

Positioning Recommendations - April 1st, 2022

Ride Away, Right Away!

It's no April Fool's gag that the first quarter was a rare down one for stock investors. That is, unless they were closely following this newsletter's repeated recommendations to have considerable hard asset exposure. The S&P 500 was down roughly 4 ½% in Q1, while the NASDAQ, most investors' favorite playground, retreated 9%. Moreover, as I've often written, the damage to the typical stock was far worse than what the averages reflected. This was despite a spirited rally in the second half of March, though it did fade right at quarter's end. On the other hand, commodities — i.e. real assets — had their best quarter since 1990.

Normally, stock market downside leads to bond market upside. Yet, like so many things these days, normal isn't the prevailing state of conditions. In fact, bonds suffered their worst quarterly performance since the summer of 1980 when Jimmy Carter was still in the White House. The main fixed-income benchmark lost 6%, one of those very rare times when bonds fall more than stocks.

This result is in synch with a point I've long made in these pages, and also in my new book, [*Bubble 3.0*](#): the probability that bonds no longer offer the risk reduction aspect they have since 1981. It's also been my contention that this decade is likely to be similar to the 1970s, when bonds and stocks were positively correlated. This is unlike the teeter-totter behavior seen pretty much right after Mr. Carter exited the Oval Office. As old-timers like me recall, the Disco Decade was brutal for both stocks and bonds. They moved down together, particularly net of inflation, meaning they were positively correlated.

When I was writing my book in the second half of last year, I couldn't have known, of course, that my fears of a renewed downside linkage between equities and debt instruments would be realized as soon as the first quarter of 2022. To be totally accurate, there were numerous episodes over the last 40 years when stocks and bonds went up together. There were also a few when they tumbled simultaneously. But during times of severe market stress, like the crash in October 1987, bonds did provide powerful portfolio protection. The punishing bear market of 2008 to early 2009 also saw long-duration U.S. treasuries rise in price as stocks were being thrashed.

The problem with bonds right now is most definitely the risk I've been highlighting since the late summer of 2020: inflation. The Wall Street consensus has been in denial about the upside inflation breakout and, frankly, it mostly still is. The prevailing belief remains that the CPI will, before long, revert back to a 2% to 3% range. Otherwise, long-term T-bond yields would be much higher than 2.35%, where they are today.

What's fascinating about bonds presently is the shape of the yield curve. No doubt, you've been reading and hearing about the inversion that's already happened between certain treasury bond maturities. (As a short tutorial, the yield curve is simply the pattern of yields and maturities ranging from three months all the way out to 30 years. Generally, the slope of the curve is positive, meaning that shorter maturities yield less than longer ones. However, at times — usually when the Fed has been raising rates for a year or more — shorter rates become higher than longer rates. One of the best predictors of a recession is when the yield curve inverts. Inexplicably, the Fed has consistently ignored this signal over the last century, further impairing

its shockingly poor economic forecasting reputation.)

What's strange about today's yield curve is that the inversion has happened *despite* the Fed remaining in an exceptionally easy mode. This is notwithstanding its recent ¼ of a percentage point rate nudge. Also odd is that the shortest end of the yield curve, from three months to 18 months, is extremely steep. Specifically, a three-month T-bill yields around 0.5% whereas an 18-month T-note returns over 2.35% (treasuries longer than a year are considered notes; those beyond 10 years are referred to as bonds).

This leads me to the key point of this missive: There is a no-brainer opportunity to move out of cash into 12-to-18-month treasuries. For those sitting with substantial sums in bank accounts or money funds, this is an easy way to pick up around 2%. Yes, that's still below inflation but it's better than staying in essentially zero-yield cash. It's my expectation, based on history, that banks and brokerage firms will move like molasses in January during a polar vortex when it comes to raising the interest rates they pay on short-term deposits. Should rates continue to rise over the next year+, you'll be able to roll over your treasuries at higher yields. If you can hold them for six months, you should also be able to sell them in case you need the money, or the market plunges, for a minimal loss, if any. This is known as riding the yield curve, which is beneficial to do when it is as steep as the short-term T-note market is presently. So, ride away, right away!

LIKE

Pursuant to the main section of this *EVA PR*, I am putting out an official buy recommendation on 1- to 1 ½-year T-notes. It's still an inflation loser, but for the liquid portion of your portfolio, they easily best money funds... and are likely to for their duration.

- Large-cap growth names at a reasonable price.
- Certain international developed markets, especially Japan
- Publicly traded pipeline partnerships, i.e., MLPs and other mid-stream energy securities.
- Gold-mining stocks
- Gold
- Silver
- Swiss franc
- Select international blue chip oil stocks
- Oil field services companies, particularly those well exposed to the Permian Basin
- Short-term, investment-grade corporate bonds
- **One- to two-year Treasury notes**
- Emerging market (EM) bonds in local currency (focusing on stronger countries, particularly in Asia)
- Large-cap value
- High-dividend equities with *safe* distributions
- Most cyclical, resource-based stocks
- BB-rated corporate bonds
- Canadian REITs
- South Korean Equities
- Certain "Virus Victim" equities, such as refiners, homebuilders, and select retail stocks
- Investment-grade, floating-rate corporate bonds
- The higher-quality mortgage REITs

- Floating-rate bank loans
- Copper producers
- Healthcare stocks
- Capital spending-related companies, mainly focused on the U.S.

NEUTRAL

For those who own the nation's largest self-storage REIT, and have not at least partially cashed in some profits, I would take advantage of the recent strength to do so – asap. It now yields just 2%, below 2-year T-note yields, a most unusual situation. (Full disclosure: I am personally short this name in my hedge portfolio.)

- Uranium and uranium producers
- Renewable yield cos
- Intermediate-term, investment-grade corporate bonds, yielding approximately 4%
- Mid-cap value
- Emerging stock markets; however, a number of Asian developing markets remain attractive
- Emerging market bonds
- **U.S.-based Real Estate Investment Trusts (REITs)**
- Canadian dollar-denominated short-term bonds
- Traditionally “safe” sectors, such as Staples and Utilities
- Virus Victors
- Small-cap value
- European banks

DISLIKE

Moving cash to Dislike due to the far better alternative of short treasuries as described above. Per this week's Guest EVA, I'd also like to reiterate my disdain for the two leading meme stocks.

- **Cash**
- The Indian stock market
- A wide range of high-income securities, including preferred stocks
- Intermediate-term Treasury bonds
- Small-cap growth
- Long-term treasury bonds
- Long-term, investment-grade corporate bonds
- Most municipal bonds
- U.S. dollar
- Many semiconductor tech stocks
- Mid-cap growth
- Lower-rated junk bonds
- Green energy stocks
- SPACs
- Most new issues
- **Most of the popular Reddit/WallStreetBets meme stocks still have material downside; despite that, they are far below their 2021 totally irrational highs.**

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