HARBOURFRONT
WEALTH MANAGEMENT

# WATERMARK PRIVATE PORTFOLIOS

## DECEMBER 2023 COMMENTARY

# Market Review in Minutes

## Equities

- The S&P 500 in Canadian dollars and the S&P/TSX Composite both posted December gains and ended the year higher, with 22.30% and 11.75% YTD returns, respectively. Equity markets rallied and cheered after the US Federal Reserve maintained interest rates at the current level and signaled that they would be cutting interest rates next year.
- The real estate sector, which is interest-rate sensitive, led the US market in December, posting a 7.96% gain as the market now expects interest rate cuts in 2024.
- Outside of North America, the emerging markets posted a gain in December but underperformed compared to Canada and the US.

## Fixed Income

- US Treasury bonds continued to rally in December, posting the second consecutive monthly gain with the longer-term bonds leading shorter-term bonds.
- Overall, the Canadian Universe Bond had another positive month, gaining 3.43% in December and ending 2023 with a 6.69% YTD return vs a return of -11.69% in 2022.

## Commodities

- Crude oil, a good measure/gauge for inflation, recorded its third consecutive monthly loss. Crude oil saw a volatile swing within the month, falling 11% until December 13 due to headlines regarding inventory buildup and slow demand. Later in the month, it had rallied about 12% due to increased geopolitical tensions in the Middle East following supply chain disruptions in the Red Sea but ended lower at around $71 per barrel.
- Gold, often considered a “safe-haven asset,” broke out to a new high early December but has given up some of those gains and ended the month 0.71% slightly higher and 13.45% YTD.
- The US Dollar fell in December as the US Federal Reserve held its key policy target range.

| **As at December 31, 2023** | **Monthly % Total Return** | **YTD % Total Return** |
|---|---|---|
| **Canadian Bonds**<br>*FTSE Canada Universe Bond Index* | 3.43% | 6.69% |
| **Canadian Equities**<br>*S&P/TSX Composite Index* | 3.91% | 11.75% |
| **US Equities**<br>S&P 500, in C$ | 1.64% | 22.30% |
| **Gold** | 0.71% | 13.45% |
| **Oil**<br>*West Texas Intermediate Crude* | -5.67% | -10.73% |
| **Canadian Dollar** | 2.30% | 2.17% |

# Notable Monthly Highlights

## USA – The US Federal Reserve held its target range at 5.25% to 5.50% at its final 2023 FOMC meeting

- As expected, the US Federal Reserve held its key policy target range at 5.25% to 5.50% as the Fed stated economic activity has “slowed” from the “strong pace in the third quarter” and inflation has eased since last year but remains elevated. Although market participants are expecting 75 basis points to be cut next year, the Fed will continue to monitor key economic data “in determining the extent of any additional policy firming that may be appropriate to return inflation to 2 percent over time.” The battle against inflation and worries about reflation remain front and centre, as evidenced by the key economic data:
    - US job market was robust as unemployment rates in November 2023 fell to 3.7% vs the market expecting an unchanged rate of 3.9%.
    - Consumer spending remained strong as retail sales increased by 0.3% in November in all areas across the board, from motor vehicles, furniture stores, sporting goods, and restaurants.
    - The closely-watched core CPI, an inflation metric that excludes volatile food and energy prices, rose by 0.3% from October to November and 4% YoY, which were both in line with consensus. This slight uptick in inflation was attributed to the increases in rent, medical care, and motor-vehicle insurance/used-car prices, which rose for the first time after 5 months.

