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THE INVASION AND YOUR MONEY

By Gordon Pape, Editor and Publisher

Sometimes, you wish your predictions would never come true. This is one of them.

In early January, I wrote that one of the headwinds facing stock markets this year was the potential for war. I specifically referenced the increased Chinese pressure on Taiwan and the massive Russian troop build-up on Ukraine's borders.

Last Monday, Russian President Vladimir Putin took the first steps to subvert Ukraine by declaring two breakaway regions to be independent states and sending in "peacekeepers". Two days later, he launched a massive invasion after delivering a highly provocative speech in which he claimed that Ukraine was an artificial country carved out of Russia and threatened any nation that dared to intervene with what many interpreted as a nuclear attack.

Continued on page 2...

The invasion and your money	1
RRSPs still a good choice	4
Shawn Allen updates CN Rail, lululemon, RioCan	5
Your Questions: 3M not performing	10
Gordon Pape updates Equitable Group	11
Your Questions: Real Return Bonds	12

Next issue: March 7

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Invasion—continued from page 1...

The West responded by piling on sanctions but, as President Joe Biden admitted during a press conference on Thursday, these will take time to have a significant impact and will do nothing to stop Russia's efforts to take over Ukraine and replace the government with a puppet regime. Let's be realistic: it was a pitifully weak response.

In fact, the sanctions may backfire. Putin anticipated this move long ago and has been solidifying his relations with China. He met with President Xi Jinping at the Beijing Olympics on Feb. 4 and it's not difficult to guess what they agreed on.

No action until the Games were over. It's no surprise that the Russian hammer was dropped within hours of the torch being extinguished.

No condemnation. Even with Russian cruise missiles blasting Ukraine's air bases and cities and live pictures of tanks rolling across the border and Russian soldiers in action, China refused to categorize the actions as an "invasion". One guess as to how Russia would respond to a Chinese assault on Taiwan.

No sanctions. The US, Canada, and Europe will impose sanctions on Moscow. China won't – at least not in any meaningful way. The result will be a strengthening of the economic ties between the two countries and a lessening of the pain the West's sanctions will inflict against Russia.

The long-term geopolitical fallout looks ugly. Russia will emerge as master of Ukraine and may feel emboldened to try the same tactics in other former USSR states that have not joined NATO. China may see the West's refusal to militarily defend Ukraine as an invitation to move on Taiwan. And the Russia-China axis will tighten as the two countries work in concert to weaken the United States.

This is the potential future. What does it mean for your investments?

In my January column, I said I expected a stock market correction in the first quarter, with a drop of 10-15%, followed by a rebound in the second half of the year.

We have experienced the correction phase, as least as far as the S&P 500, Dow Jones Industrial Average, and Nasdaq are concerned. The S&P/TSX Composite held up better, thanks to its heavy weightings in energy and materials. The S&P/TSX Capped Energy Index was up 21% year-to-date as of Feb. 23 while the Capped Materials Index had gained 6.88%. The Global Gold Index is ahead almost 10% for 2022.

North American markets rallied on Friday for no obvious reason beyond the fact that some traders perceived the fallout from Ukraine might induce the US Federal Reserve Board to slow the pace of coming interest rate hikes.

Continued on page 3...

Invasion—continued from page 2...

What stocks are benefiting? We have seen strong gains in potash producer Nutrien (TSX, NYSE: NRT), which will benefit as sanctions choke off exports from Russia and Belarus. The stock is up 18.7% since it closed at $86.94 on Jan. 10. Mining giant Teck Resources (TSX: TECK.B, NYSE: TECK) is ahead 28.4% since finishing 2021 at $36.43. Canadian Natural Resources (TSX, NYSE: CNQ) has gained 30% since closing last year at $53.45.

Gold has been whipsawing, with big gains one day and pullbacks the next. Franco-Nevada (TSX, NYSE: FNV) was trading at $163 on Jan. 27. The shares closed Friday at $186.94 for a gain of 14.7% in a month.

