

Why this money manager sold Brookfield Infrastructure and added more small-cap stocks

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Stephen Takacsy of Lester Asset Management

While North American economies have slowed, money manager Stephen Takacsy isn't anticipating a severe downturn.

"We've always been in the soft landing camp," says Mr. Takacsy, chief executive officer and chief investment officer at Lester Asset Management Inc. in Montreal, who oversees about \$350-million in assets.

He points to the relatively low unemployment rate in Canada and the U.S. as reasons not to be overly concerned about a deep recession on the horizon.

“As long as people have jobs, they’re spending and paying their mortgages,” he says.

Mr. Takacsy also expects 2024 to be a good year for stocks and bonds, but says investors need to be mindful about what investments they own. His focus is on buying value stocks he can hold for the long term and higher-yielding fixed-income securities such as corporate bonds.

His firm’s Canadian Equity Fund is up 9.8 per cent over the past 12 months, while the Canadian Fixed Income Fund has returned 7.8 per cent. The fixed income strategy has generated an annualized compound return of nearly 6 per cent since its inception 15 years ago, while the Canadian equity strategy has seen an annualized compound return of 9.3 per cent since its inception 17 years ago. The performance data is before fees as of Dec. 31.

The Globe spoke with Mr. Takacsy recently about what he’s been buying and selling, and the sector he wished he got out of before it plunged.

Describe your investing style.

We manage equities and fixed income for our private clients and also manage bonds for some Quebec pension funds. We prefer taking on credit risk and getting compensated properly for it through higher yields rather than taking on duration risk and trying to predict the shape of the yield curve. We do this by buying corporate bonds and hybrid debt and being opportunistic in the preferred share market. With equities, we are bottom-up fundamental long-term value investors.

What’s your take on the current market environment?

We see a very positive environment for both stocks and bonds for 2024. We have always believed that inflation was transitory, caused by supply-demand imbalances and supply chain disruptions post-pandemic, combined with a spike in commodity prices fuelled by Russia’s war on Ukraine.

In fact, the rapid rise in interest rates by central banks actually contributed to inflation through rising shelter costs. The rate of inflation, whichever way you measure it, has declined naturally as these anomalies normalize, not because of the rate hikes. That’s why U.S. and Canadian central banks are now pivoting. It was only a question of time before bonds would rally strongly on lower inflation data and stocks would follow.

The North American economy is slowing down due to the rate hikes, and if it slows down too much, this ‘bad’ news will be seen as good news for the bond market and, by association, stocks as well. However, investors will need to pick their spots. Since the job market remains strong and savings rates are still high, we could even get a ‘Goldilocks scenario’ in which disinflation or even deflation occurs along with a sound economy – the opposite of stagflation, which nobody has a good name for yet. This would be rocket fuel for the markets.

What have you been buying?

In fixed income, we've been like kids in a candy shop. We've been buying high-yielding shorter-term corporate bonds, hybrid debt, and rate-reset preferred shares, which are trading at historically high yields in the 6 to 8 per cent range. This represents equities-like returns with low risk.

In Canadian equity, we've been adding to beaten-up small- and mid-cap stocks. One example is Tecsys Inc., a leader in supply chain solutions for hospitals and complex distribution with a record backlog and growing recurring revenue. Another is Neo Performance Materials Inc., a pioneer in engineered materials made from rare earths used in high-tech applications such as electric vehicles (EVs). It's expanding production massively, and it's a great way to play the EV market without speculating on companies that aren't yet profitable. A third one we've been adding to is Savaria Corp., a world leader in home accessibility and patient handling equipment that's benefiting from aging demographics. More people want to retire at home, especially since the pandemic.

What have you been selling?

We sold our positions in Canadian Tire Corp. Ltd. and Brookfield Infrastructure Corp. close to their highs during the summer for different reasons. With Canadian Tire, we felt consumer spending was slowing. We sold it just before the company announced revised guidance, and the stock cratered. With Brookfield Infrastructure, we thought it was getting expensive, given rising interest rates. The stock dropped 40 per cent after we sold it.

Are there some stocks you wish you had bought or sold?

I wish we had sold more of our renewable energy stocks after the passage of The Inflation Reduction Act [of 2022] in the U.S., which includes some of the most significant climate legislation in U.S. history. It caused many renewable energy stocks to go parabolic in 2021. We didn't anticipate how hard and fast they could come down. We took a little bit of profit, but not as much as we should have, in hindsight.

What advice do you have for new investors?

Live within your means and save as much as you can so you can start investing early. It's the power of compounding that builds wealth. Also, invest for the long run and don't try to time the market because if you miss the best few days, you will fall way behind. And invest in real businesses, not in fads. Slow and steady wins the race.

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