## Canada – The Bank of Canada held its key policy rate at 5% for the third straight meeting

- The Bank of Canada increased interest rates 10 times since March 2022 from 0.25% to 5%. To wrap up 2023, the Bank of Canada held its key policy rate at 5%. For 2024, the Bank of Canada remains vigilant to see if their policy is working to combat inflation and continues to monitor key economic indicators:
    - Although the prices of food and fuel has slowed, Canada’s annual inflation rate remained at 3.1% in November vs the expected 2.9% because of growing travel prices; this has caused the market to trim its bets of cutting rates in April.
    - Canada recorded a population growth of more than 430,000 in Q3 alone, which was the largest growth in a single quarter since 1975. This accelerated immigration continues to put long-term upward pressure in rent inflation and explains why housing prices have remained elevated.
    - On the contrary, Canada’s GDP in October was flat for three months in a row, showing signs of a stagnation in economic growth and the labour market has also showed signs of easing as the unemployment rate increased to 5.8% in November.

# Notable Monthly Highlights

## World – Key central bankers held its key policy rates

- China saw its exports grow for the first time in six months in November. As its industrial output grew 6.6% YoY, it is beating the 5.6% expectations. However, ratings agency Moody's issued a downgrade warning on China's credit rating due to continued concerns on the property front.
- The Bank of England and The European Central Bank both announced they would maintain interest rates where they are as they to see some signs of inflation easing. However, both central banks remain cautious and vigilant on their fight against inflation.

# Watermark Private Portfolios Outlook and Positioning

- With both equity and bond markets continuing to rally, portfolio returns have been strong to end the year.
- With the recent run-up, we believe that the US S&P 500 is valued fairly and a short or mid-term pullback in the equity markets is likely needed to reduce overbought sentiment. We believe our positioning will continue to provide strong risk-adjusted returns.

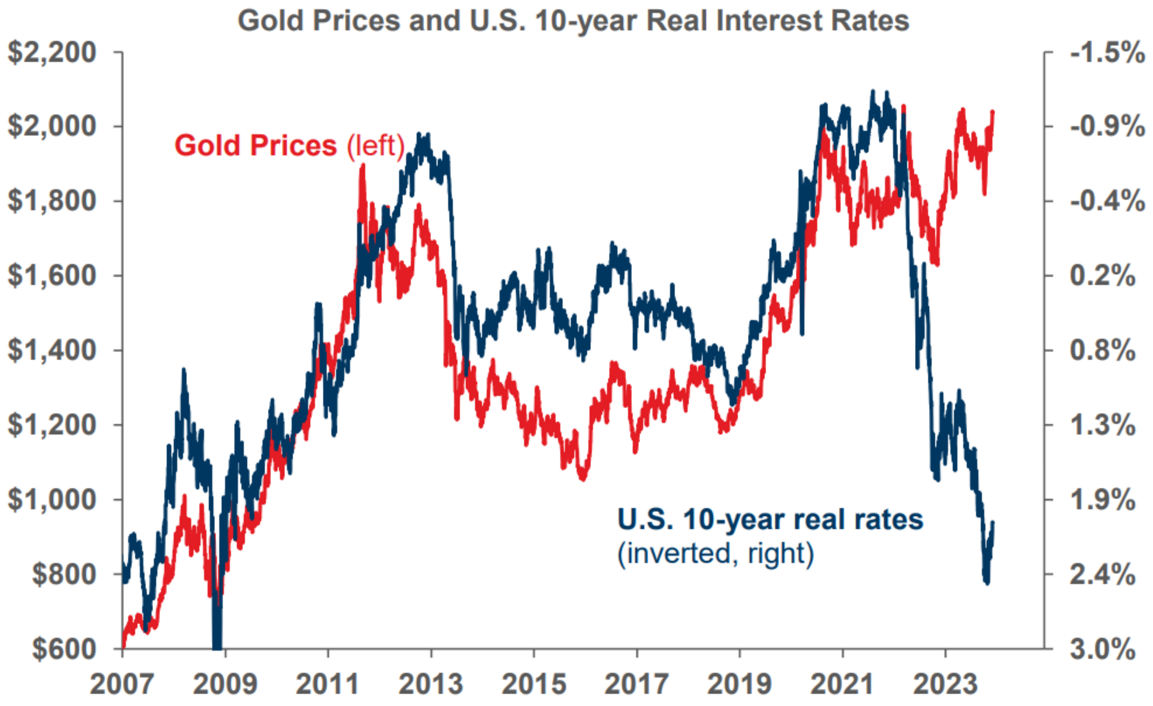
| | Underweight | Target | Overweight | November End | December End |
|---|---|---|---|---|---|
| Equities | | ● | | As public equities saw a strong November, we still like our public equity exposure currently as we believe equities may likely rally until the end of the year with strong seasonality and strong consumer spending as reported by the Black Friday and Cyber Monday sales in the USA. | No changes. Public equities have risen for the second month in a row. We maintain the current weight to target and continue to monitor the economic data, sentiment, and technical indicators. |
| Fixed Income | ● | | | For conservative portfolios, we are using proceeds from private credit to allocate to high-quality Canadian corporate bonds as we believe that rates have peaked and that the Bank of Canada is likely done raising interest rates. | No changes. We are keeping our weighting of public fixed income through high-quality Canadian corporate bonds as we continue to believe that interest rates have peaked. The public fixed income market ran up in December and could easily pullback in the short-term. |
| Private Credit | | ● | | We continue to see strong merit in a stable allocation to private credit. However, we have trimmed our long-term strategic holding to a new target for the conservative and balanced portfolios for more liquidity so that we can move the proceeds to high-quality Canadian corporate bonds. | No changes. We are maintaining our long-term allocation to private credit as we still believe that increased regulation and the tightening of bank lending conditions are pushing borrowers to look for alternative options, specifically private market lenders. |
| Private Real Estate | | ● | | No changes. We are maintaining long-term allocation to private real estate. | No changes. We are maintaining a long-term allocation to private real estate due to strong immigration in Canada as evidenced by the recent Q3 report and the existing supply and demand gap. |

