VALUE CONTRARIAN
ASSET MANAGEMENT

<u>Full Disclosure</u>

Over the coming years we want to advise investors that the Value Contrarian Fund **may** be **<u>more volatile</u>** than has been the case in the past. Here is our reasoning:

1) When your Fund is <u>fully invested</u>, we are subject to the <u>full volatility</u> of the financial markets. As we don't short stocks, **<u>cash</u>** is often the simplest, risk-free instrument to blunt stock market volatility.

2) Berkshire Hathaway, Warren Buffett's investment vehicle, represents approximately 25% of your fund's assets. We view this as a strong investment in all market conditions. Nonetheless, there will be years (like 2020 & 2023) where Berkshire <u>underperforms</u> the market and may impede your Fund's returns.

3) In general, a rising Canadian dollar and a weakening US dollar will also affect your Funds results, due to our significant U.S. holdings. Presently, the Canadian dollar is approximately 74¢. However, if over the coming years it rose to 85¢ or 89¢, this would add a stiff headwind to your fund's net results.

Predicting currency moves is about as easy as predicting the weather this time next year. Good Luck!

Benjamin Horwood

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Dear Partners,

I think it's very safe to say we're not going to be lowering rates <u>at the pace we raised them</u>.

Tiff Macklem
Governor – Bank of Canada
March 6, 2024

… <u>Today's rates aren't high</u>. They're higher than we've seen in 20 years, but they're not high in the absolute or <u>relative to history</u>… <u>I consider them normal</u> or even on the low side.

- **In 1969, the year I started work, the Fed funds rate averaged 8.2%.**
- **Over the next 20 years, it ranged from 4% to 20%. Given this range, I certainly wouldn't describe 5.25-5.50% as high.**

Howard Marks
Oaktree Capital – Client Letter
January 9, 2024

Many disregard the benefits that ensued [2009-2021] from <u>low interest rates</u>. But as one of the oldest investment adages says, <u>we should never confuse brains with a bull market.</u>

Howard Marks
Oaktree Capital – Client Letter
January 9, 2024

Many Israelis support the idea of a compromise for peace <u>but</u> are wary of abandoning the status quo without an agreement with a <u>partner they trust will provide real security and actually end the conflict</u>…

<u>The failures of Gaza and Lebanon</u> underscored by Hamas' and Hezbollah's continued unrelenting denial of Israel's right to exist, <u>shattered the premise – key to any peace deal – that withdrawal [without a political agreement] makes Israel safer.</u>

<u>The lesson for Israelis is simple</u>: without durable and substantive enforcement of <u>demilitarization of a future Palestinian state</u>, any political solution to the conflict will be under permanent threat.

David Makovsky
Washington Institute Near East Policy
February 22, 2024

> **To be sure, Palestinians have ample reason to distrust Israel. Israeli Prime Minister Benjamin Netanyahu publicly endorsed a two-state solution in 2009, but later renounced it, and several key figures in his cabinet oppose a Palestinian state on ideological grounds.**
>
> **David Makovsky**
> **Washington Institute Near East Policy**
> **February 22, 2024**

2023 ushered in a second year of rising interest rates and surprise geopolitical events (think Gaza war). From the initial quarter-point increase in March 2022, the Fed continued raising short rates until July 2023. The total cumulative rate increases were 525 basis points or 5.25%. By October 2023, a ten percent stock market sell-off coincided with the approximate peak in the yield (5%) on the 10-year U.S. treasury bond.

To the surprise of many, including your manager, the vigorous rise in both short and long-term rates failed to produce a much-anticipated recession. The fallout in the economy, so far, has been manageable. By year-end, these punishing long term interest rates started to ease (below 4% by late 2023), and the stock market indexes took off. Especially the tech-laden Nasdaq.

