Mawer Tax Effective Balanced Fund, Series A

Q4 2022 | Performance Commentary

Market overview

Equity markets had a positive return in the fourth quarter offering a brief reprieve from the turmoil that roiled markets in 2022—although December saw many give back some of these gains. And, after one of the worst years on record, Canadian bonds finished near flat for the quarter. In the end, 2022 goes down as a difficult year for financial markets dominated by widespread inflation, higher interest rates, geopolitical tensions, and global growth concerns. The Bank of Canada and the U.S. Federal Reserve continued to raise policy interest rates, and while the path forward remains uncertain, the Bank of Canada left the door open to slowing its hiking cycle. For Canadian investors, the return of many foreign asset classes, with the exception of the U.S., benefitted from a currency translation effect over the quarter.

Performance commentary

The Mawer Tax Effective Balanced fund outperformed its blended benchmark over the quarter.

Reflecting the broad nature of the market's advance during the quarter, the vast majority of portfolio holdings delivered positive returns. Some of the stronger performers across our equity funds were those that could be classified as more economically sensitive in nature, bolstered by the market's hope that central banks may not need to be as aggressive as feared in tightening monetary policy with the latest inflation prints having shown signs of moderation. This included companies such as footwear and apparel brand **Nike**, coffee machine manufacturer **De'Longhi**, and industrial equipment dealer **Finning International**. Other standout performers included health care giant **Novo Nordisk** and specialty insurer **Trisura Group**, with both companies reporting strong results.

On the other hand, several of our portfolio holdings declined in the fourth quarter. A few technology-focused companies, some having proposed or announced cutbacks in their workforce ahead of a potential recession, continued to be some of the most knocked down stocks in the market. Holdings in companies such as **Amazon.com** and **Alphabet** (Google) had their stock prices lag the broader market.

We have been working on an inventory list of high-quality ideas and we believe we are well positioned to start buying when it makes sense. In the recent past, many high-quality companies have demanded a premium in the market, and the pullback we have seen in 2022 has provided the opportunity to invest in some of these businesses at a more reasonable valuation.

From an asset mix perspective, we did not make any adjustments this quarter. The future remains quite uncertain and there wasn't a high degree of conviction or perceived edge to deviate from a near neutral equity weight while also holding a higher-than-normal level of cash equivalents. There are many narratives of possible paths forward; we are not looking to predict this path, but stay open to multiple scenarios and guard against heavily tilting towards one outcome.

Looking back over the full calendar year, a portion of the Mawer Tax Effective Balanced Fund's underperformance in 2022 can be attributed to the first quarter and the market's initial adjustment to higher interest rate expectations which disproportionately hurt many of our equity portfolios given our focus on higher quality businesses. In retrospect, we acknowledge that many of our equity portfolios could have been better balanced with respect to interest rate sensitivity, and much of the activity in the early part of the year sought to re-establish this balance.

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Looking ahead

There is little doubt that it has been a tough year for markets, and the path central banks take in 2023 is still up for debate as inflation remains high, global growth appears to be slowing, and the employment market remains resilient. Further complicating matters, yield curves are inverted which historically has been a reliable indicator of recessions. Whether we end up with a soft or hard landing may rest on how persistent inflation will be.

Compared to historical standards, we are experiencing a very rapid pace of interest rate hikes by central banks, notably after a prolonged period of loose monetary policy. With corporate debt levels higher than the recent past and with elevated interest rates, there is the potential for interest expenses to rise materially for companies with higher leverage. Depending on the path forward, the environment for companies with more corporate debt could prove more challenging.

This year we have seen gravity restored to the system as discount rates have increased. While this adjustment process, along with its impact on valuations, can be volatile and difficult, we believe we are ultimately heading to a place where returns will be driven more directly by company fundamentals. We also recognize that in times when emotions run high, we must guard most fiercely against temptations to stray from our philosophy and process. We continue to play the plan focusing on buying wealth-creating companies, with excellent management teams, trading at a discount to our estimate of intrinsic value.

Performance summary[1] (%)
As of December 31, 2022:

	YTD	3 Mo.	1 Yr.	3 Yrs.	5 Yrs.	10 Yrs.	Since Inception[2]
FUND	(12.4)	5.3	(12.4)	1.9	3.9	7.4	7.5
BENCHMARK	(9.6)	5.1	(9.6)	3.3	4.1	6.6	7.5

Calendar Year, as of December 31:

	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013
FUND	(12.4)	9.2	10.7	14.9	(0.3)	9.9	3.3	10.2	12.2	20.1
BENCHMARK	(9.6)	10.0	10.7	14.2	(2.7)	8.4	7.4	6.2	9.5	14.6

[1]Performance figures are net of management fees and operating expenses. Periods greater than one year are annualized. Performance figures are in Canadian dollar terms.
[2]Mawer Tax Effective Balanced Fund Series A Inception: January 8, 1988

Selections from Mawer's Art of Boring blog and podcast:

Quarterly Update | Q4 2022 | EP125
A review of last quarter, the major themes and takeaways from 2022, and what's on the horizon for the new year.

Inflation's One-Two Punch
It's inflation's second punch that can deliver a blow that investors may not be expecting.

S-Curves and the Adoption Cycle | EP124
What investors can learn from the S-curves of technologies both old and new.

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Benchmarks:

FUND	BENCHMARK
Mawer Tax Effective Balanced Fund	Jan 2012: 5% 91 Day Treasury Bill, 35% FTSE TMX Canada Universe Bond, 15% S&P/TSX Composite, 15% S&P 500, 15% MSCI EAFE (net), 7.5% BMO Weighted Small Cap (Blended), 7.5% Russell Global Small Cap Aug 2013: MSCI EAFE (net) returns is used to calculate the blended benchmark from inception. Previously, MSCI EAFE (gross) was used. Oct 2015: 5% 91 Day Treasury Bill, 30% FTSE TMX Canada Universe Bond, 5% FTSE WGBI, 15% S&P/TSX Composite, 7.5% BMO Small Cap (blended), 15% S&P 500, 15% MSCI EAFE (net), 7.5% Russell Global Small Cap Oct 2016: 5% 91 Day Treasury Bill, 30% FTSE TMX Canada Universe Bond, 5% FTSE WGBI, 15% S&P/TSX Composite, 7.5% S&P/TSX Small Cap, 15% S&P 500, 15% MSCI ACWI ex-USA (net), 7.5% MSCI ACWI Small Cap (net) June 2021: Jun, 2021: 5% FTSE Canada 91 Day TBill Index, 35% FTSE Canada Universe Bond, 15% S&P/TSX Composite, 7.5% S&P/TSX Small Cap, 15% S&P 500, 15% MSCI ACWI ex-USA (net), 7.5% MSCI ACWI Small Cap (net)

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