The Charter Group Monthly Letter

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Economic & Market Update

The Two-Year Story

… is different than the 2023 year-to-date story.

There have been a number of bright spots in the financial markets so far in 2023. Big tech stocks, such as the "Magnificent Seven," have been on a tear. The broad stock market indices are higher. And, bonds have recently moved into positive territory for the year, and more so when adding back the interest that has been earned.

Much of this is driven by a belief that inflation is headed back to the 2% target set by central banks which will allow for interest rates to fall materially from their current levels. That is usually considered good news for risk appetites, helping to propel investor enthusiasm.

Year-to-date, the Nasdaq and the S&P 500 (both significantly impacted by the Magnificent Seven big tech stocks) are up around 35% and 19% respectively. Even the staid Dow

Market gains this year, driven by a few big technology stocks, have given the impression that markets are on a march to significant gains, especially with the optimism for rate cuts next year.

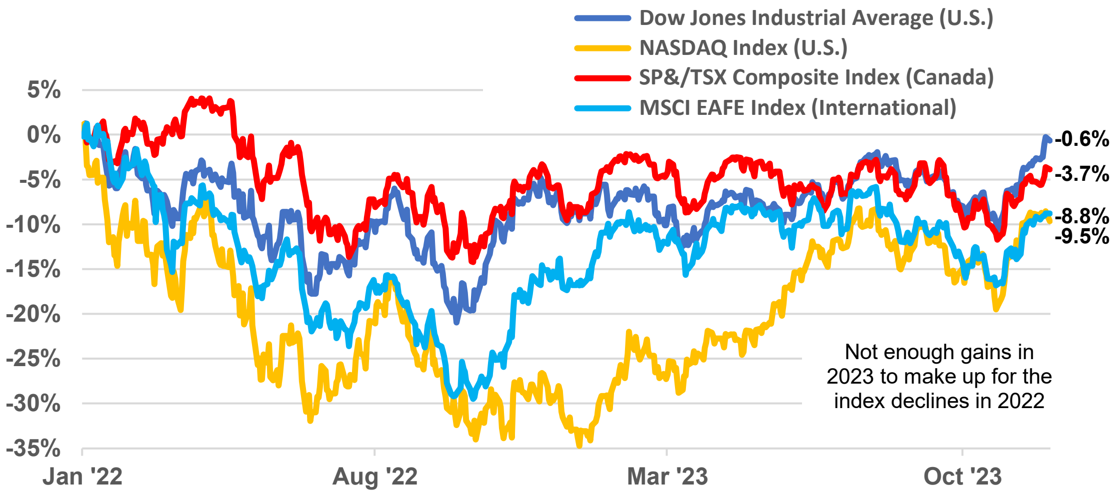
However, things do not look as rosy when looking at returns going back to the start of 2022.

Jones Industrial Average is up around 9%.[1]

However, as we progress into the future and then look back upon the charts of today, it might be hard to ignore that 2023 has merely been a bounce from the horrendous stock and bond markets of 2022 (**Chart 1**).

Main stock market indices are down over two years despite unconstrained enthusiasm for big technology stocks to harness artificial intelligence.

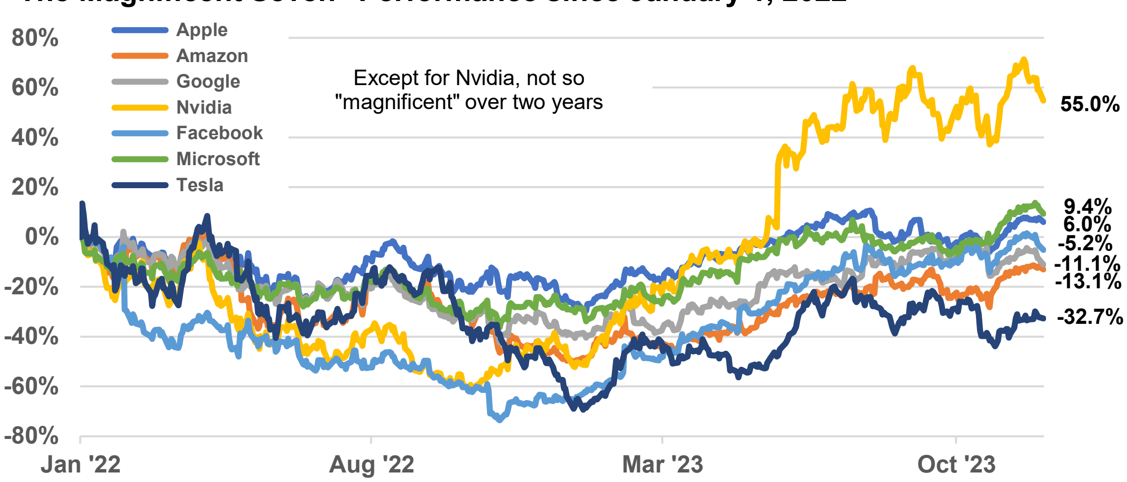
Chart 1:
Stock Index Performance since January 1, 2022