We agree with the assessment of Howard Marks whereby the 1980 to 2020 era of declining/ultra low interest rates are over. This will certainly have a profound effect on asset valuations. And other than temporary responses to a financial crisis/deep recession, we are unlikely to return to the ultra low/easy money conditions of the recent past.

The year-end and first quarter 2024 rally in stocks, has propelled the S&P 500, the Dow, and the Nasdaq 100 into record high territory (the TSX only recently). The TSX has failed to keep up with its American counterparts due to the index's underweighting in the booming technology & healthcare sectors. Moreover, the rally and "froth" in riskier assets, has extended into Bitcoin, reaching recent all-time highs in 2024.

What's behind these recent stock market gains since last fall? The Wall Street Journal summed it up simply when it wrote the other week: "Growing optimism that the economy will stave off a recession and the Federal Reserve will soon pivot to cutting interest rates has propelled major stock indexes to repeated highs to kick off 2024. And a frenzy over artificial intelligence technology has turbocharged the rally in recent weeks." This feeding frenzy, for example, has led to Nvidia's share price (the AI poster child) tripling last year, while already climbing more than 85 percent in 2024.

It now seems that U.S. Fed Chairman Powell is "not far" from winding back some of the aggressive interest rate hikes that began in March 2022. The mantra on rates, "higher for longer", has now moved into 2024.

In the U.S., with stock indexes at record highs, no financial catastrophes or contagion underway, and unemployment still low by historical standards, the Fed, in our opinion, will likely initiate limited "cosmetic" rate cuts in 2024.

Simply stated, why waste your "bullets" (rate cuts) when the U.S. economy is still robust, and the financial markets are showing signs of speculative greed and making record highs? Better to save a good portion of your "gunpowder" for a period when the proverbial, "shit hits the fan".

In Canada, without the benefit of having been able to lock in low rates on U.S. style 30-year mortgages, the Canadian consumer has less spending room. Rising inflation is less of a threat in a slowing Canadian economy.

Hence, in Canada, we would not be surprised to see rate cuts sooner rather than later. This could potentially lead to a further weakening of the Canadian Dollar.

2023 Performance: + 4.2%

It is always better [and healthier for the broad stock indexes] when the troops lead a broad-based market rally rather than when the generals [eg: the few Magnificent 7 stocks] lead a narrow advance [when many of the troops are in retreat as was the case in 2023].

David Rosenberg
Rosenberg Research
Financial Post
January 6, 2024

What I so enjoy about Edward Chancellor books is the way they illustrate how [foolish human investing] behavior that took place 200 or 400 years ago is still being repeated today and is sure to reappear again and again in the future.

Howard Marks
Oaktree Capital – Client Letter
January 9, 2024

One investment rule at Berkshire has not and will not change: <u>Never risk permanent loss of capital</u>. Thanks to the American [economic] tailwind and the power of <u>compound interest</u>, the arena in which we operate has been – and will be – rewarding if you make a couple of good decisions during a lifetime and avoid serious mistakes… <u>Quotational shrinkage for extended periods can't be avoided</u>…

Warren Buffett
Chairman – Berkshire Hathaway
2023 Annual Report

December 31, 2022 – $ 4,032.64 (NAVPS after distributions)
December 31, 2023 – $ 4,202.45 (NAVPS before distributions)
December 31, 2023 – $ 27.69 (Year-End Distribution per unit)
December 31, 2023 – $ 4,173.59 (NAVPS after distributions)

Your Fund ended the year with a net asset value of <u>$ 4,173.59 per unit</u> (+4.2%).

2023 was the year of "rate anxiety", as interest rates ground higher, quarter after quarter. JP Morgan Chief Executive Jamie Dimon warned that a "hurricane" was about to hit the U.S. economy. Hedge fund manager Ray Dalio of Bridgewater Associates warned of a looming "debt crisis". While well-known Canadian economic/stock market analyst, David Rosenberg, was recession obsessed. According to the Wall St Journal, in early 2023 "… economists predicted a 61% chance of recession in 2023".

