Update Edition

THE INCOME INVESTOR

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BALANCED PORTFOLIO CONTINUES TO GAIN

By Gordon Pape, Publisher and Editor

Nobody wants to hear about balanced portfolios these days – at least not the traditional 60/40 split type. Small wonder. The stock markets kept setting new records right up to September. Meantime, bonds were retreating on rising interest rates and cash was paying almost nothing.

At some point, all that will change, however, and a balanced portfolio will look attractive again. Consider how this one has done over the ten years since it was created in September 2011.

The Income Investor Balanced Portfolio offers a conservative mix of stocks, bonds, and cash. It’s a little light on the fixed income/cash side, with 35.9% of the total assets. But that’s reasonably close to the traditional 60/40. This type of portfolio is likely to underperform when stock markets are strong but reduces risk when bear markets emerge.

That’s what we’ve seen here. The portfolio was down about 14% at the time of the March 2020 stock plunge, but that was a much better result that the overall market produced.

One reason for that was that in 2019, I increased the bond weighting to 42.5% from 34.5%. Bonds lost ground when the market fell, but they did much better than stocks.

Since then, the portfolio has rebounded, as we’ll see in a moment.

This portfolio had an initial valuation of $25,027.75. The goal was to achieve a return that at least matched the best available five-year GIC rate plus two percentage points.

That means the target varies with the rise and fall of interest rates. The best five-year rate I can find right now is 2.3% from Oaken Financial, which would make our current target 4.3%. Yes, that’s modest but this is meant to be a low-risk portfolio.

Here’s a summary of the securities we currently hold and how they performed over the period since I last reviewed this portfolio in April. Prices are as of the close of trading on Oct. 8.

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Balanced portfolio - continued from page 1…

GIC. We have $5,000 in a one-year GIC with Peoples Bank, paying 1.55% at maturity on April 23, 2022. That's not a great return but a core GIC provides stability.

iShares Convertible Bond Index ETF (TSX: CVD). This ETF invests in a portfolio of convertible bonds. These can be exchanged for common shares in a company at a pre-determined price, so they offer the potential of a capital gain along with regular bond interest. We added this fund at the time of our last update, at a price of $18.59. The price is up by a quarter since then plus we have received monthly distributions totaling $0.425 per unit.

iShares Core Canadian Universe Bond Index ETF (TSX: XBB). This fund tracks the performance of the broad Canadian bond market. It's been a rough year for bonds as rates have been rising but we more or less broke even in the latest review period. The units lost $0.29 but we received monthly distributions totalling $0.404 per unit.

Canadian Apartment Properties REIT (TSX: CAR.UN). This REIT invests in apartment units across Canada. The units were badly hit at the start of the pandemic as investors were concerned about rent defaults. But they have since recovered and are now trading at close to their all-time high. In fact, things have been going so well that the directors approved a 5.2% increase in the monthly distribution, effective with the August payment. The units gained $3.30 during the period, and we received monthly distributions totaling $0.702 per unit.

Pembina Pipe Corp. (TSX: PPL, NYSE: PBA). Pembina's price was brutalized by last year's onset of the pandemic and the simultaneous drop in oil prices, But it has been slowly clawing its way back, boosted in part by the promise to keep paying its $0.21 monthly dividend. The shares gained $4.15 since the last review and we received five monthly dividends, due to timing.

Brookfield Renewable Partners (TSX: BEP.UN, NYSE: BEP). At the time of our last review, I wrote that we were too heavily weighted in this security and sold 50 units. Too bad we didn't sell more; they're down $5.74 since as green energy stocks as a group have taken a hit after a strong run-up in 2020. We're not selling any more, however; this one will come back. We received two quarterly distributions of US$0.30375 each.

Brookfield Infrastructure Limited Partnership (TSX: BIP.UN, NYSE: BIP). This Brookfield partnership invests in infrastructure projects world-wide: railroads; ports; transmission lines; toll roads; etc. It has performed better than Brookfield Renewables recently, with the units advancing $3.12 in the latest six months. The units pay a quarterly distribution of US$0.51.

