Points in Time: Q2 2020

Stock markets recover from the March low, led by technology and precious metals. LFA dividends remain resilient in Q2.

WATCHING

Stocks and commodities rallied strongly this quarter on growing confidence that the COVID-19-induced economic downturn will be short lived as global economies began to reopen. Massive fiscal stimulus measures and continued injection of liquidity into credit markets by central banks also provided a tailwind for risk assets. While conventional data showed a historically deep and swift decline in economic activity during Q2, recent higher frequency data have already begun to show a rebound in employment, consumer spending and manufacturing.

The S&P 500 Index gained 15% (in Canadian dollar terms) for its best quarter since 1998, while the NASDAQ Composite Index reached an all-time high during the quarter, paced by strong gains from leading technology stocks like Apple and Microsoft. We also saw similarly strong stock returns across the global regions including Canada where the S&P/TSX Composite Index gained 16% in Q2. The 10-year government bond yields in Canada and the U.S. pulled back slightly, although corporate and high-yield bond prices surged during the quarter after the U.S. Federal Reserve announced facilities that would allow them to purchase qualified corporate bonds and investment grade bond ETF's.

After the WTI crude price traded to a negative price for the first time in history in April, oil prices rebounded strongly in Q2 with WTI closing at $39.27. The Canadian dollar also closed higher in Q2 at 0.74 as the U.S. dollar weakened against most major currencies on optimism of a global economic rebound in the second half of the year. Volatility was the rare asset class that declined in Q2. After spiking to a record high of 82.69 in Q1, the VIX Index reversed lower during the Q2 and settled at 30.43.

THINKING

Stocks proved to be remarkably resilient this quarter and many stock markets retraced a significant portion of the Q1 sell-off during April and May. In North America, many parts of the economy have taken the first tentative steps to reopen for business. Investors are monitoring the recent increases in new COVID-19 cases in Arizona, California, Texas and Florida and the possibility of a second wave of infections as the shutdown restrictions are eased. The resurgence in new case growth seen in parts of the U.S. has not appeared in Europe and Canada, but the scenario of a second wave of infections is the primary concern that could derail the strength in stocks. However, if the new case growth does not lead to higher hospitalizations and fatalities, a new round of economic shutdowns is unlikely, and this will ease investor concerns about the durability of the current rally in stocks.

Lastly, stock valuations continue to be supported by the extreme low rate environment. Currently, more than 72% of S&P/TSX stocks have a higher dividend yield than the 10-year Canada government bond yield. In the U.S., 75% of the S&P 500 stocks have a higher dividend yield than the 10-year U.S. Treasury bond yield. Stimulus initiatives continue to build globally, which has helped to support risk assets and reduce the risk of a worst case depression-like scenario for the economy. The support from fiscal and monetary policies is critical as we wait for the economic recovery to broaden out and growth to resume. Earnings estimates for 2021 and 2022 have already stabilized and when the estimates show growth again, that will also alleviate some of the valuation concerns for stocks.

source: Bloomberg

Staying in the market through the turbulent first quarter has let you participate in the Q2 recovery.

DOING

As the second quarter of 2020 unfolded, equity markets displayed a somewhat unexpected resilience. The Covid-19 threat is far from over, with a great deal of uncertainty regarding both the ultimate small scale and large scale effects. Despite this, the equity markets globally marched higher through April and May, and have perhaps plateaued in June, though the daily swings are still fairly large by historical standards. Staying in the market through the turbulent first quarter has allowed you to participate in this rebound. We were not particularly active in Q2, having done most of our purchasing in the previous quarter. We put more cash to work in April by increasing our Brookfield Asset Management position. As described in our previous Points in Time, Brookfield is very well managed international asset manager. The stock also split 3 for 2 in the quarter. With the international uncertainty brought on by the Covid-19 response, we have also decided to increase our target weighting in Agnico Eagle Mines. This gold stock has seen strong price appreciation, but we have decided to continue holding it, rather than take profits, at this time.

