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THE SCHOONER

The Official Newsletter of the Dalhousie Investment Society (DALIS)

Trade of the Month

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Position:

On February 21, 2024, FCT purchased shares of Nvidia at a price of $671.20. The group regarded the dip preceding the company's Q4 2024 earnings release as an excellent entry point. Upon release of quarterly results, the stock surged 16.40%, delivering a quick and sizable gain.

Five days post-report, levels held 14.50% above our entry point and we decided to hedge our position using a collar strategy with March 15, 2024, expiry. We sold three out-of-the-money calls for $20.05 per contract at a strike price of $800 and bought three out-of-the-money puts for $17.25 per contract at a strike price of $760, thus hedging the entirety of our position and generating credit of $2.80 per share. As a result, the downside protection at $760 (13% gain) per share and our upside potential is capped at $800 (19% gain) per share.

Rationale:

Nvidia has been at the forefront of the AI-driven tech rally since 2022, more than doubling revenues to $61 billion while their share price has surged 590%. Looking into fundamentals, Nvidia's Datacenter division stands out by contributing 55% of the company's total revenue. Specifically, they sell GPUs that are critical to the functionality of cloud computing, and most importantly, generative AI. Their secret ingredient - early adoption. Over a decade ago, Nvidia's CEO shifted the company's focus from gaming to AI. Currently, the company has near monopoly on the market allowing gross margins of 74%. We see this competitive advantage as sustainable for the near future and in turn, we support a bullish thesis in the long run.

When strategizing our entry point, we saw Nvidia's Q4 2024 earnings release as an opportunity to take advantage of the volatility and achieve better pricing. The negative sentiment surrounding Nvidia's ability to meet the street's "sky-high" expectations saw shares fall over 7% in the two days leading up to the release, making entry more attractive. Additionally, our research into Nvidia's customers contradicted the bearish consensus. Microsoft, Meta, Amazon, and Alphabet, who collectively account for 40% of Nvidia's revenue, all reported strong forward guidance for their cloud computing units and/or generative AI initiatives, supporting our long-term growth outlook.

Our macroeconomic and industry outlook for the short term see elevated levels of volatility given swinging CPI data, constantly shifting rate expectations from the Fed, and the looming threat of an "AI Bubble." Therefore, in the coming months, we have decided to protect our underlying investment returns by employing a collar strategy. We opted to use options expiring on March 15, 2024, intending to roll them forward into new collar positions as we see fit.

A Glimpse of What's Inside:

Trade of the Month

The Maritime Fund Update

Alumni Spotlight: Stew Paterson

Student Spotlight: Aadhith Kumaresan

Power Play

Dollar Dynamics

Balancing Ambition and Reality

As Fringe Data Sets Move Front and Center

The Regional Bank Roller-Coaster

Water Wealth

DALIS
DALHOUSIE INVESTMENT SOCIETY

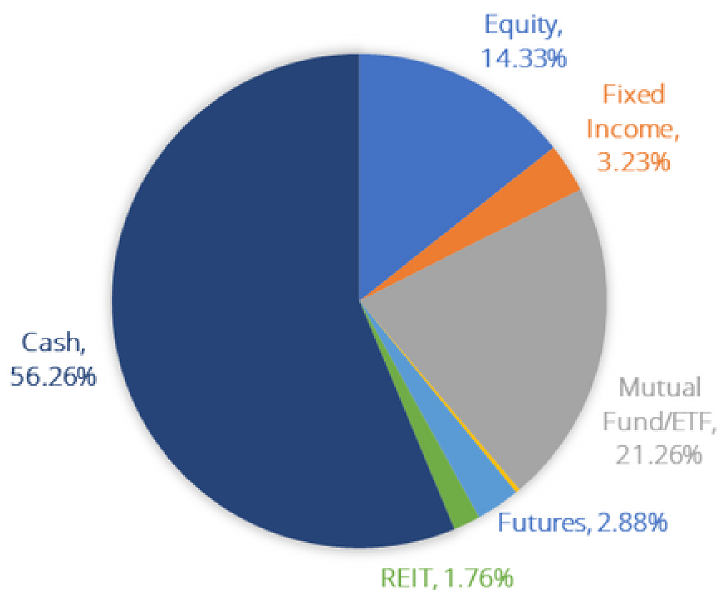
The Maritime Fund

Portfolio Overview

Portfolio	Holdings	Market Value	Change TTD	% TTD
Macro Strategy & Fixed Income	26	$32,336,237	$1,393,945	4.50%
Commodities	14	$32,317,652	$1,241,186	3.99%
Financials, Consumer, Tech	18	$32,066,777	$1,700,820	5.60%
Energy, Industrials, Real Estate	19	$31,562,266	$796,712	2.59%
Maritime Fund	77	$128,282,932	$5,132,663	4.17%

Sector	Market Value	Weight
Industrials	$11,523,171.60	8.98%
Financials	$11,490,534.13	8.96%
Consumer Staples	$6,665,402.40	5.20%
Real Estate	$5,370,857.94	4.19%
Technology	$3,298,972.69	2.57%
Metals & Mining	$3,070,302.41	2.39%
Communications	$2,518,854.81	1.96%
Energy	$2,311,683.40	1.80%
Consumer Discretionary	$1,544,194.87	1.20%

Top 10 Holdings
1. Cash (CAD)
2. US Dollar/ Brazilian Real
3. Canadian Dollar/US Dollar Cross
4. Invesco S&P 500 Equal Weight Industrials ETF
5. iShares 20+ Year Treasury Bond ETF
6. Vanguard Industrials Index Fund
7. Bank of Canada 3 1/4 12/01/2033
8. Visa US Equity
9. Procter & Gamble
10. iShares iBoxx $ Investment Grade Corporate Bond ETF



**TTD = Term to Date*
All $ Figures in CAD

DALIS
DALHOUSIE INVESTMENT SOCIETY

The Maritime Fund

Commentary

MACRO STRATEGY & FIXED INCOME

Moving into March of 2024, the global macro portfolio has followed two main themes; a Fed on the edge of softer monetary policy and a stubborn equities market. As a result, the portfolio has taken advantage of the current US rate status through the global FX markets and gained exposure to US equities via exchange-traded funds. For the equities side of the book, we remain overweighted in cyclical sectors. To gain further exposure to technology during earnings, call options on the S&P500 as well as QQQ were set in place. Both trades were profitable as large-cap tech companies reported strong earnings throughout February.

In foreign exchange, the Macro group is long in JPY against the greenback on the thesis of lower US rates and a possible hawkish BOJ. After a hotter US inflation report led to a further weakening of the yen, we decided to reallocate half the position into a CHFJPY long. Another long position is held on the peso, banking on the interest rate differential as inflation stays persistent. On the other hand, short positions are held within the Canadian dollar and Brazilian real against the US dollar. As for fixed income, we aim to continue our exposure to TLT through selling puts to gain income, with a willingness to be assigned around the $90-91 level.