BCE Inc. (TSX, NYSE: BCE). We added Canada's largest telecom company to the portfolio a year ago at this time at $56.20 per share. Since then, the stock is up almost $7, and the quarterly dividend has been raised to $0.875 per share. Total gain for the year was 18.6%.

Bank of Montreal (TSX, NYSE: BMO). The financial sector was hit hard by last year's March selloff but has recovered strongly. BMO shares were up $14.69 in the latest six-month period, and we are receiving quarterly dividends of $1.06 per share. At the sharply higher price, the yield is down to 3.2% from 6.8% last fall, however we expect a double-digit dividend hike when the Office of the Superintendent of Financial Institutions lifts its ban on increases by financial institutions.

Fortis Inc. (TSX, NYSE: FTS). We added this St. John's-based utility at the time of our last review, at $55.37 per share. It hasn't moved much since (a gain of $0.39 per share) but that's par for the course with utilities. The company is increasing its dividend by 6% in December to $0.535 per quarter.

Cash. We invested $2,508.24 in a high interest savings account with Motive Financial that was paying 1.25% at the time. We earned interest of $15.68 for the period.

Here's how the portfolio stands now. Commissions have not been factored in. For simplicity, Canadian and U.S. dollars are treated as being at par for purposes of the calculations.

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Income Investor Balanced Portfolio (a/o Oct. 8/21)

Security	Weight %	Total Shares	Average Cost	Book Value	Market Price	Market Value	Retained Income	Gain/ Loss %
GIC	9.7	1	$5,000.00	$5,000.00	$5,000.00	$5,000.00	$38.75	+0.08
CVD	8.4	230	$18.59	$4,275.70	$18.74	$4,310.20	$97.75	+ 3.1
XBB	15.8	260	$32.02	$8,326.30	$31.32	$8,143.20	$128.44	-0.06
CAR.UN	9.1	80	$49.69	$3,975.20	$58.60	$4,688.00	$276.96	+24.9
PPL	6.4	80	$47.49	$3,799.50	$41.06	$3,284.80	$184.80	- 8.7
BEP.UN	14.0	160	$11.98	$1,916.18	$45.16	$7,225.60	$187.98	+286.9
BIP.UN	12.2	90	$16.58	$1,492.30	$70.22	$6,319.80	$659.80	+367.7
BCE	7.4	60	$56.20	$3,372.00	$63.19	$3,791.40	$207.48	+18.6
BMO	10.1	40	$108.26	$4,330.40	$130.70	$5,228.00	$497.60	+32.2
FTS	4.9	45	$55.37	$2,491.65	$55.76	$2,509.20	$45.45	+ 2.5
Cash	2.0			$989.18		$1,004.86		
Total	100.0			$39,968.41		$51,505.06	$2,325.01	+34.7
Inception				$25,027.75				+115.01

Comments: The stock markets faltered in September although only one of our securities, Brookfield Renewables, took a really bad hit. Over the last six months we saw some decent gains from BMO, BCE, and Canadian Apartment REIT. Overall, we gained 3.2% in the latest six-month period.

The cumulative gain since inception 10 years ago is 115%. That works out to an average annual compound growth rate of 7.96%. That's well above target and a good return for a portfolio with a heavy bond/cash weighting.

Changes: The portfolio looks quite solid at this point so I'm not going to make any changes. We don't have adequate retained income balances in any of our positions to add another 10 shares/units, so we'll keep those earnings for future use.

We now have a cash balance, including retained earnings, of $3,329.87, which will continue to be invested with Motive Financial's Savvy Savings Account. The rate is still 1.25%. I will review the portfolio again in March/April.

TOP PICK

Here is our Top Pick for this month. Prices are as of the close of trading on Oct. 8 unless otherwise indicated.

Gibson Energy Inc. (TSX: GEI, OTC: GBNXF)

Type: Common Stock
Current price: C$23.00, US$18.44
Entry level: Current price
Annual payout: $1.40
Yield: 6.1%
Risk Rating: Higher risk
Recommended by: Gordon Pape
Website: gibsonenergy.com

The business: If you're dead set against fossil fuels, move on to the next story. This is a Calgary-based oil infrastructure company. Its principal businesses consist of the storage, optimization, processing, and gathering of crude oil and refined products. The company's operations are focused around its core terminal assets located at Hardisty and Edmonton, and also include the Moose Jaw Facility and an infrastructure position in the US.

