The Market in Review

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This week's articles and insights

"Orbit is hard. Took us four attempts with Falcon 1."

- ***Elon Musk's condolences after Virgin Orbit's unsuccessful launch***

Your Index Report

	Current	Last Week	Year-to-Date
Dow Jones Ind. Avg.	25,401	+ 3.79%	- 11.00%
S&P 500	3,030	+ 2.75%	- 6.22%
TSX	15,263	+ 2.54%	- 10.55%

Up, Up, and Away

In 2010, President Obama announced a major shift at NASA, the government space agency. He proposed that all launch vehicles would be designed, manufactured, and operated by private aerospace companies instead of government agencies. NASA would become a paying customer from that point forward.

What was the rationale behind this? As with most things, it was cost. A space shuttle launch cost about $450 million (source: NASA) before it was cancelled in 2011, which made for a very expensive plane ticket. Boeing’s proposed Starliner rocket would get that down to $345 million, but a new entrant called SpaceX would cut costs even further. Elon Musk’s company had just launched its Falcon 1 rocket into orbit in 2009 after almost going bankrupt. SpaceX’s eventual launch costs of $209 million were less than half those of the space shuttle and were the cheapest in the world. Some experts see the cost to launch a satellite dropping to 1/10th of this price in the years ahead due to competition and innovation.

SpaceX is now the clear leader in commercial launches. By 2018, the company garnered 43% of the global market and had almost put its French and Russian competitors out of business. The key to its low priced launches are its reusable rockets, which are a miracle to watch as they touch down in tandem:


Source: SpaceX

This week, we will see the (hopefully) successful launch of the Crew Dragon capsule, the first non-government space capsule to deliver astronauts to the international space station. Like most space projects, it is late – the Crew Dragon capsule was supposed to be launched in 2015. The delays were because of a failed launch and an upgraded safe-abort system.

It promises to be a busy period for SpaceX, as NASA hopes to return to the moon in 2024 using a new SpaceX rocket called the BFR (Big Falcon Rocket). The U.S. plans a manned landing on Mars in 2028, although this is more of a dream than a plan, at this point.

What does all this mean for investors? A new industry! Several new companies have been created, including Virgin Galactic (**NASDAQ SPCE**), Aerojet Rocketdyne (**NASDAQ AJRD**), as well as the older rocket companies like Boeing (**NYSE BA**) and Lockheed Martin (**NYSE LMT**). At some point, Jeff Bezos's private company Blue Origin - the largest private competitor to SpaceX - is likely to be brought public. Close to 50 countries now have space programs, with China, the European Union, Russia, Japan, and even Israel launching lunar rockets.

The bright side of this new industry is all the jobs it is creating. Globally, it is expected the space industry will almost triple from approximately $400 billion today to over $1.1 trillion by 2040. As old industries like automobiles and oil extraction wind down, we will need new ones like this to replace the lost jobs.

The dark side is that much of this expansion will be military. America's new 5th branch of its armed forces, the Space Force, is the most visible example. This doesn't mean war in space is inevitable – many inventions, from the internet, GPS, radar, to the microwave oven – all came from military research. We hope that the old saying "the best way to prevent war is to prepare for it" holds true in this case.

Fingers crossed for the launch of the SpaceX Crew Dragon and its two astronauts tomorrow.

Market Surges and Shifts

Provinces and states began opening up for business over the last two weeks, bringing a sense of optimism to markets. There has also been steady progress on flattening the curve and the race to deliver a Covid-19 vaccine.

On the pessimistic side, the economic hits are mounting. Temporary layoffs are now becoming permanent ones due to the pandemic, with large cuts announced at Boeing and Chevron (**NYSE CVX**). In Canada, the Big Six banks are building substantial loan-loss reserves in preparation for loan and mortgage defaults. CIBC (**TSX CM**) set aside a record C$1.41 billion in provisions, more than five times the amount it did a year earlier. TD (**TSX TD**), the most US-focused of the

Canadian banking giants, set aside C$2.29 billion for souring loans in both countries. Both banks missed earnings estimates but left their dividends intact.

