

# PALOS

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## Weekly Commentary

Issue No. 3 | JANUARY 16, 2023

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*By Charles Marleau CIM<sup>®</sup> and William Mitchell CIM<sup>®</sup>*

## Looking for Leadership? Follow the Chips!

Semiconductors (a.k.a. “chips”) are characterized as electronic components comprised of silicon and which possess properties of conductivity. Chips are found in thousands of consumer products we use daily (think cars, cell phones, flat screen televisions, home appliances and laptops). In addition to personal goods, chips are critically important to the advancement of medical equipment, aviation, manufacturing, telecommunications, research, and defence sectors: obviously, semiconductors play an extremely important role in the global economy.

There are three distinct segments of the chip industry: **chip design** companies are driven by a desire to innovate and profit from designing chips that are faster and smaller than their predecessors, companies that focus on the **manufacturing** of chips at fabrication plants or “fabs” and finally, the **equipment manufacturing** segment which is comprised of companies that design, manufacture, sell and service the necessary chip-making and chip-testing equipment to the “fabs”. In a sense, chip equipment manufacturers hold the most important role given the simple fact that without manufacturing equipment the fabs can’t make the chips required to produce a finished product.

The chip industry is highly cyclical. As a result, the ups and downs of share prices amongst publicly traded semiconductor companies can be volatile. This is attributable to a high sensitivity to the economic cycle; we saw this firsthand in 2022. After peaking in early January and using the **iShares Semiconductor ETF (SOXX)** as a benchmark, the chips as a group were down roughly 37% by year end; a significant underperformance compared to the broader market. Considering the growing concerns throughout 2022 that inflation and rising interest rates would impact growth companies, in hindsight this was not surprising.

Experienced investors understand that markets look forward not backward. Further understanding that technological innovation is not going away implies that demand for “faster, smaller and cheaper” equates to a perpetual demand for more and more chips. Thus, given time for recent softness to play itself out, demand will surely return and the current down cycle will eventually reverse its course. We know that as a “rule of thumb” the equipment makers are often leaders out of a downturn. With this knowledge in hand, we’ve decided to share our “technical observations” on the chip equipment companies that dominate the industry.

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The reference to our “technical observations” relates to the study of **technical analysis** which uses probability-based charting techniques to study historical prices, money flows, trends, momentum, and chart patterns to get a reliable “picture” of recent (i.e., historical) and future (i.e., probable) direction of market prices. We believe that using technical analysis in combination with fundamental analysis (i.e., the “financial numbers”) offers a thorough methodology for analysing the prospects for individual companies, different sectors and the economy.

For the purposes of this study, we chose four of the largest semiconductor equipment manufacturers: Netherlands-based **ASML Holdings (ASML:NYSE)** which is the largest with a market capitalization of \$US 265 billion, as well as three California-based companies: **Lam Research Corp. (LRCX:NYSE)** with a \$64B cap, **Applied Materials Inc. (AMAT:NYSE)** with a \$92B cap and **KLA Corp. (KLAC:NYSE)** with a \$60B cap. All are well established leaders in the industry. Without going into unnecessary detail, we will illustrate our point by providing the price changes in percentage terms since the beginning of the bear market last January and the associated lows established last October (*Source: Bloomberg*).

1. **ASML Holdings:** ASML reached an all-time high on September 15, 2021, following a roughly five-fold increase off the pandemic low in 2020. From its September peak to its recent low on October 24, 2022, ASML returned negative 57.4%. However, as of last Friday’s close, the stock has risen 74.0% from its October 14 low.
2. **Lam Research Corp.:** All-time high closing price of \$730.75 on January 14, 2022. Bear market low at \$314.95 (Oct. 14, 2022) for a peak to bottom decline of 56.8%. With a closing price of \$473.67 last Friday LRCX is higher by 50.4% from the October low.
3. **Applied Materials Inc.:** All-time high close of \$167.00 on January 14, 2022. Recent bear market low at \$74.41 (Oct. 17, 2022) for a decline of 55.4%. With closing price of \$109.97 last Friday AMAT is up 47.8% from the October low.
4. **KLA Corp.:** All-time high close of \$445.52 on January 14, 2022. Recent bear market low at \$263.22 (Oct. 17, 2022) for a peak to trough decline of 40.9%. With a closing price of \$109.97 last Friday AMAT is higher by 59.6% from the October low.