COMMODITIES

The Commodities book has made a few plays over the last month. Namely, earnings plays on Senior Canadian gold producers Agnico Eagle Mines and Kinross Gold, where we currently hold both and have made significant gains. The book recently captured alpha through short-dated calls on Chevron and Denison Mines near their earnings and centered around tailwinds in their respective sectors. We continue to stay active in trading crude contracts based on both weekly API and EIA reports, gauging market sentiment, then moving accordingly – whether that be long or short.

We have taken a modest position in a Canadian lithium exploration junior – Lithium Chile - who has a strong outlook on their South American projects. We are neutral to overweight on the sector and continue to monitor lithium spot prices in anticipation of significant downward pressure due to oversupply - hedging our positions accordingly. Since last month, we've sold our 12 contracts of Cocoa (just over a $750,000 market value) to take profits and minimize our downside in anticipation of price re-stabilization due to the ending of major weather events and the realization of Cocoa's supply loss.

The Maritime Fund

Commentary

FINANCIALS, CONSUMER & TECHNOLOGY

February was a busy month for the FCT group, driven by a large focus on the technology sector amid the AI boom. Key moves included a $226K long position in Nvidia entered into before Q4 earnings, capitalizing on heightened volatility and a 7% stock decline in the two days preceding their earnings announcement. After five days, the position achieved a return of 14.50%, prompting the subsequent implementation of a collar strategy with March 15, 2024 expiry, securing downside protection and establishing an upside cap at a price significantly higher than purchased for.

Other trades entered into in February include long positions in Uber, Vizio, Citigroup, and WarnerBros, as well as a short position in Salesforce, with a combined return of 13% and market value of $2,542,600.82. Covered calls have been placed on Citigroup to generate synthetic dividends and leverage the stock's relative stability. Regarding positions established in Fall 2023, $3M was divested from the $4M long position in Disney, initiated in December 2023, resulting in a return of 20%.

ENERGY, INDUSTRIALS & REAL ESTATE

The Energy, Industrials, and Real Estate portfolio is currently 60% allocated. Our real estate positioning is long biased with a concentration on the industrial asset class, and data center REITs. A small percentage of our current RE allocation is in REK US, an ETF that aims to track the inverse of the S&P Real Estate Sector Index, this position is in to hedge our longs in the case that negative economic data will hurt CRE markets as a whole. Our industrials positions are also long biased with holdings such as John Deere, UPS, and the RSPN ETF. We still own May 17th puts on Boeing, but have been sizing down this position at a loss as theta will continue to play an increased role as we approach expiry with our strike of $200. Our energy holdings consist of primarily oil producers in North America with recent trades being a long on FANG after there acquisition of Endeavour that added an impressive presence in the Permian Basin of West Texas.

Going forward our Commerical Real Estate preference remains the same. We hope to continue to reap benefits of a pumping industrials sector, while looking for opportunities to hedge short with single equities facing safety, or supply chain concerns. In energy, we will continue to hold oil producers long, while looking to become more active in different energy classes such as renewables, and nuclear going forward.

Alumni Spotlight

MBA, Finance '10

Stew Paterson

Managing Director, Head of European Fixed Income Sales
TD Securities (Dublin, Ireland)

Can you elaborate on your current role at TD and the journey that led you there?

I was in New York with TD when I was asked to move to Dublin. And that was because there were some challenges in getting enough people to relocate from London at the time. TD has an office in Dublin in a post-Brexit world because we could no longer cover European clients from our London office. I had put my hand up earlier in my career to move into a management role, and this was a good opportunity for me to step into a role and manage a team. That path took me over to Dublin to manage our European fixed income sales team. So de facto, we split our office, and half the team came here, and half stayed in London.

In my role, I work in Fixed Income Sales, serving institutional clients across Europe, including asset managers, pension firms, central banks, insurance companies, and hedge funds. Essentially, we function as financial advisors for institutions, specializing in fixed income, predominantly bonds, spanning various currencies and risk profiles, from government bonds to high yield. My primary responsibility is facilitating transactions between our clients and trading desks, acting as the intermediary to ensure smooth execution.

My academic journey, I transitioned from an undergraduate focus in accounting to pursuing an MBA at Dalhousie. Initially drawn to sales and trading, particularly currency trading, I navigated through TD's rotational program, gaining exposure to different facets of sales & trading. Ultimately, I discovered my passion and skills lay in sales rather than trading, a realization that has fueled my 15-year tenure in this role.

What are a few pieces of advice you would give to current DALIS members?

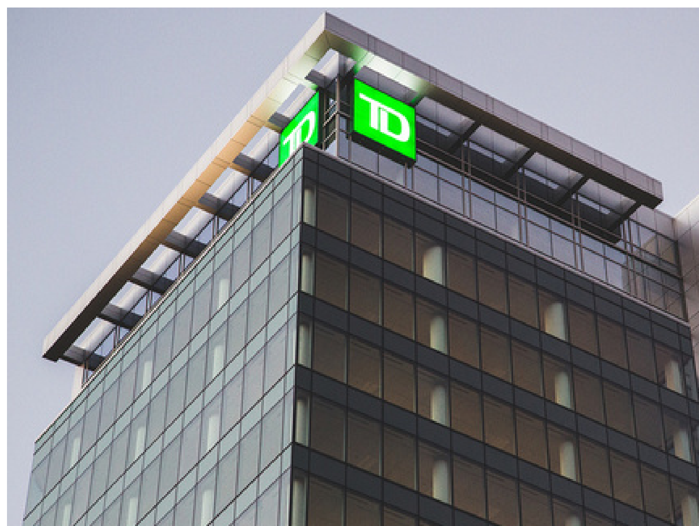
One important piece of advice that I wish I had known in school is the importance of keeping an open mind about your career path, especially as you transition from university. While it's natural to have a general direction in mind, such as banking or investment banking, it's essential not to limit yourself too strictly to a specific job or industry. Opportunities may arise in unexpected places, such as the finance department of a tech giant, and being flexible can lead to valuable experiences. Setting goals is crucial, but don't let tunnel vision prevent you from seizing unforeseen opportunities.

Another valuable insight that I have gained is the significance of networking. Success often depends on who you know, rather than just what you know. Actively engaging with people, attending events, and building professional relationships can open doors to new opportunities. It's not enough to excel academically or be involved in societies; networking is a critical component of career development. You can never shake hands and introduce yourself to too many people because that's just going to open doors.

Moreover, for those interested in fields like sales and trading, gaining firsthand experience is invaluable. It's challenging to fully understand the nuances of different roles within trading without exposure to them. Rotational programs offer an excellent opportunity to explore various facets of the industry and discover where your skills and interests align best. Embrace the chance to try different roles; it's through exploration that you'll find your niche and excel in your career journey. Within trading, different products have different workflows and different day-to-day operations, and each area has its own unique environment. If you can get into those rotational programs, just be open to trying everything, and you'll find your fit.

What is something that people misunderstand until they work in investment banking?