Source: Bloomberg Finance L.P. as of December 5, 2023

And, if we take 2023's "Magnificent Seven" back to the beginning of 2022, with the exception of Nvdia, things appear to range from "Mediocre" to "Miserable" (**Chart 2**).

Chart 2:
"The Magnificent Seven" Performance since January 1, 2022



Source: Bloomberg Finance L.P. as of December 5, 2023

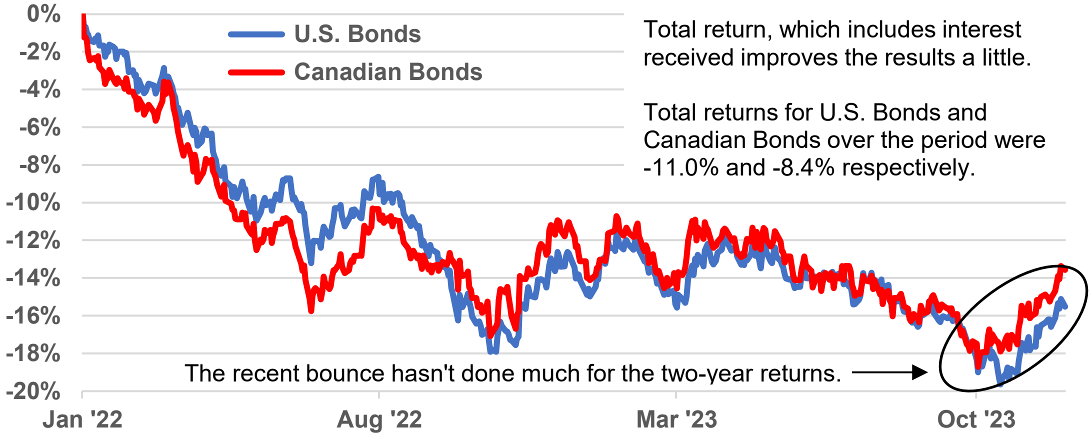
[1] Source: Bloomberg Finance L.P. as of December 5, 2023.

In last month's newsletter, I discussed the challenging stretch that bondholders have gone through. The recent slide in longer-term interest rates have helped bond prices, but nowhere near enough to ameliorate investors' woes (**Chart 3**).

It is a similar story with bonds, where the recent rally has not done much to improve returns since January 2022.

Chart 3:

Bond Price Performance since January 1, 2022



Source: Bloomberg Finance L.P. the iShares Core U.S. Aggregate Bond ETF is used as a proxy for U.S. Bonds, and the iShares Core Canadian Universe Bond Index ETF is used as a proxy for Canadian Bonds. As of December 5, 2023

Even Bitcoin, which has spiked up on the "fear of missing out" as well as hopes for the approval of ETFs that hold the cryptocurrency, is below where it was January 1, 2022.

Most of what is higher over the last two years are a few individual stocks. Of the very few themes that are higher, one could include Gold and Japanese stocks, which fortunately are represented in our model portfolios (**Chart 4**). But not much else is up.

Gold and Japanese stocks are a couple of the very few areas that have managed produce gains over the last two years.

Chart 4:

So, What is Higher since January 1, 2022? Gold & Japanese Stocks!

Source: Bloomberg Finance L.P. as of December 5, 2023

Model Portfolio Update[2]

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 specific securities holdings in the model portfolios remained unchanged in November.

No changes to the model portfolios during November.

