FOCUS PARTNERS CANADA

quarter ending in December 31, 2024

Quarterly Newsletter

A Mixed Quarter, a Banner Year

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The fourth quarter of 2024 saw mixed results with U.S. and Canadian stocks advancing, while bonds and International stocks fell. 2024 as a whole will go down as a year when just about every investment asset class contributed in positive ways to total returns. It was a strongly positive year for investors of virtually all risk profiles, whether in U.S. and Canadian stocks, floating-rate bonds, or trend following and private assets.

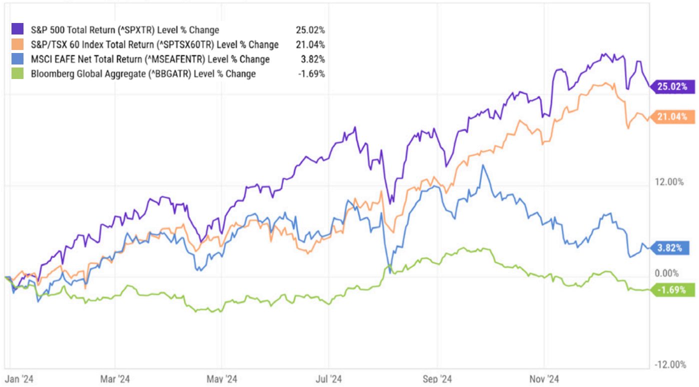
U.S. stocks gained 5.9% for the quarter in USD, with the S&P 500 finishing the year with a whopping 25.0% return. While the gains were robust, it was also impressive how smoothly markets behaved, with the S&P 500 hitting 57 all-time highs over the course of the year − without even a single typical correction of 10%.

Canadian markets also did well during the quarter, rising 3.8% in CAD to bring the return on the S&P/TSX 60 to 21.0% for 2024 − its best return since 2019. At the time of this writing, Justin Trudeau has just announced plans to resign and has prorogued Parliament until March 24th. But financial markets were not dramatically impacted, and the Canadian dollar actually rallied slightly against the USD on the news. Much will be determined in coming months, with new leadership and an election occurring later in the year. There are also some unresolved issues still pending, such as the finalization of the proposed increase in the inclusion ratio of capital gains. That being said, and despite this legislation not being officially passed or receiving Royal Assent, CRA has initially signaled that they will be assessing taxpayer returns for the 2024 tax year under the proposed rules.

International Developed were hurt by depreciating currencies compared to the USD and fell 8.1% for the quarter, bringing 2024 returns down to a meager 3.8%. Emerging Markets followed suit, off 8.0% in USD, with a slightly better gain of 7.5% in 2024.

The combination of sticky inflation numbers, robust economic growth, and uncertainty around U.S. tariff and immigration policy led longer term interest rates higher in the U.S. The U.S. Federal Reserve and the Bank of Canada both continued their rate cutting cycles, although the U.S. Fed signaled that a pause may be in store for early 2025. For the quarter, U.S. Bonds were down 3.1% − erasing much of the year's gains to finish up just 1.3%. In Canada, bonds proved more resilient, ticking down just 0.5% for the quarter and tacking on 3.0% for the year. Global bonds, as shown in the chart below, were slightly negative for the year.

Annual Index Returns



If you paid attention to financial headlines over the past few years, you were told that a recession was eminent, geopolitical events around the world would derail markets, and/or that the

