

## Likes/Dislikes - November 12th, 2021

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Below are Evergreen Gavekal's Likes/Dislikes for November 12th, 2021.

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### OUR CURRENT LIKES AND DISLIKES

Changes highlighted in **bold**.

**Most financial commentators—and certainly the Fed—were caught off-guard by this week's toasty inflation releases but EVA readers should not have been; this is a theme we've been on for at least a year. It's interesting that the Fed has dropped its now widely maligned "transitory" characterization of inflation. Consequently, markets are preparing for the first Fed tightening cycle since 2018.**

**However, Wall Street is still largely buying the transitory notion but with a delayed reversal date. The assumption is widespread on "The Street" that the CPI will settle back to around 2% by the end of next year. In my mind, that's a sucker's bet. While certainly some supply bottleneck-caused price pressures are highly likely to recede, the long-term upward impetus caused by forces such as greenflation (the sharply rising cost of energy due to the Great Green Energy Transition); the Fed's new main focus on employment vs inflation; its increasing politicization; rapidly rising wages, and surging rents, are likely to swamp easing supply chain constraints.**

**Moreover, on this topic, consider for a moment how far behind the inflation curve the Fed is presently. Its cumulative quantitative easings (QEs) that now amount to around \$4 trillion since the virus crisis began are credibly estimated to be the equivalent of the fed funds rate being at -10% (note the minus sign). Accordingly, to catch up with the present inflation rate, the Fed would need to shrink its balance sheet and/or directly raise rates by an amount that represents 16% of de facto tightening. (The 6 percent current inflation rate plus erasing the prevailing 10% effective negative fed funds rate.) That is a level of**

**monetary stimulus withdrawal that has never been done before, not even when Paul Volcker took interest rates from 10% to 20% forty years ago. The odds of this happening today are right up there with AOC switching to the GOP!**



**As a result, the Fed will be in a highly accommodative stance for as far as the eye can see; thus, fears of tapering/tightening negatively impacting assets like gold and copper are, in my view, greatly exaggerated. Perhaps others are waking up to this reality and that's why the beaten-down gold miner ETF is up 6.4% this week while silver bullion is up 4.8%. Additionally, America's biggest copper producer has been ripping higher of late.**

**My main point is to be sure your portfolio has plenty of inflation hedges. On that score, the correction in natural gas recently has created an opportunity to add producers of that critically important energy commodity as the Northern Hemisphere heads into a La Nina winter.**

**LIKE**

- Large-cap growth. (For the most part, there continues to a better risk/reward ratio with growth-at-a-reasonable-price—GARP—type issues; as with the overall US stock market, bargains are increasingly scarce.)
- **Certain international developed markets, especially Japan (Use the recent pull-back for adding to or initiating position in ETFs like EWJ. The Japanese market should be a**

**beneficiary of overseas investors pulling capital out of China.)**

- Publicly traded pipeline partnerships, i.e., MLPs and other mid-stream energy securities. (Recently, we recommended some profit-taking; based on the pull-back of late, that was decent advice.)
- **Gold-mining stocks (Despite their 18% rally this quarter, they remain very attractively valued on a long-term basis. But based on the run-up, lighter buying is appropriate.)**
- **Gold (The price of the metal itself is throwing off some technical buy signals; eventually, bullion should take out the high it set last year around \$2000 per ounce.)**
- **Silver (It, too, is acting if it wants to move higher, possibly substantially.)**
- **Select international blue chip oil stocks (Despite the 60% spike this year, energy shares remain exceedingly depressed with many producers trading at double-digit free cash flow yields; some of the mid-sized companies have free cash flow yields in excess of 20%. Some energy issues are very extended in price so it's best to focus on the laggards such as in the natural gas sector.)**
- Short-term investment grade corporate bonds (1-4 year maturities; favor shorter maturities due to rising inflation risks because of the likelihood that the Fed and the Treasury are over-stimulating the US economy.)
- Emerging market (EM) bonds in local currency (focusing on stronger countries, particularly in Asia)
- Large-cap value (This major style has been lagging its growth counterpart in recent months, making it look relatively more attractive, notwithstanding a mild recovery since mid-July. It should be a beneficiary of the economy's second reopening phase.)
- High-dividend equities with *safe* distributions (Many have rebounded, validating our earlier endorsement of them.)
- Most cyclical resource-based stocks (A number of these have also rallied back, as we had thought likely with such persistent inflation pressures.)
- BB-rated corporate bonds (Buy more selectively after a spectacular rally and favor shorter maturities.)
- Canadian REITs (Avoid office issues for now.)
- South Korean Equities (Use the recent dip to add or initiate exposure. SK stocks should also benefit from money fleeing China.)

- Uranium and uranium producers (The world's leading uranium miner has vaulted roughly 200% since early November, validating our positive stance on this sub-sector. Due to its big move, hold off on new purchases particularly given the recent surge.)
- Certain "Virus Victim" equities such as refiners, homebuilders, and select retail stocks (After a powerful rally in homebuilders and a number of retailers, be more selective; some homebuilders have had significant pullbacks due to the interest rate rise.)
- Investment-grade floating rate corporate bonds (Despite a vigorous rally this year, there remains decent long-term value in this bond market niche.)
- **The higher quality mortgage REITs (Based on a mild recent rally as well as the dual threats from rising rates and a flattening yield curve, we advise renewed profit-taking in this sub-sector; please be aware "profit-taking" does not suggest a complete exit.)**
- Floating rate bank loans (Although GDP growth this quarter came in much slower than Q2, this should be a pause not a reversal. Thus, the still healthy US economy reduces default risks and the floating-rate structure of bank loans mitigates inflation risks.)
- **Copper producers. (The largest US copper producer is up 35.2% since September low, benefiting those who followed our suggestion to buy during its summertime correction. Due to enormous demand looming from electric vehicles, the supply of the red metal should see recurring shortages in years to come.)**
- **A relatively new sector recommendation is healthcare stocks. Many have corrected and are trading at alluringly attractive valuations, often with lush dividend yields. (Use the recent weakness in some pharma names to accumulate.)**

