BNN MARKET CALL

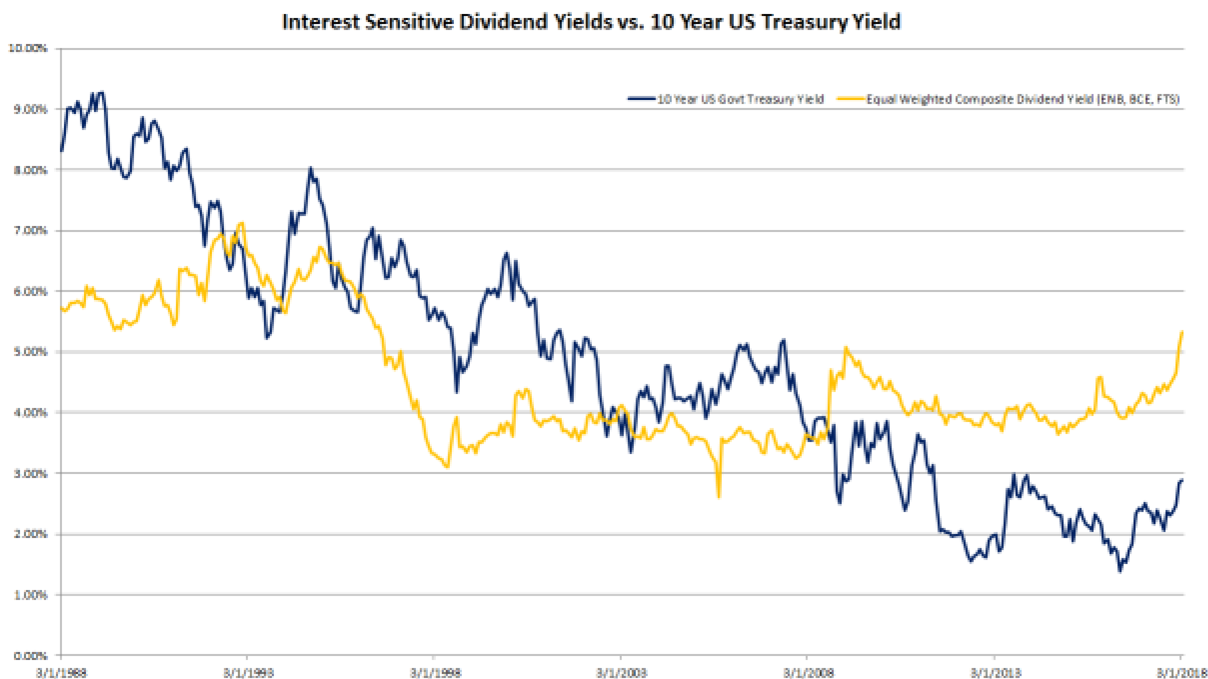
***e*Research Corporation** is pleased to provide an excerpt from the BNN Market Call Newsletter. It features Ryan Bushell, the president of Newhaven Asset Management with his Market Outlook.

Mr. Bushell's commentary is presented below.
Mr. Bushell is interviewed by BNN on his Market Outlook in a 47-minute video HERE.

MARKET OUTLOOK

Ryan Bushell, President of Newhaven Asset Management
Focus: Canadian Dividend-Paying Stocks

Canadian dividend stocks are out of favour, especially those deemed to be sensitive to interest rates.



The chart above depicts a three-decade period for the dividend yield of three Canadian bellwether dividend stocks relative to the yield on 10-year U.S. Treasury Bonds.

The equally weighted group of Enbridge, Fortis, and BCE is currently yielding over 5% for the first time since the financial crisis in 2008. They are yielding nearly 2.5% more than U.S. 10-year government bonds, which is an all-time high.

You might think that there must be something wrong with their businesses, but each company is seeing acceleration in their respective business fundamentals, and all three companies just raised dividends by an average of 6.5%.

So what gives? I believe there are three main reasons for the recent weakness:

1**. Market sentiment is against them**
Investors are once again shunning tangible cash flows and dividends in favour of potential cash flows in companies that have little (if any) earnings and pay no dividends. Amazon, Tesla, Snapchat, marijuana, cryptocurrency/blockchain … We said we would never again repeat the late '90s, but here we are.

