April 4, 2024

# Monitoring Secular Trends – April 2024

*By Pedro Ribeiro, CIM®, FCSI® – Portfolio Manager and Cross-border Advisor*

April 1st marks the official beginning of the second quarter of the year. With the new quarter, we officially end the previous, and our team will review what went right and what went wrong. From an investment perspective, not much went wrong if we judge based on the first three months performance. However, the same performance causes us to question what can change looking ahead.

The Marnoa Growth model, which is the closest to an all-equity portfolio, finished the quarter up approximately 10%. It is during times like these, I feel it is important to remind investors that markets do not go straight up. If the performance were to continue, we would be looking at approximately 40% growth by the end of the year. As much as that would make me extremely happy, the reality is, it is unlikely to occur.

The markets go up and the markets go down. It is safe to say, we will experience some down periods in the months to come. That said, we hold onto our views of being long-term investors, not timing the markets, and welcoming pullbacks so that we can add excellent businesses to our collection. After all, we are collectors of excellent businesses.

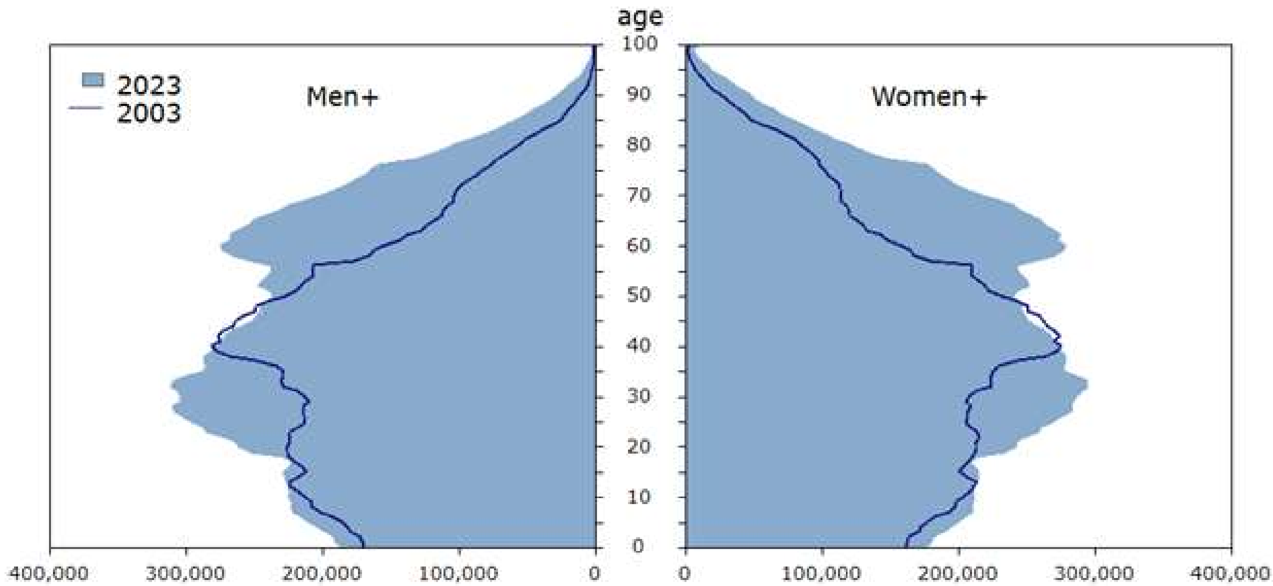
## Millennials Take Top Spot

Until recently, the baby boomers, defined as those born between 1946 and 1965 (aged 57 to 77 on July 1, 2023) held the top spot as the largest percentage of the Canadian population. As of July 2023, the millennial generation took that title. Millennials are defined as those born between 1981 and 1996 (aged 26 to 42 on July 1, 2023).

Another change occurring is the slow down in demographic aging. The proportion of the population aged 65 and older represented 18.9% as of July 1, 2023, a slight increase of 0.1 pts. However, the median age decreased and now sits at 40.6 years. According to Statistics Canada, this slow down is a result of increased immigration.[1]

Interestingly, the proportion of the working-age population—those aged 15 to 64 years—increased for the first time in 2023 after gradually declining since 2007.

[1] Statistics Canada (February 21, 2024) Millennials now outnumber baby boomers in Canada. [LINK]




Source: Statistics Canada

When taken together, the above statistics reinforce continued demand for housing. With continued demand, I would also expect valuations to remain steady going forward. I recognize there are those calling for a real-estate correction. Truth is, we've already had it in residential and office. These two segments of the real-estate market may continue to feel pressure from higher interest rates, but when we look at demographics, we remain confident that multi-family (apartments) real-estate will continue to generate attractive returns and steady income.

