Desjardins
Dividend Growth Fund

Desjardins Wealth Management Investments

QUARTERLY COMMENTARY AS OF DECEMBER 31, 2022

JARISLOWSKY FRASER
GLOBAL INVESTMENT MANAGEMENT

PORTFOLIO MANAGER:
Jarislowsky Fraser

INCEPTION DATE:
January 15, 2009

CIFSC CATEGORY*:
Canadian Dividend & Income Equity

Portfolio positioning

In the fourth quarter of 2002, we initiated a position in **TC Energy**, a Canadian company primarily exposed to natural gas transportation. The natural gas market is in transition due to the Russian invasion of Ukraine, and the company's US-bound exports are expected to ramp up considerably between now and 2030. To fund the purchase, we reduced some overweight positions (**Canadian National Railway**, **Thomson Reuters Corp.**, **Restaurant Brands**, **Alimentation Couche-Tard**) that had done quite well.

We also liquidated our position in **Ritchie Brothers Auctioneers** due to a change in alignment with our investment thesis—we're not convinced of the synergies in the company's announced acquisition of IAA. We're very familiar with the main competitor of the acquired company as it's one of the holdings in our US portfolio. In our view, IAA is at a structural disadvantage and addressing it will be more challenging and costly than assumed. In our international holdings, we significantly trimmed our position in French insurer **AXA**, which performed well.

Investment thesis

No changes were made to the investment thesis during the quarter. In terms of valuations, it's known that the longer the time horizon, the greater the correlation between current valuations and market returns. There's a higher than 80% correlation between 10-year US stock market returns and current valuation data. According to this metric, current valuations indicate positive stock market returns of up to 8%, depending on valuation levels. While it's nowhere near an exact science—the small uncorrelated component could significantly skew return projections and there's naturally some degree of variability involved with averages—it's still a good place to start for discussing future returns. And lastly, in the event the market hasn't fully priced in some headwinds, including the risk of a recession, it could create good buying opportunities for long-term investors like us. With that in mind, we'll be continuing to scope out potential buys where we can get in at a good price.

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Securities that made headlines

Top contributors this quarter include **Restaurant Brands** (+20%), **Magna International** (+17%) and **CAE** (+24%). Restaurant Brands International (QSR) reported an 11% increase in network sales, driven by impressive growth from Tim Hortons (13%), consistently strong performance from Burger King International (growth of over 20%) and continued evidence that Burger King USA is closing the gap with its rivals. On top of these outstanding results, it's an attractive stock, trading at a significant discount compared to its peers, which should help it generate differentiated returns going forward.

Magna International, the world's third largest auto parts supplier, has recovered somewhat since investor sentiment bottomed out at the end of the third quarter. With supply chains strained from the pandemic, motor vehicle production has remained at recession levels; it's expected to pick up despite recession risks.

CAE, the world's leading aviation training provider, bounced back from a lacklustre third quarter marred primarily by an untimely special expense (project impairment loss) in its defence business. The company's recent results were very strong, showing solid revenue growth and improved margins and confirming that the expense in its defence business is one-time only. The stock's margins and valuation should continue to rise as the aviation industry returns to normal.

Detractors from the portfolio's fourth-quarter performance included **CCL** (-13%) and **Brookfield** (-22%), in addition to our lack of energy exposure. In the case of global specialty packaging company CCL, despite solid results and fundamentals, cautious comments from management about short-term growth in light of macroeconomic risks caused the stock to slump. That said, the company is largely exposed to non-discretionary products, which are less economically sensitive, and CCL has a history of taking advantage of challenging economic conditions to shore up its business and make a strong return on capital. The company is well positioned, considering the $1.7 billion in excess capital it has in its coffers.

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Securities that made headlines (cont'd)

As for Brookfield, the asset management company underperformed due to the potential impact of long-term interest rates on inflows into alternative assets and the value of its real estate portfolios (Brookfield is a major commercial landlord of office space in large urban centres such as New York, London and Toronto). While there's evidence of a strong decline in real estate prices in some markets, we believe interest rates would need to be a whole lot higher than they currently are to halt inflows into alternative assets. Plus, a slide in property prices (higher capitalization rates) will likely open up acquisition opportunities for Brookfield.

*CIFSC refers to Canadian Investment Funds Standards Committee. The CIFSC has the mandate to standardize the classification of mutual funds in Canada. http://www.cifsc.org/.