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WEALTH *builder*

THE YEAR THAT WAS



By Gordon Pape, Editor and Publisher

It was a year that will go down in history. A year in which more than 1.5 million people died of a strange new disease. A year in which the world economy was decimated. A year in which our personal lives were turned upside down.

It began promisingly enough. Stock markets were at all-time highs. Unemployment was near record lows. We were in a Goldilocks economy.

There were some murmurs about a new virus in a remote part of China, but no one paid much attention except a few epidemiologists. That was the other side of the world; things were fine here.

In mid-March, we suddenly awoke with the shock that we weren't fine at all. The words coronavirus and COVID-19 suddenly became real and dangerous. Governments reacted. Businesses were shut down. Offices laid off staff or told them to work from home. People were locked in their houses or apartments, forbidden even to see loved ones. Borders were closed. Life as we had always known it suddenly vanished.

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We've been living in this bizarre new world for almost a year now. There are signs of hope on the horizon, in the form of new vaccines. But it's going to be many months before enough people are immunized to allow life to return to some semblance of normalcy.

The stock market's initial reaction to the onset of the pandemic was predictable. All the major world indexes plunged. The Dow lost 8,571 points (29%) between Feb. 5 and March 18. The S&P 500 fell 923 points (27%). Nasdaq slipped 2,400 points (25%). In Toronto, the S&P/TSX Composite was down 5,287 points (30%) in roughly the same time frame. It was a similar story no matter where you looked: London, Frankfurt, Tokyo, Hong Kong.

What was not so predictable was the sharp rebound in share prices. This turned out to be the shortest bear market in history. By mid-August, the S&P 500 had regained all the losses from the February-March plunge and moved into

new record territory. The other U.S. indexes followed suit, but the TSX is still below its record high.

Bonds also delivered a pleasant surprise for investors. The U.S. Federal Reserve Board had already started to cut rates in 2019 but the onset of the pandemic forced the U.S. central bank to take drastic action. The federal funds rate was slashed to near zero and the Bank of Canada followed suit. Yields on 10-year benchmark government bonds fell to all-time lows in both countries.

Bond prices strengthened as a result. As of Dec. 12, the FTSE Canada Universe Bond Index was up 7.75% for the year. The Long-Term Bond Index was ahead 9.98%.

In short, it was a dreadful year to endure from health and lifestyle point of view. But investors did surprisingly well, whether they were holding bonds or stocks. That's something to be grateful for. But what we all want from 2021 is an end to the pandemic and a return to a normal lifestyle.

OUR PANDEMIC STOCK PICKS

The pandemic changed our lifestyles dramatically and that impact was reflected in the stock market. Companies that had been thriving saw their business models shattered. The hospitality industry, office property REITs, the travel sector, and brick and mortar retailers were among those that saw revenues and profits plunge. At the same time, e-commerce companies, transportation firms, supermarket chains, and leading-edge telecommunications companies saw a surge in business.

Here at IWB, we moved quickly to help readers navigate the rapidly evolving stock market environment. In March, when the

devastating impact of the pandemic became apparent, we switched gears and advised buying stocks that were positioned to do well in these challenging times. Here are some of the picks we introduced that are related to the pandemic.

Gilead Sciences (NDQ: GILD). In the early days of the pandemic, we started to search for companies that were leaders in the development of a vaccine or treatment for COVID. Gilead qualified on the treatment side, with its anti-viral drug remdesivir. Early trials indicated some success in speeding recovery and remdesivir was used to treat President

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Pandemic picks—continued from page 2...

Trump when he contracted COVID. But the stock never took off. It was recommended at US\$69.36 and closed Friday at US\$60.76.

Canadian Solar (NDQ: CSIQ). Green energy companies turned out to be one of the main beneficiaries of the pandemic year as oil and gas stocks tumbled. Contributing editor Adam Mayers added Canadian Solar to our list in mid-March when it was trading at US\$16.80. The stock closed at US\$37.95 on Friday afternoon for a gain of 126%.

TeleDoc Health (NDQ: TDOC). Virtual visits with a doctor were already gaining ground but the pandemic changed what had been a convenience into a necessity. Contributing editor Glenn Rogers introduced us to this stock in late March at US\$169.50. It closed Friday at US\$199.58, for a gain of 18%.

