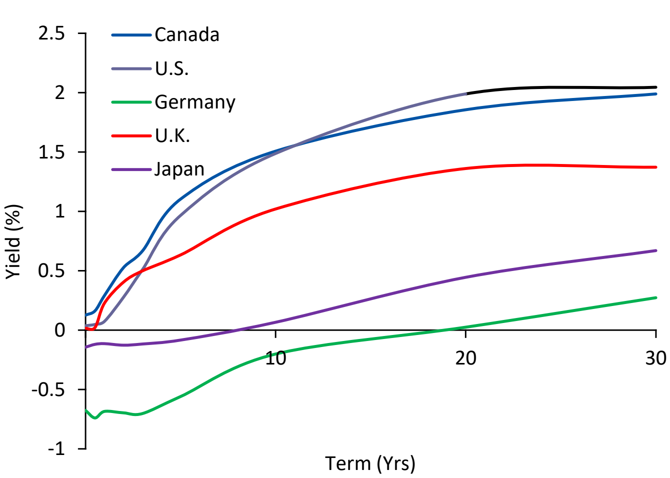
Market Statistics

	Sep/21	Jun/21	Mar/21	Sep/20
Yields (%)				
90 Day T-Bill	0.13	0.15	0.09	0.12
10 Yr. Canada Bond	1.56	1.48	1.61	0.60
30 Yr. Canada Bond	2.00	1.84	1.96	1.13
Rates				
C.P.I. (annual %)	4.09	3.06	2.20	0.51
US$/C$	0.79	0.81	0.80	0.75
Euro/C$	0.68	0.68	0.68	0.64
Prices (US$)				
Crude Oil (bbl.)	75	73	59	40
Natural Gas (mm)	5.87	3.65	2.61	2.53
Gold (oz.)	1,755	1,771	1,714	1,888

Market Returns

	Periods Ending Sep. 30/21			
			Annualized	
	3 Mo.	1 Yr.	5 Yrs.	10 Yrs.
S&P/TSX	0.2	28.0	9.6	8.8
S&P 500 (C$)	3.4	24.2	16.2	19.0
S&P 500 (US$)	0.6	30.0	16.9	16.6
MSCI EAFE Net (C$)	2.3	20.1	8.2	10.3
MSCI EAFE Net (US$)	-0.4	25.7	8.8	8.1
MSCI World Net (C$)	2.8	23.0	13.1	15.0
MSCI World Net (US$)	0.0	28.8	13.7	12.7
Bond Universe	-0.5	-3.4	2.3	3.3
91 Day T-Bills	0.1	0.2	0.9	0.9

Yield Curves



The Economy

The global economy is now on a path to recovery but concerns with regard to the fall flu season and Covid 19, product supply shortages and rising inflation remain. Government support programs for consumers and businesses are expiring with higher rates of taxation expected to help pay for the costs and debt incurred as a result of the virus. It was an unusual pandemic-induced recession as the financial risk was largely taken on by governments. Concern over the potential length and severity of the pandemic led consumers to limit expenditures which resulted in savings rates exploding, but a return to spending is now helping drive recovery. Despite higher vaccination rates, many of the changes in day-to-day life brought on by the pandemic persist. Most corporations, especially larger ones, have adapted quickly and profits now exceed pre-pandemic levels. Some sectors continue to suffer, most notably the leisure and hospitality areas. To ensure continued economic growth while increasing tax rates, governments are now focusing on longer term infrastructure projects.

OECD Real Economic Growth Forecast (%)

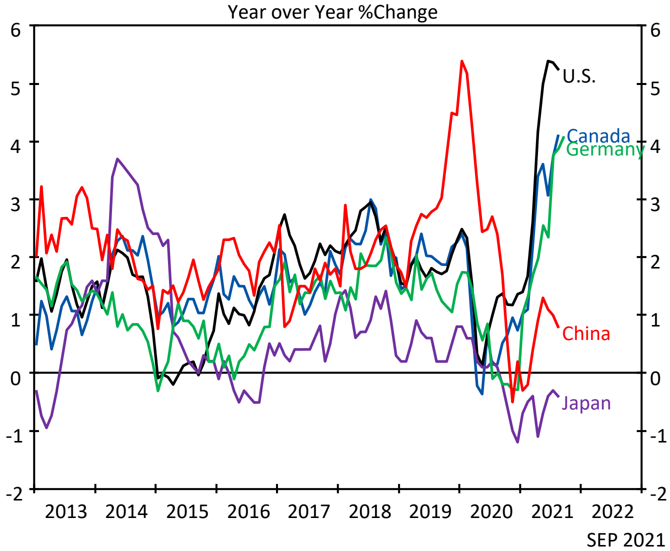
	2021	2022
U.S.	6.0	3.9
Europe	5.3	4.6
Japan	2.5	2.1
U.K.	6.7	5.2
Canada	5.4	4.1
China	8.5	5.8