At Marnoa, we attempt to identify secular long-term trends. Looking at the chart above, it is clear there is a large wave of 20- and 30-year-olds supporting the need for housing for many years to come.

**Portfolio Changes**

Marnoa Moderate:

- Purchased Atkore (ATKR) and BJ's Wholesale Club (BJ)
- Sold iShares Core S&P 500 Index ETF (XSP)

Marnoa Growth

- Purchased Atkore (ATKR) and BJ's Wholesale Club (BJ)
- Trimmed iShares Core S&P 500 Index ETF (XSP)

## Atkore Inc.

**Atkore** is a leading manufacturer of electrical products such electrical cable, metal fittings, PVC and metal piping. Atkore primarily serves non-residential end-markets including new construction, infrastructure, diversified industrials, power generation, and data centers. Atkore's competitive advantage is the ability to provide customers a full line-up of infrastructure products, whereas competitors typically only sell one product. A customer could go to six competitors for product or go to Atkore with one order, one delivery, and one invoice. Atkore adds value to the customer experience with less freight costs and faster delivery times because of their large network of regional distribution centers. Atkore is benefiting from a number of secular trends, including electrification and energy transition, reshoring, the hardening of the grid (e.g., taking electrical lines underground), and the growth of data center infrastructure to meet the increasing demand for AI and cloud computing. Additionally, government stimulus programs, namely the Infrastructure Investment and Jobs Act (IIJA), Inflation Reduction Act (IRA), and CHIPS and Science Act, are cumulatively generating demand for Atkore's electrical products.

## BJ's Wholesale Club

**BJ's Wholesale Club** is a leading operator of membership warehouse clubs in the Eastern U.S. with 244 stores and 175 gas locations across 20 states. BJ's sells groceries, general merchandise, and other ancillary services to their members. BJ's product assortment is much broader compared to Costco and Sam's Club, especially in grocery and consumable goods, and 25% or more cheaper than traditional supermarkets. We believe BJ's has a promising growth trajectory supported by the company's membership and store expansion plans in Eastern U.S. markets. In the long-term, we expect BJ's store expansion could reach as far as the West Coast. We also like BJ's private label brands, Berkley Jensen and Wellsley Farms. These brands not only present an opportunity for higher margin growth, but they are also priced 20-30% lower than alternatives, providing excellent value for customers.

## Centurion Apartment REIT

*Canada's housing and rental supply cannot keep up with demand.*

We incorporate institutional-quality alternative investments, such as private real estate, private debt, and private equity, when building investment portfolios for our clients. We use alternative investments to deliver consistent risk-adjusted returns as well as to reduce portfolio volatility. Institutional investors, such as pension funds and endowments, have extensively used private market investments as a means of diversification beyond traditional asset classes like stocks and bonds. As an example, in fiscal 2023, the Canada Pension Plan's net assets totaled $570 billion, with alternative investments comprising over half of the portfolio.[2] Our clients gain exposure to private real estate through multiple alternatives including Centurion Apartment REIT.

**Centurion Apartment REIT** focuses on multi-family rental apartment buildings and student housing properties across Canada and the U.S. The firm's investment strategy is centered on buying undervalued apartment and student housing properties at reasonable capitalization rates, with low vacancies, stable tenant bases, and room for further cash flow growth. Centurion Apartment REIT has seen a number of trends over the past few years that have created favorable tailwinds in the apartment market.

Last year, many factors including strong immigration and employment growth have contributed to lower vacancy rates and higher rents. According to the Canada Mortgage and Housing Corporation (CMHC), the national vacancy rate for purpose-built rental apartments declined to a new low of 1.5% in 2023 (vs. 3.1% in 2020 and 2021 and 1.9% in 2022). This is the lowest national vacancy rate since CHMC started tracking it in 1988. Growth in the average rent for 2-bedroom purpose-built apartments ballooned to a new high of 8% (vs. 5.6% in 2022 and 3% in 2021) and well above the 1990-2022 average of 2.8%. Strong rental demand continues to outpace supply.[3]

Canada is facing a significant housing supply shortage. And as we review the data, we have the view that the housing supply and demand imbalance could continue for a long time. Here are a few factors to take into consideration:

- CHMC estimates that 18.19 million housing units could be available by 2030. However, to achieve housing affordability in Canada, CHMC estimates that there needs to be 22 million housing units available by 2030. There is a clear housing supply gap. More housing will be needed to restore affordability.[4] According to RBC, Canada's rental housing gap could exceed 120,000 units by 2026—nearly four times the current 25,000 to 30,000-unit deficit in Canada's purpose-built rental stock. To achieve a balanced market with rent stability, Canada would need to add 332,000 units to its existing purpose-built rental stock.[5] RBC indicates that a market achieves a balanced state when the vacancy rate is at 3%, but we are far away from that optimal rate.

