

April 25, 2023

Dear clients,

*Security is mostly a superstition. It does not exist in nature, nor do the children of men as a whole experience it... Avoiding danger is no safer in the long run than outright exposure.*

- Helen Keller, The Open Door

Sitting on the sidelines seems smart in environments like this. News headlines scream about bank failures, inflation, war in Ukraine... The next recession is right around the corner! Meanwhile, financial markets are... up?

In investing lingo, markets are “climbing a wall of worry”, meaning they are rising in value even though the future looks threatening. Investing in this environment doesn’t feel comfortable, but in reality, when markets go up, it is almost always in the face of worrisome headlines. Investors who choose to avoid the danger and uncertainty often miss out on significant gains.

During times of inflation, the danger-avoiding strategy is especially unappealing. With core inflation in Canada at 4.3% over the past twelve months, holding cash in a 0% bank account would have guaranteed a -4.3% loss. And it is not all in the rear-view mirror. Despite what consensus media are telling us, I believe inflation will be with us for longer than most expect. While the demand/supply imbalance is mostly behind us now, wage inflation is still very much present (radical minimum wage policy increases and re-shoring being the most impactful and least-discussed of the causes), and governments are still printing money, having learned precisely nothing from this episode.

As always, I take a conservative approach with client capital, investing in opportunities with reasonable prospects for returns over longer periods of time, while minimizing downside risk. I am tilting portfolios towards companies that can benefit from sticky interest rates and from an economy that remains unexpectedly robust.

### **The banking crisis**

The banking crisis dominated headlines in the first three months of 2023. The cause of the crisis was mismanagement in a few smaller banks, although general weakness in the US regional system was exposed as a result. While it’s true if enough depositors pulled their money from these smaller banks it would create a major crisis in the US, I don’t believe this is likely. It is more likely that small banks will consolidate to create larger, stronger entities, moving closer to the system we have in Canada. Our banks in Canada are among the healthiest in the world, but we pay for their strength in the form of fees and interest rate spreads. US banks will likely move closer to this model.

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We had some portfolio exposure to the crisis this quarter. First Horizon Corporation is a well-run regional bank in Memphis, Tennessee which is in the process of being purchased by TD Bank. The deal has been approved by shareholders on both sides, but is being held up by partisan politicians trying to score cheap political points. TD was to buy the US bank for \$25 per share, but the crisis put the deal at risk and drove the price down to below \$15. It currently trades at \$17.60. I believe TD will attempt to renegotiate the deal for slightly less than \$25, which will mean a healthy return from here, but it would have been better to sell before the crisis. I've misplaced my crystal ball.

### Protections

In light of the banking crisis in the U.S. it is worth reviewing the protections Canadian savers and investors possess, should a crisis happen north of the border.

Cash, term deposits, and Guaranteed Investment Certificates in Canada are protected by the CDIC (Canadian Deposit Insurance Corporation) up to a maximum of \$100,000 per individual, per account type, per institution. For example, if an individual holds a bank account, a joint account, an RRSP, and a TFSA, their deposits would be CDIC guaranteed in the event of a bank failure, to a maximum of \$100,000 in each of these account types, or \$400,000 total. Further, these guarantees can be extended by holding deposits at multiple institutions. CDIC is funded by the banks and deposit-taking companies, and is backed by the Government of Canada. More information can be found at [www.cdic.ca](http://www.cdic.ca).

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### Patience and discipline

It is a challenging environment for investors. Patience and discipline are required. Thank you for putting your trust in me, and in Raymond James.

Best regards,



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