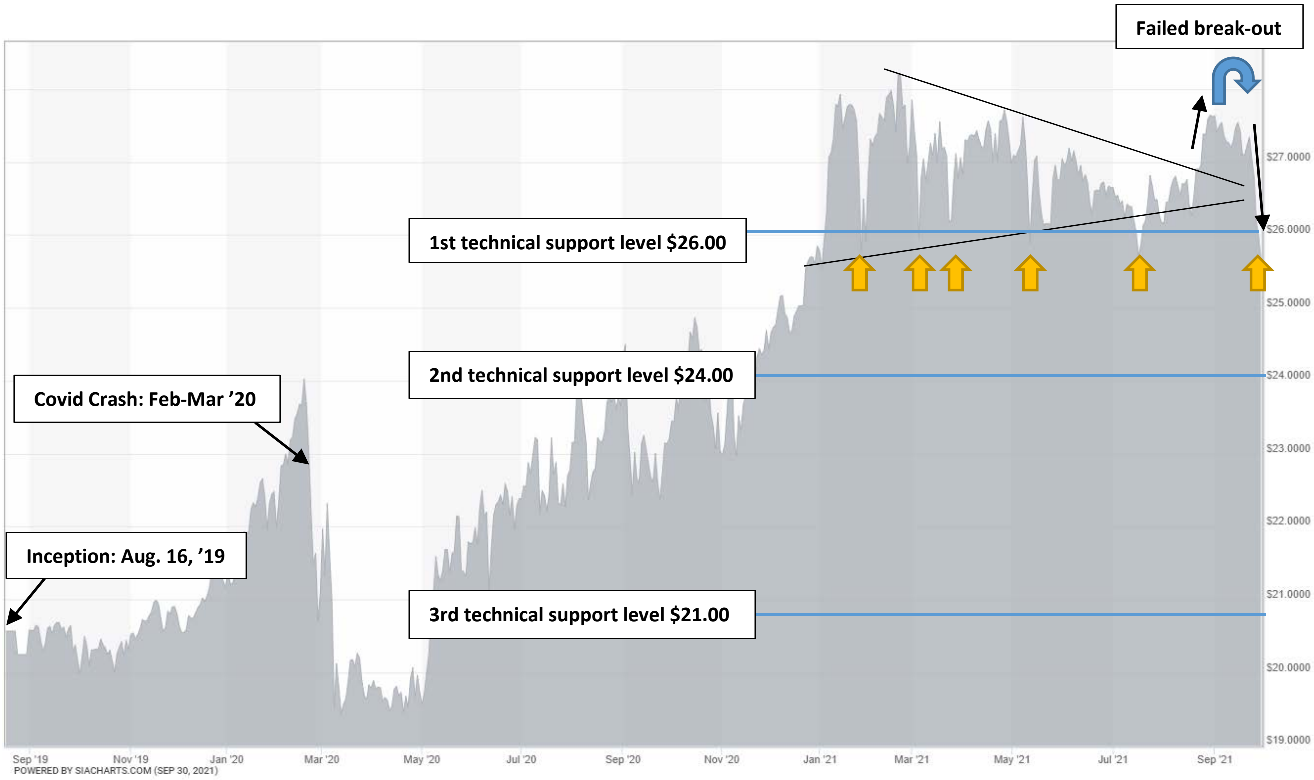
October 2021 Commentary

The August surge in performance turned out to be a head-fake as September lived up to its billing as seasonally the worst month of the year. Our model posted a loss of 4.67% for the month, bringing our year to date to 7.18%. Since the August close was an all time record high, as of this writing we are sitting about 5% off our all time highs. We're expecting more of the same in October, see below.

Market Update

Briefly, let's update where we are from a broad technical perspective. We've been following the progress of our private equity pool for several months, using it as a proxy for the overall market. We've noted that it has been forming a flag formation while also hitting, and rebounding from, the same support level several times (yellow arrows in the graph). In August we broke out of that flag formation to the upside. In our last letter we said that while the break-out was clear, most of the time break-outs fail at the first attempt. That turned out to be exactly the case.