Investors should be encouraged that the markets rallied at week's end, after opening deep in the red on Thursday morning after the invasion news broke. Historically, major geopolitical events such as this have resulted in a market decline, but it is usually a blip and short-lived. The worst, according to LPL Research, was the Japanese attack on Pearl Harbor in 1941 that led to a 19.8% market drawdown. It took 307 days to recover. On average, these geopolitical events result in a 4.8% decline and a recovery period of just over 43 days.

However, we can't view the Russian invasion in isolation. It comes at a time when overvalued markets were already showing instability, the effects of the pandemic are still causing supply chain disruptions, and inflation is running at levels not seen in decades. These conditions will continue to overhang the markets long after the Ukraine invasion fades into the background.

What should you do? I took a quick poll of my social media followers and found that 51.3% of those who plan to take action are going to focus more on specific sectors of the market. Just over a quarter of respondents intend to move to cash, while 20.5% are going to buy gold.

Here's what I suggest at this point:

Take some profits. It's going to be a volatile year for stocks. If you have some big gains, take them off the table before they become small gains, or worse. The market rebound on Friday provides an excellent opportunity to implement this strategy.

Build your resource exposure. It's been years since resource stocks have been a key part of a portfolio. But inflation and scarcity have pushed them to the forefront.

Own gold. I've always advised having a small position in gold (5-10% of your portfolio), for times like this. Don't be put off by the day-to-day price gyrations we're seeing. The trend line is moving higher. Franco-Nevada is my top choice.

Don't overreact. The Russian invasion was criminal and brutal. But unless Putin intends to launch World War III by attacking a NATO member (very unlikely), the stock markets will absorb the shock and move on. Selling everything and moving to your underground bunker will achieve nothing except leaving your money fully exposed to the ravages of inflation.

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RRSPS STILL A GOOD CHOICE

By Shawn Allen, Contributing Editor

RRSPs – Registered Retirement Savings Plans – have been a mainstay of retirement savings for Canadians since they were created back in 1957.

But with the emergence of TFSAs – Tax-Free Savings Accounts – in 2009, the RRSP faces competition. In fact, there are many writers and commenters today that call the RRSP a "tax trap" and something to be avoided. They argue that the RRSP does not really avoid income taxes but merely defers them. They are wrong.

The deadline for 2021 RRSP contributions is tomorrow, Tuesday March 1. Given that, the negative chatter about RRSPs, now is a good time to review the facts about these retirement plans and why they remain a good investment vehicle for most of us.

RRSPs or TFSAs?

I thoroughly explained the math that proves that RRSPs can trail, equal, or beat TFSAs in two prior editions of the IWB. In the archives look up IWB 21506 dated Feb. 7, 2015, and 21708 dated Feb. 20, 2017. These articles are well worth reviewing if you have any concerns about the tax implications of RRSP investments and especially if someone is advising you to "melt-down" your RRSP.

The Financial Post on Feb. 11, 2022 provided a detailed article comparing the results of investing in an RRSP versus a TFSA over a 20-year period. The writer similarly demonstrated that the RRSP could trail, beat, or tie the TFSA results, depending on an individual's marginal income tax rate bracket at the time of contribution and at the time of withdrawal.

What to hold in an RRSP?

Investing for retirement is about building up a secure source of funds for your post-work years. It's not about trying to win the lottery. Even as you enter retirement you will be planning for your funds to last decades, so the time horizon is long. So, safety and security are key considerations. But so is growth. You will need a balance of the three.

The equity portion of an RRSP should either hold a broad, fully diversified selection of equity funds or, if invested in individual stocks, should be concentrated mostly in higher quality companies. Our RRSP model portfolio, which was reviewed last week, offers some suggestions to consider. You'll find more in our primary and secondary core lists.

In my updates below I will specifically address the RRSP quality of each company.

Continued on page 8...