A bull market is widely defined as a 20% move higher from a “market bottom”. In our view, a generally positive technical structure, as well as sheer performance, indicates the chip equipment manufacturing sector is bucking the broader trend and that a sector bull market commenced last October. Of course, we never know exactly when a market “bottoms” until the indices confirm that the bear is in the rearview mirror. However, given the chip equipment group’s tendency to lead other sectors, we are encouraged that the worst may be behind us. As a cautionary note, are certainly not recommending an investment in any of these securities. While the outperformance of the sector is clear only time will tell if the “chips” are once again leading the way.

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Should you have any questions related to how your investments are managed it would be our pleasure to discuss these with you personally. Palos' portfolio managers are available to meet at your convenience, either in person, by telephone or through a virtual meeting using Microsoft Teams.

To schedule an appointment, please contact your Palos advisor or Caroline Vadboncoeur, Manager of Client Services at [cvadboncoeur@palos.ca](mailto:cvadboncoeur@palos.ca)

*Palos Wealth Management Inc. is registered as a portfolio manager with provincial regulators and with the Autorité des Marchés Financiers (AMF) in Quebec. In addition, Palos is registered as a derivatives portfolio manager and Exempt Market Dealer (EMD).*

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## Save for your future by contributing to a Registered Retirement Savings Plan (RRSP)

### RRSP Benefits:

- RRSP contributions are a good way to reduce your taxable income
- Your investments grow tax deferred while held in your RRSP
- When you retire you can use your RRSP to receive regular income
- A spousal RRSP can reduce your combined tax burden
- You can borrow from your RRSP to buy your first home or pay for your education

### RRSP Contribution Details:

- The **deadline** for making your 2022 RRSP contribution is March 1, 2023.
- Your **2022 RRSP contribution limit** is calculated as 18% of your 2022 earned income up to a maximum of \$29,210. The maximum will increase to \$30,780 in 2023.
- If you've already made your 2022 RRSP contribution, consider making your 2023 contribution in January 2023 to benefit from the power of tax-deferred growth.
- Unused contributions can be carried forward from a previous year. You can find your RRSP contribution information on your most recent CRA **Notice of Assessment**, or by calling the **CRA Tax Information Phone Service (TIPS)** at 1-800-267-6999.

The sooner you start contributing to an RRSP or TFSA, the more time you'll have to grow your money until it's time to retire. There's nothing like the power of tax-free compounding returns.

If you would like to open an RRSP account, contribute to an existing or Spousal RRSP, or if you have any questions about RRSPs, please contact your Palos Advisor.



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## Save for your future by contributing to a Tax Free Savings Account (TFSA)

### TFSA Benefits:

- TFSA investments grow tax free (Interest, capital gains and dividends are tax exempt)
- Withdrawals can be made whenever you wish and unlike an RRSP, they are tax-free
- TFSA contribution limits are not reduced following a withdrawal
- Withdrawals can be re-contributed in a subsequent calendar year(s)

### TFSA Contribution Details:

- The TFSA contribution limit for 2022 is \$6,000 and will increase to \$6,500 in 2023
- TFSA contribution limits are cumulative since TFSA's were introduced in 2009. If you were born after 1991, your lifetime contribution limit including 2023 is \$88,000
- Canadian residents 19 years of age and who have a Social Insurance Number are eligible to open a TFSA
- To determine your TFSA contribution limits, you can refer to your most recent CRA **Notice of Assessment**, or by calling the **CRA Tax Information Phone Service (TIPS)** at 1-800-267-6999

**TFSA's are an excellent way to save for your future**

**TFSA's can complement your taxable retirement income from a taxable account (RRSP, RRIF, LIRA)**

**The sooner you start contributing to TFSA, the more time you'll have to grow your money.**

**If you would like to make a TFSA contribution or open an TFSA account, please contact your Palos Advisor.**

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## Épargnez pour votre avenir en cotisant à un régime enregistré d'épargne-retraite (RÉER)

### Les avantages d'un RÉER:

- Les cotisations à un REER sont un bon moyen de réduire votre revenu imposable.
- Vos placements bénéficient d'un report d'impôt lorsqu'ils sont détenus dans votre RÉER.
- Lorsque vous prenez votre retraite, vous pouvez utiliser votre RÉER pour recevoir un revenu régulier.
- Un RÉER de conjoint peut réduire votre charge fiscale combinée.
- Vous pouvez emprunter de votre RÉER afin d'acheter votre première résidence ou pour financer des études.