# Did You Know?

As we reiterated in previous commentaries, gold has historically traded opposite to US 10-year treasury rates (gold price typically rises when the US yields fall and vice versa). This chart demonstrates how, over the rate hiking cycle, gold has held up relatively well despite the rise in US yields.

## Our opinion:

Though gold may be slightly overbought, we still see some upside opportunity in the metal if the central banks hold or cut in the upcoming year. Gold is considered a "safe haven" asset that investors often flock to amidst geopolitical tensions. In addition, China's accumulation of gold reserves could help push gold prices higher.




Source: National Bank CIO Office (data via Refinitiv).

# Key Economic Indicators

| | Inflation Rate | | Interest Rate | | Unemployment Rate | | GDP Annual Growth Rate | | Stock Market Valuation (Forward P/E) | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Last | Chg. | Last | Chg. | Last | Chg. | Last | Chg. | Last | Chg. |
| USA | 3.10% | ▼ | 5.50% | ▬ | 3.70% | ▼ | 2.90% | ▲ | 19.8 | ▲ |
| Canada | 3.10% | ▬ | 5.00% | ▬ | 5.80% | ▲ | 0.47% | ▼ | 13.4 | ▲ |
| China | -0.50% | ▼ | 3.45% | ▬ | 5.00% | ▬ | 4.90% | ▼ | 8.9 | ▼ |
| Japan | 2.80% | ▼ | -0.10% | ▬ | 2.50% | ▼ | 1.50% | ▼ | 14 | ▼ |
| United Kingdom | 3.90% | ▼ | 5.25% | ▬ | 4.20% | ▬ | 0.30% | ▬ | 10.7 | ▲ |

Source: Trading Economics

# DISCLAIMER

*The Watermark Private Portfolios team prepared this commentary to give you their thoughts on various investment alternatives and considerations which may be relevant to your portfolio. This commentary reflects their opinions alone and may not reflect the views of Harbourfront Wealth Management. In expressing these opinions, they bring their best judgment and professional experience from the perspective of someone who surveys a broad range of investments. Therefore, this report should be viewed as a reflection of their informed opinions rather than analyses produced by Harbourfront Wealth Management Inc.*