SHAWN ALLEN'S UPDATES

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

Canadian National Railway TSX: CNR, NYSE: CNI

BUY

Originally recommended by Tom Slee on May 6/02 (#2218) at C$12.98, US$8.31 (split adjusted). Closed Friday at C$158.24, US$124.60.

Background: CN rail operates across Canada and down through the central US to the Gulf of Mexico with 19,500 route miles of track. About two-thirds of CN's revenues and profits are from Canada and the rest is from the US.

Performance: CN's share price was somewhat volatile in 2021 due to the travails of its bidding war with CP in a failed attempt to buy Kansas City Southern, and the ebbs and flows of the pandemic and economic outlook.

In the end, CN rose 11% in 2021. So far in 2022, the stock is up 1.8%. CN has provided huge gains since it became a publicly traded company back in 1995. Periodic pullbacks in the share price have always proven to be buying opportunities.

Recent earnings: CN's earnings per share were up 19% in the fourth quarter of 2021 and up 12% for the full year. CN has typically managed to increase earnings year after year due to a combination of generally increasing freight levels, cost efficiencies, and rate increases.

Recent events: CN recently lost its bidding war with CP over Kansas City Southern after regulators failed to approve a crucial early step required for the merger. But CN ultimately booked a $700 million gain due to break fees from the aborted Kansas City Southern deal. This amounted to $1 per share pre-tax.

CN also recently came under major criticism from an activist share owner (known as TCI) regarding both the proposed merger and CN's recent performance. TCI proposed to replace the CEO, the chair of the board, and several other board members. CN replied in an extremely responsive and reactive manner. The dispute has been settled after CN did name a new CEO and several new board members and announced a large share buy-back program. CN's speed and reactiveness in dealing with the issue was impressive.

Continued on page 6...

CNR—continued from page 5...

Valuation: Analyzed at $160.12. CN's return on equity is very strong at 20% and it has averaged a very impressive 23% over the past ten calendar years. The price to book value ratio at 5.0 is high but reflects the attractive return on equity level. The p/e appears somewhat unattractively high at 27. The dividend yield is modest at 1.85%. Overall, these value ratios demonstrate a very strong company but one that may be about fully valued.

Dividend: CN's dividend, effective with the March 2022 distribution, was increased by a hefty 19% to $0.7325 cents per quarter ($2.93 per year) for a yield at the current price of 1.85%. This was the 26th consecutive year of dividend increases.

Outlook: The outlook for 2022 is very strong, with the company projecting a 20% increase in adjusted profit per share. CN's large share repurchase plans should also help support the stock price over the next year. It's safe to bet that CN's earnings will continue to grow over the longer term.

Quality: CN is a very high-quality company and investment. Customers often have little option but to ship by rail and in Canada there are only two rail companies to choose from. As a result, CN has been able to increase its freight rates steadily. The history of CN's rising share price and earnings are also testaments to its quality.

The company is very well managed, and this was demonstrated by its recent speedy and decisive reaction to the activist share owner, as noted above. Investors can safely predict that CN will continue to increase its earnings for many years to come.

In addition, CN is not the type of stock that ever trades at sky-high valuations. That adds to its quality as an investment since buying at the wrong time becomes less of an issue. This high-quality stock is very well suited for RRSP investments.

Action now: Buy. CN is a very strong and stable company. Investors have been rewarded for holding this stock for the long term and that is likely to continue to be the case.

Questions?

Our team of experts have the answers!

Questions of general interest to our readers may be selected for publication.

Send your questions by email to **gpape@rogers.com**

lululemon Athletic Inc. NDQ: LULU

Originally recommended on June 6/21 (#22031) at $329.52. Closed Friday at $317.58. (All figures in US dollars.)

Background: lululemon is well known as a retailer of high quality "athleisure" clothing. The fact that its products are proprietary along with their brand reputation allows them to sell at very lucrative margins. While head office is in Vancouver and its design activities are centered there, lululemon is registered as a US company and trades on Nasdaq, not in Toronto. It has over 500 company-operated stores in 17 countries. The locations of the stores are 60% in the US, 12% Canada, 11% China, 6% Australia, 3% United Kingdom, and 8% spread over 12 countries. In 2020, 69% of revenue was from women's wear and 86% of revenue was from North America.

