Quarterly Manager Letter

Q4 2023

Current News and Updates

COMMENTARY

2023 was a year punctuated by an exceptionally strong move in risk assets. The 14% rally in the S&P 500 in November and December marked the second-best end-of-year move in 95 years of data, bettered only by 2020 following the announcement of the first Covid vaccines. The nine-week positive run in the market left it close to an all-time high, coinciding with sentiment and investor positioning, which also closed in elevated territory. In fact, Commodity Futures Trading Commission data suggests that net positioning in US equity futures (a sign that investors are bullish) hit the highest in 14 years late in 2023.

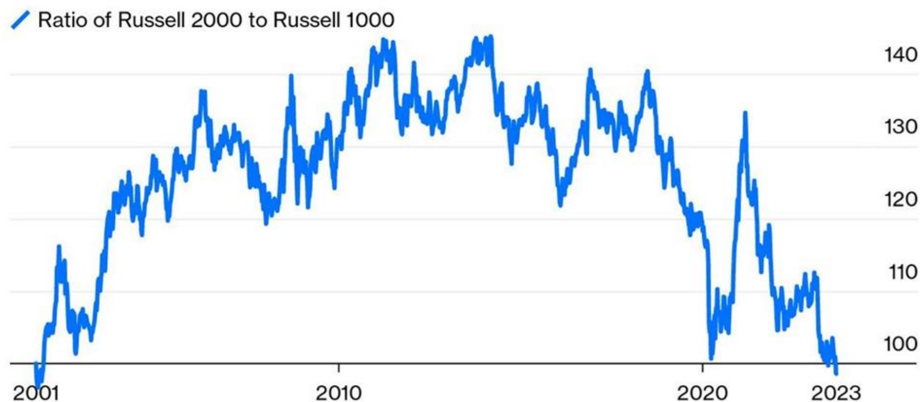
The strong end of year move helped the Balance Composite return 4.8% in the fourth quarter and 5.7% for the full year, after all fees. Clearly, declining interest rates and exposure to the US market helped results, partly offset by the 2.5% decline in the USD vs CAD in the quarter, and for the year.

This year has started off by paying for some of the end-of-year excess. Many of the themes that worked best at the end of 2023 have struggled more recently. Highly shorted stocks and those with weak balance sheets, which performed well in late 2023, have started to underperform again. Similarly, US Cyclicals vs Defensives have just endured their worst week since the start of the US regional banking crisis, while EU Cyclicals vs Defensives have seen their worst week since April.

As we look ahead to 2024, we are taking a glass half-full mindset. Economic data continues to show strength, while the labour market remains tight. Global central banks have consistently reported that the most important driver of future interest rate policy will be the path of inflation, and as a result, we don't need to see significant economic weakness to manifest lower rates over time. While the market expectations of future rate cuts might be slightly too aggressive for 2024, a repricing of future policy expectation should be possible without significant market weakness. If we combine this with the fact that equity valuations are not uniformly stretched, we see continued upside. We expect to continue increase equity market exposure in the coming weeks, while remaining extremely selective in our stock selection. On the fixed income front, we will use opportunities where the market reprices policy expectations to add exposure, as we continue to believe the trend for inflation and interest rates is lower in the coming years.