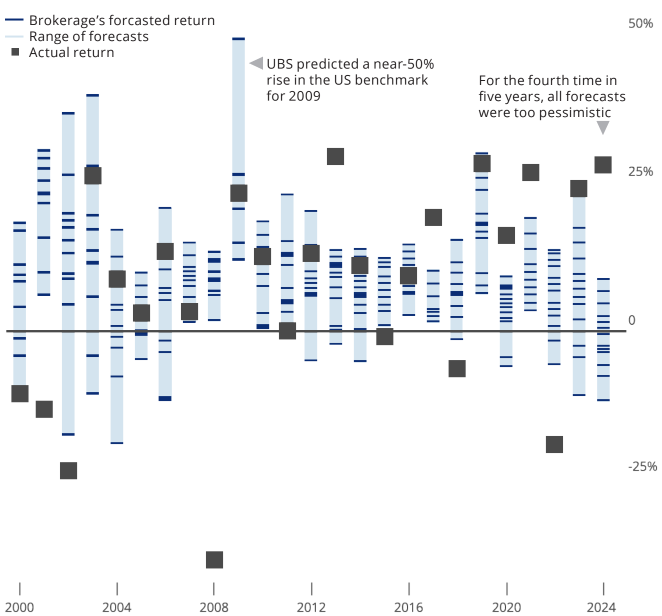
Clients of Cardinal Point are strategically invested with a focus on long-term performance objectives. We evaluate and report on market and economic conditions to provide our investors with perspective and to put portfolio performance in context, but we do not make sweeping model changes based on short term market movements.

Fed's every move was a mistake. Yet, the stock market is now 18% higher than the average Wall Street strategist anticipated for 2024, and dramatically higher than the most optimistic forecast of the bunch.

Bloomberg reviewed the range of forecasts from Wall Street brokerages predicting annual gains in the S&P 500, as shown in the chart below. The range was varied, although most of the time the consensus was somewhere around a 0-10% gain. That's reasonable given that the historical average return has been in the high single digits.

Strategic Often Miss the Mark When Forecasting

Predicted and actual returns for the S&P 500 Index



Source: Bloomberg
Note: Forecasts and actual returns are for price change only.

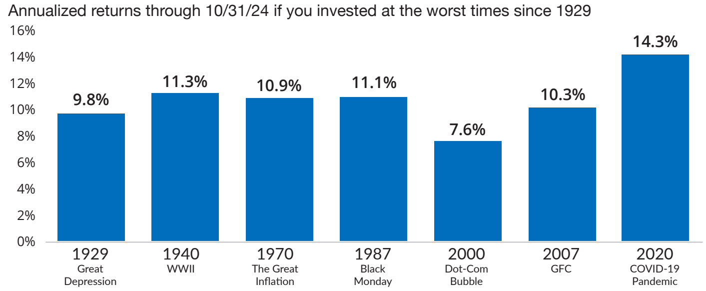
What is evident from the chart is that those forecasts do not do a good job of predicting very good or very poor market performances. Take 2008 for example. While signs of a meaningful slowdown were emerging in the second half of 2007, yet all firms in the survey forecasted positive returns. Just 12 months later the index had lost nearly 40% of its value.

Conversely, heading into last year, overall forecasts were at the lower end of forecasts over the past 20 years. Yet markets moved resoundingly higher with a 25.0% gain, marking the 4th time in five years that all forecasts were overly pessimistic.

A common concern for investors is the impact that being invested or starting to invest right before a major market correction can have on dooming their long term prospects. While losses at any point are painful, and can leave a mark on long term performance, I think the chart below (from Ben Carlson at Ritholtz Wealth Management) is an excellent illustration of just how resilient returns for long term investors have been. For example, if you had invested with the worst timing just before the Great Financial Crisis that started in 2007, and held on through Oct of 2024, you would have realized a 10.3% return on the index over that timeframe. Similar scenarios happened with those investors who got started right before the 1987 crash or World War II.

Investing at the worst times

Annualized returns through 10/31/24 if you invested at the worst times since 1929



For those investors who simply tuned out the noise and stuck to their long-term plan, these last 24 months have provided excellent returns in just about every asset class. Make no mistake − investing won't always be this easy. There are plenty of potential risks on the horizon and historical returns are no guarantee of future results. We expect markets to experience a meaningful correction in the future, as markets periodically do. If we can keep our view on the much longer time horizon historically markets have delivered excellent returns to patient long term investors.