Performance: This stock has risen spectacularly over the years and particularly since 2014 when it started the year at $59.03. In 2020 it rose 50% and was up another 12% in 2021. Considering the impact of the pandemic on retailers, this was certainly a very strong performance. However, in 2022 to date it is down 18.9%.

Recent earnings: Revenue and earnings per share growth was extremely strong in the first three quarters of the fiscal year that ended Jan. 31. This was partly a rebound from the pandemic, but it also continued the long-term growth trend.

Recent developments: The company added 31 stores in the first nine months of 2021, raising the store count by 6%. The net store count was increased by 6% in 2020 and 70% of the net additions were outside of North America.

During the pandemic, the company was successful in moving sales to its online platform. In 2020, it acquired MIRROR, an online fitness business, at a net cost of $453 million. Of that, $363 million was paid for goodwill.

Dividend: This company does not pay a dividend.

Valuation: At my analysis price of $309, the price to book value ratio is unattractively high at over 15 times – although this may possibly be justified by the high ROE and high growth. The trailing adjusted earnings p/e ratio is very high at 44 and the forward p/e based on the company's projected 2022 earnings is also very relatively high at 35.

The ROE is very strong at 38%. As mentioned, there is no dividend. Revenue per share growth in the past five fiscal years has averaged 18% and earnings per share growth has averaged 20%. This is despite the impact of the pandemic. Overall, while the ROE is

Continued on page 8...

LULU—continued from page 7...

proof that this is a very profitable company, the value ratios suggest that the shares may be about fully valued.

Outlook: The company is projecting to report an earnings per share increase of about 30% for the fourth quarter, which ended Jan. 31. Analysts are expecting an earnings per share growth of about 25% in 2022. It's a relatively safe bet that lululemon will continue to grow its earnings over the years.

Quality: lululemon is certainly a high-quality company. But due to its high valuation, the share price can be expected to be relatively volatile. This stock could have a place in an RRSP but at a lower weighting than more predictable stocks.

Conclusion: While this stock is expensive in relation to earnings, it has a strong history of growth that seems likely to continue. The recent dip in the share price may represent a reasonable buying opportunity.

Action now: Buy a modest position and continue to monitor.

RRSPs—continued from page 4...

Using an RRSP to simplify taxes

When US and other foreign stocks are held in a taxable Canadian investment account, they are subject to a withholding tax on dividends. And currency changes must be accounted for when calculating the cost basis and the capital gains or losses. Canadian stocks that feature return of capital or other unusual distributions can also create complexity in calculating the income tax due.

In an RRSP, both the taxes and the complexity are eliminated. A TFSA also eliminates the income tax and the associated complexity but the withholding tax on foreign dividends still applies.

Should you "melt down" your RRSP before age 71?

In my view, the notion of "melting down" an RRSP to try to avoid or minimize taxes is the very opposite of what investing for retirement is all about. It's true that many of us will face income taxes of about 30% and, in rare cases, as high as about 60%, on RPSP/RRIF withdrawals. But, as noted in the archived articles mentioned above, it should be remembered that about 30-40% of the RRSP was effectively funded by RRSP income tax refunds and that the contributions have grown tax-free for decades.

There are cases where early withdrawals of RRSP funds make sense. But the highest priority for most people, and especially for those who will have a surviving dependent spouse, should be to ensure availability of cash in retirement and not to minimize taxes.

Contributing editor Shawn Allen has been providing stock picks on his website at www.investorsfriend.com since the beginning of the year 2000.

RioCan Real Estate Investment Trust
TSX: REI.UN, OTC: RIOCF

Originally recommended on Aug. 31/20 (#22031 at C$15.45, US$11.78. Closed Friday at C$25.04, US$19.75.