One common misconception is the perception of investment banking as a cut-throat environment where it's every person for themselves. While it's undoubtedly competitive, especially in international banks, my experience in a Canadian bank has shown a different reality. Contrary to popular belief, it's not solely about stepping over others to climb the ladder; rather, it's a collective pursuit of success. The environment is filled with hardworking individuals striving to excel. When we refer to investment banking, we're encompassing global markets, and within this realm, cooperation and collaboration are valued alongside ambition. Understanding this dynamic is key to navigating the industry effectively.



If you were not working in sales and trading, where would you want to work and why?

If I wasn’t working in sales and trading, I'd likely pursue a career in journalism, specifically as a foreign correspondent reporting from conflict zones. I've always been deeply fascinated by foreign policy and global affairs. I think there's something inspirational and daring about foreign correspondants who go into places of conflict and tell the truth about the stories going on there. I'm drawn to the idea of shedding light on untold stories and peeling back the layers of complex geopolitical issues.

What is one opinion that you hold that most people disagree with?

In this industry, and perhaps in many others, there's a prevailing emphasis on hyper-specialization early in one's career—becoming a master in a narrow field. Whereas I feel like you should be bouncing around more early in your career, trying new things, accepting new challenges, and not being pigeonholed early. Rather than pigeonholing oneself into a single area of expertise, I advocate for exploring new challenges and gaining varied perspectives. While some argue that early specialization leads to mastery, I think that versatility and a breadth of experiences foster a more well-rounded professional. There's a lot of bias towards settling into a niche early on, but I don't necessarily agree with it.

What was your favorite memory from your time at Dalhousie?

From an educational standpoint, participating in the CFA equity research competition stands out as a memorable experience for me. It was my introduction to this world, and I was immediately hooked. Additionally, competing in the Rotman trading competition in Toronto was another highlight. Both events provided a competitive, team-based environment that left a lasting impression on me. Moreover, these experiences facilitated invaluable networking opportunities, allowing me to connect with peers and industry professionals. Overall, they remain my fondest educational memories from my time at Dalhousie.

What was your experience transitioning from North America to Europe?

My journey from North America to Europe began with a move from New York to London, followed by settling in Dublin. Despite the unique challenges posed by COVID shortly after our arrival, transitioning to a new continent was an exciting prospect. While there were inevitable hurdles to overcome, the thrill of exploring a new culture and continent overshadowed any difficulties. Notably, I didn't encounter a language barrier, which simplified the transition process compared to relocating to a country with a different language.

From a professional perspective, adapting to the European market presented its own set of challenges. While TD's reputation preceded it in North America, establishing credibility with clients in Europe required extra effort. However, this challenge was rewarding, as it pushed me to develop stronger relationships and hone my skills as a salesperson. Managing clients across diverse European regions also demanded flexibility and cultural sensitivity, unlike the relatively homogenous North American market. Despite the initial adjustments, the transition ultimately enriched my professional growth and broadened my perspective on global markets.

Anything else to add?

I'd like to add that since I left Dal 15 years ago, the reputation of Dalhousie in capital markets has grown significantly, thanks to the strong network and support among alumni and current students. Back when I started, it was rare to see Atlantic Canadian candidates in rotational programs at big banks, as they usually favored candidates from other universities. However, things have changed drastically. Now, every year, I notice Dal students joining programs like TD's, which speaks volumes about our community's dedication and mutual support. We've worked hard to change perceptions, and it's paying off. I still hear from Dal grads regularly, and that's exactly what we want—to continue building on the reputation of our world-class school and program. The progress we've made is a result of the tireless efforts of everyone involved in programs like DALIS. Let's keep up the great work.

Student Spotlight

Engagement Rep

Aadhith Kumaresan

Bachelor of Management
Data & Information
Candidate 2025
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Can you tell us a bit about yourself?

I'm in my second year at Dalhousie University, pursuing a management degree with a focus on Data and Information, and complementing it with a minor in Computer Science and a certificate in Quantitative Finance. I'm from a beautiful city in India called Chennai, where I was a national level cyclist. I work as a teaching assistant at the Dalhousie Faculty of Computer Science and manage the Dal/Kings Bike Center.

I've been actively engaged with DALIS for over three semesters, contributing to the society as an Engagement Rep and helping develop the FCT portfolio.

As a computer science student, what drew you to DALIS?

As an international student in Canada, navigating through a new educational landscape and culture, my journey to exploring various societies and interests led me to the Bloomberg lab during the winter of 2022. The vibrant atmosphere and the buzz were unlike anything I had encountered before, igniting a true sense of excitement within me.

This blend of technology and commerce drew me to DALIS. It was here, surrounded by like-minded students and under the guidance of seasoned professionals, that my fascination turned into a passion. DALIS provided not just a platform for learning but also a community where my background as a computer science student could merge seamlessly with my enthusiasm for capital markets. This unique combination, I believe, forms the core of my future aspirations in finance, which started in my high school days when I helped my coach set up a trading account.

What do you most enjoy about DALIS?

My journey with DALIS has been transformative, blending practical skill-building with the thrill of competition. Through consistent engagement and collaboration with my peers, I gradually acquired the skills necessary to pitch and execute a trade which returned 25%. Further enriching my DALIS journey was the stock pitch competition, where our collective efforts were recognized with a third-place achievement.

So, to sum it up, my greatest enjoyment from DALIS comes from it being a space for gaining knowledge while being surrounded by amazing and intelligent people to explore the field of finance.

What sector are you most interested in?

I am deeply interested in the quantitative side of equity capital markets, where finance is combined with advanced quantitative methods. This field offers a dynamic mix of technical analysis, risk management, and fundraising, ideal for someone with a passion for technology-based finance. The expanding tech sector within ECM also presents valuable opportunities for investment and innovation, affirming my decision to focus my career in this area.

How does your major leverage you in the industry?

With Algo Trading dominating almost 60-75% of the overall trading, software creation involves strategy formulation with Python libraries, back testing with tools like QuantLib, and deployment using AWS and Docker, following industry standards set by firms like Citadel Securities.

This rigorous process complements my academic background in Data and Information Studies and Computer Science, which lays the groundwork for understanding financial market analytics. Specializing in quantitative finance has equipped me with essential theories and practical skills, positioning me well within an industry increasingly focused on technological solutions and big data. Through my education, I am prepared to make substantial contributions to the field of algorithmic trading, driving innovation and shaping market strategies for the future.

What are your career goals?

My career aspirations are situated at the crossroads of technology and finance. I aim to either become a trader or drive innovation in fintech as a developer. This combination of disciplines equips me for the dynamic challenges of the financial world and aligns with my long-term goal of contributing to the development of sustainable energy and health solutions in emerging markets.

What is a piece of advice you would give to non-commerce students interested in finance?