<u>In the end, the "experts" were left in the dust</u>. Simply stated, they were "too skeptical of the Federal Reserve's ability to push inflation down without sparking a recession". Today, unemployment remains near half century lows and the stock markets are at record highs.

2023 was also the year of the "<u>Tech snapback</u>" after a disastrous 2022. In 2023: Nasdaq +54.9%, S&P500 +26.3%, TSX +11.7%. At the bear bottom in October 2022, Nasdaq was -32.6%, S&P500 -18.1%, TSX index -5.8%.

As Warren Buffett loves to counsel, "never bet against America". The large headline returns in 2023 (especially the U.S. S&P 500 index) obscured the narrowness of a stock market led by a few generals (7/500). These seven were crowned "the Magnificent Seven".

These few "mega cap" tech and AI-related companies experienced gangbuster stock appreciation. The Magnificent Seven "grew to the largest concentration the S&P500 has ever had, at 29%".

Meanwhile, the S&P500 equal-weight index (where all stocks are of equal weight) gained a more subdued 13.3% for the year, not 26%.

There was no hiding behind the fact that 2023 was a mediocre year for your manager. Although we eked out a GIC rate of return, that pales in comparison to the broad index returns.

For the most part, our largest holdings simply underperformed. Berkshire gained +15.8% while TD bank was -6.9%.

Other significant holdings in the fund, such as U.S. defense contractor General Dynamics and Insurance broker Aon, had lackluster returns, (+4.66% and -3.04% returns respectively). The Canadian rail stocks produced small single-digit gains for the year. CN Rail +3.55% and CP Rail +3.85%. The few standouts were Thomson Reuters +32.7% and CGI +21.6%. CGI is a large Canadian-based IT business consulting firm which has been a stellar performer for many years.

On a more positive note, the first 3 months of 2024 have been much more fruitful for your fund. **To the end of March, your fund is up approximately +8.0%.** Double the gains of last year in the first quarter. One never knows exactly when markets will rally sharply. Once again, it's time in the market, not timing the market.

During the fourth quarter, we added significantly to our holdings in the National Bank Quebec Growth ETF. Top 10 holdings include: CNR, National Bank, Couche Tard, CGI, Transforce, Power Corp, WSP, Dollarama, Metro, and BCE.

By purchasing a quality diversified ETF, we obtain low-cost exposure to stocks/sectors we may not own in our Fund. In particular, we like Quebec Growth, due to its exposure to quality businesses, (leaders/well run), while avoiding heavy weightings in the metals, mines, minerals, and gold sectors.

We also decided to exit our long-time holding in Saputo – the global dairy & cheese producer. Our original purchase price at the time of the IPO in 1997, was $2.12 (adjusted for splits). Our last sales were made between $27.25 and $28.55.

Foreign acquisitions in Australia, Europe and South America have not been positive value creators in our opinion. Perhaps more of a distraction.

With a Trump presidential win looking more likely day by day – this will not usher in an American administration that would be "tariff neutral" for Canada's dairy industry.

On a sad note, Charlie Munger, Warren Buffett's wise, outspoken, and brilliant "sidekick" partner, passed away this past November.

Investors are perhaps worried about the day that Buffett himself passes on. This leads us to the question, how was Berkshire's stock affected by the death of Munger? Immediately, not much.

Munger's death was announced November 28, 2023 after the market close. The stock that day finished at $360.05. The initial drop in Berkshire's stock, one week post-announcement was: – (2%). Certainly not a cataclysmic event.

On a more positive note, Berkshire's stock has gained +16.8% from November to March 28, 2024 ($360.05 to $420.52). With Berkshire representing approximately 27% of the Fund's assets, we trimmed our 30,000 share position by 2,500 shares at the end of March.

