatest number on the list, we were surprised to find that REITs (Real Estate Investment Trusts) accounted for the second highest sector. On the TSX 300 Composite Index, 6 of the 24 firms with P/S ratios over 10 were REITs.

Other sectors in the group of high P/S ratios were cannabis firms, cruise lines, stock and other market exchanges and new IPOs (Initial Public Offerings).

Below are the top five from each index – I removed the cruise lines because their numbers distort the list. For example, Norwegian Cruise Lines had a price-to-sales ratio of 325, followed by Royal Caribbean (228) and Carnival Corp. (157).

As you can see, the overall P/S ratio for each index was between 2 and 3 times. The names in the table below had P/S ratios 10-20 times greater than the average. We don't believe this is sustainable.

At Liberty, we own Shopify in our Tax-Free Savings Accounts (TFSA's). To manage the risk, we've re-balanced the position on 4 separate occasions.

The moral of the story? For investors, be forewarned about stocks like the ones below. They trade at these lofty multiples because their share prices have often risen too far, too fast and should be re-balanced after they've doubled the first time.

That's because the share prices often fall the next year as revenues can't grow fast enough to reduce the ratio to the normal average around 2 or 3 times.

TSX COMPOSITE INDEX	P/S RATIO	S&P 500 INDEX	P/S RATIO	EURO600 INDEX	P/S RATIO
Lightspeed Commerce	59	MSCI Inc.	29	Porsche Auto	234
Shopify Inc.	47	Nvidia Corp.	25	EQT AB	52
Ballard Power	45	Moderna Inc.	24	CTS Eventim AG	44
Cronos Group	38	Intuitive Surgical	23	Sagax AB	34
Nuvei Corp.	32	Adobe Inc.	22	Argenx SE	33
Average Index P/S Ratio	2		3		2

Data Courtesy of Bloomberg L.P.

CLIENT QUESTIONS

What are the portfolios telling Liberty about the stock and bond markets?

The question may appear backward but this is actually how Liberty manages individual portfolios. Individual stock weightings by percentage and even asset mixes on a percentage basis often signal what actions need to be taken next.

For example, say an investor has a target asset mix of 60% stocks and 40% fixed income. Today, that mix might be 65% stocks, 25% fixed income and 10% cash. The portfolio suggests that stocks have risen while bonds have fallen, throwing the asset mix out of whack.

It indicates that all the available cash should be allocated to fixed income. While some investors would be loathe to add to their fixed income today with yields so low, it is a good signal that equities are probably overpriced.

Since bonds are half as risky as equities, a stock market correction would hurt the portfolio badly if the cash was allocated to more equities.

If I want to buy more stocks, where should I buy?

If you're a contrarian investor like Liberty is, the best stocks to buy are the cheapest ones that offer the best long-term value. Below is a table of current Price-Earnings multiples for some global market indexes as of September 30th.

That's because bonds could rise in value while the stocks drop in price. During the market correction in March 2020, the stock market fell 35% but bond prices rose, leaving the average 60 / 40 mix down only about 8%. This helped preserve capital and let portfolios return to break-even faster.

Remember, making money in the long-run isn't how much you make in the good years, it's about how much you avoid losing during the bad ones.

The math bears this out. If you start with \$1 and drop 35%, you'll be down to 65 cents. Breakeven at \$1 now requires a 54% return, much higher than the 35% collapse.

If you drop only 8% to 92 cents, you only need a 9% return to get back to \$1, much easier to accomplish in any year than trying to earn a 54% return.

Buying bonds now is the better strategy.

From the table below and based on the lowest Price-to-Earnings figures, the cheapest market index would be the MXEF, or stocks in the emerging markets. That's because slow vaccination rates in these countries and their subsequent economic slowdowns caused stock

STOCK INDEX	CURRENT VALUE	CURRENT EPS (\$)	CURRENT P/E MULTIPLE	ESTIMATED FUTURE EPS (\$)	ESTIMATED P/E MULTIPLE
Russell 2000 Small-Cap	2204.37	\$4.97	443.5	\$68.37	32.2
Nasdaq Composite	14448.58	\$117.70	122.8	\$452.98	31.9
S&P 500	4307.54	\$166.98	25.8	\$201.87	21.3
MSCI Global	3028.75	\$128.39	23.6	\$154.70	19.6
Dow Jones	33843.92	\$1660.75	20.4	\$1841.97	18.4
Euro600 Stoxx	454.81	\$20.56	22.1	\$27.83	16.3
TSX 300 Composite	20070.25	\$1052.21	19.1	\$1258.82	15.9
Emerging Markets (MXEF)	1251.28	\$80.46	15.6	\$95.04	13.2

Data Courtesy of Bloomberg L.P.

selloffs during 2021 while the other market indexes rose through the year.