To non-commerce students keen on finance, know that your unique background is an asset. Initially, I feared my informal finance education would lead to exclusion, but I discovered that capital markets and societies like DALIS are very welcoming. Role models such as Rick Nason and Simon Carling have carved out successful careers in capital markets without conventional finance undergraduate degrees, illustrating the value of diverse experiences. They prove that passion and dedication can bridge the gap left by formal education. I urge you to seize every opportunity for learning and networking. As I continue my education, I remain committed to growing as a professional in the capital markets, taking advantage of my unique skill set.

Power Play:

How the 2024 Election Will Shape the Business Landscape

Will Kearns, Senior Analyst - Commodities
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As I try to make sense of the current market environment, it has become clear that the notoriety of fiscal spending and stimulus no longer holds the same potency it has in earlier western governments. Regarding the outcome of the 2024 United States Presidential election, voters will head to the polls to decide which government can best allocate public spending and resources to the most prominent issues.

Recently, areas of trouble have arisen from macroeconomic roots, including the future of the United States federal debt, foreign and domestic spending, international priorities, and infrastructure requirements for a carbon-neutral country by 2050. In addressing these issues, changes to government regulation and spending will be necessary to fight high inflation and allow the forces of supply and demand to determine if the clean energy transition is attainable.

Using a supply-demand analogy, the rollout of clean energy is attainable given a demand structure that is highly reliant on the clean energy transition being affordable, practical, and easily integrated. As a result, changing the current allocation of funding across the public and private sectors is needed so that the goals set forth to address climate change can be attainable.

To expand on my reasoning for why this election will influence markets more than past elections in the United States; Obama election 2012 "Healthcare stocks have reached an 11-year high" (By the Numbers, Kristen Scholer), looking to the price chart of Johnson & Johnson my analysis concludes that after Obama came into power many stable healthcare companies developed into strong growth companies. Now why was this? My interpretation is due to a change in government investment, the Obama administration held high regard for a social safety net in addition to affordable healthcare.

Targeting affordable healthcare Obama drove growth in the private sector, to reduce monopolies and incentivize low-cost health-related goods and services. Obamacare aimed to deliver wider access to health insurance, and more money in the pockets of Americans for prescription drugs and general health supplies. Segmenting JNJ revenues, 55% of revenue came from pharmaceutical sales at the time.

The conclusion drawn here is now you have a consumer who no longer bears the same cost they once did, making them able to buy the prescriptions they once couldn't. In fact, at this time 37% of people would not fill a prescription due to the cost. Now as Obama was set to take office JNJ stock rallied under the impression individuals would now be more inclined to fill prescriptions and seek help for an ailment they once could not afford to fix.

Reality of the Clean Energy Transition

The reason I bring the clean energy transition to focus is due to the reasonable ease of integration given an incentivized private sector. Obama understood Healthcare companies such as Johnson & Johnson needed substantial amounts of capital in exchange for the development of low-cost health products and services.

Shifting focus to 2021, Approaching the Biden administration's inauguration in January of 2021 the lead-up to the election posed an enticing opportunity to invest in small-cap clean energy firms. As the Biden campaign heated many clean energy stocks rallied under the expectation that the shift to a "cleaner energy grid" was now foreseeable given a willing and able governing body. A clear support by Biden's campaign for alternatives to potent GHG-emitting fuels communicated the next 4 years would be the beginning of the modern power grid expansion. The result was a defiant bull run within clean energy stocks, exacerbated by Biden's "Announce[ment] of [a] $2 trillion climate plan" (The New York Times, Glueck and Friedman).

Integrating Clean Energy

Fundamentally, the United States is a mixed economy, in terms of government intervention and money supply, the government is highly involved. In keeping a mixed economy surely, the hands-on approach ought to be reduced in other areas of the market, to ensure a balancing of both capitalist and socialist economic ideals. So far, I have brought forth a comparison on the rollout of both Obamacare and clean energy mandates including vehicles and energy production. The key difference is that Obamacare used basic economic principles that consumers make informed rational decisions when making meaningful changes to consumption, in this case switching from gasoline to electric vehicles.

It becomes clear, that the Biden administration differs from Obama's economic analysis in deciding if the market is both willing and able to determine an agreeable market equilibrium. I will provide some questions to ask yourself; is the consumer ready to adopt clean energy vehicles in 2024? Are they affordable? Can it be produced in an efficient timeline? Can we meet the resource needs of clean energy vehicles? Toyota Motor Company crunched some numbers and found the same number of critical materials needed for one electric vehicle could make 6 plug-in hybrid vehicles and 90 non-plug-in hybrids. In addition, "the overall carbon reduction of those 90 hybrids over their lifetime is 37 times [more than] a single battery electric vehicle" (Energyminute, Spencer Hay).

Final Remarks

Looking to the next year I argue many of the same issues will arise from the 2024 Presidential election, the stakes are crucial in determining how we will meet our GHG emission targets. As mentioned previously, are we ready? Is there a relatively low-cost solution? Ease of implementation, which makes sense for the average consumer? Again, comparing the rollout of Obamacare and Biden's clean energy agenda, Obamacare used a consumer demand for low-cost healthcare, to incentivize the private sector to produce low-cost goods and services.

On the other hand, the Biden administration has provided a mere solution to a consumer who is overwhelmingly willing to change their consumption behaviors. At the same time the current administration has spent insatiable amounts of taxpayer dollars with modest improvement in the consistent supply of clean energy for battery-powered vehicles.

Dollar Dynamics:

The Impact of a Weaker CAD/USD in our economy.

Kyle Stammers, Senior Analyst - Fixed Income & Macro Strategy
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The Canadian dollar (CAD) or 'Loonie', has slumped over the past 13 years and now hovers around $0.74 to one American dollar (USD) or greenback. In just 5 years, CAD recovered from a low of US$0.61 in 2002 to a high of US$1.10 in 2007 which demonstrates both its volatility and potential value. We often hear about the exchange rate between CAD/USD or USD/CAD on the news, but why has the dollar slumped in value, and what are the ramifications of a depreciating Canadian dollar?

To answer that question, we must start by understanding why the Canadian dollar has lost value relative to the greenback. To start, when a currency loses value, it is always concerning another medium of exchange. In this case, USD is the best comparison and the most popular as it is the world's reserve currency and the United States is Canada's number one trading partner. From an economic standpoint, we can interpret the declining value of CAD as an overall decrease in demand for the Canadian dollar. When the money supply increases, the inherent value of the currency will fall. We may be able to correlate the Bank of Canada issuing more money during the recent pandemic to the currency's declining value, however many other factors impact the exchange of rate of CAD/USD, such as confidence in the Canadian economy from foreign investors, commodity prices, as well as economic productivity.