We believe Berkshire is the perfect stock for these unsettled times. The last time the stock market was tested by a sustained 40%+ decline was during the 2008-2009 Great Financial Crisis. With $169 billion in cash at year-end 2023, Berkshire should end 2024 (barring a major acquisition), with $180-$190 billion of cash on its balance sheet. The stock is also a hedge against a falling Canadian Dollar.

Upon Buffett's demise, we would not be surprised to see Berkshire stock temporarily falter 5%-10%. From his grave, it would be classic Buffett to throw his shareholders a parting gift in recognition of their loyalty. The initiation of a "special" dividend could be Buffett's final legacy and act of "largesse" to his long-time devoted investor base. A $12 billion special dividend would represent an approximate 1% yield on a $400 B stock/$600,000 A stock. In 2023, Berkshire produced $30 billion of free cash flow (after CapEx).

OUTLOOK 2024

Three [Clinton/Bush/Obama] presidents have all come to New York and not one of them is here to appear in court.

Stephen Colbert – Talk Show Host
Democratic Fundraiser
New York City – March 28, 2024

There are plenty of people who would like to vote for Trump if he narrowly defined some of his more sensible issues – a strong America, lower taxes, less regulation, the border, [but] <u>the problem with Trump is Trump.</u>

Paul Levy – JLL Partners
Financial Times London
March 2/3, 2024

<u>[Hezbollah has] depopulated an entire region of Israel</u>, and for months it has been getting away with it. <u>War in the North</u> [between Israel and Hezbollah in Lebanon] <u>could dwarf the Gaza fight and change Lebanon and Israel forever</u>.

Elliot Kaufman
Edition – Wall St Journal
March 22, 2024

The hypothetical merits of a <u>two-state solution</u> and the Palestinian right to self-determination are not in dispute. <u>The problem is context</u>…

… Recognizing a Palestinian state <u>without handling any of the conflict's substantive constituent issues</u> – the status of Jerusalem, the Palestinian right of return, [demilitarization], or the composition of Palestinian leadership – would all at once hand Hamas both a reward and a further opportunity.

Jay Mens
Fellow – Harvard Kennedy School
February 22, 2024

When it comes to predictions, I always like to defer to the words of the late great economist John Kenneth Galbraith: "There are two kinds of forecasters: Those who don't know, and those who don't know they don't know". Here are some of our thoughts for 2024:

<u>2024: The Positives</u>

1) The market has finally started to broaden beyond the "Magnificent 7". By the end of March 2024, more than half the stocks of the S&P 500 have hit 52-week highs. A broadening market [more troops than generals] is always <u>a positive technical indicator</u>.

2) Inflation, while not yet at 2 percent, is moving in the right direction – below 3 percent. Take out mortgage interest costs from the consumer price index (CPI), and the recent Canadian inflation rate is <u>well below 2%</u>.

3) Modest interest rate cuts are coming. Perhaps not at the speed, or to the degree, some investors may want, but that's actually a positive, as employment and the economy are not falling off a cliff. Yes, the ultra easy money of 2020 & 2021 is over.

4) Investors not too long ago, endured a bear market which bottomed in October 2022. Historically, business cycles don't produce a new bear market a mere 2 years after the previous bear bottom. Technically, it's too soon (barring some black-swan event).

5) While the Magnificent 7 are not inexpensive, narrow-driven stock markets don't fall merely because they are historically expensive. It takes a major catalyst. Today, the general market indexes, while above their historical valuations, are not in "bubbly" territory. This leaves room for upside, despite the occasional 5%-15% correction.

6) Despite the naysayers, the present war between Israel and Palestinian/Hamas supporters has not wrecked the global economy or stock markets. History has shown, despite 2 Lebanese/Israel wars, 2 Intifadas, Israel taking out 2 Middle Eastern Nuclear Reactors, and Trump recognizing Jerusalem as Israel's capital, all have not led to global bear markets, or the "Arab street" overthrowing their autocratic leaders.