Bitcoin in Investment Portfolios:
Balancing Opportunity and Risk

The recent rise of bitcoin's price and prominence has sparked intense debate in the investment community about its role in modern portfolios. Recent developments, particularly the approval of spot bitcoin ETFs and increased institutional adoption, have further intensified this discussion. Before we elaborate on the current status, it's useful to take a step back and review the origins and original intent of this cryptocurrency.

Understanding Bitcoin

Bitcoin emerged in 2009 as the world's first decentralized digital currency, introduced by an anonymous creator or group using the pseudonym Satoshi Nakamoto. At its core, bitcoin is a peer-to-peer electronic payment system that operates without the need for intermediaries like banks or governments.

Key Characteristics

- **Fixed Supply**: Only 21 million bitcoins will ever exist, with new coins released on a predetermined schedule through a process called mining
- **Decentralization**: No single entity controls the network; it's maintained by a global network of computers
- **Transparency**: All transactions are recorded on a public ledger called the blockchain
- **Security**: Protected by advanced cryptography and the distributed nature of the network
- **Accessibility**: Can be sent anywhere globally, 24/7, without traditional banking infrastructure

The Case for Bitcoin in Portfolios

Bitcoin can potentially offer two main benefits as a portfolio component:

Asymmetric Return Potential: Bitcoin's structure as a fixed-supply digital asset creates the potential for significant price appreciation if institutional adoption continues to increase. The asymmetric nature of potential returns means that a small allocation could have a meaningful impact on overall portfolio performance.

Inflation Hedge Properties: Bitcoin's fixed supply cap of 21 million coins provides theoretical protection against monetary debasement and inflation. While this theory remains largely untested across different economic environments, it may offer a unique potential hedge against monetary policy risks.

In 2024 the cryptocurrency landscape underwent significant transformation with several key developments:

- **Spot Bitcoin ETF Approval** The SEC's approval of spot bitcoin ETFs in U.S. markets marked a watershed moment for the asset class, providing easier access for institutional investors and retirement accounts. This development reduced many of the technical barriers to bitcoin investment while also adding regulatory clarity.
- **Institutional Adoption** Some financial institutions have expanded their cryptocurrency offerings, reflecting growing mainstream acceptance. Traditional finance's increasing embrace of bitcoin has contributed to more stable market infrastructure and improved liquidity.

Key Risks to Consider

While these developments have been positive, no asset is a guarantee and price is simply a function of the interaction of buyers and sellers in the market. Investors need to be aware of the substantial risks that must be carefully weighed:

Extreme Volatility

Bitcoin's volatility has been remarkably high throughout its history, far exceeding that of traditional assets:

- The asset has experienced multiple drawdowns of over 80%, including an 84% decline from December 2017 to

December 2018, and an 83% fall during 2022's "crypto winter."

- Even with increased institutional involvement in more recent years, 30-day price swings of 20-30% remain common.
- Bitcoin's historical annual volatility has averaged around 60-80%, compared to roughly 15-20% for the S&P 500.
- The asset has seen single-day price movements exceeding 10% more than 200 times in its history.
- In the bull market of 2021, bitcoin saw a rise from around $29,000 to $69,000 before falling back to under $16,000 in 2022 − that's a 138% gain followed by a 77% decline.

These extreme price movements mean that investors must be prepared for:

- Portfolio values potentially dropping by 50% or more in relatively short time periods
- Years-long recovery periods following major drawdowns
- The psychological challenge of maintaining positions during severe market stress
- The possibility that historical drawdowns could repeat despite increased institutional involvement

For context, traditional assets rarely see drawdowns of this magnitude - the S&P 500's worst drawdown was approximately 86% during the Great Depression, with its next largest being 56% during the 2008 Financial Crisis. But bitcoin has seen multiple drawdowns exceeding 70% in just its first 15 years of existence.