Now that we've covered why the loonie is depreciating, it's important to understand the profound impact a weaker loonie has, and who it impacts. CAD being weaker relative to USD is not necessarily bad for the Canadian economy. Canada is a strongly export-oriented economy, meaning a weaker Canadian dollar is beneficial for certain industries. A weaker loonie is beneficial for Canadian manufacturing because foreign markets gain more purchasing power. Another sector of the economy that benefits is tourism. The higher cost of travel that Canadians may incur when going south to a popular destination like the United States makes domestic tourism more attractive. On the flip side, Americans get the longer end of the stick as their greenbacks go further in Canada. Canadian oil and gas companies are positioned advantageously for a weaker dollar. Most of their costs come in the form of a loonie, while their revenue is sold in greenbacks, allowing them to benefit from the discrepancy in the value of CAD versus USD. It's worth highlighting that a Canadian post-secondary degree becomes a more attractive to foreign students. This is because of its lower costs compared to attending college or university in the United States. The reality is that many industries experience significant advantages when the Canadian dollar weakens and depreciates.

On the other hand, Canadian businesses that import a lot of goods, or have significant expenses in USD and revenue in CAD, are hurt the most by a weak loonie. A great example of this is a Canadian hockey team in the NHL, where all salaries are paid in USD. Consider the most valuable team in the NHL, the Toronto Maple Leafs, they become even more disadvantaged when you consider that their main source of revenue is in Canadian dollars, but their largest expenses are in American dollars, not to mention their teams playoff track record... A weaker dollar increases daily financial challenges for households as imported goods become more expensive. Canadian produced goods, such as the Dodge Charger that used to be produced in Brampton, Ontario, and dependent on imported components, could experience an additional increase in price. Due to Canada's geography and climate, some products have to be imported. Importing essential groceries like fruits and vegetables becomes more expensive when the loonie is weak, higher prices of these essential foods are not solely due to the cost of importation, but primarily stem from the fact that international produce is typically priced in USD.

We've covered why the loonie has lost value and who it impacts, but it's important to touch on what may happen going forward, the impacts that may be felt, and to note that the price of money is the central banks interest rate. To recap, one of the key reasons why the loonie is losing value compared to the greenback is because of the United States central bank's interest rate and attractive economy. The Federal Reserve currently has a higher interest rate than the Bank of Canada. This encourages global investors to make deposits in American financial institutions instead of Canadian ones, effectively decreasing the demand for the Canadian dollar. The United States economy has been defying post-pandemic economic expectations, which boosts its attractiveness to foreign investors. If the Federal Reserve were to achieve their goal of a soft landing, they likely won't aggressively cut rates because that could lead to inflation, as it would encourage borrowing and investing that if improperly timed, could spur excessive growth and subsequent inflation.

Canada, on the other hand, is in a different economic situation as real GDP per capita has grown only +0.4% annually, paling in comparison to the advanced economy average of +1.4%, resulting in Canada being less attractive to foreign investors. This could potentially create a dilemma for the Bank of Canada as a central banks would typically consider cutting rates more aggressively in an attempt to stimulate economic growth, but if the Bank of Canada were to do so, Canada could potentially risk further depreciation of the dollar and inflation. Alternatively, the Bank of Canada may try to keep rates in line with the United States, but this strategy may risk further economic decline and other economic challanges due to the impact higher rates have on investment and production domestically, as well as inflation.

The takeaway is that there's no simple solution to this dilemma and that Canada might need to shift towards building a more productive economy to give the loonie more intrinsic value, instead of trying to find ways to cope with a weaker Canadian dollar.

The value of the loonie is something that should be taken seriously, it has a profound impact on Canadians' lives and the livelihood of business in Canada.The depreciating loonie, a result of various factors, highlights the need to prioritize productivity for competitiveness with the United States and on a global stage. Staying informed and considering foreign investments may prove to ve advantageous for both Canadian households and businesses amid the uncertain future value of the Canadian dollar and economy.

Balancing Ambition and Reality:

The Saudi Arabian Spending Strategy and Challenges Ahead

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In April of 2016, Saudi Arabia unveiled Vision 2030, an ambitious economic development plan aimed at creating a vibrant society, fostering a thriving economy, and enhancing the Kingdom's global influence. This plan, led by Crown Prince Mohammed bin Salman has involved unprecedented levels of spending that has garnered the attention of worldwide media since its inception. Some of the plans most expensive elements, often referred to as "gigaprojects" include Neom, a $500 billion city-state that involves the construction of two 110-mile-long buildings taller than the Empire State Building and New Murabba, a Riyadh development that features a 400-metre-high cube named Mukaab and a yacht resort on the Red Sea.

Economically, these projects are designed to help diversify the country's economy away from crude oil and transform it into a global leader in tourism. The desire to diversify away from oil comes at a time when the consumption of fossil fuels has never been more heavily scrutinized. Vision 2030 is thus reminiscent of the efforts of other global leaders who are increasingly focused on transitioning towards a future powered by renewable energy sources.

The Public Investment Fund (PIF) plays a vital role in financing Saudi Arabia's economic transition. With over USD 700 billion of total estimated assets, the PIF is among the largest sovereign wealth funds in the world. Last month, the PIF announced that current cash levels had fallen by approximately 75% to $15 billion, the lowest since the fund began reporting data. This development has raised questions regarding the government's ability to continue funding its expansive ambitions. In fact, in order to meet the targets, set out by the Saudi government it has been estimated that they will need to spend upwards of $175 billion on an annual basis between 2025 and 2028. This year, Saudi Arabia is projected to run a budget deficit of $21 billion, about 2% of the country's gross domestic product. Beyond that however, the kingdom expects to run small deficits through 2026. All of this goes to say that Saudi Arabia is experiencing a significant strain on its cash reserves.

Tim Callen, a visiting fellow at the Arab Gulf States Institute has gone on the record to say that Saudi Arabia will need to take on additional risk to meet the funding requirements of these projects. This can be done in one of two ways; either by adding debt to their balance sheet or by lowering reserves that keep the Saudi riyal pegged to the United States dollar.

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Historically, the Saudi government has been hesitant to issue new debt. However, because of the size and scale of their spending they have been left with few other options. In January of this year, Saudi Arabia announced a $12 billion bond offering. Additionally, they announced plans to borrow roughly $9 billion from international debt markets in 2024. Despite the recent increase in debt, the country is not considered at risk of an imminent financial crisis. This year Saudi Arabia's debt is estimated to reach 26% of its gross domestic product, a relatively conservative and budget conscious number. Germany for example has a debt-to-GDP ratio of more than 52%.

Beyond the issuance of new debt, Riyadh has made clear their intention to sell 1% of Saudi Aramco, the country's state oil company. Saudi Aramco first went public in 2019, raising a record $25.6 billion in their initial public offering. Much of the funds generated from Saudi Aramco's IPO went directly to the PIF who currently owns 8% of the company. In terms of the effect the sale of this equity will have, it is likely the deal could bring in as much as $20 billion. It is important to note however, that the sale of Saudi Aramco equity has a list of potential drawbacks. Namely, it would decrease one of the largest sources of revenue generated by the kingdom, dividends paid out to Saudi Aramco shareholders.

