Likes/Dislikes – October 1st, 2021

Below are Evergreen Gavekal's Likes/Dislikes for October 1st, 2021.

OUR CURRENT LIKES AND DISLIKES

Changes highlighted in **bold**.

The mini-correction that has been playing out in the stock market over the past month became less mini this week. The S&P retreated 4.65% in September and we're now entering the often plunge-prone month of October. Moreover, the bond market continues to weaken with the 10-year T-note having pushed near 1.6% earlier this week, up from a low of 1.17% this summer, before falling back down to just below 1.5%.

However, there are two pieces of distinctly positive news. First, Delta infections continue to fall, supporting the views of those (like this author) who believe the worst is over for its proliferation. Second, Merck announced today that Phase III trials of its Covid anti-viral revealed a 50% reduction in deaths and hospitalizations compared to the placebo group. These results were robust enough to cause Merck to ask the FDA for emergency approval of its med known as molnupiravir (admittedly, not the catchiest of names; it's time to call in the marketing department!).

Accordingly, this news strengths the odds of the scenario I've been describing of a second reopening surge for the US economy (the first being after last fall's vaccine announcements). If so, it is highly likely to revive the performance of more economically-sensitive stocks which have struggled since Delta went viral in recent months. Energy shares continue to be favored by Evergreen and they have been showing commendable resilience during the recent mini-correction. Precious metals, unfortunately, have not. We remain bullish on their prospects though we concede higher bond yields are a negative.

On the other hand, we expect real (after-inflation) yields to stay in minus territory for many months, if not several years. If that view become widely embraced, we expect a significant rally by the extremely out-of-favor gold and silver miners. (What a difference a year makes! In the early fall of 2020, this group was going vertical, causing Evergreen to do extensive profit-taking.)

Overseas, the evolving energy crisis is hitting both Asia and Europe extremely hard. In China, a multitude of factories are being taken off-line due to power rationing. This will aggravate global supply chain problems and create even more "transitory" inflation. For Europe, the energy shortage threatens some countries with another recession, particularly in the UK where a number of utilities are on the brink of failure and/or nationalization. Welcome to the wonderful world of recurring energy shortages!

From an investment standpoint, we think this reinforces the need to invest in scarce resources. This should be particularly rewarding where there are strong and persistent pressures working against increased supply (such as in the case of oil and natural gas).

- 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, though there has been some value restoration lately.)
- Certain international developed markets, especially Japan (The Japanese market has continued to move higher and has achieved a multi-year breakout, boding well for future gains. It remains an excellent way to benefit from the next leg up in the global economy once the Delta variant is perceived to be under control.)
- **Publicly traded pipeline partnerships, i.e., MLPs and other mid-stream energy securities. (MLPs have had an extraordinary run since last November, despite a 19% correction from their June peak to the low seen, for now, on August 19th. Even so, the MLP index is up roughly 41% on a total return basis for the year and it successfully held the 8/19 low in recent weeks.)**
- Gold-mining stocks (please see above)
- Gold (Its recent weakness is likely just a pause in a powerful long-term up-trend.)
- **Silver (It has been lagging gold lately and may be poised to run once again though that will probably require improved pandemic news. Silver did rebound about 5% in recent weeks but has surrendered that and then some. It is now down 18% for the year.)**
- Select international blue chip oil stocks (Despite the aforementioned snap-back, 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%.)
- 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 second economic reopening phase.)**
- High-dividend equities with *safe* distributions (A number of these have fallen further due to Delta variant worries.)
- Most cyclical resource-based stocks (Previously, we recommended some profit-taking which turned out be decent advice; now, as described above, it’s timely to look for bargains in these issues. Copper issues in particular look interesting due to a demand spike that seems inevitable, due to the electric vehicle push, along with challenged supply.)
- 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 (Delta variant concerns have hit the Korean market much more than the S&P 500; the former is now down 16.5% from its early year peak. We like its long-term prospects.)**
- **Uranium and uranium producers (The world’s leading uranium miner has vaulted 139% 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; subsequent to breaking support and falling initially post that break, refiners have roared

back on the vaccine news. Some, however, have pulled back enough to warrant light buying.)

- Investment-grade floating rate corporate bonds (Despite a vigorous rally in recent months, there remains decent long-term value in this bond market niche.)
- The higher quality mortgage REITs (Previously, we'd advise profit-taking on these but at least one has come down hard enough to justify re-purchasing.)
- Floating rate bank loans (Although GDP growth this quarter is likely to be 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. (Moving these to Like based on both the retracement they've had and the looming demand boom due to drastically increased electric vehicle production. Additionally, there appears to be a number of supply constraints, including in Chile as a result of a new, less producer- friendly, political regime. The news of Chinese property giant's Evergrande financial distress, along with increasing evidence the planet is entering a third energy crisis, has pushed this group lower yet, enhancing its long-term appeal.)**
- **A new sector recommendation is healthcare stocks. Many have corrected and are trading at alluringly attractive valuations, often with lush dividend yields. (Today, Merck is rewarding those who picked it up at bargain prices recently.)**

- 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.)
- 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.)
- 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 last fall. 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 (Thanks to a rebound in the Canadian dollar, these have provided solid returns this year. Recently, the loonie has weakened a bit creating a better entry point for those bond investors looking to diversify out of the US.)
- 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 notwithstanding the spread of the Delta variant.)
- 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 8% recently before bouncing back a bit.)
- 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.)

- 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. As noted above, longer-term treasuries have been hard hit of late.)
- **Small-cap growth (Since late-February, around the time of our negative call on this style, it is down roughly 9%.)**
- 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 approximately breakeven.
- **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 7.5% 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 are down 3% for the year, including cash flow.)**
- Most municipal bonds (Munis have bounced a bit lately but we remain negatively disposed to longer issues.)
- **US dollar (The dollar has rallied further this week, pushing it up 4 ½% 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 (We do have a number of semi holdings for Evergreen client; however, these were typically acquired far lower than where they trade today. To its credit, however, the semi index recently broke out to a new high. Despite that, its lofty valuations render it an unappealing area for new capital commitments.)
- Mid-cap growth
- Lower-rated junk bonds
- 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.)
- **SPACs (Special Purpose Acquisition Companies, which are structured to greatly favor insiders and disadvantage retail investors. The SPAC ETF has fallen 34.6% from its February highs, validating our negative stance on this highly speculative slice of the market. The *Wall Street Journal* noted recently that $75 billion of SPAC market value has been wiped out since February.)**
- 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. These meme-type stocks are sliding once again though they remain absurdly overvalued, in my view.