Background: RioCan Real Estate Investment Trust is one of Canada's largest REITs. It is in the business of developing, owning, and managing buildings (and usually the associated land) that are leased largely to retailers.

RioCan currently has 194 income producing properties and another 13 under development. Only 9.3% of its space consists of older-style enclosed shopping malls as most of its properties are open air big box/power centres. It has a very diverse mix of tenants with a heavy focus on grocery, pharmacy, and liquor as well as discount retailers and essential services. It has virtually no exposure to traditional department stores.

The majority of its current development projects consist of high density urban residential apartments, condos, and townhouses. The condos and townhouses will be sold while the apartments will be held for rental income.

RioCan focuses largely on the six largest Canadian cities, which now account for 90% of its rental revenue. There is a particularly heavy concentration on the greater Toronto area, which accounts for 51% of rental revenue.

Performance: RioCan was recommended at $15.45 at the end of August 2020 after its unit price had fallen significantly from about $27 due to the pandemic. Since that recommendation, the units are up 62% and have continued to rise in recent weeks.

Recent earnings: Adjusted earnings per unit (funds from operations) have, to a large degree, recovered from the impact of the pandemic and rose 22% in the latest quarter.

Tax status: REIT distributions do not qualify for the Canadian dividend tax credit. Typically, about 75% of RioCan's distributions has been taxable at full rates, similar to interest income, while about 25% has been taxed as capital gains. If you are holding this in a taxable account, the adjusted cost base must be reduced by "return of capital" distributions and must be tracked. Holding these units in an RRSP account avoids that complexity.

Recent events: In late 2020, RioCan announced that its distribution would be reduced by one-third. In January 2022, the distribution was increased by 6.25% but remains 29% below the pre-pandemic level. Other impacts of the pandemic included a write-down in building values in 2020 that averaged 3.1%, as well as a reduction in rents collected due to expected bad debt and rent forgiveness associated with a government program. But occupancy

Continued on page 10...

REI.UN—continued from page 9...

declined only marginally and remains very strong at 96.8%. The situation with unpaid rent has improved dramatically as the provision for rent forgiveness and bad debt has declined to 1.2% in the latest quarter after peaking at 6.8% in the second quarter of 2020.

Distribution: The units currently pay a monthly distribution of $0.085 ($1.02 per year) to yield 4%.

Valuation: Analyzed at a price of $24.52. The yield at 4% remains attractive. The price to book value ratio appears reasonably attractive at 1.0. The payout ratio is just 61% of trailing year funds from operation. The adjusted p/e ratio is neutral in attractiveness at 14.8. The adjusted ROE in the past 12 months is relatively modest at 6.7%. Overall, the value ratios would suggest that the units are fairly priced.

Outlook: Management is projecting modest earnings growth of 5-7% per unit for the next five years. The distribution will likely be increased modestly again next year but is unlikely to be fully restored anytime soon since RioCan has a goal of reducing debt and has significant capital spending plans. Investors should expect a modest capital gain in the next year or so, but the units should now be purchased mainly for the distribution, which will also increase modestly over time.

Quality: RioCan is a relatively high-quality company and investment in terms of being well managed and offering a relatively predictable income stream, although it faces some risks due to the changing nature of physical retail. By nature, this is not a high return business, but it tends to be a stable business. It is suitable as an RRSP holding.

Action now: Buy. RioCan is very well managed and provides a reasonably attractive cash yield that can be expected to increase over the years.

? YOUR QUESTIONS 3M not performing

Q – What are your thoughts about the stock of 3M (NYSE: MMM)? I find it's not doing so well these days, and I am wondering why. – Claude V.

A – 3M is a Minnesota-based manufacturing giant, producing a wide range of products from building materials to medical supplies. Its brands include N95 masks, Scotch Tape, and Post-It notes. The company is included in the Dow Jones Industrial Average and has a market cap of more than $91 billion. The stock has been in a downward trend since May of 2021. There is no obvious reason for this, beyond the fact it's a slow-growth company and doesn't seem to be taking any steps to improve that. The company recently released fourth quarter and year-end results. Sales were up 9.85% for the year while earnings gained 8.66%. The dividend yield is 4.15% and the p/e ratio is 14.87. None of these are bad numbers. But investors are showing little interest and I don't see a catalyst that will change that. – G.P.