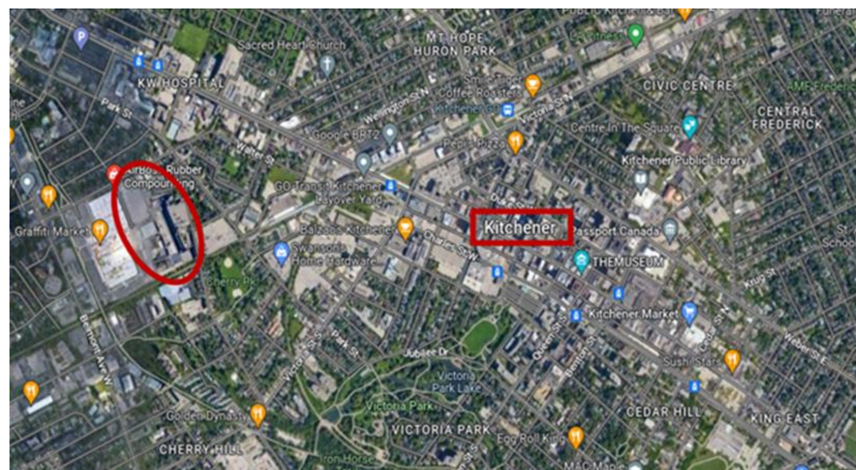
Aventine Canadian Equity ("ACE") Fund

The Aventine Canadian Equity Fund had a solid end to the year, returning 3.7% in the quarter. Despite the strong close, it was not the “bounce back” year we had anticipated. Valuations at the outset of 2023 were pricing in near-worst-case scenarios, and as the year progressed it became clear that a sharp recovery was unlikely. However, patience will be rewarded as easing financial conditions, and a return to more normalized valuation methodology, should have a significantly positive impact on the fund’s future performance. For example, the valuation differential between small and large capitalization stocks hasn’t been this wide in 22 years.



As a result, throughout 2023, the fund made a conscious shift towards larger capitalization equities which significantly dampened volatility and improved returns. Alimentation Couche-Tard (+31% YTD), Element Fleet (+17%) and Otis Elevators (+14% YTD) all performed extremely well last year and continue to impress. We continued with this approach in the fourth quarter, adding FirstService (FSV-TO) and Winpak (WPK-TO), two companies whose management teams have stood the test of time and have created significant shareholder value through all market environments.

Looking ahead, we are encouraged to see some positive developments on the catalyst front from some of our larger legacy holdings. The management team of AirBoss of America (BOS-TO) have finally spoken publicly regarding their intention to monetize their ~1 million square foot facility in the heart of downtown Kitchener.



Currently being zoned for mixed-use, this asset would likely have a price tag of approximately $110 million. When your entire market cap is $126 million, we believe this creates substantial downside protection and optionality at current levels.

Additionally, our recent management meetings with the new leaders of Sangoma Technologies (STC-TO) has been very encouraging. The team has a clear growth strategy and presents exceptionally well, which should help attract new investors and customers, in our view. Their experience running multi-billion-dollar enterprises including Infosys and Bell Canada is a massively mispriced asset. While it will take time for the new management team to prove themselves, and reinstate guidance, we believe the company that emerges from their leadership will be much stronger and should trade closer to peer multiples (nearly 2x higher!).

We are excited about the year ahead as we have maintained our focus on quality and value. We acknowledge that this has not been an easy stretch to hold an all-cap strategy such as the ACE Fund, but our patience and deep fundamental research will be rewarded, and we look forward to keeping you updated as we progress through the year.

Aventine US Equity Fund

The Aventine US Equity Fund had a very strong end to the year, returning 10.5% in the quarter, and 10% for the full year, in USD. We are extremely pleased with our performance in 2023 considering our lack of relative exposure to the highly valued technology stocks which drove the majority of the S&P 500's performance.

In a sharp reversal to Q3, our second largest position, Brookfield Infrastructure Partners (BIP-US), performed well in the final months of the year, returning 7.1%. We maintain that BIP is still greatly undervalued considering their strong management team, irreplaceable suite of assets, double-digit FFO per unit growth, attractive yield, and a robust acquisition pipeline. While the stock tends to be inversely correlated with interest rates, we believe positive fundamentals will outweigh fluctuations in bond yields over the medium term. Other notable performers in the year included Microsoft (MSFT US: +57%), Costco (COST US: +45%), and Zoetis (ZTS US: +35%), while detractors included Nutrien (NTR US: -23%) and Agilent (A US: -7%).

In Q4 we added a new position to the portfolio – Cemex (CX US). Cemex, while headquartered in Mexico, is a global building products company which produces, distributes, and markets cement, ready-mix concrete, aggregates, and related building materials. The big story here remains "nearshoring". The growing role that local economies are playing in global manufacturing will cause a dramatic increase in demand for labour, electricity, and facilities. This, in turn, will elevate prices and incentivize new investments. For example, in the US, construction for manufacturing has risen from an $80 billion annual run rate to US$220 billion, and it could continue to rise. Combine this with an extremely undemanding valuation, and we believe Cemex is set for a solid 2024.

Finally, in Q4, we initiated short positions in the US Equity Fund covering several hotel companies. This trade was in anticipation of travel demand normalization and diminishing pricing power. The industry benefitted from strong post-pandemic travel demand that led to multiple quarters of volume-driven strength, and relatively inelastic pricing. We believe the easy leg work for hotel operators has since passed. Revenue per available room, or RevPar, an

important metric in hotel-stock analysis, has finally begun to decline. From our channel checks, we believe this moderation will materialize into cuts to corporate guidance in upcoming quarters, and a reduction of inflated valuations.