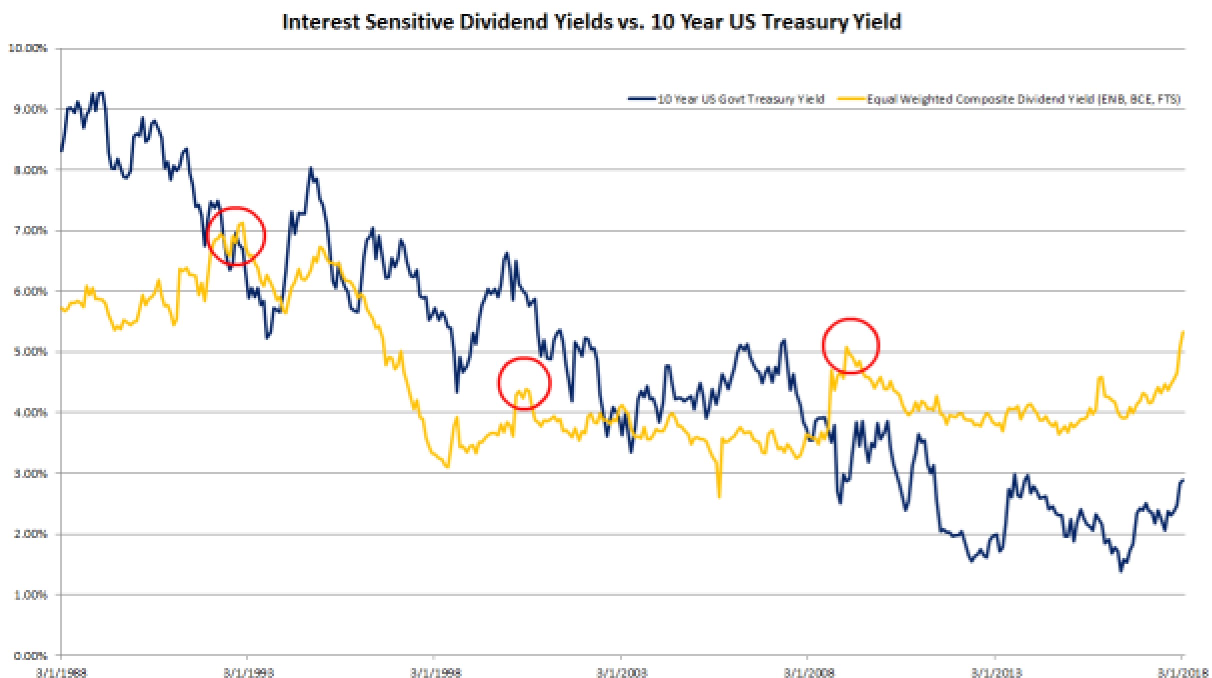
2. **Interest rates are rising — for real this time**
The rise in interest rates from all-time lows reached in the summer of 2017 has been dramatic and, with the global economy accelerating, uncertainty surrounding trade and already low unemployment, the potential for inflation is greater than at any point in the last decade. But there's context necessary here. The last time 10-year bond yields rose to 3 %, the yield on the above basket of stocks was around 4 %. The last time these stocks yielded 5.3 %, 10-year bond rates were 7 %. Sure, rates are rising, but how far? The middle of the baby boom generation just turned 64, meaning they're just retiring or newly retired and will continue to be a deflationary force to be reckoned with for some time yet. We're nine years into this economic expansion, input costs and interest rates are rising while the U.S. dollar is falling. The next recession is coming and what happens to rates then?

3. **The war on … Trade?**
NAFTA could be dissolved at any moment. Canada and the u.s. have the largest “free” trade relationship in the world. The Canadian dollar unexpectedly rallied nearly 10 % last summer to more than US$0.80. If I'm an international investor, why would I put capital to work in Canada, even with compelling valuations, when the currency could fall out of bed at any moment? Not to mention fears about an extended Canadian consumer, oil prices and our own political and taxation issues. This last point is hurting all Canadian stocks, even our financial and energy companies that should be benefitting from these late cycle conditions.

So, what are we to do as Canadian dividend investors: Give up? Move on? Stay the course? First some context:

Over the last 20 years, the TSX has returned 6.5%/year on a total return basis. The S&P 500 has returned 6.3% in Canadian dollars, yet it is now trading at nearly a 50% book value premium to the TSX, with about 30% in technology.

Looking at the chart again, the last three times the average yield on Fortis-Enbridge-BCE peaked out (January 1993, August 2000, March 2009) their returns the next five years were compelling both on an absolute and relative basis:



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5-YEAR TOTAL RETURN (ANNUALIZED)			
START DATE	ENB/FTS/BCE (EQUAL WEIGHT)	TSX COMPOSITE	S&P 500 (CAD)
JANUARY 1993	30.20%	17.80%	23.70%
AUGUST 2000	16.20%	0.70%	-6.80%
MARCH 2009	18.90%	13.70%	18.00%
AVERAGE	**21.77%**	**10.73%**	**11.63%**

We know what the last five years have looked like, but what matters today is the next five. Being a successful long-term investor is less about what you do when times are good and more about remaining disciplined at all points during the cycle and having the conviction to buy and hold quality companies when others are selling or ignoring them.

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