NCM

Core Global/Core International

Quarterly Update

Phil D'lorio, CFA
Portfolio Manager
Cumberland Investment Counsel Inc.,
affiliate of NCM Asset Management Ltd.

Q3 2022 Review

Market volatility remained elevated during the third quarter of 2022. After experiencing the largest first half decline since 1970, the S&P 500 started Q3 on a strong note by climbing nearly 14% during the first six weeks of the quarter. This rally created a lot of optimism for investors with market experts starting to believe that a soft landing in the economy had been achieved. However, this optimism proved to be short lived as the S&P 500 fell by nearly 17% during the last six weeks of the quarter. The challenging market conditions during the third quarter were global in nature as equity markets throughout Europe and Asia experienced significant bouts of volatility just like the S&P 500. Market volatility during Q3 was driven by the same factors that led to market weakness in the first half of the year. These factors include persistent inflation, tightening by central banks around the world, and the war in Ukraine.

Portfolio Review

In February of this year, we started repositioning our portfolios due to several factors including the outbreak of the war in Ukraine and the fact that inflation data had not improved. At that juncture back in February, we felt that the environment had changed for the worse, that the risks were higher, and that the range of potential outcomes was wider for both the global economy and global equity markets. Through our repositioning efforts we reduced our exposure to cyclical sectors such as Technology, Communication Services, Banking, and Consumer Discretionary. Companies in these sectors are more sensitive to economic downturns and are more vulnerable to significant earnings downgrades so we made the decision to lighten up in these areas. Some of the proceeds from these sales were redeployed into companies within the Consumer Staples and Healthcare sectors. Companies in these sectors tend to be more defensive given their stable free cash flow generation and they are less susceptible to large earnings downgrades.

During the third quarter, portfolio activity remained busy as we continued to reduce our cyclical exposure and increased our weight in defensive areas such as Consumer Staples. Some of the notable activity during the quarter included a reduction of our weighting in Accenture (Technology) and Howden Joinery (Building Materials), and we also established new holdings in Pernod Ricard and Heineken Holding. A brief business description of each company follows:

Founded in 1975, Pernod Ricard is the world's second-largest spirits manufacturer. The company owns more than 240 brands and it sells its products in more than 160 countries around the world. Pernod's key spirits brands include Absolut (vodka), Chivas Regal and The Glenlivet (scotch whisky), Jameson (Irish whiskey), Malibu (rum), Martell (cognac), and Beefeater (gin). The company has been able to generate above average growth through the premiumization of its products, a strong presence in fast growing emerging markets such as China and India, and strong pricing power. We are attracted to the company's strong brands and the product breadth of Pernod's portfolio across various categories including both global strategic and local niche brands.

Heineken is the largest brewer in Europe and the second largest brewer on a global basis. The company has more than 300 brands and sells its products in more than 190 countries around the world. The company's key brands include Heineken, Sol, Amstel, Tiger, and Birra Moretti. We are attracted to Heineken's suite of high-margin premium brands, its strong footprint in high growth markets across Asia, Africa and Latin America, and the significant economies of scale that come with being the second largest brewer in the world.

Outlook

As we look ahead to 2023, we have a cautiously optimistic view for our portfolios and there are several reasons for this. First and foremost, the valuations for our portfolio holdings are much more attractive given the significant share price declines experienced thus far in 2022. We have also repositioned the portfolios to be more resilient with an increased weighting in sectors that have higher earnings stability such as Consumer Staples and Healthcare. Furthermore, investor sentiment measures are very depressed and have reached levels seen at the height of the Great Financial Crisis in 2008-09 and the COVID pandemic in 2020.

Another reason that we are cautiously optimistic is related to stock market history. Based on historical data, once the S&P 500 has a 20% drawdown there is a strong likelihood of strong returns over the next 1, 3, and 5 years. As seen in the chart below, the S&P 500 has gained 16% on average over the next year and 13% annually over the next 3 and 5 years following a 20% drawdown.

Start Date	End Date	Duration (Mo.)	Drawdown (Peak to Trough)
10/25/1939	6/10/1940	8 Months	-32%
11/7/1940	4/28/1942	18 Months	-34%
5/29/1946	5/19/1947	12 Months	-28%
6/15/1948	6/13/1949	12 Months	-21%
8/2/1956	10/22/1957	15 Months	-22%
12/12/1961	6/26/1962	7 Months	-28%
2/9/1966	10/7/1966	8 Months	-22%
11/29/1968	5/26/1970	18 Months	-36%
1/11/1973	10/3/1974	21 Months	-48%
11/28/1980	8/12/1982	21 Months	-27%
8/25/1987	12/4/1987	3 Months	-34%
7/16/1990	10/11/1990	3 Months	-20%
3/24/2000	10/9/2002	31 Months	-49%
10/9/2007	3/9/2009	17 Months	-57%
2/19/2020	3/23/2020	1 Months	-34%
Average		13 Months	-33%
Median		**12 Months**	**-32%**

The 3-year and 5-year returns noted above are annualized returns. The rows shaded in grey are periods when the economy went into a recession.

But there is a caveat. Based on history there could be more downside in the short term. During the time period under consideration, once the market dropped 20%, there was an average additional downside in the mid-teens percentage range. While another 10-15% downside in the market wouldn't feel very good, it must be viewed in the context of the cumulative 3-year and 5-year returns of 42% and 68% respectively for the S&P 500 following a 20% decline.

At its low point on September 30th, the S&P 500 was down nearly 25% on a year-to-date basis. This is not too far off the average bear market decline of 33% noted in the table above. This leads us to believe that we are getting closer to a bottom.

While 2022 has been a challenging year and our portfolio returns have not met our expectations, we believe that a significant amount of bad news has been priced into stocks. More importantly, we are very encouraged by how well our companies have performed in terms of growing their business with many of them gaining market share from competitors during a very challenging period. We believe this bodes well for future share price performance.

NCM

NCM Asset Management Ltd.

Head Office 1850-333 7th Avenue S.W., Calgary, AB T2P 2Z1 | 310-99 Yorkville Avenue, Toronto, ON M5R 3K5

client services: (877) 531-9355 | toll-free: (877) 431-1407 | info@ncminvestments.com | ncminvestments.com