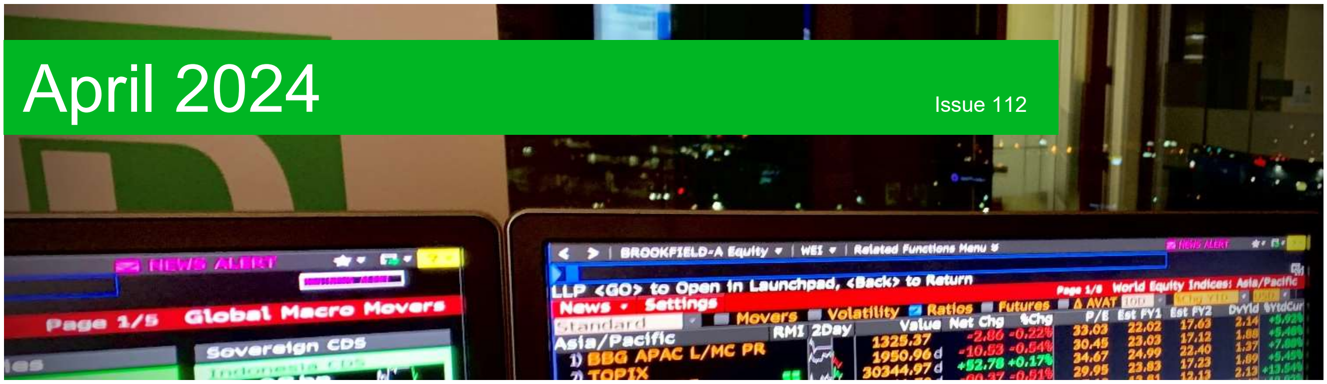
The Charter Group Monthly Letter



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Mark Jasayko, MBA, CFA
Senior Portfolio Manager & Senior Investment Advisor
TD Wealth Private Investment Advice
The Charter Group, Langley, BC

Economic & Market Update

Springtime Gold Rush

Gold has suddenly raced to new all-time highs. What's driving this? And, where might things go from here?

At the beginning of March, gold bullion rose to fresh all-time highs **(Charts 1&2)**.

Most of the gold price forecasts at the beginning of the year were generally positiive, citing the potential for geopolitical risks and a weaker U.S. dollar. We have seen about the expected number of geopolitical headlines in the news. However, the U.S. dollar has actually strengthened this year (**Chart 3**). Yet, despite that, we are three months into the year and the price of gold has already exceeded almost all of the year-end forecasts.

My experience with gold over the last four decades is that it has been a commodity that will rise over the long-term. However, for periods of a decade or more, it can go on some seemingly perplexing detours. Part of its mystery is that much of the price can be primarily determined by investor psychology for stretches of time when fundamental factors, such as industrial & jewlery demand, central bank accumulation or reduction, high inflation, persistent geopolitical strife, etc., are not as prominent. And, investor psychology can be fickle, which adds to the challenge of forecasting its price over the shorter term.

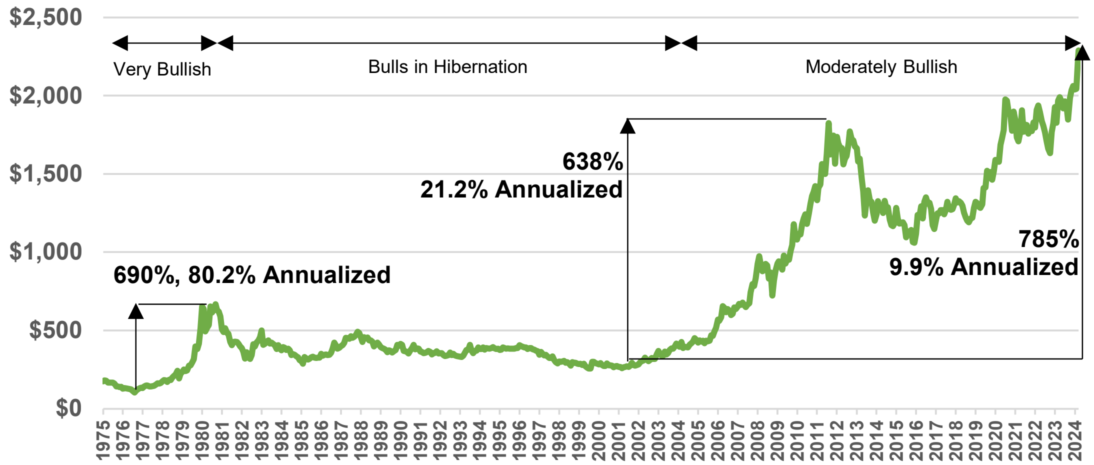
Chart 1:

Gold - U.S. Dollars Per Ounce - April 1, 2023 to Present

Source: Bloomberg Finance L.P. as of April 5, 2024

Chart 2:

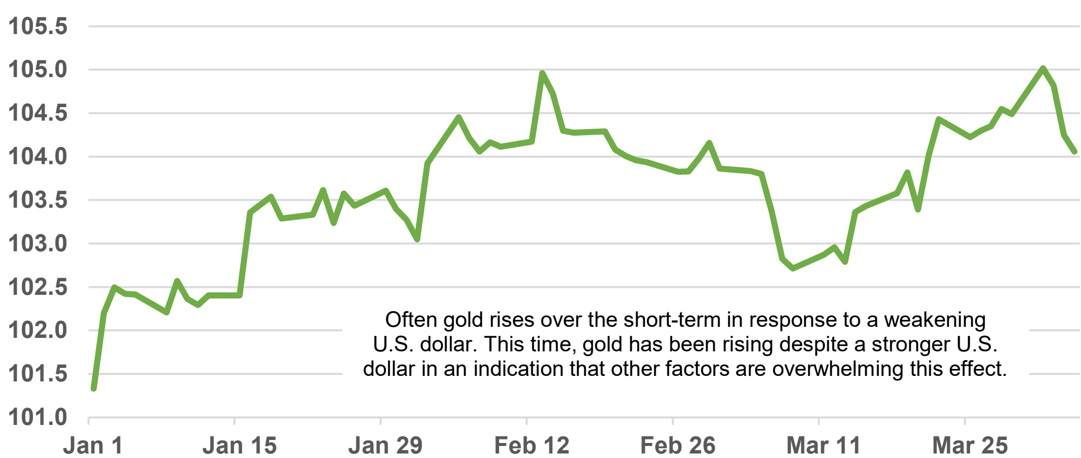
Gold - U.S. Dollars Per Ounce - 1975 to Present



Source: Bloomberg Finance L.P. as of April 5, 2024

Chart 3:

DXY Index - U.S. Dollar Strength vs Other Major Currencies



Source: Bloomberg Finance L.P. as of April 5, 2024

The 1970s saw a euphoric level of psychology towards gold. Although there was a big problem with inflation and plenty of geopolitical issues related to the Cold War, the gains in gold were well in excess of what was needed to hedge against these situations.[1]

From the mid 1980s to the mid 2000s, that psychology when into a hibernation. There where a few market crashes, and some geopolitical events (ie: 9/11), yet the price barely budged. Investors were able to look past those situations or have the confidence that government officials would come to the rescue with a fiscal package or by suppressing interest rates, and that everything would be fine again in relatively short order.

However, by 2005, that psycholgy began to tilt positive again. Although inflation had been subdued for the previous two decades, there was still enough of it to have a more notable cumulative effect. Gold needed to catch up in order to account for the erosion of the U.S. dollar's purchasing power over that time.

Since then, there has been a little bit of a tug-o-war with investor psychology and gold. Generally, it has been biased to the positive, as evidenced by the price gains over the last two decades,[2] but it has not approached the enthusiastic zeal of the 1970s.

So, what might be behind gold's recent ascent to new highs?

One thing that would have been hard to anticipate is the jump in retail demand in the People's Republic of China. Obviously, the country is facing significant economic challenges, but this has been the case since the post-covid reopening there 15 months ago. Perhaps the concerns among citizens took a while to reach a critical mass at which point there was a desire to seek safety in something other than yuan-denominated assets or cash. The yuan has fallen back to the lows during the severe lockdows there (**Chart 4**) and this may have been enough to trigger the capitulation involving the selling of yuan and the buying of gold. It is very difficult to quatify the amount of this type of buying, but it appears to be at a sustained high level since the beginning of the year. In addition, the central bank, The People's Bank of China, has also been making notable net purchases.

