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July 12, 2022

"That's an absolute maybe!"
— Barbara Spence, April 2022

Dear Friends,

This is one of those times (common amidst Bear Markets) when clarity, logic, common sense and predictability simply get mauled. Throw in COVID Part IV, war in Europe, gasoline at $6.00 a gallon and the Crypto Circus folding up its tent and you have yourself a state of perfectly *Absolute Maybe*. Pure conditionality. Sadly, neither Barb nor I can remember the question I asked which earned her witty response effectively telling me to go figure it out for myself. As investors, we have to do much the same. Seldom is there only one answer. One possibility. History can be helpful. It is somewhat comforting if there are familiar circumstances to which we can refer such as the Bear Markets of 1973-74, 1980-82, 1987, 1990, 2000-02, 2008-09, 2020 and 2022. (That would be eight maulings over the 51 years we have been investing… lots of excesses and opportunities to learn). The life rings we grasped each time were somewhat alike but we can assure you were subject to the tyranny of yes… *Absolute Maybe*.

Bear Tracks

Clearly we had 'em. Our letter last January cautioned against "speculative impulses of the markets to include stocks, bonds and real estate, not to mention things we choose not to own such as NFTs, cryptocurrencies and tulip bulbs especially when coupled with a growing rate of inflation." We characterized asset prices as "reaching unsustainable levels." Selected stocks were sold last year and continuing into the new year. The allocation of your assets to stocks was reduced. It was a good call. According to Barron's, a Wall Street Journal publication, *"The S&P 500 index dropped 20.6%, marking its worst first six months of a year since 1970… while plunges of 29.5% by the Nasdaq Composite and 23.9% by the Russell 2000 produced each index's worst first half on record."* Of late we (meaning you) have caught a bit of a break with the rise in interest rates. The CDs we are now purchasing on your behalf have increased by two full percentage points in yield as compared to this time last year. As of the date of this writing, the yield on a one-year US Treasury now exceeds 3% (per Tradeweb).

We always look back on these events wishing we had done more defensively but at this point are putting our energy into what comes next: the opportunities we can reasonably expect to arise in the months ahead. But it is a process, not an event. As we have postulated many times before, the leading indicator of high returns is low returns. We certainly have the latter. By the time you receive this letter companies will be in the midst of announcing their earnings for the second quarter and commenting on the outlook for the balance of the year. It is our expectation that corporate guidance will be cautious due to issues relating to inflation, rising interest rates induced by the Federal Reserve to combat same, consumers pulling in their horns and companies having over-ordered to guard against shortages. This will collectively lead to increased risks of a recession. The weakness in stock prices supports this proposition. Recessions in turn often lead to some opportunities to acquire stocks at meaningfully discounted prices. We (meaning you) will have the cash to capitalize on this scenario as a result of the de-risking achieved earlier. And, as they say… the Big Wheel keeps on a turnin'.

Dividends – The Stock Market's Profit Sharing Plan

We like them. Especially when stock prices are stumbling. If you can't count on appreciation, a dividend rate of three to four percent and more becomes especially welcome. But dividends also perform a second task: stocks providing substantial dividends tend to go down less in declining markets than those that pay little or no dividends at all. Think here… shock absorbers. With that said, a major caveat is also involved: a high dividend rate may also be the market's way of communicating that the dividend is at risk of being cut or eliminated. As an illustration of the power of dividends, let's take a look at one company that can be fairly classified as a "yield stock": Pfizer.

We all are aware of the success Pfizer has enjoyed with their products to help prevent and treat COVID. Equally important is that this new class of drugs may be adaptable for other applications. Great news for mankind and for Pfizer shareholders as well. To the extent that the cash generated from sales is in excess of what the company needs to grow the business, those funds become available to reward its owners (*aka* shareholders) with a bonus in the form of dividends. The final piece to this puzzle is the frequency with which dividends have been or can be raised. Pfizer has a fine track record in this department having raised its dividend each year for the last ten (possibly longer but that is as far back as we researched).

2012: 90 cents	2013: 98 cents	2014: $1.06	2015: $1.14	2016: $1.22
2017: $1.30	2018: $1.38	2019: $1.46	2020: $1.53	2021: $1.57

*Source: FactSet

Past dividend payments do not guarantee future dividends

A final nuance: if you were fortunate enough to purchase the stock at $37 fifteen months ago or even less in earlier times as opposed to today's quote at $52.04, the current dividend at $1.60 a share would amount to a yield of 4.3% on your cost as opposed to 3.1% at today's price. Another way to look at the benefits enjoyed by longer term shareholders. No absolute maybe about this one!!

An Absolute-Absolute

On a personal note, this coming Labor Day your writer will celebrate his 51st anniversary in the investment business. It has been a remarkable journey chiefly because of all of you, our extraordinary clients and, more importantly, friends. At age 75, it is time for me to pass the baton to my partners and co-workers who have prepared literally for decades to take on full responsibility for serving all of you. You will be in the best of hands. Barb and I will be retiring to our home in the San Juan Islands on February 1 of next year. I struggle mightily to find the words to express my appreciation for the trust you have placed upon us and the opportunity to be a part of your lives. I am the most fortunate guy I know. No "maybe" about it!

The Klavins Report – Thoughts From Outside the Corner Office

What a first half! It is amazing how quickly things can go from feeling good to feeling, well, cruddy. At least we think that's how many of us are feeling…about COVID, about politics (regardless of affiliation), and of late about the stock market. As people who pore over research reports, and think about stocks and markets for a living, we can tell you that it is definitely more fun when markets are regularly making new annual highs, as opposed to new lows. That said, selloffs are a normal part of being a long-term investor. So, take a deep breath and try to remember that investing is about time **IN** the market, rather than tim**ING** the market. And while holding firm can feel tough when statements show smaller balances month after month, there is wisdom in the approach.