Another thing to consider is the rate at which Aramco will be able to continue producing oil into the future. Earlier this month Aramco issued a statement referencing the fact that they are currently losing six million barrels per day in production each year because of the natural depletion of their oil fields. This speaks to the fact that their oil fields have hit peak production and are currently experiencing an inevitable decline. It could therefore be argued that now is a suitable time to sell shares in the state oil company given the grim outlook on future growth it currently faces.

In 2023, the PIF spent $32 billion across 49 acquisitions and other deals, making it the world's most active sovereign wealth fund. Two things are happening here; first spending has dramatically increased, and second oil revenues have begun to slow down. It therefore makes sense that the Saudi government would like outside investment to help fund their massive amounts of spending. However, concerns about earlier projects that did not come to fruition, coupled with the 2018 killing of Jamal Khashoggi, have limited the impact of direct foreign investments in these newer projects.

As we move closer towards 2030, the situation in Saudi Arabia will be an increasingly interesting story to follow. While spending is expected to remain at elevated levels, questions surrounding the financing of these projects are sure to persist until their completion. Essential to ensuring the timely and successful diversification of the Saudi Arabian economy will be the ability for non-oil related projects to generate significant returns. Without this sort of internally sourced revenue, Saudi Arabia will need to expose themselves to the added risk associated with increased debt, sell off more equity in Saudi Aramco or be forced to scale back on some of their ambitious targets.

In conclusion, completing Vision 2030 as outlined is of the utmost importance to Saudi Arabia. If they do not achieve these goals, their reputation among the international investment community will be further tarnished, making it even more difficult than it is now to raise capital abroad. However, the potential upside to completing this goal is almost unlimited; global capital inflows could increase, helping to further grow their economy into 2050 and beyond.

As Fringe Data Sets Move Front and Center

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Alternative Data

Behind the scenes, investors jobs have been getting harder; after years of refining and disseminating fundamental strategies, we have slowly but surely been whittling away at whatever marginal advantage can be gained from traditional channels. The floor has been continually lifted thanks to the new augmented capabilities of a world with too much information on its hands, and in this new world fundamental analysis is still important – but it is the baseline. Thankfully for those investors or funds with an enterprising spirit, there is a new frontier.

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Alternative data is a blanket term, and can broadly be classified under the financial services umbrella as anything that is not directly put out by companies or institutions like reports, filings, statements, price data, etc. This means it could be anything from a social media post that expresses an opinion, all the way to satellite imagery, aggregated anonymized email receipts, and natural language processors that detects and quantifies the stress in chief executive's voice on an earnings call. Leveraging alt data sets has allowed savvy operators to generate alpha in the past, but just as in traditional channels, the goal posts are perpetually moving.

Mind-blowing as it may be, alternative asset managers like hedge funds, along with PE and VC firms have done the most to move the needle in the alternative data industry - if you can believe it - as the largest single source of new demand in recent years; according to an annual survey put together by Lowenstein Sandler LLP, in 2023, 62% of the 109 funds surveyed reported that they use alternative data in some capacity – more than double the year before. Funnily enough, Deloitte has also recognized this trend and estimates that alternative data will be bigger than traditional financial services data by 2029 (in terms of the revenue it generates). This aligns with other popular estimates that the industry will grow at a 40-to-50% CAGR through the end of the decade. If you assume the average, this would translate to annual sales of nearly $67B (USD) for the industry based on $7.2B in revenues last year. This growth potential has of course translated to an influx of new supply in the market, as Deloitte also noted a 36% increase in the amount of data sets offered and a 30% increase in the number of providers last year.

Feels Like Cheating

Sergey Brin, after co-founding Google and seeing the preponderance of data his young company was raking in, advocated for Google to start its own hedge fund. Fear of the optics and associated negative press eventually stopped the idea before it could get off the ground, but Brin does maintain a notoriously tight-lipped family office that manages his $100B+ fortune.

Funds do generally keep their cards pretty close to their chest when it comes to novel alpha generations strategies, but data providers can't help but gush about how popular their data is. Some of the popular sets currently available from a multitude of providers are:

- Credit & Debit Transactions
- Web Scraped Data
- Geolocation of Ships and Planes
- IoT Devices
- Weather & Climate Data
- Biometric Data
- Cargo Manifests
- Executive Movements
- And More

And if those don't get your gears turning, there is a range of bespoke solutions like anonymized email receipts – where built-in protocols scrape your email and tabulate your spending habits. Or when insurance companies sell client policy data so funds can know which car models are selling better than others and what demographics are buying them. Alternative data companies would then aggregate and transform the data into a neat and digestible form - when plotted on a time series, the end user could very-well be able to infer an online retailer or auto companies' quarterly results before their own CFO.

In the same vein, another common example is satellite imagery. Sam Walton used to stand outside his stores and count the cars in his parking lots to get a sense of how well Walmart was growing. These days, we do the same thing, only from space. Another place where an eye in the sky can come in handy is when dealing with crude and distillate inventories. Meaningful insights can be gathered from simply examining the shadows cast by commercial storage tanks. This is thanks to the floating lids that these tanks must manage vapour space – by looking at the shadow cast by the rim, analysts can easily tell how full it is. Similar techniques can of course also be applied to different resources.

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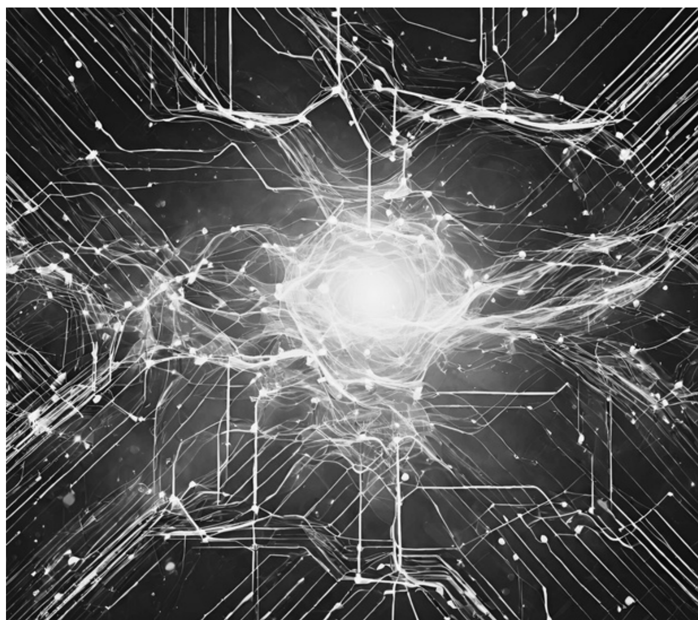
Feels Like Cheating

Most firms have a solid handle on alternative data by now, whether they admit it or not. Now, the real advantage lies in an analyst's skills to create a mosaic out of multiple data sets with the hopes of improving signal strength and consequently gaining a more resilient edge. Soon – if not already – it will be a fact of life that some quant at Renaissance Technologies or Two Sigma has modeled the McDouble you will eat in three weeks into his macro projections for Honduras because that's where your local McDonalds sources its beef.