Since 2005, gold has benefitted from a return of relatively positive views from analysts compared to the 20 previous years.

This might have helped set the foundation for its increase in price over the last two decades.

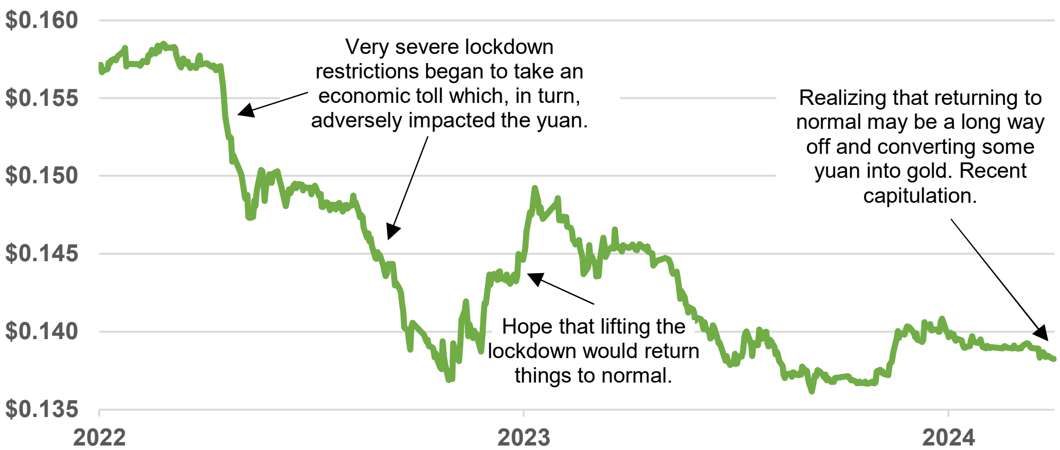
Now, more investors may be seeing the merits of owning gold in an uncertain world which has turbocharged prices recently.

Factors which may be fueling the uncertainty include inflation, higher interest rates, economic difficulties in China, and a return of geopolitical conflict to levels that we have not seen since the 1970s.

[1] In 1975, Americans were once again permitted to own gold in forms other than just jewelry and collector coins. Perhaps there was some pent-up demand. But, even with that, it would still be hard to explain the stratospheric jump in price over the decade.
[2] I bought gold bullion in the model portfolios for the first time during the spring of 2004 and have held it in varying portfolio percentages since then. The price has more than quintupled since then. However, spread over two decades, the compounded growth rate has been a little over 9%. That compares with a compounded growth rate of over 80% during the last few years of the 1970s.

Chart 4:

Chinese Yuan - Value in U.S. Dollars



Source: Bloomberg Finance L.P. as of April 5, 2024

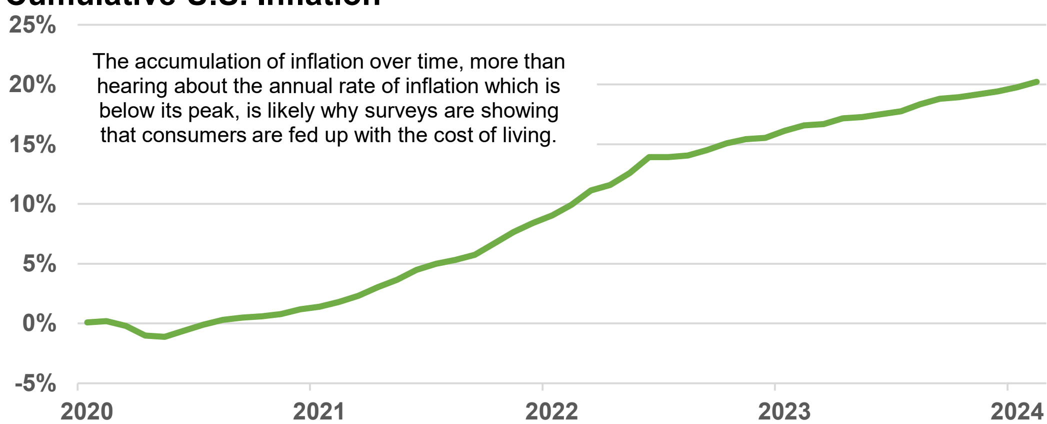
There also appears to be buying from other central banks around the world in an effort to diversify out of holding the U.S. dollar as a reserve. Countries fearful of U.S. sanctions may see this as a form of insurance.

