

The Goodreid Gauge

Winter 2024



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2023 was a surprisingly resilient year in North American equity markets. Both the S&P/TSX Index and the U.S. S&P 500 Index started the year strongly, but only one index continued to experience sustained strength throughout the year.

The U.S. S&P 500 Index continued to steadily gain ground over most of the year, before losing some steam in the autumn, then finishing with strength toward the end of the year, up a very impressive 26.3% in local currency and 22.9%, when translated to Canadian dollars.

In Canada, the S&P/TSX Index began the year impressively, before moving sideways in a sawtooth pattern, experiencing periods of intermittent strength and weakness throughout the year. Finally, by year-end the TSX finished on a positive note, grinding higher by 11.8%.

If we consider monetary policy, the impact of rising rates was felt earlier in Canada than in the United States. The household debt service ratio, which tracks the total payments that Canadians are required to make as a proportion of their disposable income, reached over

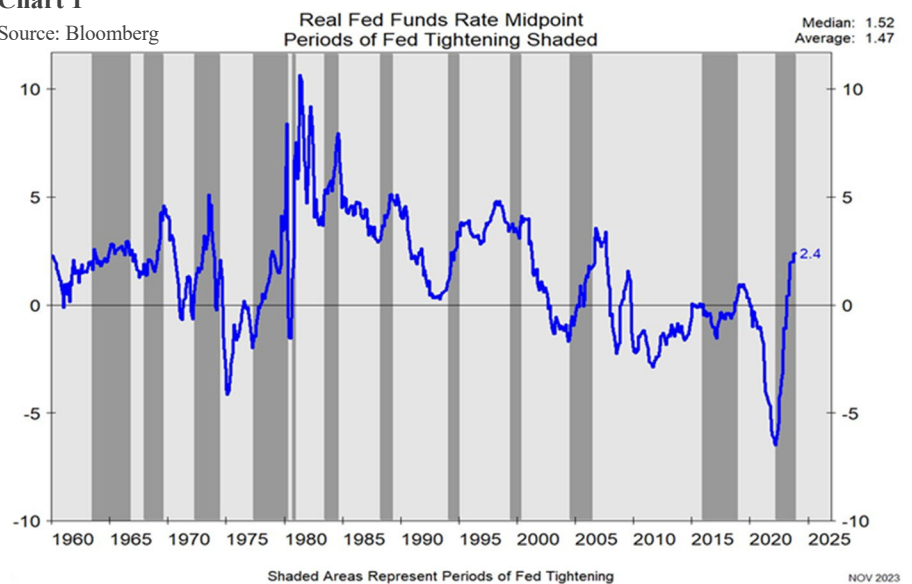
15% in the third quarter. This is the highest level since data started being collected in 1990. Going forward, these elevated debt levels are expected to be a hindrance to consumer spending. **Chart 1** illustrates real interest rates (taking inflation into account) over the past 60+ years.

There are two key takeaways from the chart:

1. The increase in interest rates over the past two years are the sharpest rise in rates in over 40 years; and
2. Interest rates are now normalizing and reflating to their long-term averages. North American economies have not only survived, but thrived, with mid-single-digit rates throughout most of the modern era.

Chart 1

Source: Bloomberg



In 2023, the Canadian equity market improved 11.8% in local currency with dividends reinvested back in the index. Strength was broad with nine of 11 sectors finishing in positive territory.

The top performing sector in the S&P/TSX Index this year was Information Technology (IT), which finished the year up 69.2%. This remarkable performance was driven by broad strength in the sector. Goodreid was able to participate in this positive price performance through our holdings in CGI Inc., Constellation Software, Lumine and Topicus. The second-strongest sector over the course of 2023 was Financials, which finished the year up 13.9%. Our Canadian equity portfolio has a broad representation of Financials including banks, insurance companies and diversified financials. Our best performers this year were Brookfield Asset Management, Manulife Financial, and Brookfield Corporation. Consumer Discretionary was the next best performing sector in the TSX, advancing 11.0% over the year. We were able to benefit from our holdings in Canadian Tire and Restaurant Brands International, both of which added positively to our returns.