Going forward, firms will need to adopt alternative data to drive alpha, or risk losing out on deals and opportunity's to more adroit competition. Not to mention the new age of regulatory scrutiny were in for as lawmakers play catch-up. This will also come with a consolidation of jobs in the hands of those capable enough to either discovering new data sets or downstream users who can manipulate it and map it to their needs. Then lastly, for those of you who thought you could read an article today that didn't mention AI – I'm sorry to let you down, but it's already being used for things like the cleaning and recognizing useful data, natural language processing, and even sending false signals to manipulate closely followed trading sets like social media sentiment. Only time will tell how this shakes out, but in the not-so-distant future, institutions that have not explored alternative data sets are doing their shareholders a disservice.



The Regional Bank Roller-Coaster

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It seems like regional banks can't catch a break, first the failures of Silicon Valley Bank, Signature Bank, and First Horizon, now New York Community Bank just slashed dividends to try and meet capital requirements on bad commercial real estate loans, putting its future into question and risking another bank run. The industry has been through a tough time during the Fed's aggressive rate hiking cycle to tame inflation, and continues to feel major pressure, this article dives into their recent challenges and explores the shifting landscape US regionals will enter in the near future.

First, let's look at the sector as a whole to provide some context. What classifies as a regional bank? Banks are classified based on the size of their assets, a bank with between $10-$100 billion in assets is considered a regional bank. What is their business model? Regionals operate like the retail division of any large bank, they offer loans, deposits, credit cards, and investments, however, they don't offer corporate or investment banking services. Why are they so important to the US economy? Because of whom they serve, regionals cater to borrowers that large banks won't, low-income households, small businesses, and start-ups that drive innovation and growth in communities.

A Year of Trouble

When the Federal Reserve first started hiking rates in March of 2022, banks had a rosy outlook for their Net Interest (NI) Margins as the economy came out of a near-zero interest rate period. However, what they didn't anticipate was the aggressiveness of the coming hiking cycle, and the effects it had on their customers and portfolios. Ever since the 11 hikes of over 500 bps, regional banks have been suffering, first came the massive unrealized losses that drove three bank runs, then huge provisions on commercial real estate loans, and finally credit downgrades hit troubled lenders, further eating away at sentiment.

Unrealized Losses:

This was a phenomenon unique to regionals due to their lack of diversification and risk management. When rates were low and the banks needed to see yields on cash, they bought up large amounts of long-term US treasuries. This strategy was risk-free and predictable until the Fed hiking cycle started and their held-to-maturity securities shot down in value. According to research, the median fair value of twenty-eight regional banks' assets was 41-41% below book value. The reason this caused so much havoc and led to multiple bank runs is it reflects poorly on the bank's health and ability to meet short-term obligations. The forthcoming bank runs are estimated to have cost the FDIC close to $17 Billion and shattered faith in the sector, seeing large deposit flights to the large money center banks link JP Morgan.

Commercial Real Estate Woes:

Bloomberg found that twenty-two regional banks have swelled their commercial real estate loan portfolio to triple their capital available. Why is this a problem? Ever since the COVID-19 pandemic shifted work culture online, global demand for office space has never recovered. This massive drawdown in demand coupled with high rates has exacerbated the pain for owners. As a result, a large portion of the loan book has been deemed at risk of not being collectible, requiring large sums of reserves to be set aside as provision, souring public sentiment, and lowering share prices, with extreme cases like New York Community Bank losing nearly half its value after reporting earnings.

Credit Downgrades:

In the wake of the SVB failure, Moody's has cut the credit ratings of ten regional banks, sighting nervous investors and depositors, high interest rates, and the deterioration of commercial real estate. What does this mean for them? At a time when banks are struggling to meet capital requirements, it has become even more expensive to raise capital and has increased scrutiny from investors, depositors, and regulators.

Outlook

The future for regional banks looks extremely uncertain, amid rocky economic forecasts, constantly shifting interest rate expectations, and new regulatory requirements.

Interest Rate Direction and the Macro-Economy:

Interest rate cuts will be a double-edged sword for the sector. The positive aspect, even as NI margins recover with stable rates, cuts will bring down the cost of deposits and incentivize lending. Another potential benefit comes if base rates stay higher after a series of cuts, i.e., we will not return to the near-zero rates environment that a lot of assets were priced at during COVID-19, setting the stage for a lot of incremental revenue once rates normalize and the assets are repriced.

The negative side, however, comes if the cuts are a result of a recession. This raises concern for regional banks given their customer base and loan portfolio, since they mostly lend to low-income households, small businesses, start-ups, and commercial real estate owners, who all face severe challenges during economic slowdowns.

Regulatory Tightening:

There are big new regulatory and disclosure requirements coming to the sector following the year of unfortunate events. They will be hit with increased liquidity requirements, that will force them to maintain a full liquidity coverage ratio, to be able to cover all deposit outflows over a specific period, typically 30 days. Secondly, they will face increased debt requirements, needing to hold long-term debt to move funding dependency away from deposits, which are volatile during economic cycles, stabilizing their funding structure. Lastly, there are a series of new disclosure requirements, the most impactful being in-depth performance disclosure of their loan portfolio and unrealized losses. Even though these measures will drive up the bottom line, they will drastically improve risk management and help stabilize the sector.

To conclude, the US regional banks have been through a roller coaster year, filled with bank runs, defaults, and bailouts. The future does look bright however, as they might be susceptible to economic cycles in the short term, but in the long term, they will emerge from this crisis-ridden period stronger, smarter, and more efficient.

Water Wealth:

Investing in the Liquid Asset?

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71% of the Earth's surface is covered by water. Of that 71%, only three percent is composed of fresh water, and of that fresh water, less than one percent is potable. 40% of the world's population is affected by water scarcity issues: one-in-ten people do not have access to clean water worldwide; and around 70% of all deaths associated with natural disasters are related to water scarcity. It suffices to say that access to clean water is a global issue. As the global population continues to grow, contamination increases, and planetary temperatures rise, this issue will only intensify. This looming future of anticipated hardship has sparked an increased interest in water management, conservation, and investment amongst the business community.

A 2015 film called The Big Short , features a notable Wall Street hedge fund manager, Michael Burry, who predicted and profited massively from the 2008 financial crisis. Following that dark period, Burry decided to close his hedge fund and focus solely on his own trading. As mentioned in the closing credits of the film, his new center of attention would be water.

What does it mean to invest in water? Although its value is clear, and it is relatively scarce, it is not a listed commodity, it flows from place to place, and issues of jurisdiction can be complicated. For many, the obvious way to invest in water is through acquiring control of supply, often through implementing water management and storage strategies – a viable option.

Consider the Southwestern United States: a vast region largely composed of arid land, which provides few sources of clean water. The Colorado River, which starts in Colorado and crosses through Utah, parts of Nevada, California, Arizona, then crosses into Mexico, serves as the primary water source for this region. It serves upwards of 40 million people and supports roughly 5.5 million acres of agricultural land. Managed through an extensive array of dams, aqueducts, and water basins, supply is diverted to different communities and agricultural lands, after which very little supply is left over, and sometimes, there are shortages.