Much of the other recent buying may be the result of a perceived need to "catch up." Both inflation and geopolitical strife have proved to be more persistent than originally expected.

Inflation, which U.S. Federal Reserve Chair Jerome Powell promised would be "transitory" three years ago is still with us, at least at a level which makes it a political issue. Plus, cumulative U.S. inflation since the beginning of 2020 now stands at over 20% (**Chart 5**).

Chart 5:

Cumulative U.S. Inflation

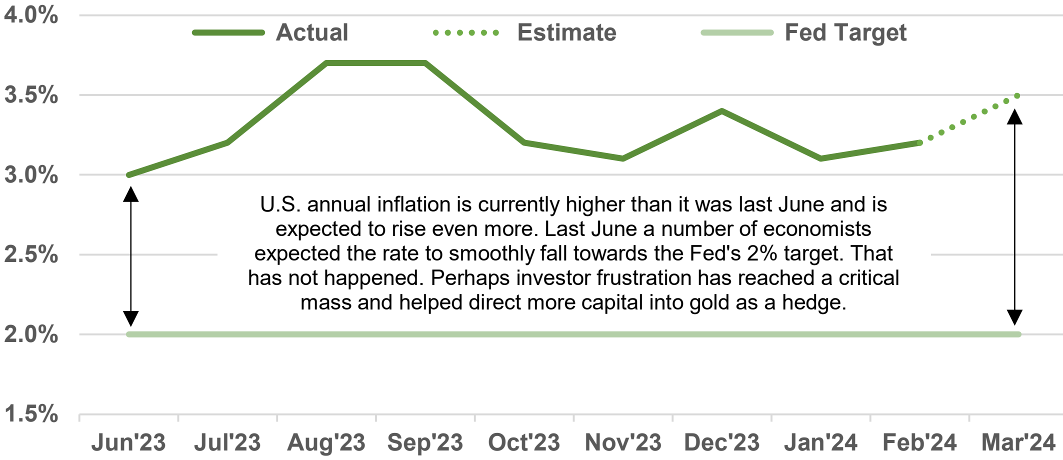


Source: Bloomberg Finance L.P. as of April 5, 2024

Gold investors may also be looking to the potential of future inflation with a little more concern than they had a year ago. Despite annual inflation having fallen from its recent 2022 peak, the central bank promises of 2% are increasingly in doubt as inflation has settled into a range of between 3.0% and 3.7% since last June (**Chart 6**). Perhaps controlling future inflation will be more challenging than investors were led to believe.

Chart 6:

U.S. Annual Inflation Readings - At Monthly Intervals



Source: Bloomberg Finance L.P. as of April 5, 2024. The estimated figure for March to be released on April 10 represents a median of the forecasts from economists surveyed by Bloomberg. Oscar Munoz, at TD Securities USA LLC in New York and who participated in the survey, is expecting 3.3%.

Finally, geopolitical uncertainties have grown in the last six months. In addition to new hostilities in the Middle East and the possibility of a wider war there, the war in Ukraine has likely stretched on longer than investors had initially expected. In many scenarios there is no end in sight at the current time. Until there are potential and plausible resolutions on the horizon, gold may be attractive as a relative safe haven compared to other assets.

Near terms risks to gold's price advance include higher real rates of interest and quicker than expected resolutions to various conflicts around the world.

I think that most of those scenarios have low probabilities at the moment.