- To ensure stability and affordability in the rental market, the obvious solution is to increase the supply of purpose-built rentals and housing in general to meet current and future demand. However, it will be challenging to meet housing demand when there is a

[2] CPP 2023 Annual Report. [LINK]
[3] CHMC (January 2024) Rental Market Report. [LINK]
[4] CMHC (September 13, 2023) Housing shortages in Canada: Updating how much housing we need by 2030. [LINK]
[5] RBC Economics (March 22, 2023) Canada's shortage of rental housing could quadruple by 2026. [LINK]

shortage of skilled labour in the construction industry in Canada.[6] According to CIBC, one-fifth of Canada's construction workforce is nearing retirement. No fewer than 300,000 will retire in the coming decade. This comes at a time when the industry is currently struggling to fill a gap of around 80,000 job vacancies—a record high vacancy rate. Like housing, the imbalance in the jobs market has contributed to rising labour costs. In fact, wages in construction are rising double the rate of other industries. Overall building costs have surged (51% in 2022 vs. 2020) because of rising prices of concrete, steel, lumber, and other materials, as well as the rise in borrowing costs due to higher interest rates.[7] Rising costs could prompt developers to slow down, which would then add more pressure to housing supply.

- Canada's population growth is outpacing housing development. The Fraser Institute reports that the difference between the number of new homes constructed and the increase in population is at its largest in the past 50 years.[8] From 2018 to 2022, Canada's population grew by 553,568 people (each year, on average) compared to an annual average of only 205,762 new homes built. In Ontario, housing completions equaled less than 30% of population growth over the same time period. Canada's population growth for the first nine months of 2023 (+1,030,378 people) surpassed the total growth for any other full-year period since Confederation in 1867.[9] A large contributing factor to population growth is immigration. Canada's immigration goals have been very aggressive, with plans to admit 1.485 million new permanent immigrants between 2024 and 2026.[10] As previously discussed, there is a shortage of homes. Canada's population growth will only add more demand into the mix, make vacancies tighter, and erode housing affordability. Housing construction simply cannot keep up.

All of these trends point to a strong apartment market. Housing shortages, rising interest rates, and cost inflation are contributing to affordability issues that have pushed individuals and families out of ownership entirely and towards rentals for accommodation—which in turn is increasing competition and pricing for rental units as rental apartment supply cannot keep up with demand.

In our view, Centurion Apartment REIT is a key beneficiary of these secular trends in the apartment market.

[6] CIBC (June 20, 2023) If they come you will build it — Canada's construction labour shortage. [LINK]
[7] RBC (June 28, 2023) Soaring construction costs will hamper Canada's homebuilding ambitions. [LINK]
[8] Fraser Institute (October 12, 2023) Housing completions not keeping pace with population. [LINK]
[9] Statistics Canada (December 19, 2023) Canada's population estimates, third quarter 2023. [LINK]
[10] RBC (March 13, 2024) How to align Canada's immigration with the future economy. [LINK]

As always, please do not hesitate to reach out, should you have any questions or wish to discuss any matter in further detail.

Yours truly,

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## OUR TEAM

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# Performance as of March 31, 2024

Gross performance results as of March 31, 2024 for our discretionary model portfolios are as follows:

| | Performance Summary (%) as of March 31, 2024 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Portfolio Mandate | 3 months | 6 months | 9 months | Year-to-date | 2023 | 2022 | 2021 | 2020 | 2019 |
| Marnoa Strategic Allocation | 5.33 | 12.28 | 10.15 | 5.33 | 10.54 | -12.70 | 12.38 | 18.01 | 15.78 |
| Marnoa Conservative | 2.23 | 5.48 | 4.20 | 2.23 | 5.69 | -12.05 | 10.86 | 9.90 | 19.86 |
| Marnoa Moderate | 6.02 | 10.47 | 13.16 | 6.02 | 12.35 | -13.55 | 12.92 | 20.79 | 25.52 |
| Marnoa Growth | 10.26 | 16.69 | 19.81 | 10.26 | 19.28 | -17.26 | 15.00 | 29.74 | 28.70 |

*The returns above are gross of fees. Individual performance may vary based on cash flows and fees. Performance figures for periods greater than 1-year are annualized. The performance data quoted represents past performance. Past performance is no guarantee of future results.*