J.B. Hunt Transport (NDQ: JBHT). On a harrowing drive in late March from Florida back to Toronto, I was struck by the fact the highways were almost deserted except for transport trucks moving essential supplies. On my return, I reintroduced this company to our Recommended List at US\$89.76. It closed Friday at US\$138.89 for a gain of 54%.

Pfizer (NYSE: PFE). We continued to look for pharmaceutical companies that we felt would be in the forefront of vaccine development. In April, I recommended Pfizer, which is now the first company to bring a vaccine to market. The price at the time was US\$35.38. It is now US\$41.12 for a gain of 16%.

DocuSign (NDQ: DOCU). Working from home meant important documents had to be signed legally but remotely. Glenn Rogers introduced us to DocuSign in May, which provides the software for

such transactions. The price at the time was US\$116.56. The stock closed Friday at US\$225.49, up about 93%.

Metro Inc. (TSX: MRU). Most retail businesses had to close down or reduce capacity, but grocery stores thrived. In June, contributing editor Shawn Allen advised buying Metro Inc. at \$57.42. The stock hit a high of \$66.25 in September but has since pulled back to \$59.27.

The Clorox Company (NYSE: CLX). The demand for cleansers and sanitizers kept companies like Clorox working overtime. I recommended the stock in June at US\$197.57. It flirted with US\$240 in July but has since pulled back to US\$201.73.

Pinterest (NDQ: PINS). In late June, associate publisher Richard Croft added social media platform Pinterest to our list. With people encouraged to remain at home, on-line communications flourished, and this company gained millions of new users. Richard advised buying the stock at US\$23.21; it closed Friday at US\$71.13 for a profit of 206%. In the same issue, Richard also recommended Facebook at US\$238.79. It is now trading at US\$273.55.

Johnson & Johnson (NYSE: JNJ). The hunt for leading vaccine developers brought Glenn Rogers to JNJ in June. Its product is behind by a few months, but some experts believe it could eventually dominate as it requires just one shot. The stock was recommended at US\$143.83 and is now at US\$152.95.

Roku (NDQ: ROKU). Staying at home meant higher demand for television and streaming services. That boosted revenue for Roku, which provides platforms for most streaming companies. Glenn Rogers recommended the stock in August at US\$146.85; it has now more than doubled to US\$330.87.

THE WORLD OF 2021



**By Richard N. Croft,
Associate Publisher**

I intend to stay awake this New Years' Eve. Not so much to welcome in 2021 but to make sure 2020 fades into oblivion. I

would like to say that 2021 will be a better year but that would be redundant. It is hard to imagine it being any worse!

What I *can* say is 2021 may be better than many base case scenarios are suggesting. Bay and Wall Street watchers are cautiously optimistic, once we get through North America's dark winter. It is clear, as COVID waves intensify, that a return to normalcy will rest on the efficacy of the vaccine. Which, by the way, some 40% of Americans say they will not take!

The other risk relates to logistics: how soon will the vaccine get approved, delivered, and injected into the arms of willing participants? Both Canada and the U.S. intend to rely on the logistical support of their respective Armed Forces. However, Canada is at a disadvantage in that we do not manufacture the vaccine. That means getting into a queue behind other countries that have manufacturing facilities. The expectations for the economy to return to some semblance of normalcy will hinge in large part on the time it takes for the vaccination process to surpass herd immunity.

I may be the consummate optimist, but I think we may have herd immunity by

early second quarter 2021. I also think the November rally and rotation into value stocks is a pre-emptive move to front run a back to normal scenario. This will likely continue in January 2021, just in time for President-elect Joe Biden to take credit for a recovering economy!

Assuming this optimistic forecast becomes reality, what should investors expect in terms of 2021 market performance? There is not much to draw from in terms of historical precedence. The closest example would be the 1918 Spanish flu epidemic that stretched across four waves before dissipating in 1920, about one year after the conclusion of World War One.

During the winter of 1919, global economies were floundering. Unemployment was rampant as workers opted to stay at home rather than risk getting sick. The Spanish flu killed more Americans than World War I and II, the Korean war, Vietnam, and the skirmishes in Iraq and Afghanistan combined. There was no safety net for small business or for workers. No central bank quantitative easing and no vaccine. The only path to normalcy was to let the virus run its course and eventually weaken to the point that it was no longer a threat.