In 2023 the major detractors in the Canadian equity portfolio included Communication Services which finished the year down -4.0%. In this space, we have been taking advantage of share price weakness to build a position in BCE. The other sector that declined in 2023 was Materials, which was down 3.8%. Our only holding in this space was Stella Jones, which bucked the trend and finished the year up nearly 60%. It seems as if demand for utility poles and railway ties continue to drive higher prices for these products.

South of the border, the U.S. based S&P 500 Composite Index had a stellar year, finishing up 26.3% in U.S. currency with dividends reinvested in the index. The strength of the index was broad, with eight of 11 sectors finishing in positive territory, but the sector driving

performance, as was the case in Canada, was Information Technology, which finished the year up an incredible 57.8%. This remarkable performance was broadly distributed across many index constituents. Goodreid was able to participate in this positive price performance through a number of our holdings including Amazon, Apple, and Qualcomm. All three companies performed impressively.

With performance almost as strong as the IT sector, Communication Services was the second-best performing sector in the S&P/500 last year. This sector posted an extraordinary return of 55.8% last year. Major contributors to this performance included the tech-focused communication services companies. Goodreid benefited from our holding of Alphabet which added positively to our returns.

The third-strongest sector over the course of 2023 was Consumer Discretionary which finished the year up a very impressive 42.3%. Our U.S. Equity portfolio had a broad representation in Consumer Discretionary companies, including online travel company Booking Holdings and car manufacturer General Motors. Our best performer in this sector in 2023 was Booking Holdings which returned over 75% in 2023.

In the U.S. market, three sectors sold-off in 2023 with Utilities being the worst performing sector. Utilities finished the year down materially at negative 10.2%.

Goodreid was not invested in any utility companies in 2023. The Energy sector declined modestly, providing a negative return of 4.8%. Our only holding in this space was Chevron which experienced some weakness toward the end of the year due to higher feedstock costs in their downstream business. The company also announced a major purchase of competitor Hess Corp. This acquisition was another step in the growth strategy of Chevron, which continues to put their recent windfall in profits to work by acquiring smaller competitors. Lastly, Consumer Staples declined 2.2%. Goodreid does not have any portfolio holdings in this sector.

Small Cap stocks continued to be a good asset class to be invested in for 2023, as the Russell 2000 Index returned an impressive 16.9% in U.S. dollar terms. Recall that rapidly rising rates can be challenging to smaller companies which tend to have a more susceptible balance sheet and less access to the capital markets as a funding mechanism. Toward the end of the year, macro-economic conversation regularly turned to a discussion about how quickly rates would decline in the New Year. These discussions regarding potential rate cuts next year helped boost the performance of small cap companies, which should benefit from cheaper funding sources, particularly in the back half of 2024. In the meantime, small cap companies continue to represent compelling value relative to larger U.S. companies as can be seen from **Chart 2** below.

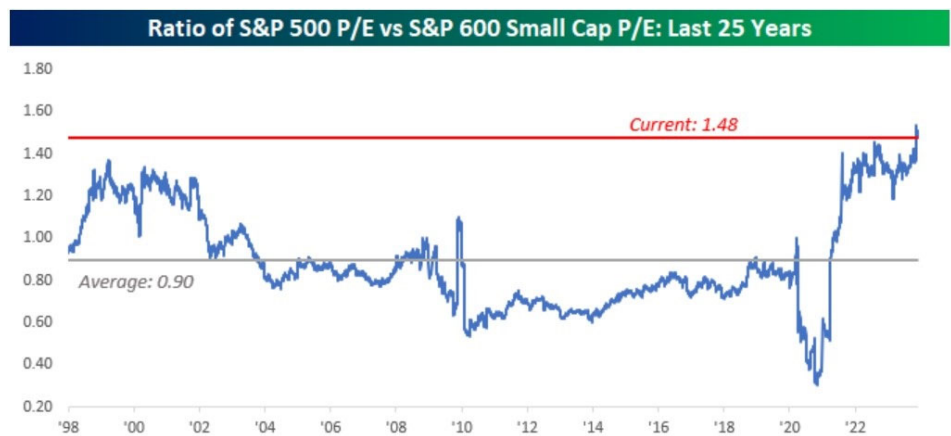


Chart 2

Source: Bespoke Investment Group

In 2023 fixed income began to once again play a more important role in our portfolios. After years of relatively tepid returns, fixed income re-emerged as a viable asset class and contributed to portfolio returns for more conservative investors. Short term bond returns rose 5% in 2023 as central banks raised interest rates in an effort to battle inflation. Their measures appear to have been effective, with inflation dropping to more reasonable levels in recent months (see **Chart 3**). Nevertheless, after many years of consistently underweighting fixed income in an environment of low rates, in 2023 Goodreid pivoted by shifting cash and very short duration bonds to longer midterm maturities. We were able to lock in rates of 5% or more with 3-to-6-year bonds. We start 2024 with a neutral portfolio weighting of high-quality corporate bonds, which are laddered up to the end of 2029.