By acquiring properties adjacent to abundant surface water sources like rivers or streams, landowners can leverage their riparian rights, which grant them access to water for agricultural, livestock, or domestic purposes. This allows them to either store water or sell their access rights or supply to communities or farmers facing water shortages during dry periods. Another set of rights, known as the "Appropriative Rights" which follow the doctrine of prior appropriation, are tradable contracts allowing the owner a certain allocation of water including that from underground water tables or aquifers, which too can be sold, as either contracts or actual supply, to farmers or municipalities in need.

Other investment opportunities lie in infrastructure related to the maintenance and management of water sources and supplies across the United States, including the Colorado River, as existing infrastructure ages and innovative technologies emerge.

Today, water pipes across the United States have reached an average age of 45 years, and an elevated rate of breakage across these pipes, specifically in the Midwest and Southeast, has been reported. Nearly 14% of daily household water usage is lost due to cracked or broken pipes. This poses an increasing burden as water supplies continue to diminish. The United States Environmental Protection Agency ("EPA") estimates that pipe replacement rates will reach a high of 16,000 to 20,000 miles of pipe per year by 2035, which is reported to be over four times higher than the current rate. In addition, there are still a significant quantity of lead pipes, some of which over 100 years old, which require replacement.

But, returning Dr. Michael Burry, he is focused on an alternative way of investing in water. Considering a moderate climate, the average person requires about five litres of water every day to survive. With the additional considerations of factors such as bathing and sanitation, housekeeping, and other miscellaneous uses, the average consumption per capita in the United States is between 380 and 700 liters of water per day. However, it is food that makes up most of the individual water consumption.

The agriculture and food industry uses upwards of 69 percent of the Earth's total fresh water supply. On average, individual water consumption via food and agriculture amounts to roughly 3,500 liters per day, which is more than 9.2 times the aforementioned direct daily usage. To put this into perspective, consider a cup of coffee. The average volume of one cup of coffee is equivalent to five fluid ounces, or 150 milliliters, which is a relatively small amount. But, when considering its lifecycle, including production, harvesting, transportation, and so on, studies have shown that it requires around 140 liters of water to produce a singular cup of coffee, and that is a small number in comparison with other consumables. For a few more extreme examples, an avocado requires around 272 litres of water to produce, and a kilogram of beef requires upwards of 15,415 liters of water.

Playing into the usual issues of supply and demand found in the water business, Michael Burry's angle is to maximize utility and profit by transporting water-heavy foods from a water rich area to one with limited access. He is interested in indirect water as a resource; the water "embedded" in food. His favourite crop to use as a vehicle in this context is almonds: they require an immense amount of water to produce, quantified at one gallon per almond. Furthermore, 80–90% of global almond production is set in California, which, as discussed, is an arid, drought-prone, geography. Like other tree-based crops, almonds are particularly vulnerable to disasters such as droughts. This susceptibility is exacerbated by their lengthy maturation period of three years before production begins. Michael Burry's investment thesis is very considerate of the future– as access to water continues to be limited (as it already is in California), the almond farms with onsite access to water will survive, while those dependent on limited and other sources could fail.

The growing interest and concern around the investment of water is beginning to paint a picture that emphasizes the absolute necessity to preserve the basic natural resources that we all depend on. Water, among other basic natural resources, will likely become the most valuable and sought after commodities in the coming decades, yet right now its value is not truly appreciated, nor is it completely priced in. According to research conducted by Truecost, more than half of the profits of the world's largest companies could be jeopardized if the price of water reflected its true value. This underscores the significance of water as a critical resource and the potential economic implications of undervaluing it. This indicates that Michael Burry's thesis, among many others interested in water investment, are only going to become more powerful and profitable as time goes on and climate patterns shift.

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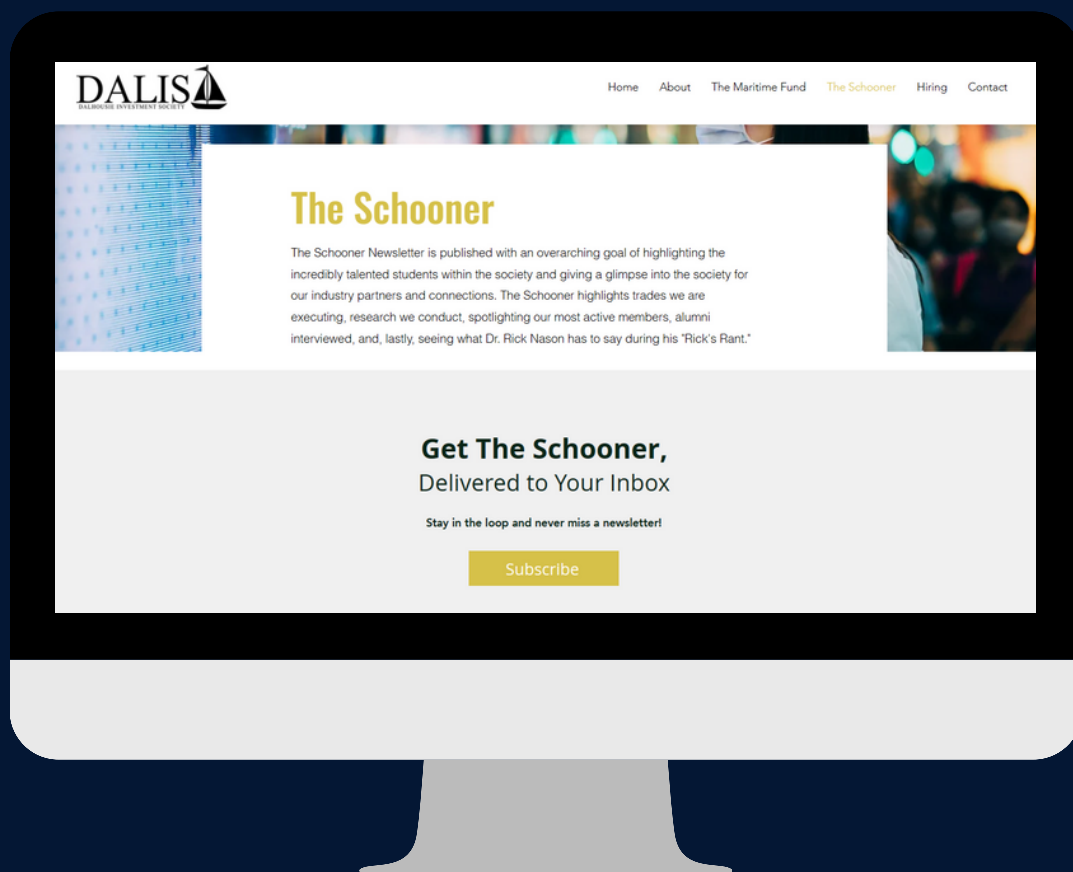

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