As World War I ended, the Spanish flu was going through its second wave. Returning veterans brought the virus with them, which caused the third wave to roll in like a tsunami. At the same time factories were re-tooling assembly lines,

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shifting production away from guns and tanks into consumer goods like autos and household appliances. But workers were hard to find given the virality of the virus.

By 1920, the influenza virus was still a threat, but fewer people were dying. Workers began to feel comfortable returning to work, which allowed businesses to expand, thereby creating an abundance of good manufacturing jobs. At the same time, governments rolled out massive stimulus programs to help with Germany's reconstruction efforts and rebuild North America's infrastructure. Trade unions promoted a solidarity movement, wages increased, and the economy gained momentum, giving rise to the roaring '20s.

Aside from not having to rebuild after a prolonged global conflict, the similarities are striking. The U.S. government will almost certainly approve massive stimulus to rebuild the country's infrastructure. Business will quickly expand to meet pent-up consumer demand.

From what I can see, consumers are in better shape, with less debt and more equity. Consumer sentiment is positive, thanks to the wealth effect bolstered by rising house prices and historically high stock values.

A cocktail that includes disposable income, positive sentiment, and pent-up demand should have an outsized impact on global growth. This is especially true in North America, where consumer spending accounts for 70% of GDP. The numbers could be staggering, and that consumption will flow to many of the biggest companies that influence the broader market indexes.

U.S. stocks

It is not a question of *if* consumer spending will bolster 2021 earnings for the S&P 500 companies. The question is by how much?

The service sector, particularly restaurants, should rebound quickly. Travel will experience a slow recovery, not likely returning to pre-COVID levels for three years. Within the travel and leisure sector, airlines face the greatest challenge as business travel will be muted. Having experienced three years of Zoom meetings, it is hard to imagine that businesses will re-discover the need to expend capital to engage in face-to-face meetings.

The same reasoning would apply to office space. Office rental REITs will have a difficult time maintaining pre-COVID distributions after experiencing 12 months where work from home was as productive without the challenges of fighting traffic to get to the office.

However, real estate experts remain split on whether the post-pandemic norm will embrace work from home or back to work. Most likely we will see a compromise; say two days at home, three days at the office! Ultimately, it will come down to weighing the work from home cost savings to the negative impact from lost collaboration within the office culture.

Brick and mortar retailers will also face hurdles as online shopping will continue to take a bite out of their operations. Seniors who typically would visit stores have become a meaningful cohort in online shopping and I doubt that will change post-pandemic.

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Financial services (i.e., money centre banks) should see a surge in valuations through 2021. As the pandemic recedes, governments will loosen dividend and stock buyback restrictions at a time when banks have an inordinate amount of capital that can be returned to shareholders. Most likely, banks will find they have far more capital than needed to deal with potential loan losses, which is why I suspect, there was such a strong resurgence in bank valuations over the past three weeks.

And then there is T.I.N.A. (There is No Alternative). With ultra-low interest rates, which should remain in place for the foreseeable future, bonds will languish to the benefit of equities. In fact, one could argue that the main risk through 2021 will be inflation, which will suppress bond prices. This suggests that fixed income investments may be the highest risk asset class in the current environment.

The broader market indices should flourish. The Nasdaq 100 index will benefit from its weighty exposure to tech giants. I think the Nasdaq could add 20% in 2021 with slightly lower double-digit returns for the broader S&P 500 Index and the Dow Jones Industrial Average.

If you think my position is too speculative, consider the role that small retail investors may play in 2021. Round number milestones tend to embolden small investors and the Dow hitting 30,000 on Nov. 24 is a viable jumping-off point.

My best guess would see the Dow hit 33,000, the S&P 500 top 4,200, and the Nasdaq 100 eclipse 15,000 by 2021 year-end. Like I said, I may be overly optimistic, but one does not want to miss upside opportunities when they appear so randomly.

The Canadian story

Canada should be able to take advantage of the same opportunities. One could argue that Canadian consumers are better off than their American counterparts. Government benefits that were extended during the pandemic lockdowns were more generous than what was provided to U.S. consumers. This was made possible by a good working relationship between federal and provincial leaders, buoyed by the view that “too much” is better than “not enough.” Canada should benefit from these efforts during the recovery phase.