With respect to the current composition of our investment portfolios, we continue to be quite comfortable with our existing holdings. On a consolidated basis, our portfolios demonstrate superior profitability metrics, impressive growth, and they trade at significant discounts to their respective benchmark index valuations. That said, we continue to actively monitor the companies we own on our clients' behalf and we will continue to make necessary changes.

We would like to take a moment to recognize the passing of an investment legend in 2023. Billionaire Charlie Munger passed away in November at the age of 99. He spent many decades alongside Warren Buffett at the helm of the massive holding corporation Berkshire Hathaway. Together, Buffett and Munger grew Berkshire from a small textiles firm into a massive and diversified conglomerate with a market capitalization of about \$780 billion at the time of Munger's passing. During his career, Munger demonstrated himself to be an unconventional thinker, who applied the importance of psychological factors to better understand business and investing.

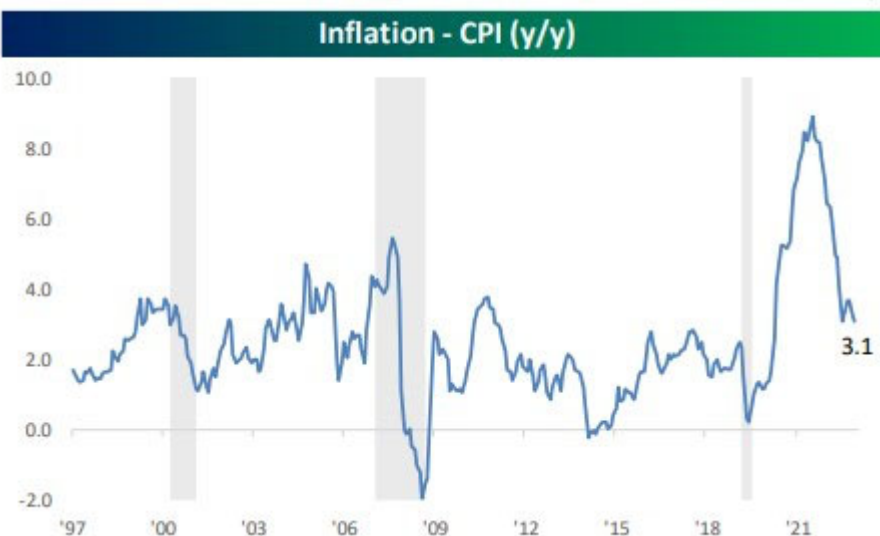


Chart 3

Source: Bespoke Investment Group

At Goodreid, as quality-first investors, we have been heavily influenced by Charlie Munger's investment style. A core component of Munger's approach to investing was to invest in quality businesses. Munger was credited for influencing Warren Buffett to focus less on price; and more on the quality of the business that he was buying. He is known to have said, "Forget what you know about buying fair businesses at wonderful prices. Instead, buy wonderful businesses at fair prices." Buffett famously transitioned from buying the cheapest businesses he could find, known as "cigar butts" to buying quality businesses with strong brands, competitive advantages, and the ability to raise prices over time. He largely came to make this transition because of Charlie Munger.

Not surprisingly, the lessons from Charlie Munger extend beyond the realm of investing; they offer a blueprint for a fulfilling and successful life. Charlie's wit and wisdom will certainly live on well into the future, influencing and molding investment minds with entertaining nuggets of timeless wisdom for many years to come. If you are interested in reading more about Charlie Munger, Goodreid has an article published in the Financial Post that you

can find here:

<https://financialpost.com/investing/5-lessons-charlie-munger-test-of-time>

We look forward to building on the success of last year and continuing to serve our clients in 2024!

Want to learn more about Goodreid Investment Counsel?

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