The yellow arrows show five prior occasions where we bounced off a major support level at around the $26 per share level. With the failure of the break-out in September, we find ourselves back at that same support level but threatening to breach it to the downside decisively. This is supported by an array of fundamental factors lining up against us. Our next level of support is about 5% below where we are at the end of September. This level could be reached in a single day with the speed of market corrections these days. If we breach that, there is nothing but air until just under $21 – the 3rd technical support level noted below. While certainly not a prediction, if we do get there it would be the fourth time we have experienced a correction in the range of 20% since we went live with our model at that start of 2013.



Covid Chaos

As we've said many times, we never use our predictions to make changes in your portfolio. Often things seem obvious in hindsight and it feels like you could have done something to navigate a better path. The reality is you can get lucky once or twice but long term it is hard to do consistently and consistency is what you need for success.

Having said that, we can analyze what we see around us and prepare to act. We see a lot of potentially bad things on the immediate horizon in October. As it stands, our model has still not fully re-entered the market so we've remained somewhat cautious. About 20% of what we would normally allocate to stocks is still cash. We think the full impact of the draconian Covid shutdowns is about to be felt. There are severe supply shortages in basic shipping and manufacturing inputs like cardboard, rubber, and semi-conductors. The U.S. has bizarrely choked off their own nascent energy production so gas prices have skyrocketed to the point where they are back begging the Saudis to pump more oil. Covid benefits have seen a huge swath of the labour force decide to stay home and collect benefits instead of working, causing a labour shortage. That's a partial list.

Creative accounting has allowed companies to paper over these cracks in the first two quarterly earnings seasons of 2021. Q3 earnings are upon us in mid-October and we think they could be ugly. You can only shuffle things around an income statement for so long before reality has to be reflected in earnings and thus stock prices. Indeed, in the lead up to October, companies are already starting to give cautious guidance to their upcoming earnings reports.

Inflation is heating up, driven by a complex brew of factors. Covid policies have choked off production leading to supply shortages. Interest rates have been lowered to avert a crisis thus goosing anything financed. Government deficits have exploded. People are losing confidence in the political process and the competence of their leadership. We've been writing about this for years and it's here. This is causing money to flow into anything that has tangible value. You are seeing and feeling the effects of this in your house values. One of the biggest and most influential money managers in the world, Blackrock, has purchased more than 20,000 private residences in Florida in the US$300-500k range as an alternative to buying government bonds.

Inflation is not as simple as many think. It is not the result of excess money printing. If people trust your money you can print it without inflation. If it were so simple, Europe would have been able to engineer some inflationary relief for their off the rails spending over the last decade. No, money printing is usually a *symptom* of lost confidence. When people no longer trust money to keep it's value, they spend it as fast as they get it. That is when governments resort to printing to keep up.

So we would not be surprised for October to deliver a big negative result for stocks. That's the bad news. The *good* news is that investment results are like a clubhouse sandwich. You get bread, then bacon, then bread, then chicken, then bread and so on. Every market crack-up both follows, and is followed by, a big surge in performance. A big decline in stock prices is far and away the most reliable predictor of a surge in stock prices. We should be ready to take advantage of this.

Remember what we have said repeatedly for a few years now. We believe the stock market is nowhere near a long term peak. We see that about ten years down the road. Prices will be driven, ironically, by bad news. As things worsen and our confidence in government declines, it will drive money out of government bonds and into private assets. The biggest private asset category is stocks. So the good news is that if we have indeed started a correction, it will offer the latest opportunistic entry point into a stock market that has a long way to go. What's more, going by history, after September we are probably a quarter to a third of the way to the bottom already.

Practical Actions

We keep a list of clients who fall into one of three groups:

1. they've got a bunch of cash to invest
2. they are contemplating changing their long term asset allocation to hold more stocks
3. they want to leverage to invest

If you are in one of these groups and we haven't had a conversation, let us know. We'll add you to our list. When the opportunity happens, we'll let you know immediately.