Along those lines, while most of our stocks and accounts are down in the first half, there are loads of stocks that we are happy if not outright thrilled not to have owned…

FOMO (Fear Of Missing Out)/Momentum…Did you miss out? During the earlier stages of COVID a number of companies had businesses that seemed to be obvious beneficiaries of the "stay at home" phenomenon that was forced upon most of us. Examples of such hot stocks include:

- Amazon (AMZN) and Shopify (SHOP) as shopping from home accelerated, became ubiquitous, and businesses small and large tried to adapt to stay relevant
- Zoom Video (ZM) and Docusign (DOCU) as meetings moved online and documents were "signed" digitally
- Peloton Interactive (PTON) because gyms were closed
- Netflix (NFLX), because what else was there to do in home confinement, after a long day of Zoom meetings, but binge watch streaming TV between alternating sessions on one's Peloton and online retail therapy marathons

The stocks of some of these companies rocketed higher for a time, and we know for a fact that some of you were wondering why we weren't buying them. After all, they were obvious, right? To those who asked us, we said…VALUATION. As a broad generalization these companies traded at multiples to earnings or sales that were simply too high for price sensitive folks like ourselves. In situations like that we typically choose not to pay stratospheric sums that, in our opinion, would take many years of extremely high growth to begin to justify.

With the benefit of hindsight, and lockdowns hopefully behind us, we thought it might be interesting to revisit these six companies to see how their stocks have fared. To be clear, our goal is not to throw stones nor make any recommendations about these stocks one way or another, but rather to illustrate how we, on our team, think about investing generally and thought about certain highly valued stocks over the last couple of years. With that in mind, the following table looks at prices/performance of these stocks from three starting points through June 30, 2022: since February 19, 2020 (just before lockdowns), since their peaks over the last 12 months, and since the start of 2022.

Name (Ticker)	**Closing Price on 2/19/20 (pre-shutdown)**	**Intra-day Peak since Pandemic Began**	**Closing Price on 12/31/21**	**Closing Price on 6/30/22**	**Cumulative Return since 2/19/20**	**Decline from Post-Pandemic Peak**	**Decline Year To Date**
Amazon (AMZN)	108.51	188.65	166.72	106.21	*-2.1%*	*-43.7%*	*-36.3%*
Shopify (SHOP)	54.32	176.29	137.74	31.24	*-42.5%*	*-82.3%*	*-77.3%*
Docusign (DOCU)	91.49	314.76	152.31	57.38	*-37.3%*	*-81.8%*	*-62.3%*
Zoom Video (ZM)	103.93	588.84	183.91	107.97	*3.9%*	*-81.7%*	*-41.3%*
Peloton (PTON)	27.10	171.09	35.76	9.18	*-66.1%*	*-94.6%*	*-74.3%*
Netflix (NFLX)	386.19	700.99	602.44	174.87	*-54.7%*	*-75.1%*	*-71.0%*
					-33.1%	***-76.5%***	***-60.4%***
Dow Jones Ind.	29,348.03	36,952.65	36,338.30	30,775.43	*4.9%*	*-16.7%*	*-15.3%*
S&P 500	3,386.15	4,818.62	4,766.18	3,785.38	*11.8%*	*-24.5%*	*-20.6%*

*Source: Factset

So, this basket of six stocks had an average decline of 33.1% since just *before* the world shut down, an average decline of 76.5% from their respective peaks, and an average year-to-date decline of 60.4% in the first half of 2022. We stipulate that one or more of these may be truly remarkable companies. We have no doubt that some of them will remain viable and growing businesses for many years. Heck, given sharp price declines there might even be a company or two on the list that eventually piques our interest. However, we hope this illustrates clearly the notion that price matters. Just because a business is benefitting from a trend, getting a lot of attention, and has a lot of momentum does not mean its high valuation is justified.

In a similar vein, other fashionable instruments, cryptocurrencies chief among them, are taking it on the chin of late. Per Nasdaq's website, Bitcoin closed the first half at $19,854, down 71% from its 52-week high of $68,493 hit on November 8 and 58% in the first half of 2022. Some so-called stablecoins (the ultimate misnomer) have been wiped out, and various crypto entities are extending loans to one another to try to shore up the industry. To all of that we say: NO THANK YOU!!! We refer you to our January 2018 client letter, wherein we wrote "*...we believe that buying these currencies, coins, or tokens is more akin to pure speculation than investing. We therefore choose not to play.*" We feel the same way today. Don't even ask us about NFTs.

For our part, we'll continue to focus most of our attention, and your investment dollars, on the stocks and bonds of real businesses operating in less exciting and far cheaper parts of the market. We won't always be right, especially in the short term, and we'll definitely make our own mistakes. We'll be early. We'll be wrong. We'll succumb to the occasional value trap. No doubt about it. However, we'll do our darndest not to chase expensive momentum stocks, or the new-new thing, even if there is a good story behind them. You've worked too long and too hard for your capital.

One more thing, and this is important…remember that in bear markets even the shares of good companies typically go down in value, sometimes significantly, and we never get to know where the bottom is. Hold on and think like an owner. Investing isn't about the next 3-6 months or even the next 1-2 years. It is about the next five to ten years and much longer…your financial *lives*! While the short term can at times feel uncertain or even scary, there is comfort in the long term. Looking at the long term, we believe to our cores that despite current challenges we live in an amazing country inhabited by industrious people that together make up the most dynamic economy the world has ever known. If you share our view, then the long-term prospects for the market seem meaningfully brighter.

Warmest regards,

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