Going forward, there are a few potential hurdles that could trip up gold's advance. The most notable near term risk involves stubbornly high U.S. interest rates. Higher interest rates have the potential to attract capital towards the U.S. dollar which could strengthen it. Since gold is primarily denominated in U.S. dollars, a strong dollar will usually lead to a weaker gold price.[3] However, there is an opposing force involved with this argument. Higher U.S. interest rates could be a signal that the inflation problem is worsening in which case there could be an increase in capital flowing into gold in order to protect purchasing power. Things might depend on relative perspection at the time: with higher rates driven by inflation, will it be the U.S. dollar or gold that looks more attractive?

The other risk involves comparatively rapid resolutions to the factors that are driving up

[3] As mentioned earlier, other factors are currently overwhelming the ability of the strengthening U.S. dollar this year to drive down the price of gold.

the price of gold. A quick settlement to the wars and/or a decline in inflation that brings it back to the 2% annual target. However, those types of "Goldilocks" scenarios may not be highly probable.

With a longer-term perspective, gold benefits from a generally rising tidal force caused by the reduction in U.S. dollar purchasing power (all paper currencies are subject to this). One example is an oft quoted saying: an ounce of gold will buy a decent bespoke suit on London's Savile Row. This is hardly an exact rule of thumb at any one time, but the fact that this phrase goes back to the 1800s and is still generally true, it shows that gold's value tends to keep pace with paper currency inflation (Pound sterling in this case).

At present, despite the recent spike in price, gold is still a little behind pace in terms of keeping up with U.S. dollar inflation. **Chart 7** shows that when adjusted to real dollars in 1975, we are still below the peak set in January 1980. In order to match the inflation-adjusted high of January 1980, gold would need to currently trade at about $2,630 USD, more than $300 higher from where it is today. So, despite the potential for a correction driven by investors sentiment or economic/geopolitical factors, it appears likely that the direction will be higher over the longer term regardless.

Even if there are shorter-term hurdles, gold's future looks bright because of our habit of devaluing paper currencies in order to fund promised government spending.

With very rare deflationary exceptions, inflation is almost always present. It is only its rate that varies.

Chart 7:

Price of Gold in USD - Adjusted for Inflation Using 1975 Real Dollars

Source: Bloomberg Finance L.P. as of April 5, 2024

Model Portfolio Update[4]

The Charter Group Balanced Portfolio
(A Pension-Style Portfolio)

	Target Allocation %	Change
Equities:		
Canadian Equities	12.0	None
U.S. Equities	38.0	None
International Equities	8.0	None
Fixed Income:		
Canadian Bonds	22.0	None
U.S. Bonds	6.0	None
Alternative Investments:		
Gold	8.0	None
Silver	1.0	None
Commodities & Agriculture	3.0	None
Cash	2.0	None

The asset allocations and the individual investments in the model portfolios remained unchanged in March.

No changes in the model portfolios in March.

As the above section might hint, gold *was* the biggest contributor to the results during the month, rising almost 9% in Canadian dollar terms.

Gold was the big positive contributor.

Stocks in Canada, the U.S., and internationally all generally had a good month as the positive psychology ignited by artificial intelligence plus the seemingly eternal promise of lower rates encouraged equity investors to continue the buying spree that they have been on since late October. We are also in a good time of year for historical seasonal performance. May has traditionally marked the end of this traditionally good stretch, so we'll see if the bright mood can be challenged at that point. Also, by that time, the heat might be on the U.S. Federal Reserve to convince the markets that there will be the latitude to cut rates before the presidential elections in early November.

Stocks also provided a lift for the portfolios as their rise since late last October continued.

Value stocks got a little more attention that growth stocks, which helped us.

[4] The asset allocation represents the current *target* asset allocation of the Balanced Model Portfolio as of April 5, 2024. The asset allocations of individual clients invested in this Portfolio may differ because of the relative performance of the asset classes since the last rebalancing and because of differences in the timing of deposits and withdrawals. The Balanced Model Portfolio is part of a sequence of five portfolios ranging from conservative to aggressive: Conservative, Balanced Income, Balanced, Balanced Growth, and Growth.

