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QUARTERLY COMMENTARY

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Moguls To Navigate

2024 was an exceptional year in many ways, especially for North American equity markets. Despite economic uncertainties and geopolitical complexities, equity returns delivered a surprising upside, showcasing the resilience of businesses and the adaptability of markets. The S&P500 finished 2024 with a return of 23% marking its second consecutive year of 20%+ returns (the first time since 1995-1998 that the US market achieved such a milestone) and the TSX gained 18.5%. Most investors will look at this and despite having a great year think "Geez – how come I didn't get anywhere near that kind of performance!" Well, it's because the average stock was up 13% in the US and a little less in Canada. You see, while the benchmark returns were strong, the underlying performance was more divided, with approximately 30% of S&P 500 constituents finishing down for the year, about 28% of them in a bear market (off 20% from their highs), and nearly two-thirds down over 10% from their respective 52-week highs. The "Mag 7" large cap technology stocks accounted for a whopping 57% of 2024 S&P 500 returns (around 60% over the past two years). That being said, I think the "Trump Bump" is now over and that pullback I've been expecting has begun. Indeed, the US markets and the TSX are back trading to where they were in mid-October. This year I believe we are set up favourably for the "average" stock to begin to play catch-up, leading to a preference for diversification over concentration. Here at home, while it's little surprise the Technology sector led the charge, gold stocks were up 28% and the energy sector performed well - up 24%, but the shocker was the -26% price decline in the Telcom sector with BCE Inc.

closing the year at a price level last experienced during September of 2010. The impressive returns were supported in the U.S. by strong consumer spending, cooling inflation and a solid job market. Tech companies were buoyed by strong earnings growth and stocks in general surged following President-elect Trump's re-election in November with strong and uncontested results. In Canada many people (including myself) thought that we would be in a recession by now, and even though the country is showing signs of slowing, the economy is not contracting (yet). The continuation of rate cuts is helping but the upcoming U.S. tariff threat will be the deciding factor for Canada's economic health this year. My hunch on tariffs is that 2025 will be a repeat of 2016-2017 when Trump talked tough but in the end mostly punished China. I'm cautiously optimistic that Trump's tariff threats are nothing more than a bargaining strategy. He's already received our commitment of improved border security and he hasn't even taken office yet. But to be safe – it's important to be prepared for anything and that's why cash is king right now. It's always good to have some ammunition when a better buying opportunity presents itself – and it will.

The US economy is strong and as always it is the consumers that drive it - they not only account for roughly 70% of U.S. GDP but also a staggering 31.5% of overall global personal consumption, according to figures from the U.N. Annual consumption levels in the U.S. are greater than the next six nations combined. Consumer strength together with Trump's business friendly tax cuts and deregulation policies will propel US growth higher. Add in the huge amount of corporate and government investment in AI and the US again will lead the developed world's economies. However, it also will most likely lead to higher inflation (we're just now starting to see higher long-term yields) and the likelihood of no more than one or two more interest rate cuts. I really do not believe the Department of Government Efficiency (DOGE), led by Musk and Ramaswamy can cut US$2T from U.S. Federal spending without Trump reneging on his pledge to not cut entitlements. The overall effect of higher debt with a strong economy is inflation. That said, the year ahead is likely to present a more tempered environment. I anticipate higher volatility and lower returns this year, following an exceptional 2024.

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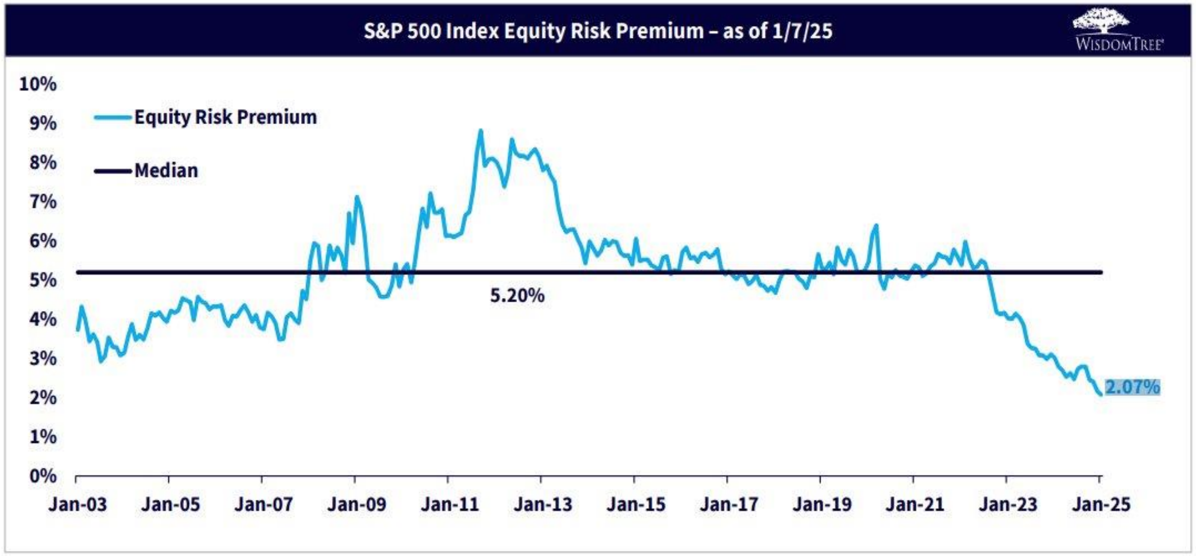
The so-called U.S. 'equity risk premium' (ERP) measures the value of stocks relative to bonds. It is essentially the difference between the earnings yield on the S&P 500 index and the 10-year Treasury yield. In 'normal' times the ERP should be positive, offering investors a reasonable premium for holding stocks over 'risk-free' government debt. It basically tells us whether investing in stocks makes sense compared to what you can make by holding a government bond. Right now the 10 year US bond yield is around 4.8%. Some analysts say that if and when the rate moves back up to 5.2% or so it can be expected that stocks will be sold to purchase bonds which can be a major factor that will depress stock markets. It's one of the reasons market watchers pay so much attention to inflation and bond yields. Here is a chart that illustrates how far the ERP has dropped in the last few years – down to a 23 year low.



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There are attractively priced stocks, especially among U.S. mid-caps, but the indices are far from cheap, and it's important to note that price alone is unlikely to dictate the near-term outlook for stocks. The overriding takeaway is that while markets entered 2025 on a wave of enthusiasm, valuations, Trump, the outlook for long bonds and other variables gives pause to any investor who has lived through a few cycles, as only life itself is more humbling than markets.

As always if you have any questions, are interested in a particular investment or you would like to have a comprehensive financial plan created for you please don't hesitate to call. In the meantime, stay warm!

Regards,

Richard