Portfolio Allocation Guidelines

As an Investment Committee we have reviewed bitcoin exposure options. Considering some of the regulatory and volatility concerns, we have determined that at this particular time it does not merit a place as a default option in our clients' portfolios. Yet we have discussed the asset with many clients, some of whom have then invested in it on their own through outside platforms, and for a small number of clients we have helped implement a bitcoin position in their portfolios at Cardinal Point.

In general we have suggested that for most investors who are interested in the asset class something between a 2-4% position would be enough, so that in the event of continued outperformance by bitcoin it would have a meaningfully positive impact on total portfolio returns. That would also help ensure that if the price were to fall dramatically or stagnate for the long term, it would be unlikely to derail a long term investment plan. If we assume that the historical volatility of bitcoin will continue into the future at around 70%, and examine other historical correlations, an introduction of a 3% weight introduced into a 60% stock, 40% bond portfolio would increase overall portfolio volatility by about 5-10% from previous levels.

In a recent paper from BlackRock, *Sizing Bitcoin in Portfolios*, Dec 2024, they viewed volatility from a different lens and showed that a 2% allocation to bitcoin would introduce a level of risk similar to what a traditional 60% stock, 40% bond investor would see from any one of the largest companies by market cap, such as Apple, Microsoft or Nvidia (the study looked at the Magnificent 7: Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla from 2012 to 2024) . They noted that adding higher amounts than that can dramatically increase the overall volatility of a portfolio, as bitcoins' contribution to risk has historically risen during periods of overall stock market volatility. They believe there is a higher risk of bitcoin going toward a low level than the risk that one of those large technology companies cited above might experience a similar scenario.

While we do not recommend the asset class for everyone, for those who are interested in it, here are some additional considerations:

Implementation Strategies

ETF Consideration: With the introduction of spot bitcoin ETFs earlier in Canada and more recently in the U.S., investors now have a regulated, traditional investment vehicle option. These products may be suitable for investors seeking simplified exposure without direct cryptocurrency custody.

Dollar-Cost Averaging: Given bitcoin's volatility, a disciplined dollar-cost averaging approach often makes more sense than large lump-sum investments. This helps reduce the impact of timing decisions and psychological pressure.

Regular Rebalancing: Bitcoin's price movements can quickly shift portfolio allocations away from targets. Regular rebalancing (quarterly or annually) helps maintain intended exposure levels and can potentially improve risk-adjusted returns.

Investment Vehicle Selection: Investors must choose between direct bitcoin ownership, ETFs, or other investment vehicles. Each approach has distinct tradeoffs in terms of costs, security, and complexity that should align with the investor's capabilities and preferences.

Exit Plan: Is bitcoin going to represent a long-term hold and allocation within your portfolio, or is there a shorter-term goal to hold for the next 2-3 years or to realize a certain return figure? With an asset class that can see dramatic moves and is still highly speculative, having an exit plan in place can help combat the emotions that come with large price swings. Having a plan for both the upside and downside ahead of time is paramount regardless of the asset, and with a more volatile asset like bitcoin it is more important to remove the emotions that come with volatility.

Conclusion

Bitcoin represents a unique asset that can potentially enhance portfolio returns and diversification. Recent developments, including the Trump election win, have made it more accessible and institutionally accepted, but its risks still demand a thoughtful and measured approach to allocation.

It's impossible to know where the price will be a year or a decade from now, or what the 'right' or 'fair' price should be. For most investors, the risks and volatility involved mean that bitcoin likely does not merit consideration as a holding. But for those where it does, they should treat bitcoin as a small, speculative portion of their portfolio, rather than a core holding.

The appropriate allocation ultimately depends on individual circumstances including risk tolerance, investment timeline, and technical sophistication. Regular review and rebalancing of bitcoin exposure helps ensure that it remains aligned with overall investment objectives while managing its unique risks.