That said, the Canadian economy will face the same challenges as the U.S., in terms of excess office space, business and leisure travel, and brick and mortar retail. As for the big five Canadian banks, I think they are better positioned than the U.S. money centre giants.

Compelling balance sheets should allow more capital to be returned to shareholders through dividend increases and stock buybacks. I can see a 20% bump in Canadian bank valuations through 2021.

We should also see a revival of cross-border trade now that we do not have to face the whims of a tweeting President. The new trade pact with Britain and the return to normalcy across Asia will likely bear fruit within the Trans-Pacific Partnership.

Politically, I believe there is a high probability that a federal election will occur in 2021. The Liberals are a minority government and could be forced into an election should there be challenges with vaccine availability. If

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Canadians see inoculations occurring in Britain and the U.S. while we wait in the international queue for supplies, the bloom of Prime Minister Trudeau's rose will quickly fade. That would be fodder for the opposition parties.

The more likely scenario would see a successful launch of the vaccine, the onset of herd immunity, and the beginning of a return to normal. At that point, as the Liberals outlined in their economic update, they would unleash a massive stimulus program to jump-start the economy. I suspect the Liberals would be willing to call an election at that point and take their chances at the polls.

The other wildcard is our relationship with China. Fortunately, for the world, the Chinese Communist party remains a relic in terms of its feeble attempts to mesh capitalism within a worker state. Were it not for the Communist Party intrusions into private enterprise China would already be the world's biggest economy!

It is my hope that Canada will be able to engage in serious trade with China as the case against Huawei Executive Meng Wanzhou works its way through the system. In fact, recent negotiations with the U.S. Justice Department that would see Meng return to China make that a distinct possibility, perhaps before the swearing in of the new U.S. President. In my world, we will see the return of the two Michaels to Canada and Meng to China. Although, this may simply be my predilection for optimism.

Risk factors

The main challenge facing a post-pandemic era is the surge in government deficits. On the positive side, governments can manage higher deficits

as ultra-low interest rates suppress carrying costs. At this stage, governments are constantly rolling debt with 4% to 6% coupons into new debt yielding 1% to 1.5%. In theory, governments could borrow four times as much with the same carrying costs. The debt load should not be a major issue until rates begin to rise.

That said, low interest rates cannot immunize governments from taking action to reduce the overall debt levels before it becomes an inflationary threat. It is one thing to stimulate the economy through infrastructure spending, it is quite another to lose sight of longer-term fiscal prudence.

The other black swan risk rests with efficacy of the vaccine. Certainly, the results from the stage 3 trials were encouraging, but we will not know the long-term impact until we see the results from mass inoculations. I do not see this as a major risk, but it does exist on the margins.

Summary

Despite the risks, I think 2021 will set the stage for a roaring '20s redo, cutting a broad swath across the economic landscape, boosting wealth for those in the accumulation phase, and preserving income for those making regular withdrawals from their portfolio. Markets will not go straight up...they never do! Volatility will experience periodic spikes...it always does! But, within those fits and starts there will be an upward bias that, dare I say, will be alchemy for the optimists.

Finally, I want to wish everyone the best for the holidays. Perhaps they will not be what we all had hoped for. But take comfort in knowing it will get better!

RICHARD CROFT RECOMMENDS PIC.A

Premium Income Corporation Class A

TSX: PIC.A *Closed Friday at \$4.82*

BUY

Given my 2021 outlook, I want investors to put some aggressive capital towards Canadian banks. One way to do this is through the Premium Income Corporation Class A shares (TSX: PIC.A, closed Friday at \$4.82). This is the capital share in a split share structure managed by Mulvihill.

The capital shares are essentially a long-term call option on the big five Canadian banks. The return is generated through quarterly dividends rather than price

appreciation in the shares. Currently, PIC.A pays a \$0.10 per share quarterly dividend which produces a yield of 8.3%.

If the big five banks rally in 2021, we will see an increase in the dividend or a spike in the price of the shares. One cautionary note: this is a volatile and not very liquid security. It is suitable only for your risk capital.

Action now: Buy.