GORDON PAPE'S UPDATES

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

Equitable Group TSX: EQB, OTC: EQGPF

BUY

Originally recommended by Irwin Michael on Aug. 10/08 (#2828) at C$10.52 (split-adjusted). Closed Friday at C$77.38, US$58.52.

Background: This company provides mortgage lending services to individuals and businesses in Canadian urban markets, with a focus on entrepreneurs and new Canadians. It carries on operations through its wholly owned subsidiary, Equitable Bank. It's Canada's eighth-largest Schedule 1 bank by market capitalization. Equitable Bank serves 325,000 Canadians and employs about 900 people. It also has a digital banking operation, EQ Bank, with its flagship product being the EQ Bank Savings Plus Account.

Performance: The stock hit an all-time high of $84.78 last November but has been trending down since.

Recent developments: The company's fourth-quarter results were the best in its history. Earnings were up 12% year-over-year, to $80.1 million ($2.29 per share, fully diluted). Analysts were looking for $2.11. Return on equity was 17%.

For the 2021 fiscal year, Equitable posted revenue of $642.9 million, up almost 25% from $514.6 million in 2020. Net income available to common shareholders was $288.1 million ($8.36 per diluted share), compared to $219.3 million ($6.37 per share) in the prior year.

Total loan originations were ahead 39% year-over-year, to $14 billion. Assets under management were up 17% to $42 billion.

Acquisition: On Feb. 7, Equitable announced it has entered into an agreement to acquire Concentra Bank, the 13th largest Schedule I bank in Canada with $11.3 billion in assets as of Nov. 30, 2021. Concentra is a mid-market digital bank. The total cost will be $470 million.

The deal will add $7.4 billion in personal loans and $1.6 billion in commercial loans to Equitable's portfolio. The purchase is expected to close in the second half of this year.

Equitable CEO Andrew Moor described

Continued on page 12...

EQB—continued from page 11...

the deal as "one of the most important and consequential transaction in our 50 plus history, and it accelerates our growth plan by several years."

Dividend: The company is increasing its quarterly dividend by 51%, to $0.28 per share ($1.12 per year), effective with the next payment. The new rate translates into a yield of 1.4% based on the current price.

Outlook: The Concentra purchase is expected to be single-digit accretive to Equitable's earnings in the first year after closing. Overall, the company is expecting another strong year in 2022.

Action now: Buy the dip.

? YOUR QUESTIONS Real Return Bonds

Q – You, and other investment writers constantly refer to the "fact" that bonds rise and fall in price and are therefore may not be a good holding. But if I buy a bond at issue (or any price for that matter) I will receive exactly the return that I expect if I hold it to maturity. The ups and downs of the asset price are irrelevant. I do have to rely on good credit checking, but that is a different issue.

My point is even more relevant for a Real Return Bond. Once I buy it, I receive the coupon rate plus inflation, and get the capital plus inflation when it matures. Again, the gyrations in price are irrelevant, particularly the changes in the RR Bond Index. Or am I missing something? – John D.

A – There are a few things to consider. First, most investors do not buy bonds directly. They buy bond funds, which do not have a maturity date, so there is no guarantee of what price they will get when they sell.

For those who do invest directly, your argument is correct, to a point. You get what you pay for in terms of the interest on the bond and repayment of your capital at maturity – assuming you buy at par or below. But the purchasing power of the interest and repayment at maturity will be eroded by inflation.

So, are Real Return Bonds the answer? The principal and interest are adjusted for inflation. But what is the underlying return on the bond? According to the Bank of Canada, as of Feb. 18 the real yield on a long-term government Real Return Bond was 0.51%. Do you really want to tie up your money for a decade or more for that kind of payout? - G.P.