Remember that the cryptocurrency market continues to evolve rapidly, and these guidelines should be regularly reassessed as the asset class matures and market structure develops. If you would like to discuss the asset class further, please reach out to your portfolio manager and we'd be happy to review some of the pros and cons above in further detail.

Financial Markets Review

The USD View

Data from recent months indicates that the U.S. economy is still growing at a robust pace. Job growth numbers were slightly erratic last fall, with multiple labor strikes and large natural disasters disrupting figures, but significantly bounced back recording over 200k new jobs created in November and December. For 2024 the economy added an average of 186k jobs a month, which is a very healthy level. The unemployment percentage rate was steady in the low 4s for the second half of the year, most recently at 4.1%. That's higher than the lows of 2023, but not showing any concerning signs of spiking.

Our most recent measure of overall growth in GDP came in at 3.1% for Q3 2024, a continued recovery from the slightly lower Q1 growth rates. As we start to get the last of the data for Q4 2024, early indications are that growth has remained solid, around 2.7%. That indicates that the economy is still nowhere near the recession or hard landing feared and predicted over the past few years.

Inflation appears to be stuck in neutral. We've now seen a moderate growth rate of 2.7% over the last 12 months, slightly higher than a quarter ago. Those numbers are still above the Fed's target of 2.0%, and appear to be stubbornly sticky. However, the volatility within the monthly data was dramatically lower in 2024, and there are currently very few signs of any runaway or accelerating inflation.

The continued strong economy and the concern that some Trump administration proposed policies such as tariffs or immigration changes could add to inflationary pressures led to a down quarter for bonds, as rates rose throughout the quarter. Modestly higher yields aren't necessarily a bad thing. I'd much rather see a strong economy and yields at 5% than a recession and yields at 2%. Those rising borrowing costs can be a headwind to bond returns and act as a drag on businesses and consumers. The Bloomberg U.S. Aggregate Bond Index declined by 3.1% for the quarter, dropping its 2024 return to a measly 1.3%. Most recently, in December the Fed made a much-anticipated additional rate cut, bringing overnight rates down into the mid 4% range. Expectations are now for just 1-2 additional cuts in 2025, with an expected pause to start off the year. With overnight rates unlikely to dip below 4% in the near term, 10-year rates around 4.5-5.0% levels seem reasonable.

For stock markets, the S&P 500 tailed off in December, but still had a positive quarter, advancing 2.4% to end the year with a tremendous gain of 25.0%, nearly matching the previous year's gains of 26.3%. There were minor down days and wobbles here and there, but overall the year was remarkably smooth, and the index made 57 new all-time highs, the 5th most in history! International Developed Market companies, on the other hand, as measured by the MSCI EAFE Index, struggled – due in large part to a surging U.S. Dollar and concerns about the impact tariffs may have on foreign companies. The index declined by 8.1% for the quarter, turning in a lackluster annual gain of just 3.8%. Emerging Markets, as measured by MSCI Emerging Markets, after a fantastic Q3 gave back half of those gains with an 8.0% loss for the quarter and an annual return of 7.5%.

Within the U.S. market, returns were highest among large and mid-sized Growth companies. Value oriented stocks took a small step back in the quarter, though all broad areas of the U.S. market finished well into positive territory for the year.

US Stocks
Q4 2024

	Value	Blend	Growth
Large	-2.0%	2.7%	7.1%
Mid	-1.7%	0.6%	8.1%
Small	-1.1%	0.3%	1.7%

International Stocks
Q4 2024

	Value	Blend	Growth
Large	-6.4%	-7.6%	-8.7%
Mid	-7.0%	-6.8%	-6.6%
Small	-8.1%	-7.9%	-7.6%

International Developed Markets were a sea of red this quarter, impacted broadly by the impact of a strengthening USD, which makes International returns appear weaker when converted into USD. At some point that will likely reverse, but 2024 was another year of International falling behind.