2020 Dividend Performance Summary

Canadian Dividend Portfolio

Number of companies in the equity portfolio	30
Number of companies that declared an increased dividend	13
% of companies that declared an increased dividend	43.3%
Weighted average of dividend increases	1.3%
Consumer Price Index Increase (YoY*)	-0.4%
Equity portfolio dividend yield**	4.7%
S&P/TSX dividend yield	3.4%

Income Stability Portfolio

Number of companies in the equity portfolio	28
Number of companies that declared an increased dividend	12
% of companies that declared an increased dividend	42.9%
Weighted average of dividend increases	1.9%
Consumer Price Index Increase (YoY*)	-0.4%
Equity portfolio dividend yield***	4.6%
S&P/TSX dividend yield	3.4%

Top 10 Dividend Growers

Agnico Eagle Mines	14.3%
Canadian Natural Resources	13.3%
Manulife Financial Corporation	12.0%
Enbridge	9.8%
Intact Financial Corporation	9.2%
TC Energy	8.0%
Canadian National Railway	7.0%
Toronto Dominion Bank	6.8%
Pembina Pipeline Corporation	5.0%
BCE Inc	5.0%

* Estimate from Bank of Canada, May 31st, 2020
** The dividend yield is based on the Leon Frazer Canadian Dividend Fund using the target weight for cash
*** The dividend yield is based on the Leon Frazer Income Stability Fund using the target weight for cash

source: Leon Frazer & Associates, June 30, 2020

A Closer Look: Canadian Utilities

Canadian Utilities Fact Sheet:

Trading Symbol:	CU
Market Cap (Mil):	$9,238
Dividend Yield:	5.15%
Dividend Growth 3 Year:	21.8%
Dividend Growth 5 Year:	47.6%
Dividend Growth 10 Year:	130.7%
Sector:	Utilities

Overview

Companies in the utility sector are essential services, which generally have either stable regulated earnings or use guarantee purchase price agreements. Companies that operate in the utility sector typically earns a stable rate of return, which is regulated by the local utility commission, and therefore produces stable and growing income, which translates into stable and growing dividends.

Canadian Utilities is engaged in the following business activities:

- Electricity: electricity distribution and transmission, distributed generation, electricity generation, and infrastructure development
- Pipelines & Liquids: natural gas transmission and distribution, infrastructure development, energy storage, and industrial water solutions

The majority of Canadian Utilities' assets are located in Canada, specifically Alberta and the Northwest Territories. Other countries of operation includes: Australia, Chile, Puerto Rico and Mexico.

Strengths

48 years of annual dividend increases, the longest track record of any public Canadian company.

Canadian Utilities expects net rate base growth in their utilities to average between 3 and 4 percent per year over the next three years, for which dividends are expected to grow in line with rate base growth.

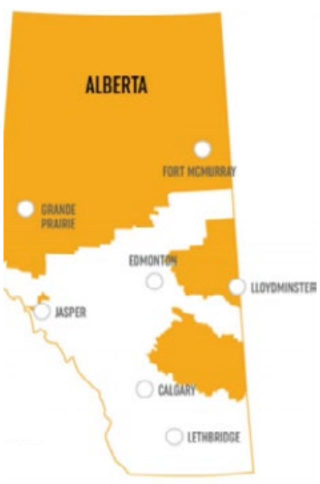
Strong investment grade credit rating, the majority of Canadian Utilities' cash flow are backed by stable regulated utility operations.

Recent increased geographic diversification, expanded asset ownership and services in Mexico and Puerto Rico.

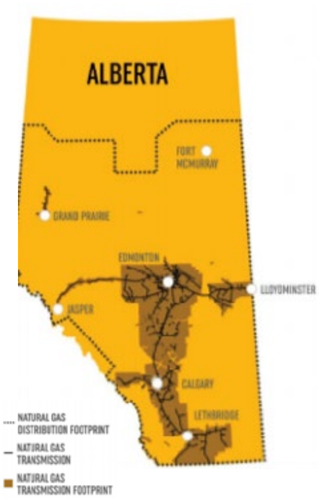
Due to the regulatory nature of their assets, Canadian Utilities does not expect material changes to ~81% of their 2020 revenue as a result of COVID-19 or macroeconomic global market conditions.

With their recent divestiture of most natural gas and coal-fired electricity generation assets, the carbon footprint and environmental impact from Canadian Utilites operations has improved.

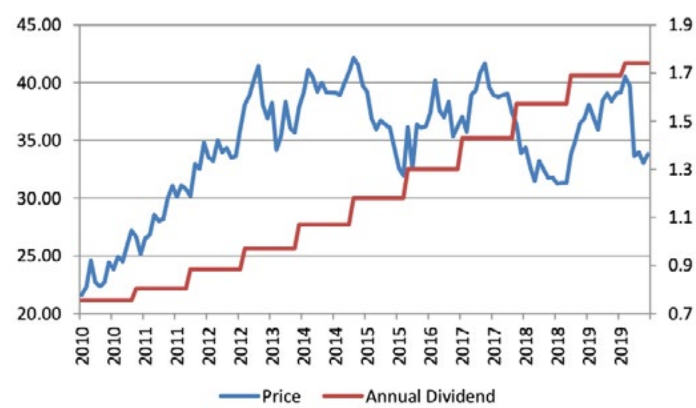
Alberta Electricity Distribution and Transmission area served by Canadian Utilities



