June 1, 2023

One Dimensional

For the month of May, our managed model portfolio's generated results as follows:

Marnoa **Growth** mandate being the closest to all equity generated returns of -0.09% for the month of May compared to -5.06% for the S&P/TSX.

Marnoa **Moderate** mandate which targets a 60% equity, 30% income/cash and 10% alternative generated -1.30%.

Marnoa **Conservative** mandate with a target allocation of 40% equity, 50% income/cash and 10% alternatives generated -1.12%.

Marnoa **Strategic Allocation** which follows a typical 60/40 model but uses only ETFs and the occasional mutual fund was up -1.60%.

Monthly Activity:

Marnoa Growth:
Buys – Activision Blizzard Inc.
Sells – Trimmed Apple, Microsoft, Amazon, and Alphabet back to target weight.

Marnoa Moderate:
Buys – None
Sells – Trimmed Apple, Microsoft, Amazon, and Alphabet back to target weight.

Marnoa Conservative:
Buys – None
Sells – Trimmed Apple, Microsoft, Amazon, and Alphabet back to target weight.

Marnoa Strategic Allocation: No changes

We remained fairly quiet in the month of May. We added only a starter position in Activision Blizzard in the Marnoa Growth mandate.

Activision Blizzard ("Activision") develops, publishes, and distributes videogames for gaming consoles, PCs, and mobile devices under three operating divisions: Activision Publishing, Blizzard Entertainment, and King Digital Entertainment. Activision owns an impressive intellectual property portfolio including some of the largest and most-popular videogame franchises such as Call of Duty, World of Warcraft, Diablo, Starcraft, Overwatch, Crash Bandicoot, and Candy

Crush. In our view, these are some of the most valuable IPs and brands in the gaming industry. Activision's games are played by nearly 400 million people each month.

ATVI reported first quarter results ahead of expectations with net revenue growing by 35% y/y to $2.38B. Activision segment revenue was +28% y/y to $580M, Blizzard was +62% y/y to $443M, and King was +8% y/y to $739M. Activision's operating margin was 40% and EPS rose +70% y/y on an adjusted basis. These results are being driven by strong net bookings (+25%) growth across the company's five largest IPs (i.e., Call of Duty, Candy Crush, Warcraft, Overwatch, and Diablo).

For the next quarter, Activision expects revenue to grow at least 10%, net bookings to grow at 30% and operating income to grow at least 40%. We could see upside to Activision's outlook as pre-sales for Blizzard's Diablo IV point to a very strong launch (release date is June 6). Activision has a fortress balance sheet with a net cash position of nearly $9B.

Microsoft plans to acquire Activision for $95.00 per share in an all-cash transaction. The transaction has been approved by the boards of directors of both Activision and Microsoft and by Activision's stockholders. The deal is still undergoing regulatory approvals. A failure to close the deal will result in Microsoft paying Activision a $3 billion breakup fee. To be clear, we did not originally purchase Activision for the merger arbitrage opportunity. We consider Activision to be a great business trading at an attractive valuation today.

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Our cautious approach and under-weight allocation to equity across our model portfolios served us well compared to the S&P TSX which generated a 5% negative return for the month and up 1% year to date. In the US, the Dow Jones Industrial Average declined over 3% for the month and negative on the year, whereas the S&P 500 managed to squeeze a small gain of 0.29% for the month, but is up over 8% year to date.

In our view, the market remains one dimensional. Looking deeper, just five stocks, including Nvidia, account for over 90% of the S&P 500's gains as of month-end. Big tech has been dominating performance this year while the average performance of the remaining 495 companies within the S&P 500 has been relatively flat to negative for the year.

The stand-out was the tech-heavy Nasdaq gaining 5.92% for the month on the back of a handful of technology names. In fact, the results would be significantly different if we strip out Microsoft, Apple, Alphabet, Nvidia, Amazon, and Meta Platforms.

