Likes/Dislikes – September 24th, 2021

Below are Evergreen Gavekal's Likes/Dislikes for September 24th, 2021.

OUR CURRENT LIKES AND DISLIKES

Changes highlighted in **bold**.

The two main market-moving news items this week were related. Last weekend's announcement of the effective collapse of the Chinese property giant, Evergrande, caused the worst one-day decline by the S&P 500 since   this past Monday.   (Based on its towering debt and long-struggling operating results, perhaps the company should have been called "Nevergrande".)

However, as usual in this era of trillions of central bank fabricated liquidity, Monday's swan dive has been systematically reversed through the balance of this week. Thus, it's been another rewarding event for the buy-the-dip crowd (which is almost everyone these days!).

The other major development was another supposedly hawkish Fed meeting, similar to what happened back in June. However, as CNBC's veteran Fed watcher, Steve Liesman, noted right after its conclusion, the Fed remains highly accommodative and that's likely to persist for a considerable time. In my mind, what constitutes hawkish these days is borderline comical (maybe not even borderline).

Stocks have taken the Fed's attitude shift in stride (of course!) but bonds are a different matter. The 10-year T-note is nearing 1 ½% this morning, up from a low of 1.17% last month. This price decline—and yield jump—validates our negative stance on long treasuries, especially after their strong summer rally.

A key theme of this EVA section over the last month or so has been the probability of Delta infections peaking soon. The evidence of that continues to build (for more on this topic, please go to the Hussman Funds website and check out the conclusion of his current letter.) Consequently, I anticipate that the more cyclical parts of the US stock market are likely to outperform the S&P 500 over the balance of the year.

In Europe, the big story is natural gas prices. These have tripled this year and are creating extreme distress, particularly in the UK. This is strong validation of the investment thesis of investing where future shortage are likely to occurs. The continued shocking drawdown of oil inventories is strongly suggestive that crude prices may continue to surprise on the upside.

- 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 39% 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 7% in recent weeks but has surrendered that and then some. It is now down 15% 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.)**
- 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 14% from its early year peak. We like its long-term prospects.)**
- **Uranium and uranium producers (The world's leading uranium miner has vaulted 125% 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 due to a new, less producer- friendly, political regime. The Evergrande news has pushed this group lower yet, enhancing their 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.

- 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 6.4%.**
- 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 rally over the last couple of months, long-treasuries remain down 4% 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 now flat 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 rebounded lately, moving back close to its highs for the year. Its long-term outlook appears very challenging and it remains overvalued versus many currencies, especially those in Asia. The new King of Bonds, Jeff Gundlach, opined on CNBC recently that, long-term, the dollar is "doomed".)
- 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 33% from its February highs,validated 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.**

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