Alberta Natural Gas Distribution and Transmission area served by Canadian Utilities



Canadian Utilities Price and Dividend History



Sources: Thomson Eikon, Canadian Utilities

Standing in solidarity

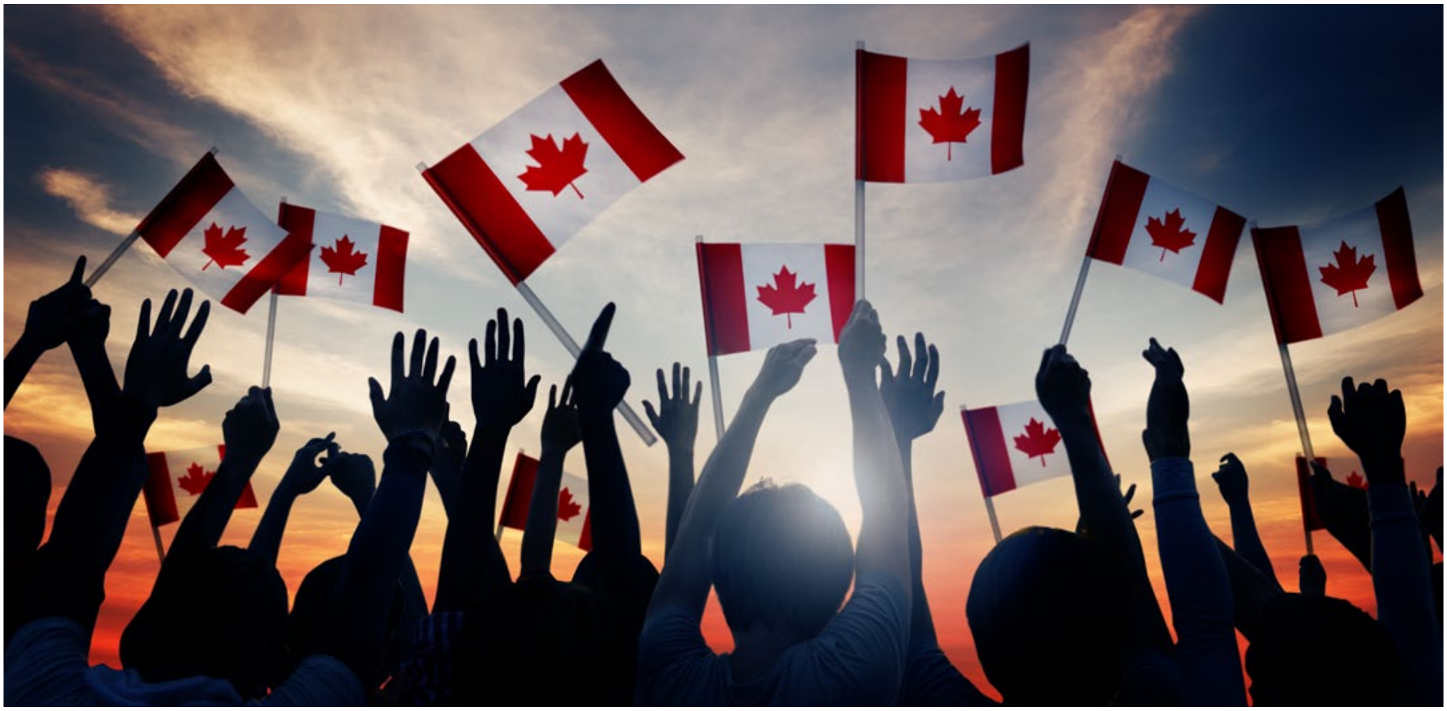
We are deeply saddened and concerned about the prevalence of racism and the violence that led to protests in the United States, Canada and beyond. We want to stress that as a firm, we are strongly committed to our diverse culture and people regardless of their race, religion and any other factors that may lead to possible discrimination. We stand in solidarity with all those pursuing peaceful courageous protest against racism in our world.

Our firm's corporate code of ethics specifically addresses racism and we have strict policies that immediately deal with any incidents involving discrimination against employees, clients and/or service partners. In response to recent events, we are reviewing these policies, educating our people and ensuring our commitment to confronting racism and discrimination.

We know that dismantling racism in our world cannot be achieved in a day and will continue to do our part to establish inclusion and equality in our firm, by ensuring that our policies and actions promote the well being of everyone ongoing.

Steven Belchetz

SVP Business Development and Client Relationships,
Leon Frazer & Associates



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