Asset classes ranked by annual returns (in USD)

2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2024 Q4
US REITs 4.5%	US Small Value 31.7%	Emerging Markets 37.3%	Cash 1.9%	US Stocks 31.5%	US Stocks 18.4%	US Small Value 28.3%	Cash 1.5%	US Stocks 26.3%	US Stocks 25.0%	US Stocks 2.4%
US Stocks 1.4%	Canadian Stocks 24.9%	Intl Stocks 25.0%	US Bonds 0.0%	Canadian Stocks 29.5%	Emerging Markets 18.3%	US REITs 24.5%	Alternatives -5.7%	Intl Stocks 18.2%	Canadian Stocks 13.0%	Cash 1.2%
US Bonds 0.5%	US Stocks 12.0%	US Stocks 21.8%	Alternatives -3.2%	US REITs 23.1%	Intl Stocks 7.8%	Canadian Stocks 19.8%	Canadian Stocks -11.4%	Canadian Stocks 16.0%	US REITs 8.1%	US Small Value -1.1%
Cash 0.1%	Emerging Markets 11.2%	Canadian Stocks 16.8%	US REITs -4.2%	US Small Value 22.4%	US Bonds 7.5%	US Stocks 15.9%	Intl Stocks -14.5%	US Small Value 14.6%	US Small Value 8.1%	Canadian Stocks -1.5%
Alternatives -0.7%	US REITs 6.7%	US Small Value 7.8%	US Stocks -4.4%	Intl Stocks 22.0%	Canadian Stocks 6.6%	Intl Stocks 11.3%	US Bonds -13.0%	US REITs 14.0%	Emerging Markets 7.5%	Alternatives -1.9%
Intl Stocks -0.8%	Intl Stocks 1.0%	Alternatives 7.1%	US Small Value -12.9%	Emerging Markets 18.4%	Alternatives 6.4%	Alternatives 7.2%	US Small Value -14.5%	Emerging Markets 9.8%	Cash 5.2%	US Bonds -3.1%
US Small Value -7.5%	US Bonds 2.6%	US REITs 3.8%	Intl Stocks -13.8%	Alternatives 9.3%	US Small Value 4.6%	Cash 0.1%	US Stocks -18.1%	US Bonds 5.5%	Alternatives 4.3%	US REITs -5.9%
Emerging Markets -14.9%	Alternatives 1.3%	US Bonds 3.5%	Emerging Markets -14.6%	US Bonds 8.7%	Cash 0.7%	Emerging Markets -1.2%	Emerging Markets -20.1%	Alternatives 4.4%	Intl Stocks 3.8%	Emerging Markets -8.0%
Canadian Stocks -23.5%	Cash 0.3%	Cash 0.8%	Canadian Stocks -15.3%	Cash 2.3%	US REITs -11.2%	US Bonds -1.6%	US REITs -26.0%	Cash 5.0%	US Bonds 1.3%	Intl Stocks -8.1%

The CAD View

Growth and employment rates for the Canadian economy continue to lag behind the U.S. The unemployment rate ratcheted up to 6.8% during the quarter − a concerning rise from 5.7% at the start of 2024. New job creation was stronger at the end of the year, which was a bright spot, most recently with 54k jobs added in November.

Real GDP growth in 2024 was steady yet sluggish, with a 1.0% annualized growth in Q3, a bit lower than the first half the year. Inflation continued to be a bright spot, with year-over-year price increases falling to just 1.6% in November, and a meaningful reduction in monthly volatility over the last six months.

Bond yields in Canada ticked up very slightly during the quarter, causing the Bloomberg Barclays Global Canada Index to register a slight decline of 0.5%, finishing 2024 with a 3.0% gain.

