BCV Asset Management Inc.

Q4 2023

ANTARES VALUE PORTFOLIO

The Antares Value Portfolio focuses on companies that, in our analysis, are underpriced in the stock market relative to their underlying worth as businesses. Our strategy aims first to protect investors' capital by not overpaying for a given company - holding fixed income or cash when bargains cannot be found - and second, to grow that capital through share price appreciation as the company's value gets properly recognized within the equity market.

VALUE COMMENTARY

Looking back

We have always maintained that it is protection in down years that sets up a portfolio for long term success.

The last few years have confirmed the benefits of our conservative, value-based approach to investing. The thinking is straightforward...it is easier to see long-term gains when you can keep the number of times you see declines in your portfolio, and the severity of those declines, to an absolute minimum. We have always maintained that it is protection in down years that sets up a portfolio for long term success and looking back on the last few years confirms this point. There were positive results in your portfolio in 2023, despite carrying high levels of short-term bonds. But it is really what happened in 2022 that made possible the multi-year results you are seeing now for the period ending December 31, 2023.

Some market indices have still not recovered what they lost in 2022, but your portfolio is ahead.

In both 2021 and 2023 your portfolio had positive gains, but in both years your portfolio did not grow as much as overall markets. Part of the reason for this is the high levels of cash ("dry powder" in the form of short-term bonds) your portfolio held when compared to a market that is fully invested by definition. This cash dampens returns when stock prices are otherwise rising, but protects your portfolio when stock prices are generally in decline. 2022 was a particularly bad year in the markets but not in your portfolio. Your portfolio sustained a decline of only a few percentage points, while indices declined between 9% (Canada) and 33% (NASDAQ in the U.S.). Some market indices have still not recovered what they lost in 2022 but your portfolio is ahead.

The impact of higher interest rates is likely only starting to play out in Canada and the United States. Canada is more susceptible to these higher rates.

It is precisely this protection on the downside that we believe will lead to better long-term results. The history of the value approach we take in managing your portfolio confirms the benefits of downside protection when markets are particularly risky. When you do not have to dig out of a deep hole, it is easier to climb out of it. One does not have to beat the market in the up years to beat the markets overall, if one does not participate in the market declines.

We are satisfied with the performance this past year, but not content. Our search will continue for well-run companies selling products and services that people will buy almost regardless of the economy; and of course, we will be diligent to purchase an ownership stake in those companies for your portfolio only at prices that make investing sense.

Looking ahead

Most stock prices are simply too high when compared to the actual earnings of their respective underlying companies. Stock prices (compared to underlying earnings) are still much higher than they were just before the 2008 crash. Further, U.S. stock market capitalization is currently 3 times the size of U.S. GDP. That was also the case in early 1966. Twelve years later, in 1978, the stock market was still at the same level as 1966, despite the fact the economy had grown tremendously. High prices in relation to earnings make stock prices vulnerable to sudden and severe downturns. On top of generally high prices, there is a plethora of other factors that could affect stock prices.

The impact of higher interest rates is likely only starting to play out in Canada and the United States. Canada is more susceptible to these higher rates because Canadians generally are second only to the Australians in terms of household debt in the developed world (See chart on next page). Combine already high debt levels with substantially higher interest rates and it will inevitably lead to a squeeze. At some point, higher mortgage, vehicle, and other financing costs are likely to take a bite out of other consumption. As you know, there is only so much money to go around in any household, and mortgages and car payments take precedence over trips, toys, and eating out.

The Restaurants Canada organization has stated that half of all restaurants in Canada are not breaking even right now. On top of that, many of those restaurants took out CEBA (Canada Emergency Business Account) loans during the Covid years and are now not able to pay them back. It is likely that many more restaurants may close their doors before the dust settles.

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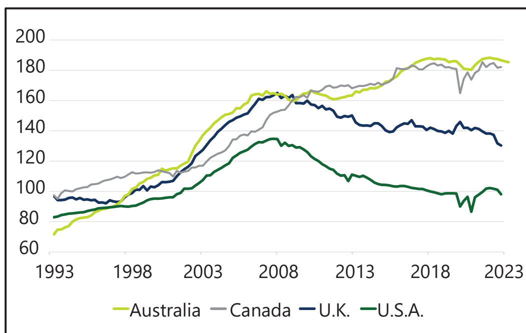
One needs to remember that interest rates respond to the expectation for inflation, and there are many factors driving up prices.

Many well known investors share a reluctance to buy in at current prices including Warren Buffett (Berkshire Hathaway), Prem Watsa (Fairfax Financial), and Tom Gaynor (Markel).

Your portfolio is invested in companies that overwhelmingly provide goods and services that people will continue to buy irrespective of how things play out economically.

Household Debt as % of Disposable Income



Source: Bloomberg.

According to the Canadian Chamber of Commerce, of all the CEBA loans taken, and despite lengthened grace periods for repayment, only 1/3 of the loans have been paid back so far. The final deadline is looming and many businesses are now scrambling to find the funds, or financing, to pay these loans back. It is likely that any re-financing is going to be more expensive than any loans that could have been taken out a few years ago when interest rates were much lower.

There is speculation that central banks will cut interest rates this year; in fact that is a major reason that stock markets rose sharply in the last three months of 2023. However, any cuts are unlikely to bring rates back to what they were before Covid, and anyone renewing a mortgage is highly likely to see larger monthly payments at renewal time.

One needs to remember that interest rates respond to the expectation for inflation, and there are many factors driving up prices, some temporary and others permanent. With the number of attacks on ships in the Red Sea, many shipping companies have started to travel the long way around Africa. That will have an impact on a significant number of goods as shipping costs will need to account for the extra days at sea to deliver goods. Paying for military escorts through the Red Sea and Suez Canal will likewise end up costing consumers more.

Inflation is also becoming more deeply seeded through various labour dispute resolutions. Stellantis (formerly Chrysler), Ford, and General Motors all settled labour disputes this year with substantial concessions and wage increases. Likewise, healthcare professionals, teachers, transit workers, and other civil servants are pushing for higher wages. These are trend setters for the broader society. When powerful labour unions extract large wage increases, even private companies are faced with raising wages to compete in the marketplace.

Your Portfolio

Stock prices are still no bargain and many well known investors share this reluctance to buy in at current prices including Warren Buffett (Berkshire Hathaway), Prem Watsa (Fairfax Financial), and Tom Gaynor (Markel). These companies (you are part owner of each of them) are sitting on high levels of cash, mostly in the form of short-term bonds. It gives me great comfort knowing that these esteemed investors are also shying away from buying at current prices. That suggests that it may be best to sit on the sidelines for now, even while we search for new investment opportunities.

One thing that bears repeating is that your portfolio looks nothing like the stock index, and as a result it will not behave or perform like the index. Your portfolio is invested in companies that overwhelmingly provide goods and services that people will continue to buy irrespective of how the various scenarios mentioned above play out. I believe your portfolio is very well protected, and having cash in the form of short-term bonds with which to go shopping when equity prices make sense, provides protection AND upside opportunity.

Thank you for your continued support and trust.

Gerry Bettig, CFA

VALUE PORTFOLIO

The Antares Value Portfolio is available to investors within a Separately Managed Account ("SMA") that holds securities directly, and through the Antares Value Pool ("Pool") which is held in the accounts of multiple investors. Data presented refer to the Pool. SMAs are customized and therefore their holdings and weights may diverge from those within the Pool. Sources for the data include: Bloomberg, NDEX, and Antares calculations. Unless otherwise stated, all data are as at quarter end.

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