We value stocks based on earnings, which are dropping. But, stocks rise when new money enters the markets. Europe plans another US $800 billion stimulus package and there is already US $4 trillion sitting in cash on the sidelines that could flow into stocks. Earnings say “sell” but money flows say “buy”. It makes for a very distorted landscape.

We are also seeing tensions growing between China and the US (and the rest of the world) as China forces new security laws on Hong Kong. The bill will bypass Hong Kong’s legislature, raising concerns over the longevity of Hong Kong’s “one party, two systems” principle, which allows additional freedoms mainland China does not have. This move could now trigger a range of actions by the Trump administration, from sanctions on Chinese officials to revoking the city’s special trading status with the US.

In just the last two months, there have been 11 bills introduced in the U.S. against China and its corporations:

Recent Actions	Agency	Date	Status
New Export Controls on Military End Use/Military End User	Commerce Department	4/27/2020	Final Rule
Removal of Civilian End Use License Exemption	Commerce Department	4/27/2020	Final Rule
Changes to Re-Export of Controlled Technology	Commerce Department	4/27/2020	Proposed Rule
Delay of Federal Employee Investments in Chinese Equities	FRITB	5/13/2020	Pending
Prohibition Using US "Technology" and Software" - Huawei	Commerce Department	5/15/2020	Interim Final
Extension of Huawei Entity List Designation/TGL	Commerce Department	5/15/2020	Final (90-Day)
Uyghur Human Rights Policy Act	US Senate	5/14/2020	Passed Senate
WHO Status for Taiwan	US Senate	5/11/2020	Passed Senate
Delisting Chinese Equities	US Senate	5/20/2020	Passed Senate
Bills to Allow Suits Against China - COVID-19	Congress: Senator Cotton	4/16/2020	Introduced
Sanction Bill Against China - COVID-19 Investigation	Congress: Senator Graham	5/12/2020	Introduced

Source: Raymond James Research

From an investor’s point of view, it remains a bit of a mystery how the market can continue to rise even as economic worries mount. Some forecasters have gone so far as to say we have just come through the shortest bear market in history and are now back in a bull market.

To us, the most interesting shift has been the one from growth to value. For example:

- Since March 31st, Exxon (**NYSE XOM**) has risen exactly the same amount as Amazon (**NASDAQ AMZN**).
- Since the market bottom in March, Cameco (**TSX CCO**), the beleaguered uranium producer, has outperformed Zoom Video (**NASDAQ ZM**), the most recognized winner of the Covid-19 era.

It is too early to know if this is a permanent change, like we saw in 2000 when investors fled the "dotcom" stocks and bought banks and oil companies. The disparity between expensive growth stocks and cheap value stocks is as wide as it was then, though.

Three Unintended Consequences

The first is an unexpected response to the immediate and generous unemployment benefits: a reluctance to go back to work. A recent University of Chicago report suggests that 68% of jobless workers will collect more through unemployment insurance and the federal government's added $600 than they would receive from their working wages. A similar dynamic is occurring in Canada. This may delay a recovery.