Cdn Stocks
Q4 2024

	Value	Blend	Growth
Large	4.3%	4.3%	4.5%
Mid	3.0%	5.4%	6.4%
Small	-1.4%	2.9%	7.2%

Canadian stocks, as measured by the S&P/TSX 60, continued an excellent year with a 3.8% return, bringing the annual gain to 21.0%, the highest since 2019. U.S. stocks, as measured by the S&P 500, rose by 9.0% in CAD for the quarter, to finish the year up 36.4% in CAD terms. International stocks fell 2.2% in CAD for the quarter, up 13.2% for the year.

Canadian markets saw robust gains in most areas. Large companies and more Growth oriented areas led the way for the quarter, with all segments seeing strong annual returns.

Asset Classes Ranked By Annual Returns (In CAD)

2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2024 Q4
US Stocks 21.6%	Canadian Stocks 21.1%	Intl Stocks 16.8%	US Stocks 4.2%	US Stocks 24.8%	US Stocks 16.3%	Canadian Stocks 17.5%	Canadian Stocks -5.8%	US Stocks 22.9%	US Stocks 36.4%	US Stocks 9.0%
Intl Stocks 19.0%	US Stocks 8.1%	US Stocks 13.8%	Canadian Bonds 2.5%	Canadian Stocks 22.9%	Canadian Bonds 7.4%	US Stocks 15.3%	Intl Stocks -8.2%	Intl Stocks 15.1%	Canadian Stocks 21.0%	Canadian Stocks 3.8%
Canadian Bonds 3.7%	Canadian Bonds -0.3%	Canadian Stocks 9.1%	Intl Stocks -6.0%	Intl Stocks 15.8%	Intl Stocks 5.9%	Intl Stocks 7.7%	Canadian Bonds -9.9%	Canadian Stocks 12.1%	Intl Stocks 13.2%	Canadian Bonds -0.5%
Canadian Stocks -8.3%	Intl Stocks -2.5%	Canadian Bonds 0.1%	Canadian Stocks -8.9%	Canadian Bonds 3.7%	Canadian Stocks 5.6%	Canadian Bonds -3.8%	US Stocks -12.2%	Canadian Bonds 5.0%	Canadian Bonds 2.9%	Intl Stocks -2.2%

Indexes used: Cash represented by ICE BofAML 3M U.S. Treasury Notes. MSCI Canada, MSCI World Ex USA and U.S. Russell series used for Large Value, Large Blend, Large Growth, Mid Value, Mid Blend, Mid Growth, Small Value, Small Blend, Small Growth representations. Alternatives in USD and CAD charts represented by Credit Suisse Liquid Alternative TR USD . Nominal Broad U.S. Dollar index for USD comparisons. Additional representations in CAD: Canadian Bonds- Bloomberg Barclays Global Canada, Canadian Stocks- S&P/TSX Composite TR, U.S. Stocks S&P 500 TR, International Stocks- MSCI EAFE NR. Additional representations in USD: Short International Bonds- FTSE WGBI 1-5Yr Hdg, U.S. stocks- S&P 500, U.S. Value- Russell 1000 Value, U.S. Small- Russell 2000, U.S. REITs- DJ U.S. Select REIT, Canadian Stocks- FTSE Canada, Intl Stocks- MSCI World Ex USA Large, Emerging Markets- MSCI EM NR. ETFs were used to represent sector returns, Clean Energy represented by iShares Global Clean Energy ICLN, Energy by The Energy Select Sector SPDR Fund XLE, Defense by iShares US Aerospace & Defense ETF ITA, and Financials by SPDR S&P Bank ETF KBE.

Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, Bank of Canada, Capital Economics, Bloomberg Economic Calendar, U.S. Department of the Treasury, CME Group, Trading Economics, "Sizing bitcoin in Portfolios," Dec 2024, BlackRock Investment Institute, "Wall Street's Market Forecasts Are Out for 2025- Be Dubious," Bloomberg Dec 2024 "The Miracle of U.S. Equities," Ben Carlson A Wealth of Common Sense Blog, Nov 19, 2024, JP Morgan Guide to the Markets Q4 2024, YCharts, Morningstar Direct 2025.

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