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DM MONTHLY REPORT
May 2022

PORTFOLIO ACTIVITY

In April, we sold our position in Saputo Inc. and used resulting proceeds to add to other positions within DM Canadian Equity.

FEATURE STOCK
Carlisle Companies (CSL)

CSL is a leading supplier of building envelope materials (including roofing and insulation) for residential and commercial construction, and also provides products to the aerospace and medical technology industries. The company has not only benefitted from the surge in building activity in the US, but it has been able to raise prices for its proprietary products faster than input costs. This favourable combination has led management to raise its guidance for full year margins to the high 20% range vs. CSL's historical rate of 22%, while continued catch-up in covid delayed projects has extended order backlog well into 2023. The company is also thriving under tighter environmental requirements, as its innovative roofing products help to reduce energy waste at factories and warehouses. Integration of last fall's purchase of Henry Company, a leader in systems to control the flow of water, vapour, and air, is ahead of plan and expected to add to profitability in the quarters to come. Income for Q1-22 was 70% ahead of expectations and CSL said that it expects full year earnings to exceed $15/share, a significant spread over the $12 forecast by analysts. CSL shares have returned more than 28% over the past 12 months.

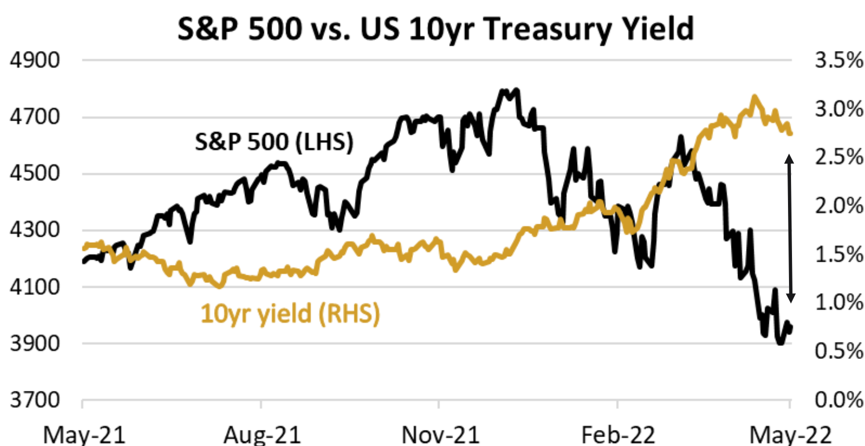
INFLATION, INTEREST RATES, AND STOCKS

As everyone knows well by now, the equity market has been presented with much to worry about in a very short space of time. Paramount among concerns is surging inflation, which is almost certainly a by-product of the extraordinary conditions brought about by the covid crisis and which is definitely being exacerbated by the war in Ukraine. Inflation on its own, however, is not necessarily perilous for a business and companies that can boost selling prices for their products and services by more than input costs are rising may even thrive in such an environment. Instead, it's the eventual jump in interest rates that most often trips up stock prices in an inflationary environment.

Higher rates exert their impact in a number of ways. First, when money becomes more expensive, investors naturally grow more cautious with how they allocate it, a maxim which is now being painfully felt by several of last year's high flyers. For example, while this nugget from Snap's IPO prospectus might have been overlooked when the speculative train seemed unstoppable, the market is clearly taking a less generous view now, having chopped 85% off its share price since last September:

> *"We have incurred operating losses in the past, expect to incur operating losses in the future, and may never achieve or maintain profitability."*

For public companies which do generate earnings, higher rates can significantly affect how these future income streams are valued. In a typical equity valuation model, forecasted cash flows are "discounted" back to the present using a specified rate, typically the prevailing risk free yield plus some premium to account for the higher risk of equity investment. When either the base rate or the required risk premium rises, the present values of future cash flows decline and stock prices adjust accordingly. Rising discount rates also have a greater impact on cash flows that are further in the future, meaning that companies with lofty but distant growth expectations tend to be more negatively affected. The graph below shows how the rise in 10-year rates over the past year has coincided with the S&P's decline – as the market finds its footing, the recent retreat in bond yields may offer some relief to equity valuation pressure .



Source: *Bloomberg*