### Les choses à savoir :

- **La date limite** de cotisation au RÉER pour 2022 est le 1er mars 2023.
- Votre **plafond de cotisation au RÉER pour 2022** est calculé à partir de 18% de vos revenus gagnés en 2022, jusqu'à un maximum de 29 210 \$. Ce maximum sera augmenté à 30 780 \$ en 2023.
- Si vous avez déjà cotisé à votre RÉER pour 2022, envisagez d'effectuer votre cotisation de 2023 en janvier 2023 afin de bénéficier dès maintenant de l'effet différé des impôts.
- Les cotisations non-utilisées peuvent être reportées d'une année précédente. Vous pouvez vous renseigner sur vos cotisations à un RÉER en consultant votre **avis de cotisation le plus récent de l'ARC** ou en appelant **le Système électronique de renseignements par téléphone (SERT)** au 1-800-267-6999.

**Le plus tôt vous commencerez à cotiser à un RÉER ou à un CELI, le plus longtemps vous disposerez pour faire fructifier votre argent jusqu'au moment de la retraite. Rien ne vaut la puissance des rendements composés non imposables.**

**Si vous souhaitez ouvrir un compte RÉER, contribuer à un RÉER existant ou à un RÉER de conjoint, ou si vous avez des questions sur les RÉER, veuillez communiquer avec votre conseiller Palos.**

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## Épargnez pour votre avenir en cotisant à un compte d'épargne libre d'impôt (CELI)

### Les avantages du CELI:

- Faire fructifier votre épargne à l'abri de l'impôt (les intérêts, les gains en capital et les dividendes seront non taxables)
- Vous pouvez effectuer des retraits quand vous le désirez et contrairement à un REER, ils ne seront pas taxables.
- Vos limites de contribution à un CELI ne seront pas réduites à la suite d'un retrait de celui-ci.
- Vos retraits peuvent être de nouveau cotiser dans les années subséquentes.

### Les choses à savoir :

- Le montant limite de cotisation à un CELI pour 2023 est de \$6,500
- Depuis leur introduction en 2009, les limites de contributions à un CELI sont cumulatives. Si vous êtes nés après 1991, votre limite de contribution à vie est de \$88,000 (2023 compris) .
- Si vous êtes un résident canadien de plus de 19 ans et que vous détenez un N.A.S. Vous êtes alors éligible à un CELI.
- Si vous voulez connaître vos limites de contribution, vous trouverez toutes les informations pertinentes sur votre plus récent **avis de l'ARC**. Vous pouvez obtenir également ces renseignements par l'entremise du **Système électronique de renseignements par téléphone (SERT)** en composant le 1-800-267-6999.

**Le CELI est un excellent moyen d'épargner pour votre avenir**

**LE CELI est un appoint de revenu qui vient compenser les montants qui sortiront des régimes enregistrés et qui eux sont imposables (REER, FERR & CRI)**

**Le plus tôt vous commencerez à faire des contributions à votre CELI, plus vous aurez du temps devant vous pour faire fructifier votre épargne.**

**Si vous souhaitez ouvrir un compte CELI ou faire une cotisation à votre CELI, veuillez contacter votre conseiller à Palos.**

Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) <sup>1</sup>	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$8.68	5.30%
Palos Equity Income Fund - RRSP	PAL101	\$6.81	4.57%
Palos WP Growth Fund - RRSP	PAL213	\$13.36	7.06%
Palos-Mitchell Alpha Fund <sup>3</sup>	PAL300	\$8.18	2.65%
S&P TSX Composite (Total Return with dividends reinvested)			5.15%
S&P 500 (Total Return with dividends reinvested)			4.22%
S&P TSX Venture (Total Return with dividends reinvested)			7.87%
Chart 2: Market Data <sup>1</sup>			Value
US Government 10-Year			3.50%
Canadian Government 10-Year			2.90%
Crude Oil Spot			US \$79.86
Gold Spot			US \$1,921.70
US Gov't 10-Year/Moody BAA Corp. Spread			196 bps
USD/CAD Exchange Rate Spot			US \$0.7465

<sup>1</sup> Period ending January 13th, 2023. Data extracted from Bloomberg

<sup>2</sup> Fund is priced annually

<sup>3</sup> Fund is priced weekly on Tuesdays



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