HIGHLIGHTS

Economic Review

- The global economy continued to recover slowly with some regions such as the United States outpacing others like the eurozone.
- Bond markets posted one of their weakest performances in history as rising government yields weighed on overall bond market sentiment.
- In equity markets, the first quarter maintained the continuation of the recovery trends we saw during the second half of last year with ongoing optimism that the vaccine rollout will eventually quell the resurgent virus variants.

Investment Outlook

- The second quarter should bring about a dramatic rise in vaccine availability in most major markets, hopefully paving the way for a return to a more normalized environment.
- The unprecedented levels of support given as we have faced this pandemic are unsustainable over the longer term, and there will undoubtedly be consequences as they are tapered off.
- A patient long-term approach with risk management at the forefront will likely provide long-term benefits.

ECONOMIC REVIEW

The global economy continued to recover slowly with some regions such as the United States outpacing others like the eurozone. The pace was largely reflective of success in vaccine distribution against the rapid spread of new coronavirus variants. It is clear that policy officials will continue to provide support for economies either in the form of easy financial conditions, such as interest and exchange rates, and/or fiscal policy support, such as the United States' approval of a $1.9 trillion stimulus package. There is intense debate as to whether all of this support and the fundamental change in policy are sowing the seeds of long-term inflation.

When looking at inflation there are a number of factors to consider, which we will discuss briefly. Policy is a key consideration as is the tremendous growth in debt levels (e.g. US federal debt has increased from $9T to $27T since 2008 while US corporate debt has doubled to $12T). Some would view that developed economies are in a debt trap where each additional dollar of debt is producing a diminishing dollar of GDP growth. This speaks largely to the uses of debt financing: debt used to finance investments that increase economic productivity would leave the economy in much better health than debt used to finance consumption. Other factors to take into consideration when discussing long-term inflationary pressures are demographics, globalization, labour market dynamics, exchange rate regimes, resource market pricing, and banking behavior, to name a few. In addition, we should question if the US can succeed in raising inflation when Japan and the eurozone have failed. With all this said, the most accurate predictor of future inflation has historically been past inflation, which has averaged about 1.5% over the past 10 years.

Market Returns (as at March 31, 2021)

(%)	3M	1 Yr	5 Yrs	10 Yrs	15 Yrs
S&P/TSX	8.1	44.2	10.1	6.0	6.0
S&P 500 (C$)	4.7	38.1	15.6	16.9	10.6
S&P 500 (US$)	6.2	56.4	16.3	13.9	10.0
Russell 2000 (US$)	12.7	94.8	16.3	11.7	8.8
DJIA (C$)	6.1	33.4	12.6	13.2	8.1
DJIA (US$)	7.8	50.5	13.3	10.3	7.5
MSCI EAFE Net (C$)	2.1	27.7	8.2	8.3	4.6
MSCI EAFE Net (US$)	3.5	44.6	8.8	5.5	4.1
MSCI Emerging Mkts Net (US$)	2.2	58.4	12.1	3.7	5.9
FTSE Canada Universe Bond	-5.0	1.6	2.8	4.0	4.4
FTSE Canada 91 Day T-Bills	0.0	0.2	1.0	0.9	1.4
C$/US$	1.4	13.2	0.6	-2.5	-0.5

Converted to CAD using London 4pm rates. Returns are annualized for periods greater than one year.

BOND MARKETS

Bond markets posted one of their weakest performances in history while equity markets touched new highs in the quarter. Corporate bonds modestly outperformed their government counterparts although the tone weakened into quarter-end as rising government yields weighed on overall bond market sentiment. Some large mergers and acquisitions also contributed to the softer market environment as investors weighed the possibility of increased corporate issuance to lock in rates.

Inflation expectations continued to increase with central banks encouraging the move through their lack of resistance. Bond markets are still trying to determine at what point the US Federal Reserve will care about higher interest rates. So far, the Fed has not shown much concern as the increases are primarily due to positive economic news, and the pace has been relatively orderly. Some of the traditional inflation hedges such as gold suffered losses as the interest rate increases started to shift towards the realm of real rates, which has traditionally had a negative correlation with gold prices.

EQUITY MARKETS

The tone in equity markets remained positive in Q1, despite mixed progress around containment of the COVID-19 pandemic. The Canadian market was amongst the strongest globally, as higher rates propelled financial shares higher and commodity exposed stocks also advanced. US markets were also firm (+4.7% in CAD), as progress around vaccinations and the passing of a major $1.9T stimulus program provided continued support for an economic recovery. In Europe, a slower vaccine rollout and resurgent infections dampened expectations for a quick domestic recovery. Emerging markets also showed mixed results, primarily because of differing levels of COVID progression and lower vaccine availability versus developed markets.

From a sector standpoint, more traditionally value-oriented sectors tended to lead markets globally. Energy was a major contributor, as optimism around recovery and travel along with continued OPEC+ compliance drove oil prices higher. Financials also continued to recover vigorously as bottoming bad debt provisions, along with a steepening yield curve, provided optimism for future earnings. Conversely, defensive sectors that typically correlate inversely with yields performed less favourably, such as the weakness seen in Consumer Staples, Healthcare and Utilities. In many respects, the first quarter maintained the continuation of the recovery trends we saw in the second half of 2020 with ongoing optimism that the vaccine rollout will eventually quell the resurgent virus variants.

OUTLOOK

Global markets continue to recover as prospects improve for an eventual normalization. In many regions, the vaccine rollout has been slower than many would have liked; however, the second quarter should bring about a dramatic rise in vaccine availability in most major markets, hopefully paving the way for a return to a more normalized environment.

In the medium term, it will be once again important to monitor how the global economy reacts to a reduced level of monetary and fiscal stimulus. The unprecedented levels of support given as we faced this pandemic are unsustainable over the longer term, and there will undoubtedly be consequences as the stimulus is tapered off. In the U.S., spending agendas will likely be funded by the higher income earners and corporate taxes. This trend will likely be followed in other regions, as the pandemic has served to further stretch gaps between the more and less wealthy.

Our approach remains to focus our efforts on identifying higher quality, resilient businesses that can thrive in many scenarios. The future, as always, remains uncertain although a patient long-term approach with risk management at the forefront will likely provide long-term benefits in client portfolios.

All returns are expressed in Canadian dollars unless otherwise indicated.