The low P/E ratio is also indicative of the concerns over China’s economy and whether or not we’ll see the opposite of globalization of trade with more barriers to trade.

The table also suggests that analysts’ expectations of earnings growth is around 25% in 2022. I’m hard-pressed to see that happen because of all the economic pressures we’re facing today: Wage increases, higher taxes, supply chain logistics problems, Covid19 shutdowns, inflation, a slowdown in Chinese demand and higher energy prices.

In Liberty portfolios, Jardine Matheson has suffered stock price malaise in 2021 because its sales are all in emerging markets. As a result, the percentage weighting of a 30-stock portfolio might have Jardine

What makes European shares attractive?

While U.S. companies enjoyed better earnings after a corporate tax cut in 2017 from 35% to 20%, low interest rates in Europe made borrowing costs cheaper there.

Looking at corporate income statements, a reduction in taxes payable helped U.S. firms report higher net profits. A cut in interest expense did the same for European corporations.

The table below shows two things: The weighted-average coupon of corporate debt by its Index members and the weighted-average years to maturity of that debt.

INDEX	WEIGHTED-AVERAGE COUPON	WEIGHTED-AVERAGE YEARS TO MATURITY
TSX 300 Composite Index	4.12%	7.23
S&P 500 Index	3.59%	9.10
Euro600 Stoxx Index	2.24%	6.04

Data Courtesy of Bloomberg L.P.

at 2% with a high-flyer like Danaher Corp. at 4%. If the average holding is 3%, the portfolio signals that more Jardine shares should be purchased.

We don’t have to sell Danaher shares because it hasn’t yet breached the 6% weight when we automatically re-balance. Instead, the signal is to allocate more cash to Jardine shares.

The logic is that if all the companies in the portfolio have the same historical growth rates, Jardine’s share price in 2022, all things equal, should rise faster than Danaher’s.

Hedge funds are into this logic too. Many are buying the Emerging Market Index (MXEF) and shorting both the Russell 2000 (RTY) and Nasdaq Composite Index (CCMP) as a long-short trade because of the undervaluation of the former and the overvaluation of the latter two indexes.

It makes sense that Canadian companies pay a higher coupon than their U.S. and European counterparts because they’re smaller firms and carry a lower credit rating – the lower the rating, the higher the borrowing cost.

Currently, European companies pay an average 2.24% on their outstanding debt, far lower than U.S. or Canadian firms.

What looks great today (European stock prices) may not look so great tomorrow. That’s because these firms may have a problem in 6 years. If rates are higher but revenues are not, their profits will suffer because of higher expected interest expenses and lower net income.

Also, if rates rise, this could signal the end of companies using leverage to buy back shares, leading to lower earnings and lower payouts for executives who may find it harder to grow their business.

IN OTHER NEWS:

While the world searches for kindness during this COVID-19 lockdown period, Liberty has continued to focus on doing our share to make the world a better place for our employees and our clients.

Some progressive actions that we've taken internally include fully paid maternity leave, equal pay regardless of gender and opportunities for women and other minorities to grow in the organization in roles that aren't usually available to them in our industry.

When we started our firm in 2015, we made a promise to our clients to cut our fees. Today, we're announcing our second fee cut. It will take effect on October 1, 2021.

Asked by some in the industry why we might jeopardize our profits in favour of lower fees, our response is this:

- There's no Liberty without the client. Something that's often lost in the industry is that it's not the firm's money, it's the client's money. It should be a privilege to manage that money. This is our way of saying to the client, "Thank you."
- The lower the fees, the better the performance. Compounded over many years, the cost savings add up, leaving more money for the client.

→ We're cutting fees because we can. Our business model was created to take advantage of scale. Now that we have it, we can continue to build the firm successfully, even with lower fees.

→ As we reach our future goal in assets under management (AUM), our objective is to have our retail clients paying institutional rates, unheard of in this industry and a challenge to others to cut their fees.

Combined with solid performance, constant investor education, unparalleled customer service and customized, global portfolios, cutting fees is just another way for Liberty to separate ourselves from the thousands of rival firms and provide our clients with the business relationship they want.

The new fee tier is noted below:

ASSETS UNDER MANAGEMENT	RATE PER ANNUM
Up to and including \$2,000,000	0.95%
\$2,000,001 to \$3,000,000	0.90%
\$3,000,001 to \$4,000,000	0.85%
\$4,000,001 to \$5,000,000	0.80%
\$5,000,001 to \$7,000,000	0.75%
\$7,000,001 to \$10,000,000	0.63%
\$10,000,001 to \$20,000,000	0.50%
Over \$20,000,000	Negotiable

If you have any questions, let us know.

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