Source: Organization for Economic Cooperation & Development Sep. 2021

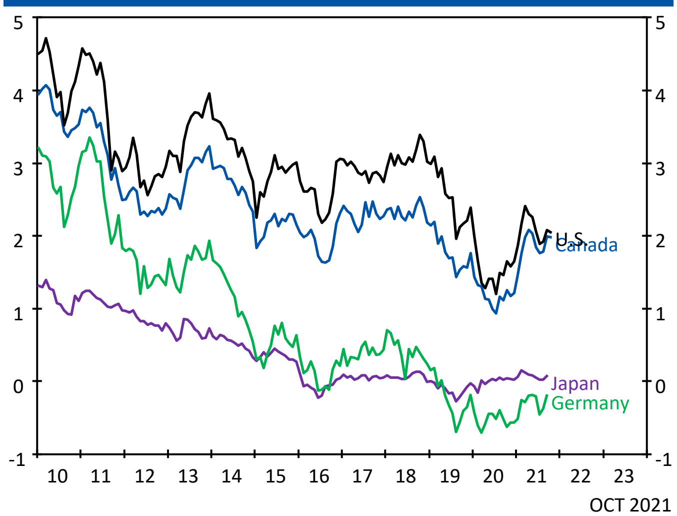
The table above indicates economic growth rates for democratic countries in 2021 will be approximately twice the normal annual average of 2.0-3.5%. The current rapid recovery is causing bottlenecks as surging consumer demand cannot be met with sufficient supply. The shortfall is the result of a lack of investment over the last two years and ongoing government wage subsidies that help people stay healthy at home. There will be a lag in terms of the return to work with some rethinking their career choices. A change in global trade relationships is also fueling disruptions. The U.K. is dealing with the consequences of Brexit and the U.S. is trying to wean itself from its dependency on cheap Chinese labour. Eventually the supply side will catch up but it may take several quarters and perhaps stretch into 2023.

Inflation rates beyond the 2% level have consistently been stated as a concern by central banks. Despite historically low rates since the great recession of 2008, inflation has remained largely in check. In fact, disinflation has pushed interest rates to negative levels in Europe and Japan (see opposite chart).

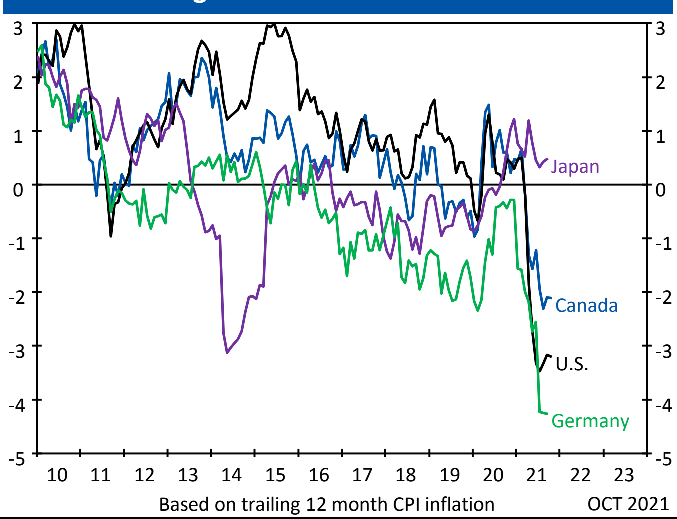
Global CPI Inflation



Long Term Government Bond Yields



Real Long Term Government Bond Yields



Short-term interest rates were further reduced as a result of Covid 19 and central banks initiated massive bond-buying programs to help lower longer-term rates as well. With the global economic recovery taking hold, inflation rates are now spiking upward (see top chart opposite). What remains uncertain is how much of this inflation is simply due to short-term supply shortages.

The Markets

A rise in long-term interest rates at quarter-end added market volatility and resulted in both stock and bond markets correcting. This erased most of the gains earned earlier in the third quarter as the S&P/TSX returned 0.2% and the World index 0.0% (in local currency terms). The Canadian dollar did, however, decline versus its U.S. counterpart which led to a 2.8% gain for the World Index in Canadian dollar terms. Most fixed income securities provided negative returns for the quarter with the Bond Universe index losing 0.5%. Longer maturity bonds suffered the greatest losses while short maturity bonds were slightly positive.

The unanimous message conveyed by global central bankers during the quarter was that with economic growth returning, bond-buying programs would be halted before any increase in short-term interest rates. The spike in inflation has made bond yields very unattractive as they now reflect negative real yields (yield minus the rate of inflation – see bottom chart opposite). At the time of this writing, long bond yields are continuing to increase providing for added bond losses. Our view is that some inflation will be sustained during this economic cycle as costs are passed along and wages rise to attract labour.

In an economic environment characterized by recovering global growth, higher levels of inflation and rising interest rates, bonds remain unappealing except for shorter-term maturities that provide portfolio stability and liquidity. Ownership of assets including equities can offer inflation protection but not all to the same extent. Companies in the consumer, pharmaceutical and banking industries have typically been successful in inflationary environments with their ability to pass along cost increases to customers. Utilities and some discretionary products/service companies on the other hand have not. Companies in technology related sectors tend to experience shrinking valuations as there is added difficulty in achieving above average growth rates in a higher interest rate environment. We remain comfortable with our portfolios which are dominated by companies that can provide protection during periods of rising inflation. Valuations are also supported by earnings that have increased to levels in excess of pre pandemic levels.