## NEUTRAL

- Renewable Yield Cos (Based on the hefty rally that has occurred with this group in recent months, justifying our buy rating on them earlier this year, we are downgrading them to neutral; some profit-taking is reasonable despite bright long-term prospects.)
- A wide range of high-income securities, including preferred stocks (Preferred stocks look less attractive with prices up, yields down, and inflation risks on the rise. As with bonds, we prefer the floating-rate variety.)
- **Intermediate-term investment-grade corporate bonds, yielding approximately 2.25% (Now rated neutral due to our increasing inflation concerns and the paucity of**

**attractive yields; they have been under pressure lately due to rising rates overseas and escalating inflation concerns.)**

- Mid-cap value
- Emerging stock markets; however, a number of Asian developing markets look undervalued (Caveat investor: These are much less bargain-rich than they were a year ago. China is an exception; its market has been crushed creating interesting value plays for brave investors. However, it's continuing war on its best companies is a large and legitimate concern.)
- US-based Real Estate Investment Trusts (REITs) (It is critical to be highly selective with this sector; however, the reopening of the US economy, despite recent challenges, should relieve pressure on some of the most impaired sub-sectors of the REIT universe—unless they are exposed to cities and/or states that are seeing significant population and business outflows.)
- Cash
- Canadian dollar-denominated short-term bonds (The recent yield spike makes these even more interesting—literally.)
- One- to two-year Treasury notes
- Traditionally “safe” sectors such as Staples and Utilities (Most utilities have had healthy price bumps lately; consequently, they are less appealing.)
- Virus Victors (I.E, those companies that have benefitted from global lockdowns and now sport premium valuations. Many have retreated significantly of late; Clorox, for example, remains down materially from its peak.)
- Small-cap value (Moving to neutral due to high valuations and the massive appreciation since last fall; justifying our prior caution, small cap value did swoon down 10% recently before bouncing back. However, it has had a bullish multi-year breakout; thus, it might be advisable to accumulate small cap value on any material weakness.)
- European banks (Shifting these back to neutral due to improving vaccination prospects on the Continent. Still-prevailing negative interest rates in Europe are very hard on bank profitability.)

## DISLIKE

- **Intermediate-term Treasury bonds (Moving these to Dislike due to rising risks of another price down-leg caused by the realization that after-inflation yields are becoming increasingly negative. Validating our bearish stance on them, longer-term**

- treasuries have struggled lately and for the year as a whole.)
- **Small-cap growth (Since late-February, around the time of our negative call on this style, it is essentially flat. After selling off earlier this year, this style has been rebounding of late. It remains extremely pricey and could actually be hurt by the so-called “Great Rotation” from the long-outperforming growth style into value.)**
  - As a relatively new tactical recommendation related to the above bullet, investors seeking to reduce equity exposure might want to buy an inverse small-cap ETF. One of these offers twice the upside—and downside—of the small cap index; i.e., should small caps fall 10%, this ETF will rise roughly 20% and vice versa. Thus far, this trade is slightly in the red.)
  - **Long-term treasury bonds (These are in the dislike category due to both Evergreen’s and Gavekal’s rising conviction in a looming burst of inflation; despite a now faltering rally over the last few months, long-treasuries remain down 5.3% on a total return basis this year.)**
  - **Long-term investment grade corporate bonds (These are viewed negatively because of the narrow yield gap, or spread, between corporate debt and treasuries combined with our escalating inflation fears. However, there are a smattering of long-term issues that still offer attractive yields. Long-term corporate bonds have had a negative total return of -0.7% for the year.)**
  - Most municipal bonds (Munis have bounced a bit lately but we remain negatively disposed to longer issues.)
  - **US dollar (The dollar has rallied recently, pushing it up roughly 5.8% for the year. This is despite the fact that the US is running a trillion-dollar trade deficit and the Fed continues to fabricate money at a \$1.5 trillion annualized rate. Thus, the dollar’s long-term outlook appears very challenging and it remains overvalued versus many currencies, especially those in Asia.)**
  - **Many semiconductor tech stocks (Some semi issues have come down hard, enhancing their future return potential. Evergreen is particularly pleased with the recent powerful rebound in Qualcomm.)**
  - Mid-cap growth
  - Lower-rated junk bonds (For the first time ever, junk bonds “provide”, on average, a yield below inflation; thus, their other moniker, high yield, no longer applies. In my view, the lowest rated junk

bonds offer the worst/risk reward.)

- **Green energy stocks (Note, this refers to equities not the Renewable Yield Cos; most of the former had explosive up-moves in 2020 and into this year; lately, though, many green energy plays have been hit hard, especially the dodgiest issues like Lordstown Motors and Nikola. The recent new EV truck maker Rivian looks ludicrously overvalued.)**
- **SPACs (Special Purpose Acquisition Companies, which are structured to greatly favor insiders and disadvantage retail investors. The SPAC ETF has fallen 28% from its February highs, justifying our negative stance on this highly speculative slice of the market.)**
- Most new issues (Earlier this year, the IPO market was as frothy as I've seen it other than the giddiest days of the dot.com era; there are also signs the new-issue craze is fading. A number of IPOs are trading below their offering prices.)
- Despite a disastrous February, most of the popular Reddit/WallStreetBets stocks still have material downside. The recent bounce in two of the highest profile "meme stocks" provides another shorting, or put-buying, opportunity.

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