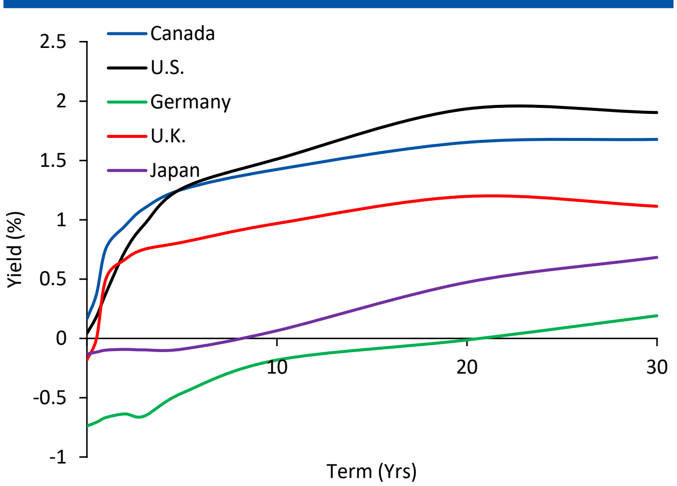
## Market Statistics

| | Dec/21 | Sep/21 | Jun/21 | Dec/20 |
|---|---|---|---|---|
| **Yields (%)** | | | | |
| 90 Day T-Bill | 0.12 | 0.12 | 0.15 | 0.06 |
| 10 Yr. Canada Bond | 1.52 | 1.56 | 1.48 | 0.74 |
| 30 Yr. Canada Bond | 1.70 | 2.00 | 1.84 | 1.21 |
| **Rates** | | | | |
| C.P.I. (annual %) | 4.72 | 4.38 | 3.06 | 0.73 |
| US$/C$ | 0.79 | 0.79 | 0.81 | 0.79 |
| Euro/C$ | 0.69 | 0.68 | 0.68 | 0.64 |
| **Prices (US$)** | | | | |
| Crude Oil (bbl.) | 75 | 75 | 73 | 49 |
| Natural Gas (mm) | 3.73 | 5.87 | 3.65 | 2.54 |
| Gold (oz.) | 1,828 | 1,755 | 1,771 | 1,893 |

## Market Returns

| | Periods Ending Dec. 31/21 | | | |
|---|---|---|---|---|
| | | | Annualized | |
| | 3 Mo. | 1 Yr. | 5 Yrs. | 10 Yrs. |
| S&P/TSX | 6.5 | 25.1 | 10.0 | 9.1 |
| S&P 500 (C$) | 10.5 | 28.2 | 17.1 | 19.1 |
| S&P 500 (US$) | 11.0 | 28.7 | 18.5 | 16.6 |
| MSCI EAFE Net (C$) | 2.2 | 10.8 | 8.3 | 10.4 |
| MSCI EAFE Net (US$) | 2.7 | 11.3 | 9.5 | 8.0 |
| MSCI World Net (C$) | 7.2 | 21.3 | 13.7 | 15.2 |
| MSCI World Net (US$) | 7.8 | 21.8 | 15.0 | 12.7 |
| Bond Universe | 1.5 | -2.5 | 3.3 | 3.3 |
| 91 Day T-Bills | 0.1 | 0.2 | 0.9 | 0.9 |

## Yield Curves




## *The Economy*

It has now been two years that the world has been overwhelmed by Covid. While we had at first hoped it would pass as quickly as SARS, this has not happened. Governments of most developed nations abbreviated any recession by assisting consumers and businesses with immediate, direct support and by taking on significant debt, thereby, bearing much of the economic cost related to the pandemic. Moving forward, government spending is shifting toward longer-term programs related to infrastructure.

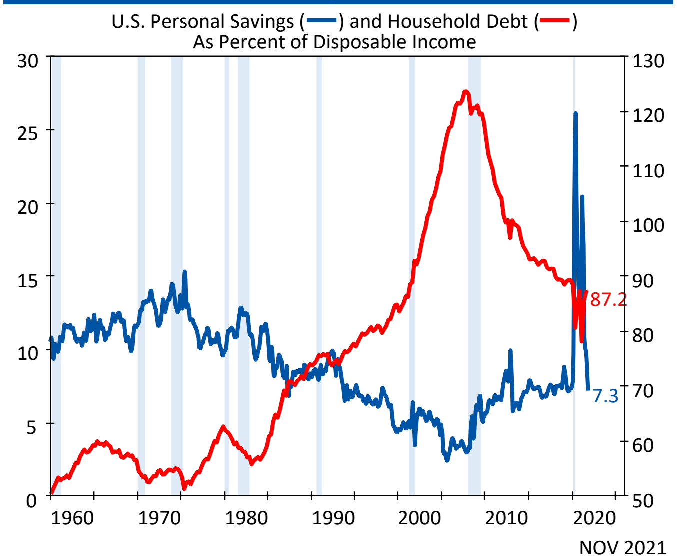
Economic growth has also been fueled by large corporations that have been particularly adept at navigating change and continuing to drive profitability beyond pre-pandemic levels. The consumer, with a stay-at-home mandate, has been unable to spend on many discretionary items pushing personal debt levels lower and savings rates higher. Nowhere has this been more apparent than in the U.S. (see top chart on page 2). As a result, **the economic environment for developed nations remains relatively favourable for continued economic improvement and recovery in 2022.**

For the first time in over a decade, inflation has become an issue. It now significantly exceeds the 2% level in the largest nations (see second chart on page 2) and as a result, monetary support is being withdrawn. So far, in North America we have only seen a reduction in quantitative easing (the purchase of bonds and other securities in order to keep longer-term interest rates low). Elsewhere, however, some countries have also experienced an increase in short-term interest rates instigated by their central banks. The Bank of England very recently raised rates by 0.15 percent. It remains unclear as to how much of the current upward spike in inflation is transitory and therefore the magnitude and timing of any potential interest rate increase is uncertain. Our view is that the longer-term rate of inflation will most certainly be higher than the levels experienced pre-pandemic for three reasons.