7) China, always a potential geopolitical hotspot, is likely too wrapped up in numerous of its own domestic economic/real estate/banking problems to take on Taiwan in 2024.

8) The IPO market has been "graveyard" quiet for two years now. This shows a lack of froth in the stock markets, and a sign that a market peak is not at hand. Contrast this with 2021, when the market for IPOs was exploding amid a retail trading mania fueled by pandemic stimulus.

9) Finally, while you personally might not like to hear this, a Trump win in the November election (if he can stay alive financially, legally and healthwise) would be seen as a positive for the stock markets and the economy [at least in the short term], while also pleasing the Saudis, Emiratis and Israelis.

2024: The Uncertainties (Market Corrections)

1) The northern border of Israel with Lebanon represents "unfinished business" (think: Hezbollah). Herein lies a potential "Act II" in the conflict between Israel, Iran and its Arab proxies. Sixty thousand Israeli evacuees have yet to return to their homes in Northern Israel. Getting these evacuees back into their homes represents a catalyst for an additional looming conflict/showdown. An upcoming conflict that could be much more devastating than the present war in Gaza.

2) It appears that Iran presently prefers low level skirmishes with the U.S. through its proxies. However, should these incidents spiral out of control, a sustained direct confrontation between the U.S. and Iran is always a possibility – and a bear market catalyst.

3) In postwar Gaza, there are two diametrically opposed visions:

   A) According to Mohammed Dahlan, the former head of security in Gaza for the Palestinian Authority, before fleeing in exile to the UAE: "I am no friend of Hamas… but do you think anybody is going to be able to run [Gaza] to make peace without Hamas? Simply stated, Hamas has labeled anyone who works with the Israelis as traitors and threatened them with death. Several elite Palestinian families once thought to be open to the idea, are no longer.

   B) "Gaza will be run by those who do not seek to kill Israelis" according to a senior Israeli official.

The reality of the situation in postwar Gaza seems both simple and complex. As long as Gazans feel threatened by a Hamas "bullet" to the back of their heads – no new Palestinian leadership will likely arise, and the Hamas rules of Mafia-style intimidation will continue to prevail in the strip. If this were the case, Israel would be hard pressed to make political gains in postwar Gaza without the help of "Arab Friendlies", if they even exist.

In war, the "winner's curse" was well described by General Collin Powell, who was apprehensive about the U.S. invasion of Iraq. As General Powell so eloquently expressed: "you break it – you own it". In essence, the so-called "victor" is often stuck with a dirty, ugly, and thankless initial victory. Moreover, they are hardly viewed as liberators by the local population.

Perhaps, that's why the Israeli leadership has deliberately made no substantive promises or detailed plans for Gaza. Simply stated, postwar Gaza is just too unpredictable, with a question mark as to its governing body, and a territory containing a hostile population of 2 million people, the majority who remain Hamas supporters. Under these circumstances, it's not too hard to predict the rise of a future postwar guerilla insurgency.

In conclusion, in the coming months, there will be many "uncertainties", "unknowns" or a "black swan" event lurking in the background. I continue to have the majority of my wealth in equities, and the Value Contrarian Fund remains my single largest equity position. This past November I notified all investors that I was making an additional investment in the VC Fund.

The Dow Jones Industrial Average fell below 100 in 1942 when Warren Buffett made his first stock purchase. Buffett reminisces today that, "… On that fateful day in 1942 when I "pulled the trigger", I was down about $5 by the time school was out…"
Today, the Dow hovers around 39,000.

As many have pointed out before me, "It's time in the market, not timing the market".

Respectfully yours,

Domenico Marti
Contributing Editor

Benjamin D. Horwood
Portfolio Manager
March 29, 2024

Value Contrarian Equity Fund
Next Fund purchase
Date: April 22, 2024
Call today: 514–398-0808

P.S. Do visit us at our web site: **www.valuecontrarian.com**

**We're often asked: "When is the best time to invest in the Value Contrarian Fund?" Although there is no best time, since it is impossible to time the market, a preferable entry point is when the Fund has produced a month of negative returns or a year of underperformance. Unfortunately, human nature prefers the exact opposite.