PRICE INCREASE

This is a final reminder that the annual price of the IWB will increase by \$10 plus tax effective Jan. 1. You can beat the increase by renewing any time before then, no matter when your membership expires. Call us toll-free at 1-888-827-8229 or go to www.buildingwealth.ca/subscribe.

LAST ISSUE OF 2020

This is our final issue of 2020 (we publish 44 times a year). On behalf of our staff and contributing editors, I'd like to wish everyone a safe and happy holiday season. We'll see you again on Jan. 4, for what will hopefully be the start of a much better year.



GLENN ROGERS LOOKS TO THE FUTURE

Contributing editor Glenn Rogers join us with a recommendation for a beaten-down company that is the backbone of the travel industry. Glenn has worked with private equity and venture groups on a variety of projects leading to successful exits for investors. He held senior executive positions in both Canada and the U.S.

Now that 2020 is finally, mercifully, drawing to a close we can begin to look forward to next year with renewed hope for a less traumatic 2021. Politically, things should settle down in the U.S. and there are two, possibly three, vaccines about to be deployed. It will take time before everyone can get access but at least there's a possibility for return to some form of normalcy over the next several months. There's already been a fair amount written about stocks that will benefit from the reopening of the economy and I intend to add to that narrative today.

A number of stocks have done well during the closedown, like Home Depot, Lowe's, and anything to do with outdoor activities like bicycles and golf. We will likely see a rotation out of those sectors into some of the more beaten down areas that will benefit most from a turnaround.

Highfliers like Zoom, Netflix, and Roku will likely face some profit taking, not because there's anything fundamentally wrong with the companies but because they're priced for perfection. I have begun to take profits in some of those stocks while still maintaining a position, but I'm also looking for areas that are the most likely to improve once this nightmare is behind us.

Stocks that will benefit from infrastructure and increased economic and industrial activity include the resource stocks which have already been moving up.

Companies like Freeport McMoRan and Southern Copper are showing strength based on the hope that manufacturing countries like China will be ramping up and the demand for those basic materials will continue to accelerate. I share that point of view and own both those stocks, along with companies like Boeing and General Electric, which I have recommended in the past.

In addition to the sectors mentioned, many analysts like the airline stocks along with the hotel and resort stocks, of which Disney is a good example. In fact, anything to do with travel should see an improvement since there is so much pent-up demand. I own Jets, which is an EFT that holds a basket of airline stocks and have also added Hilton and Marriott.

However, the company I want to focus on now is called Sabre Corp. (NDQ: SABR). It's a software for services firm that powers the back end of many travel related companies. These include airlines, airports, car rental companies, cruise lines, hotels, search engines, and online travel agencies.

Prior to the pandemic, the company's

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stock was trading north of \$27 (figures in U.S. dollars) but it got crushed earlier this year for obvious reasons, trading down as low as \$8. It closed Friday at \$10.97.

The company performs essential services for its clients, which has made it indispensable to them. It's a huge addressable market, with the industry generating over \$8 trillion annually when things are normalized.

Located in Texas, the company has a number of business platforms and two main business groups. The hospitality group provides technology for over 40,000 hotels and resorts in 160 countries. The platform allows these clients to optimize revenue and improve the guest experience.

All this is invisible to the public but essential to making sure the travel experience runs smoothly. So, when you phone or go online to book a hotel room you are likely using the Sabre central reservation system.

Beyond the reservation platform, the company provides software that manages inventory, guest profiles, staffing, and payment systems. As you can imagine, these services are very sticky, so that once a customer is fully integrated into the system it's very difficult switch to a competitive platform.

The second area is centered around the airlines and travel agencies. Sabre provides the technology for mobile devices and all other platforms people use in their daily lives. This provides clients with data rich solutions, which are essential to remain relevant in a

competitive marketplace like travel.

Recently, the company partnered with Google to build and deploy an AI informed retail package that provides adaptive pricing capabilities. This allows clients to further fine tune and monetize their various services. Sabre has always been innovative and this recent partnership with Google is just another example. If you use companies like Bookings.com and Expedia, they're both built on the Sabre platform.

Financially the company recently reported third-quarter results and they were way down from last year, as you would expect. Revenue totaled \$278 million and the company reported a large \$312 million dollar net loss. All this is due to COVID-19. By comparison, last year in the same quarter the sales were over a \$1 billion.