Be forewarned. When the time comes and we call, conditions will be such that the last thing you are going to want to do is buy more stocks. The market will be all red, you won't know how far down things are going to go because they are still falling and you'll just want the ride to stop before making any moves. By the time you are comfortable, the opportunity to get in cheap and set yourself up for a huge advance will be lost. So visualize it now, like a downhill skier practising in their head before going down the slope. That way when the time comes, you'll be half way to executing instead of starting from zero. It could be soon.

October 2021 Portfolio Review

Mott Liokossis Hypothetical Model sector breakdown at the end of September 2021:

Cash	6.49%
Diversified Global Equity Portfolio	38.32%
Diversified Canadian Equity Portfolio	12.28%
Specialty Retail	9.24%
Electronics & Semi-Conductors	8.45%
Energy	6.70%
Aerospace & Defense	6.66%
Conglomerates	6.00%
Computer Software	5.86%

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Hypothetical Model Growth Portfolio Holdings at the end of September 2021:

% Held	Security	Symbol	Sector	Price	Yield
6.49%	Cash				
6.66%	Airbus SE ADR	EADSY	Aerospace & Defence	$ 42.34	0.00%
8.45%	ASML Holding NV	ASML	Electronics & Semi-Conductors	$ 944.87	0.35%
12.28%	BMO SIA Focused CDN EQ ETF	ZFC	Canadian Equity Portfolio	$ 39.30	1.62%
6.70%	Cheniere Energy Inc.	LNG	Energy	$ 124.21	0.00%
9.24%	Dicks Sporting Goods	DKS	Specialty Retail	$ 151.88	4.59%
5.86%	Infosys	INFY	Computer Software	$ 28.22	1.29%
38.32%	SIA ML Global Tactical Pool	SWI220	Global Equity Portfolio	$ 25.67	6.13%
6.00%	Textron Inc.	TXT	Conglomerates	$ 88.53	0.09%

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	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Yearly Returns	
2021	1.62%	5.68%	-3.36%	0.16%	-0.85%	0.93%	0.28%	7.23%	-4.67%				**7.18%**	**YTD**
2020	4.33%	-3.90%	-8.54%	-0.42%	9.70%	2.13%	5.75%	4.27%	-2.33%	-1.79%	7.32%	6.07%	**22.93%**	
2019	1.36%	5.01%	3.75%	3.46%	-1.58%	2.58%	0.97%	1.13%	-3.33%	-0.78%	3.76%	2.09%	**19.73%**	
2018	2.84%	0.81%	-0.31%	-0.79%	5.53%	8.19%	-0.60%	8.18%	-2.65%	-14.70%	-0.14%	-2.73%	**1.60%**	
2017	-1.26%	3.11%	0.49%	3.26%	1.45%	-3.95%	0.50%	2.31%	3.43%	7.33%	2.38%	-3.57%	**16.08%**	
2016	-3.29%	-2.97%	-3.70%	-3.30%	5.04%	1.01%	3.03%	-0.56%	1.02%	-1.70%	1.56%	0.82%	**-3.36%**	
2015	9.73%	2.78%	3.71%	-8.98%	10.69%	-4.34%	7.93%	-5.39%	-3.05%	0.23%	-0.08%	1.84%	**13.89%**	
2014	6.39%	6.38%	-5.18%	-4.67%	1.52%	1.94%	-1.25%	5.18%	-2.40%	0.44%	5.70%	3.57%	**18.08%**	
2013	6.00%	4.20%	3.95%	-2.83%	9.64%	-3.67%	4.06%	3.65%	3.29%	3.42%	4.68%	2.66%	**45.96%**	

Monthly Returns

Monthly & Annual Returns for the Mott Liokossis Hypothetical Model Growth Portfolio.
Performance reflects actual trades executed in our maximum growth model and does not include fees or expenses.
We use this hypothetical model as the basis for our clients' portfolios.

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Growth of $10,000	Jan. 04, 2013 - September 30, 2021
Mott Liokossis Model (MA02)	$33,111
World Stock Equal Weight Index (EWI785)	$22,475
Canadian Stocks (XIC.TO)	$20,460
Canadian Bonds (XBB.TO)	$12,952
Commodities (DBC)	$9,567

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