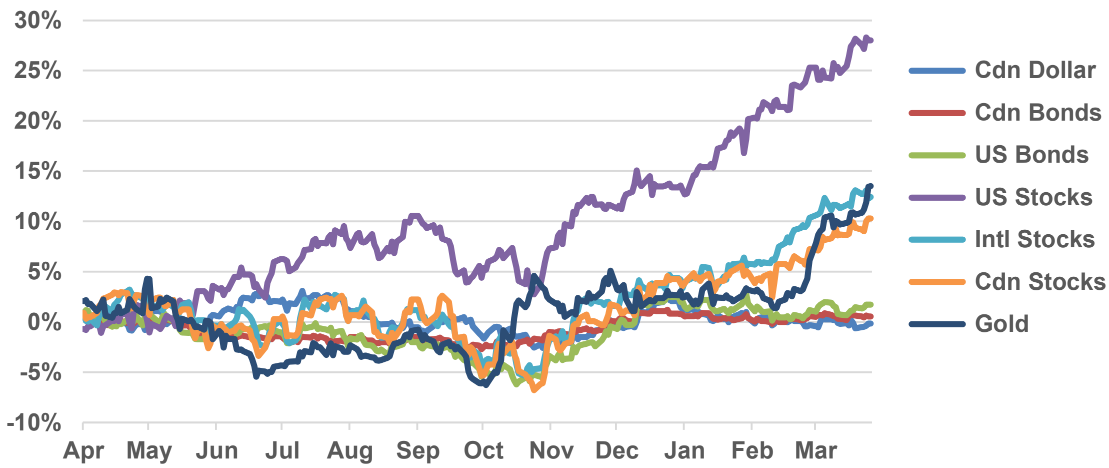
It should be noted that not everyone is bristling with optimism. Within the markets, there was more buying of quality value companies than growth-fueled tech companies last month, a possible sign that investors were looking for opportunities to protect themselves if inflation and higher interest rates turn out to be more stubborn than expected.

Bond markets around the world continued to struggle this year. Our lack of longer maturity bonds in the portfolio was a positive in this environment.

This concern was even more amplified in the bond markets as bonds continued their selloff that began in late December, which helped to drive market-determined interest rates higher. This could be a sign that bond investors are getting out ahead of any further declines that might result if inflation is not squelched anytime soon.

Below is the 12-month performance of the asset classes that we have used in the construction of The Charter Group's model portfolios. (**Chart 8**).[5]

Chart 8:
12-Month Performance of the Asset Classes (in Canadian dollars)



Source: Bloomberg Finance L.P. for the interval from April 1, 2023 to March 31, 2024

[5] Source: Bloomberg Finance L.P. – The Canadian dollar rate is the CAD/USD cross rate which is the amount of Canadian dollars per one U.S. dollar; Canadian bonds are represented by the current 3-year Government of Canada Bond; US bonds are represented by Barclays US Aggregate Bond Index; U.S. stocks are represented by the S&P 500 Index; International stocks are represented by the MSCI EAFE Index; Canadian stocks are represented by the S&P/TSX 60 Composite Index; Gold is represented by the Gold to US Dollar spot price.

Top Investment Issues[6]

Issue	Importance	Potential Impact
1. Global Geopolitics	Significant	Negative
2. Canadian Federal Industrial Policy	Moderate	Negative
5. Inflation (Portfolio Impact)	Moderate	Positive
3. China's Economic Growth	Moderate	Negative
4. Canadian Dollar Decline	Moderate	Positive
7. Short-term U.S. Interest Rates	Medium	Negative
6. U.S. Fiscal Spending Stimulus	Medium	Positive
8. Long-term U.S. Interest Rates	Medium	Negative
9. Global Trade Wars	Medium	Negative
10. Canada's Economic Growth	Light	Positive

[6] This is a list of the issues that we currently deem to be the ten most important with respect to the potential impact on our model portfolios over the next 12 months. This is only a ranking of importance and potential impact and *not* an explicit forecast. The list is to illustrate where our attention is focused at the present time. If you would like an in-depth discussion as to the potential magnitude and direction of the issues potentially affecting the model portfolios, I encourage you to email me at mark.jasayko@td.com or call me directly on my mobile at 778-995-8872.