The chart below highlights our point that a few names are driving a majority of the gains. The six companies we listed make up more than 51% of the Nasdaq-100 index.
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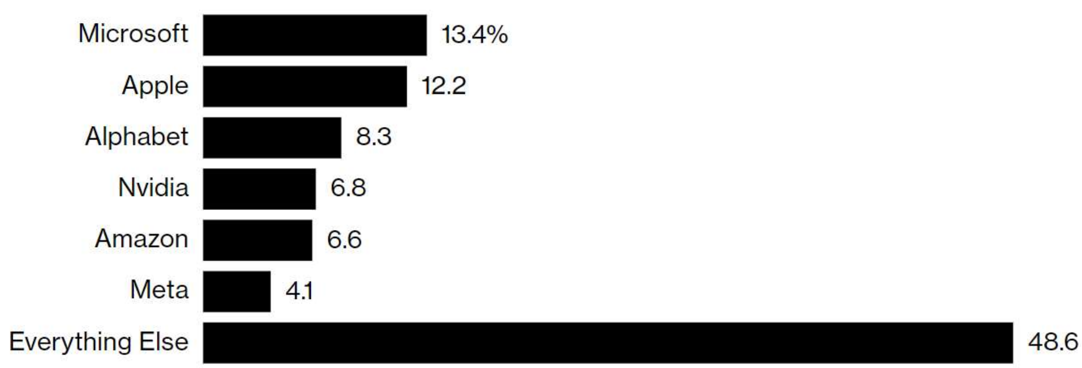
Weighing the Nasdaq 100

Stock from six companies now makes up more than 51% of the index



Source: Bloomberg
NOTE: Alphabet total is the sum of Class A and Class C shares

The bond market didn't fare much better than most indexes with yields up across the board. Except for the Canada 10 year and 20 year treasuries, bond yields ended the month all higher than where they were at the beginning of the year. As readers, you know that when bond yields rise, bond prices fall. We also know, higher bond yields are no friend to borrowers.

You may be hearing a lot about equal weighted indexes versus cap weighted. The S&P500 is a cap weighted index, and if the largest companies in the index perform well, in theory so should the index. This is exactly what is happening so far this year. The mega cap names have driven performance. If we look under the hood, we would see a different story. Companies such as Hanesbrands, Dollar General, MetLife, Estee Lauder, Pfizer, and 3M to name a few were all down over 20% year to date as of the end of May.

Cap weighted indexes work great when the mega caps are rallying. However, when the mega caps fall, the results are the opposite. A great example is Canada's very own Nortel. If you remember the name, you are probably dating yourself, but at its height in 2000, the company represented over 35% of the TSE 300 (today's S&P/TSX Composite Index).

Not only was it the most valuable company by market cap at the time, it was the ninth most valuable corporation in the world. At that time, if you bought the index you were basically buying Nortel. As Nortel rose, so did the index. However on the way down, Nortel was no friend.

For a 5 minute history lesson on Nortel's rise and fall, check out this video (click here). Disclosure: I know nothing about the YouTube channel or its content.

The point I'm trying to make, is we need to know what we own and why. We are fans of concentrated portfolios, but we also implement diversification by industry and asset class. As holdings increase in value and look great, a prudent investor is wise to trim and manage risk. Hence, the reason we trimmed some of the names we own.

Stock Market Theories

There is an old adage that goes as follows: “Sell in May and Go Away.” For those that follow seasonality trends, the belief is that you should sell your equity holdings in May and buy them back in November. Another adage is the Presidential Election Cycle theory that states the markets peak in the third year, before falling in the fourth.

A theory is exactly that – a theory. For all the evidence supporting such claims, we can produce evidence to the contrary. Evidence that cannot be disputed, is the fact that quality businesses outperform bad businesses over the long run.

A quality business in our opinion has a strong balance sheet to help it weather turbulent economic times. Growing sales, high margins, pricing power, and is a leader in its industries. The companies we hold, are in our opinion quality businesses.

As we look under the hood and identify businesses that have sold off significantly last year and continued to do so this year, our optimism as investors is growing. We are approaching a time where we will be adding to our “collection of great businesses.”

“A market downturn doesn’t bother us. It is an opportunity to increase our ownership of great companies with great management at good prices.”

Warren Buffett

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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Performance as of May 31, 2023

Gross performance results as of May 31, 2023 for our discretionary model portfolios are as follows:

	Performance Summary (%) as of May 31, 2023							
Portfolio Mandate	3 months	6 months	9 months	Year-to-date	2022	2021	2020	2019
Marnoa Strategic Allocation	1.19	-1.27	2.99	2.79	-12.70	12.38	18.01	15.78
Marnoa Conservative	0.71	-0.60	3.51	3.10	-12.05	10.86	9.90	19.86
Marnoa Moderate	1.61	0.35	4.87	4.68	-13.55	12.92	20.79	25.52
Marnoa Growth	4.70	2.87	7.15	8.56	-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.