Outlook

We view 2024 as an important transition year as we are finally forecasting below consensus inflation lending credibility to our "higher-for-shorter" rate thesis from earlier this year. While we do believe that inflation will stabilize at a higher level than many anticipate, primarily resulting from sticky labour costs, a messy energy transition, and the restructuring of global supply chains, government support and less hawkish central banks means that a recession in the short term is unlikely.

To us, the most underpriced risk in the market is that central banks don't deliver the magnitude of rate cuts that the market is expecting. Currently, the market expects a total of 7 rate cuts from the federal reserve, and 6 from the Bank of Canada in 2024. Regardless, we continue to maintain a constructive view on markets. We also maintain that too many people believe that stocks are all trading at lofty valuations and that developed economies are topping out and headed for a hard landing. As a result, many investors are sitting idle as they feel that there is little to no value in the market beyond cash. This is evidenced by the nearly $9 trillion of assets parked in money market accounts currently. However, outside of the S&P500's magnificent 7, there are some very compelling macroeconomic and equity-focused stories which should dramatically outperform cash.

Although there is quite a bit of optimism currently priced into markets, we remain focused on the following tailwinds:

1. Central bank balance sheets are near record levels providing support for asset prices.
2. Earnings for the cycle bottomed in Q2 2023.
3. New issuance supply of equities and corporate bonds are near record lows.
4. Major Central Banks are soon to begin their easing cycle.

As a result, we lean more optimistic than many in 2024. Although monetary policy might in effect become more restrictive as inflation falls and lagged effects kick in, we are unconvinced this will be enough to tip the economy into recession while financial conditions are now much looser, and the job market remains structurally tight.

Finally, if you haven't recently, please visit our website as we have been publishing more of our research than we have in the past.

Thank you for your continued support of Aventine as your Investment Manager and Investment Counsellor. Please do not hesitate to reach out to learn more about our investment strategies. We are always excited to discuss our clients' accounts with them and how we may be of greater value.

Best as always,
James, Jim, David, Shannon, and Nicho

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Aventine Performance Update
December 31, 2023

Aventine's Partners and their families are among the largest investors across each of our strategies.

Aventine Balanced Composite
Inception: June 1, 2009

Aventine Balanced is our core portfolio for separately managed accounts following a "balanced" mandate. It is an actively managed, endowment-style portfolio that offers investors diversified exposure to a broad variety of markets and asset classes. This diverse portfolio produces below average volatility and high income generation as we include asset classes such as private debt, mortgages, traditional and non-traditional fixed income, all-cap equities, alternatives and portfolio protection through prudent risk management strategies.

	Q4	2023
Aventine Balanced Composite	4.8%	5.7%

Annualized	3 Year	5 Year	Inception
	2.1%	5.6%	6.3%

Additional performance information and disclosures on composite construction is available upon request.

We encourage new clients to join Aventine by investing in our customized portfolio solutions which are tailored to your specific goals.

To learn more about how our independent approach to managing wealth differs from traditional models please feel free to contact us anytime.

This email communication is intended to provide you with information about the Aventine Balanced Composite (the "Composite"), the Aventine Canadian Equity Fund and the Aventine Dividend Fund (the "Funds") managed by Aventine Management Group Inc. The Funds are distributed by prospectus exemption in various jurisdictions across Canada, please contact Aventine Management Group Inc. to discuss if you may be eligible to invest. Important information about each Fund is contained in its Offering Memorandum which should be read carefully before investing and may be obtained from Aventine Management Group Inc. upon request. The Offering Memorandum does not constitute an offer or solicitation to anyone in any jurisdiction in which such an offer or solicitation is not authorized, or to any person to whom it is unlawful to make such an offer or solicitation. All investors should fully understand their risk tolerance and the suitability of the Composite and the Funds prior to making any investment. Rates of return presented for all periods greater than one year are the historical annualized compound total returns for the period indicated. For periods less than one year the rates of returns are a simple period total return. Rates of return do not take into account income taxes payable that would have reduced net returns. The performance presented for the Funds is the performance of the target series of F Class units. The value of the Composite and the Funds is not guaranteed and will change frequently. Past performance may not be repeated. All credited third-party information contained herein has been obtained from sources believed to be reliable at the time of writing, but Aventine Management Group Inc makes no representations as to its accuracy.

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