Overall, long-term shareholders in the V/C Fund benefit from a sinking stock market, the same as a regular grocery shopper benefits from declining food prices. So when stock markets plummet – as they will from time to time – "neither panic nor mourn". It's good buying news for your Fund.

VCAM TECH/CRYPTO CORNER

Electric Vehicle Hangover: Is the Electric Dream Dead?

Recently, demand for electric vehicles has fallen off a cliff. While U.S. EV unit sales growth rate was 46% in 2023, this reflected a significant drop from the 76% growth the industry experienced in 2022 (according to Motor Intelligence). With interest rates at 23-year highs, one could reasonably expect a slowdown in overall vehicle demand. Analysts have explained that slowing EV sales are also due to high repair costs, vehicle range anxiety, and reliability in cold weather.

Responses

Car manufacturers and most Western governments are all in agreement – the future of fully-electric vehicles is still intact. However, it may take longer than initially expected, especially until pricing becomes more affordable for the masses. Thus, many carmakers are putting electrification investments on hold and instead placing their bets on plug-in hybrid vehicles as an interim solution to these concerns. General Motors recently announced it would be reintroducing Plug-in Hybrid EVs. Ford also postponed its planned $12 billion EV manufacturing plant investment to "more gradually" expand EV production.

According to Cox Automotive, EV owners currently complete 80% of their recharging at home. This is a significant problem for those living in buildings/complexes which have not yet been retrofitted with sufficient EV chargers. This may take many years to play out. While going fully-electric may come with vehicle range anxiety and charging station infrastructure constraints, hybrid vehicles are an easy immediate solution. Hybrids resort to their combustion engine should they run out of battery charge, thus avoiding stranded owners.

Electric Future

Overall, EV demand has undoubtedly hit a rough patch, but from its small base, EVs are far outpacing growth in the broader vehicle market. Although electric is where the future is headed, the road there will have many roadblocks. No new technology is perfect - electric vehicles are no exception. However, with all technological advances, as EVs continue to scale, initial vehicle & repair costs will fall to levels more comparable to ICE vehicles. Hopefully, buyer hesitations will be alleviated through innovation.

Year-End Management Note

It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you'll do things differently.

Warren Buffett
Berkshire Hathaway

As we have always stated, we cannot promise any particular results, only that investments for your Fund will be selected based on **value not popularity**. We view our Fund shareholders as our partners, and we assure you that the protection and growth of your capital will continue to be paramount in our thinking.

We aim not to be the biggest but to ensure consistent performance, even if that means limiting the Fund's size or closing it to new investors in the future. We want to enjoy coming to work every day and view the Value Contrarian Fund more as a private partnership, where "membership has its privileges".

Secular or disruptive technological changes to an industry or company is what truly destroys shareholder wealth and keeps us up at night (think Nortel, Abitibi, Kodak or Blockbuster). Conversely, stock-market volatility or the fear and panic of a bear market are merely temporary but opportunistic events for the rational buyer. At the end of the day, "**price paid**" is what matters most when investing for the long-term. **"Price is what you pay, value is what you get".**

Being the largest shareholder and the Manager of your Fund is certainly no guarantee of superior long-term results. But I do think one's comfort level is enhanced by having my financial interests aligned with yours. **Simply stated, your returns are my returns**.

Congrats to our new staff, Dom Marti and Moody Shaker. Both had some tough shoes to fill with Chiraz no longer with VCAM. Happily, I can say with two full audits now behind us, both of our staff have come through the fire with proficient results and dedicated teamwork.

We would like to thank our shareholders for the trust you have placed in us during this volatile past year. And again, **thanks for your referrals – much appreciated – keep them coming.**

Ben Horwood
March 29, 2024