STODGELL INVESTMENT MANAGEMENT

2023 in Review

A year ago, our hope was that COVID was well behind us, and the geo-political conflict involving Russia and Ukraine would be contained, possibly resolved by now. Instead, COVID variants remain persistent and pervasive while geo-political conflict has spread to the Middle East and may prove equally contagious. Other concerns involved turmoil in the U.S.Congress where Republicans had trouble deciding who would become Speaker prompting concerns about the legislative competency of a dysfunctional House. Last year, concerns of a U.S. recession predominated forecasters predictions as upward inflationary pressures were countered by Central Banks hiking interest rates. Our prediction a year ago was that, at worst, a recession would be mild. Neither economy, in Canada or the U.S., declined in 2023.

Last year's predictions for 2023 were;

1) Growth stocks will return to favour in 2023. As interest rates stabilize investors will return to growth stocks. We do believe that defensive names will continue to perform well in 2023.
2) Given our first prediction, U.S. equities will outperform Canadian equities, in constant dollars, as measured by the SP500 versus SP TSX.
3) Oil prices (Light Crude) will average above $70 bbl.
4) U.S. Interest rates will peak by the fourth quarter 2023.
5) At worst, North American economies will experience a mild recession in 2023.

Growth stocks, particularly in the U.S. markets, returned to favour. The NASDAQ index significantly outperformed the SP500 and the Dow Jones Average, posting impressive returns particularly in the first three quarters of the year. Remember, the NASDAQ index posted a significant loss in 2022 and even with the dramatic turnaround in 2023, barely posted a positive return over a two-year period. To put 2022 tech returns into context, one of the lines from last year's review was "...Elon Musk, the second person in history to amass a fortune over $200 billion, was the first person in history to lose as much." (TESLA shares were down 65% in 2022).

U.S. Equities did outperform Canadian equities (as measured against the SP/TSX Composite Index) which gained just under 12%. Bond returns were broadly positive for the year but most of the total return was achieved toward year end. For example, the Government of Canada Long Bond, maturing 2053, gained over 19% in the final quarter of 2023. For the year, that GOC bond returned 9%.

Crude prices peaked at the end of the third quarter in the low $90's per barrel and lost significant ground for the remainder of the year but averaged in the high $70's in 2023. Returns of Canadian integrated oil companies suffered in the last quarter and were basically flat last year.

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With the interest rates peaking in October 2023, defensive names rebounded significantly gaining just under 13% in the last quarter, overcoming ground lost during the early part of the year.

So, what do we have to look forward to in 2024?

Conflict in Ukraine and the Middle East are of great concern and the second Speaker of the House seems to be on untenable ground trying to lead the legislative body. The former U.S. President who presently is leading his party's race for nomination in the 2024 general election, continues to sow division and espouse authoritarianism, all while facing increasing odds that one, if not more, of his various federal and state lawsuits against him will be successful.

History has shown that election years in the U.S. have been, on average, positive for the equity markets. Since the SP500 index began, there have been twenty-four U.S. Federal elections. In those 24 years, only four years posted negative returns and one of those was 2008 when the year ended with the U.S. embroiled in the mortgage related financial crisis.

The direction of inflation and interest rates are influential indicators for the capital markets. Will interest rates come down in 2024 and if so, by how much? Last month the U.S. Federal Reserve rate setting committee "…..reaffirmed that it would be appropriate for policy to remain at a restrictive stance for some time until inflation was clearly moving down sustainably." This was in reaction to U.S. inflation in November coming down under 3% though core inflation (without food and energy) annualized higher at 3.2%. The U.S. Fed's target is 2%. Wall Street is awash with projections of how many interest rate cuts will take place in 2024 but our view would be that if the U.S. economy remains sound (nothing worse than a soft landing) then rate cuts will be limited to two, possibly three, times in 2024 as the Federal Reserve will want to remain impartial with the upcoming election in November. Regardless, lower interest rates in 2024 will be constructive for equities and bonds.

Over the past year, higher rates and inflation have changed consumers' mind set, particularly the younger generation of consumers (and investors) who have known little else other than historically low interest rates. Carrying costs for housing, car loans, increased prices for grocery and day to day items has curbed discretionary spending significantly.

With all this in mind, our predictions for 2024 are.

1) Both equities and bonds will both post positive returns in 2024 but equities will outperform long term bonds (SP500 vs U.S. 30 Year Treasury Bond).
2) Defensive stocks will outperform growth stocks.
3) U.S. Inflation will average more than U.S. Central Bank target (2%) in 2024.
4) North American Industrial Demand will start to pick up in the latter half of 2024, putting upward pressure on material and metal prices. Crude oil (WTI) will average above $65 bbl.

Best wishes for a healthy and happy 2024 and thank you for your confidence in SIM LTD.