All the asset classes used in the model portfolios were higher, especially Canadian stocks.

The prospect of lower interest rates in 2024 is getting investors excited.

All the asset classes that I use in the construction of the model portfolios were up during the month. The across-the-board advance was led by Canadian stocks, an asset class that was notably lagging since the beginning of the year. That said, the relative outperformance of Canadian stocks during the month hardly put a dent into the formidable leads of U.S. and International stocks since January. Canada just does not have the highly-rewarded technology companies that they have in the U.S. And, international stocks, which were disproportionally punished as interest rates were increasing, have correspondingly been a disproportionate benefactor from the markets belief that low inflation and lower interest rates are on the horizon.

The "Santa Claus Rally" that I discussed in last month's newsletter might have come too quickly and could have trouble persisting through to the end of the year. With the gains

[2] The asset allocation represents the current *target* asset allocation of the Balanced Model Portfolio as of December 5, 2023. 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.

since the latter part of October, markets might have now fully discounted the most optimistic 2024 forecasts with respect to inflation and interest rates. There may not be enough further news this month to significantly add to the handsome returns of the last five weeks.

There may not be much in term of news that has to potential to extend the rally at the pace it has run over the last few weeks.

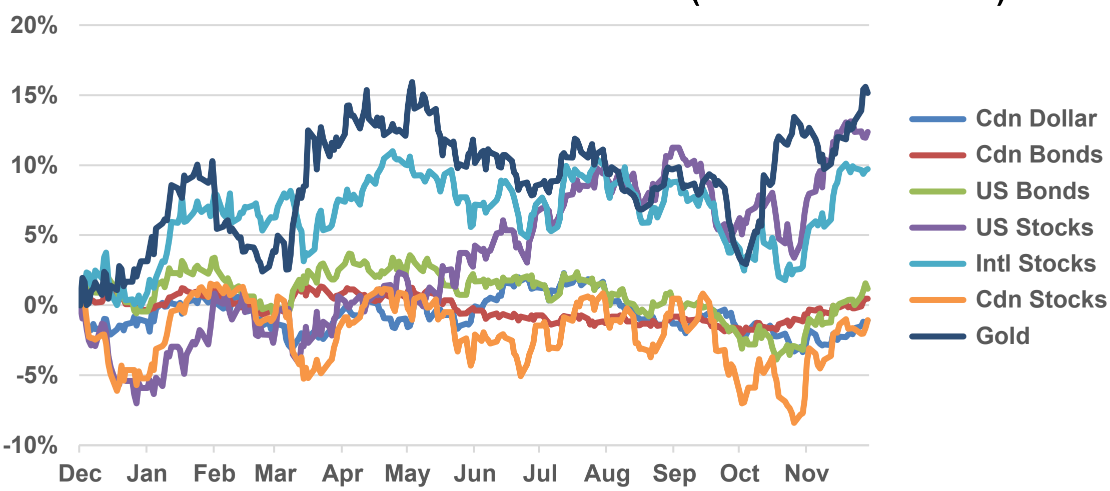
Looking at the trading in interest rate futures contracts, there is an implied 100% probability that the U.S. Federal Reserve will vote for *at least* a 0.25% cut in the Federal Funds Rate by May 1, 2024.[3] With respect to Canada, there is an implied 100% probability that the Bank of Canada will cut the Bank Rate by 0.25% no later than April 10, 2024.[4] A caveat though: the interest rate futures market has been far too optimistic with respect to lower levels of rates going back a few years now. Although the Spring feels like a long time from now during the dark days of early winter, it would be the conditions we are presently experiencing that would constitute much of the data on which interest rate decisions will be made in four months. If we enter the New Year with stubborn inflation, continued government spending, and a lack of demand to meet the supply of newly issued government bonds, Springtime rate cuts could be in jeopardy. The problem is that this would constitute a negative surprise with the current consensus of investors.

News in early 2024 could challenge investor expectations with respect to subdued inflation and interest rate cuts.

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 5**).[5]

Chart 5:

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



Source: Bloomberg Finance L.P. for the interval from December 1, 2022 to November 30, 2023

[3] Source: Bloomberg Finance L.P. as of December 5, 2023.
[4] Source: Bloomberg Finance L.P. as of December 5, 2023.
[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.

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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.

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

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