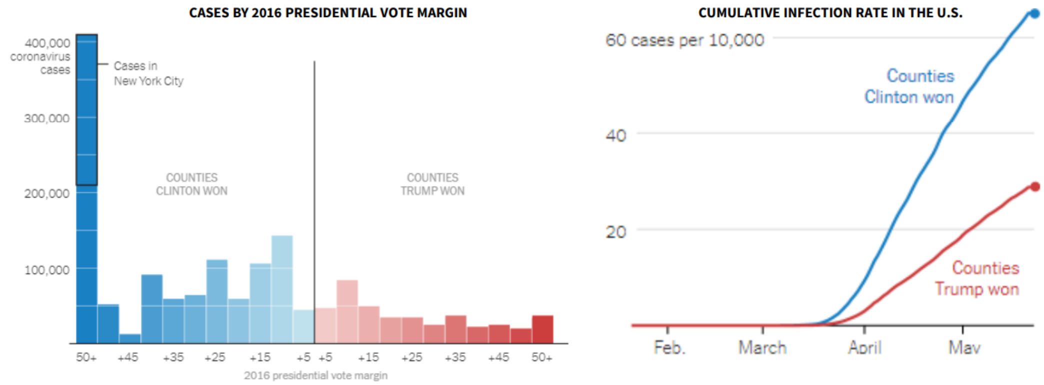
The second is China's bumpy recovery. Traffic patterns show the country has mostly resumed going back to work. However, *weekend traffic* is still down by over 60%, which suggests that Chinese consumers are reluctant to spend. Data shows this: demand for apparel, jewelry, and household appliances has failed to recover.

However, car sales have surged. It seems people may be turning away from crowded mass transit and the germs that congregate there. The coronavirus certainly makes autonomous vehicles even more compelling. Tesla (**NASDAQ TSLA**) expects to begin a driverless ride-hailing service this year.

The third unintended consequence is how the pandemic may affect the U.S. election later this year. Those counties most affected by Covid-19 tend to be Democratic ones where lockdowns are more prevalent, while the less affected were more Republican ones where lockdowns were resisted.

POLITICS OF THE PANDEMIC

The New York Times put out an excellent piece over the weekend (read here), looking out how counties Trump won have been (with few exceptions) dramatically less impacted than counties Clinton won in 2016. Though counties, regardless of political preference, are feeling the economic pain, not all are seeing the health devastation from the pandemic. These facts are likely going to continue to impact how politicians respond to the threat going forward.



Sources: New York Times database of reports from state and local health agencies and hospitals (coronavirus cases); Dave Leip's Atlas of U.S. Presidential Elections (election results, except Alaska) Data is as of May 21, 2020. By Jugal K. Patel. https://www.nytimes.com/2020/05/25/us/politics/coronavirus-red-blue-states.html

What We've Learned

Every week, we know more about the coronavirus and the human body. Mass testing and all this new knowledge should help blunt a second wave later this year.

For example, we know the virus can spread through particles in the air. Enclosed spaces with a lot of heavy breathing can become danger areas. Science Magazine reported that 53 people in a 61 person choir in Mount Vernon, Washington became infected after a 2 ½ hour rehearsal. They also report that while "Zumba classes have been connected to outbreaks, Pilates classes, which are not as intense, have not." This suggests "slow, gentle breathing is not a risk factor, but heavy, deep, or rapid breathing and shouting is."

Japanese data also shows that, of 318 virus "clusters", only one originated outdoors. This suggests our chances of getting infected is minimal when outside.

New data from the Center for Disease Control in the U.S. has lowered the overall infection fatality rate to 0.26%. This is still higher than the seasonal flu, but not 10-20x as bad, as earlier feared. The CDC further estimates that people under age 50 have a 99.97% survival rate.

The surge in medical research to combat the coronavirus is leading to groundbreaking discoveries in inflammation, how viruses work, and new ways to stop them. Boosting our immune systems against viruses will also lead to new therapies against cancer and possibly even Alzheimer's in the future. We have not had a new antibiotic developed in the last 25 years. This shortfall has been made very apparent with all the pneumonia cases that can accompany Covid-19, so research money is finally moving back towards antibiotics.

Artificial intelligence has been harnessed and sent in entirely new directions, as well. It has been used to map the genome of the virus and then identify entirely new molecules to neutralize it. A decade's worth of work has been compressed into months.

The entire biotech sector has been somewhat ignored for the last decade. Recent events suggest it may become one of the hottest areas for investment in the years ahead.

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Prices as of May 28th, 2020

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