The Charter Group

Mark Jasayko, MBA, CFA | Senior Portfolio Manager & Senior Investment Advisor
Mike Elliott, BA, CIM®, FCSI® | Senior Portfolio Manager & Senior Investment Advisor
Laura O'Connell, CFP®, FMA | Associate Investment Advisor
Kelsey Sjoberg | Administrative Associate
Esther Truong | Administrative Associate

604 513 6218
8621 201 Street, Suite 500
Langley, British Columbia V2Y 0G9

The Charter Group is a wealth management team that specializes in discretionary investment management. For an annual fee, we manage model portfolios for private clients and institutions. All investment and asset allocation decisions for our model portfolios are made in our Langley, B.C. office. We do not outsource any of the decision-making for our model portfolios – there are no outside actively-managed products or funds. We strive to bring the best practices and the calibre of investment management normally seen in global financial centres directly to the Fraser Valley and are accountable for the results.

Accountability is further enhanced by the fact that we commit our own investable wealth to the same model portfolios in which our clients are invested.

The information contained herein is current as of April 5, 2024.

The information contained herein has been provided by Mark Jasayko, Senior Portfolio Manager and Senior Investment Advisor, TD Wealth Private Investment Advice, and is for information purposes only. The information has been drawn from sources believed to be reliable. Graphs and charts are used for illustrative purposes only and do not reflect future values or future performance of any investment. The information does not provide financial, legal, tax or investment advice. Particular investment, tax, or trading strategies should be evaluated relative to each individual's objectives and risk tolerance.

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Index returns are shown for comparative purposes only. Indices are unmanaged and their returns do not include any sales charges or fees as such costs would lower performance. It is not possible to invest directly in an index.

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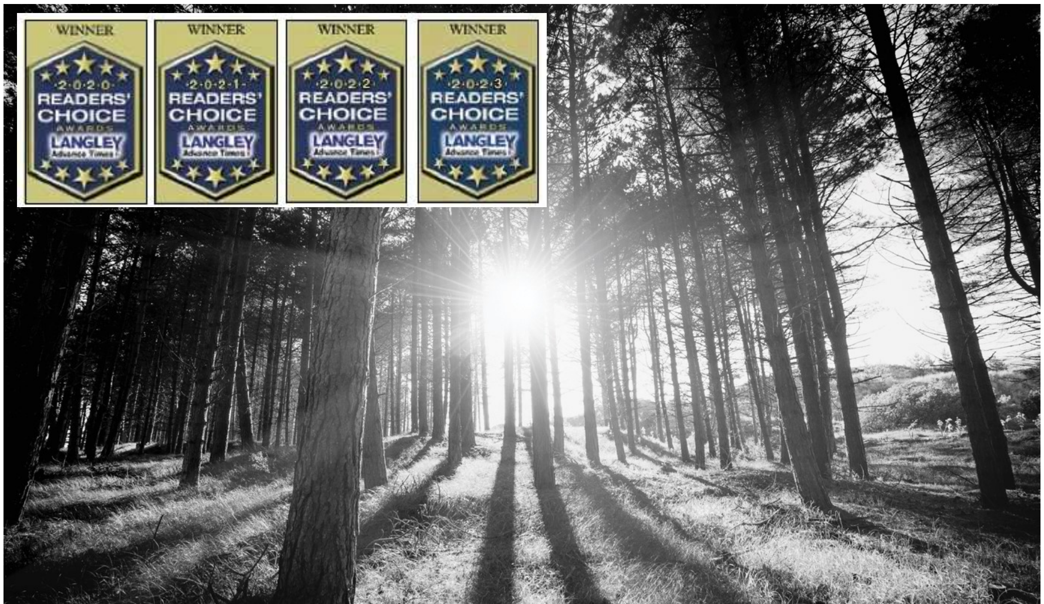

TD Wealth Private Investment Advice

Thank you from The Charter Group at TD Wealth

Thank you to our clients and community for voting The Charter Group, your favorite for Investment Management and Financial Planning in Langley for the fourth year in a row.

The Charter Group

8621 201 Street, Suite 5000
Langley, BC V2Y 0G9
Tel: 604-513-6218
Toll free: 855-822-8921 | Fax: 604-513-6217
TD.thechartergroup@td.com
advisors.td.com/thechartergroup