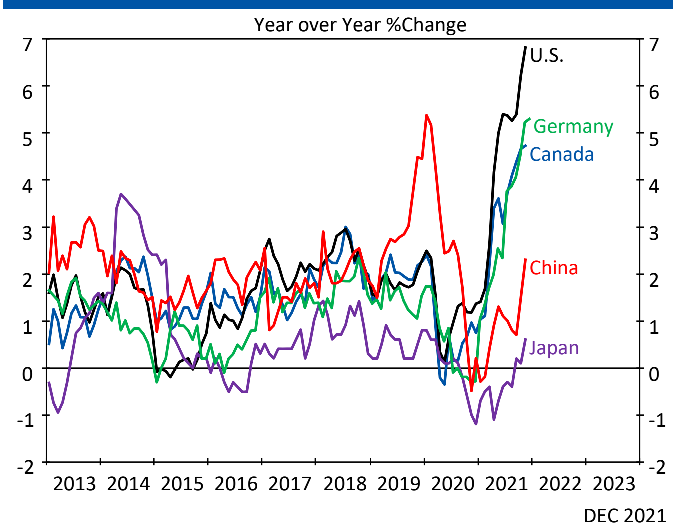
Firstly, the current supply shortages are not simply commodity or product driven, rather they are also the result of labour disruptions that will take time to resolve. The pandemic has created a unique environment where many have stepped back, reprioritized and prefer the stay-at-home setting. Some are now working less, others are between jobs or have simply left the labour force. Wages will need to increase in order to attract workers, not just over the coming quarters but years. Those higher wages will be very difficult, if not impossible, to retract. Renewed immigration programs may help solve part of the problem longer term.

Secondly, one of the greatest inflation killers of the last decade, the shift of production to China and other low-cost labour countries, will not be as prevalent post pandemic. Covid has reminded us that maintaining domestic manufacturing is

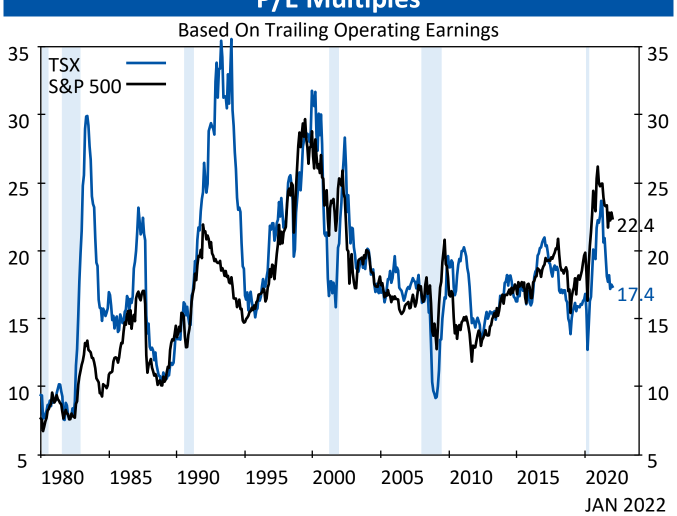
### U.S. Personal Savings & Household Debt




### Inflation




### P/E Multiples




important for essential industries such as vaccines, drugs, computer chips, etc. As well, there is a greater awareness of the poor environmental, social and governance policies in many of the low wage economies.

Finally, taxes will be increased in most of the developed world. This will come in many forms as the amount of debt taken on by governments cannot simply be solved by a "tax the wealthy" approach. There will be increases in inflationary "consumption taxes" including sales taxes, tariffs and more user fees for services.

## *The Markets*

Double-digit stock market returns were experienced in 2021, with North American indices leading, as economic growth accelerated and interest rates remained low. Overseas market returns were strong but lagged as did their economic growth rates. Virtually all industry sectors participated in the gains with the exception of those severely hit by the pandemic, notably travel and leisure. Technology, financials and energy provided the best returns. The slowing and reaccelerating of virus infections held back the performance of most economically sensitive company shares except for energy where renewed discipline by OPEC restrained supply growth and boosted the price of oil.

The lower level of bond purchases by the Bank of Canada (i.e., the wind down of quantitative easing) resulted in long-bond returns turning negative for the year. Short-term interest rates have not yet risen in Canada despite the rapid acceleration of inflation. Given the negative real yields (bond yield minus inflation) available today, bonds provide an unattractive investment alternative except for the liquidity and capital preservation characteristics available in short-term bond maturities.

**Equities remain the preferred asset class in times of inflation and particularly, the equities of companies that can more easily pass along cost increases (ex. healthcare, food, financial sectors).** As developed economies continue to improve, so will corporate profits and this should help offset the lower valuations that higher interest rates may bring. The chart opposite indicates price/earnings multiples within the U.S. market are in their upper historical range. This would perhaps imply more attractive valuations in Canada but it is the make up of the indices which drive the overall valuation figures. In Canada, the lower figure is largely due to the low double-digit valuations in the bank and insurance sectors which dominate the index (32% of the TSX). Similarly, the higher number in the U.S. is largely the result of the technology and technology related company valuations (35% of the S&P 500). Portfolio risk can be moderated by reducing exposure to the extraordinarily high valued companies in these sectors.





*Sources: TD Securities Inc., BlackRock, Bloomberg*