In response to the huge revenue declines, the company cut \$200 million out of their annual cost base, extended long term debt, and raised additional capital to provide liquidity until the environment improves. It saw steady improvement in the last quarter and bookings have begun to recover. Once the vaccines are widely distributed this company should return to growth.

Baron Rothschild once famously said: "The time to buy is when there is blood in the streets." That is certainly the case here. I personally have taken a large position and believe over the next couple of years we will see the stock price triple once business returns to normal.

Action now: Buy with a target of \$30.



GLENN ROGERS'S UPDATES

Recommendations are
colour-coded:
Green indicates Buy
Yellow indicates Hold
Red indicates Sell

Vail Resorts NYSE: MTN

*Originally recommended on Jan. 29/18 (#21805) at \$229.88.
Closed Friday at \$277.98. (All figures in U.S. dollars.)*

SELL

Background: This company owns 37 ski resorts in North America and Australia, including Canada's famous Whistler Blackcomb. It also operates three urban ski centres.

Performance: The stock was trading at over \$250 a share in late February. Then came the virus and it dropped as low as \$125 before turning around. The shares are now about 14% higher than at the start of the year. That's an amazing performance in the time of a pandemic.

Recent developments: Vail's results for the 2020 fiscal year (which ended July 31) saw a sharp fall-off in revenue due to the pandemic. Nonetheless, the company was able to post net income of just under \$100 million (\$2.42 per share, fully diluted).

Dividend: The stock was paying a quarterly dividend of \$1.76 per share but the company suspended it in April due to the financial uncertainty created by the pandemic.

Comments: This stock has held up amazingly well during the pandemic. The strategy of preselling season passes has kept the cash position in much better shape than you would have guessed. This will be the third season in a row that I haven't skied out my pass and yet they've got my money and had to provide no services to keep it.

But things are locking down in the U.S. again, as they are in Canada. We recently canceled a planned ski trip to Colorado so it's hard for me to imagine that this company can continue to defy gravity from the stock price point of view.

We've made a nice profit since we recommended Vail in January 2018 at \$155.60. The stock closed Friday at \$277.98 for a gain of 78.7%. However, I think it's time to ring the register on this one and have another look at it once the ski season is over and we can assess how badly impacted the company was once the results come in.

Action now: Sell.

Nike Inc. NYSE: NKE

Originally recommended on July 24/16 (#21628) at \$56.73. Closed Friday at \$137.41. (All figures U.S. dollars.)

**SELL
HALF**

Background: Nike is based near Beaverton, Oregon. It is a world leader in designing, marketing, and distributing athletic footwear, apparel, equipment, and accessories for a wide variety of sports and fitness activities.

Wholly owned subsidiary brands include Converse, which designs, markets, and distributes athletic lifestyle footwear, apparel, and accessories, and Hurley, which designs, markets, and distributes surf and youth lifestyle footwear, apparel, and accessories.

Performance: This has been another surprise pandemic winner. People have been getting outside for exercise and they've been investing in new runners and apparel. We recommended Nike in July of 2016 at \$56.73 and updated it last June when it was trading at \$95.73. It closed Friday at \$137.41 for a gain of 142.2% since the original recommendation.

Recent developments: Nike recently reported results for the first quarter of fiscal 2021 (to Aug. 31). Revenue for the quarter was \$10.6 billion, about the same as the year before on a currency-

neutral basis. On-line sales were up 92%, offsetting revenue declines in wholesale and Nike-owned stores.

Earnings per share were \$0.95 (fully diluted), up 10% from the same period in fiscal 2020.

Dividend: The company increased its dividend by 12.2% to \$0.275 per quarter (\$1.10 per year), effective with the December payment. The stock yields 0.08%.

Comments: Like Vail Resorts, the company now has a very rich valuation, trading at about 35 times 12-month forward earnings. Analysts have had targets in the low \$140s for a while and the stock is now bumping up against those numbers.

The company has far outpaced its competitors like Adidas and Under Armour, both of which are down for the year. But at this price you have to wonder whether a lot of the future growth is already in the stock.

At this point you should consider booking half profits for a gain of 142.2%.

Action now: Take half profits.