A year ago, nobody wanted energy stocks based on fossil fuels. Green was in, black was out. Shares of Gibson traded as low as $17.60 last fall. The dividend yield at that point was 7.7%. But a year later, everything has changed. Green energy stocks are in a prolonged bear market. Traditional oil and gas stocks are riding high.

The security: We are recommending the common shares of Gibson Energy, which trade mainly on the TSX.

Why we like it: Yield. The company raised its dividend by a penny last March to $0.35 per quarter ($1.40 annually). That's a return of 6.1%. Equally important,

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Gibson did not cut its dividend during the drop in oil prices that coincided with the onset of the pandemic.

Financial highlights: Second quarter results showed an increase in revenue of 111% over the same period in 2020 to $1.675 billion. However, net income was down 22% to $32 million ($0.22 per share). The company said this was "driven by the availability of time-based opportunities created by significant volatility in commodity markets during the prior quarter as well as limited opportunities and reduced margins within the Crude Marketing business in the current quarter".

Distributable cash flow was $92 million, a $2 million or 2% decrease over the second quarter of 2020. Payout ratio on a trailing twelve-month basis was 73%, near the low end of Gibson's 70% – 80% target range.

Risks: Obviously, anything associated with the oil industry is risky these days and subject to high volatility. But the fact that Gibson came through the 2020 oil crunch and the pandemic without major damage and felt confident enough to raise its dividend this year is encouraging.

Distribution policy: Dividends are paid quarterly, in March, June, September, and December.

Tax implications: Payments are eligible for the dividend tax credit if the shares are held outside a registered plan.

Who it's for: This stock is for investors seeking a high yield security who are willing to accept above-average risk and are comfortable investing in fossil fuel companies.

How to buy: The shares trade actively on the TSX. They are also listed on the Pink Sheets (over the counter) in the US as GBNXF, however volume there is very light, and a limit order is advised.

Summing up: This is one of the best yields you'll find from a quality company. But let your conscience be your guide when it cones to the global warming issue.

Action now: Buy.

YOUR QUESTIONS

Canadian General Investments

Q – I was wondering if it would be possible for you to comment on Canadian General Investments Ltd. This company appears to trade at a discount to its NAV. Can you please explain why? Is this a potential value trap? Also, this company has a history of consistently increasing it dividends. - Stewart B.

A – This is a closed-end fund that trades on the TSX under the symbol CGI. To my knowledge, it's the oldest fund of its kind in Canada, having been launched in 1930. Since 1956, it has been managed by Morgan Meighen & Associates.

Closed-end funds have a limited number of shares. There is no new supply unless the company implements a secondary issue, which is rare.

You would think that, logically, units of closed-end funds would be worth more because of the limited supply. But that's not the case. Many closed-end funds trade at a discount (sometimes a deep one) to their underlying net asset value. For example, CGI closed on Oct. 8 at $38.25. The NAV on that day was $58.18. That's a discount of almost $20!

This fund has historically traded at a discount to net asset value, but this is close to the extreme end of the range. What's behind it? It's not the portfolio. The top 10 holdings are solid, growing companies like Shopify, NVIDIA, Lightspeed Commerce, CP Rail, TFI International, Descartes Systems, and Amazon.com.

But income investors won't be excited by the quarterly dividend of $0.22 a share ($0.88 a year). That translates into a yield of 2.3%. However, as our reader points out, the fund does have a history of raising its payout annually, usually by a penny per quarter.

The law of supply and demand plays a role in the pricing as well. Average trading volume for CGI is only 3,784 units per day. If more people are looking to sell than to buy, it drives down the trading price. Some investors track the discount ranges of closed-end funds, buying when they are at their peak and selling when they approach their lows. But finding the information can sometimes be difficult. Many of these funds are not known for their transparency, CGI shows a 10-year average annual compound rate of return of 14.25% on its share price. That makes it worth considering, especially if buying stocks at a deep discount appeals to you. But be warned: the units are trading at close to their highest price in 25 years. If the market hits a correction, they're going to drop in value. – G.P.