OPTIMUM Asset Management

Financial Outlook June 2022

By Martin Delage, Canadian Chief Investment Officer

In Brief

- As the central banks accelerated the tightening of their monetary policies, volatility increased in the various financial markets.
- The FTSE Canada Universal Bond Index returned -5.66% in the second quarter of 2022.
- In Canada, the S&P/TSX Index returned -13.19% in the second quarter, with all sectors in negative territory.
- In the United States, the S&P returned -13.35% in Canadian currency in the second quarter.
- The MSCI World Index returned -16.06% on the quarter, recording its worst quarterly performance since the first quarter of 2020.

Economy

In the second quarter, the central banks adopted more aggressive rhetoric in response to persistent inflation and took bold action by raising interest rates significantly, with hikes of 1.25% in the United States and 1.00% in Canada. These actions created a very high level of volatility on the financial markets.

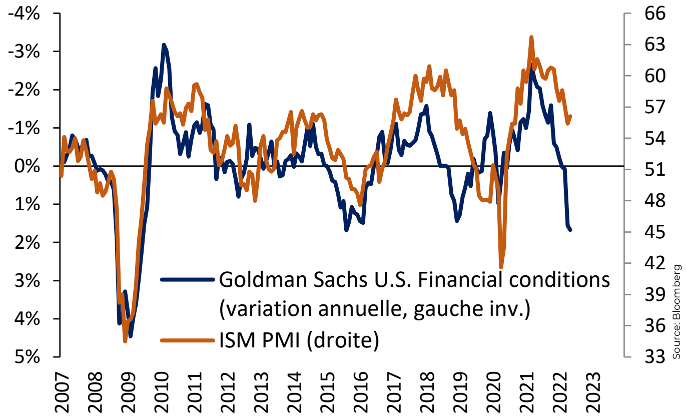
SLOWDOWN OR RECESSION?

Several factors are pointing to an economic slowdown. High energy prices, consumers' loss of purchasing power and the conflict in Ukraine to name only a few – all these factors are indicative of an economic slowdown.

This economic slowdown could lead to a recession.

Even so, the term recession, often thought of in black or white terms, is actually more finely shaded. While there are always risks, we still have a healthy labour market, which, combined with strong household and corporate balance sheets, could act as a mitigating factor if a deep recession occurs.

In our view, the main risk is still inflation. Its sensitivity to slowing growth is debatable, given that it originates partially on the supply side. Moreover, even if it seems that inflation in goods has peaked, the services side is not as clear.



High commodity prices continued to underpin the Canadian economy's growth. That being said, higher household debt, a faster mortgage refinancing dynamic and a more restrictive housing market are fuelling concerns about future growth.

Bond Market

By Hugues Sauvé, FVP, Fixed Income and
Executive Assistant to the Canadian Investment Officer

FTSE Russell Index Returns/ January 1 to June 30, 2022 (%)

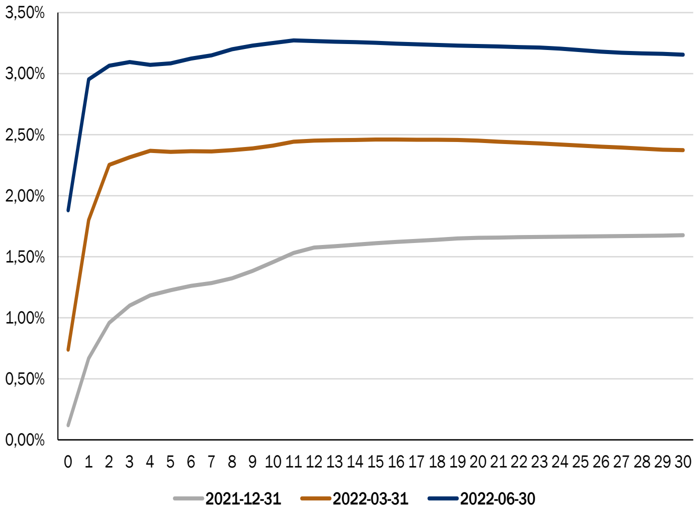
	Federal	Provincial	Municipal	Corporate	Total
Short	-3.92	-4.18	-4.14	-5.21	-4.39
Medium	-11.67	-10.92	-10.67	-11.58	-11.34
Long	-23.22	-22.67	-21.22	-20.08	-22.13
Universe	-9.47	-15.62	-14.08	-10.97	-12.23

Source: FTSE Russell

The Canadian bond market had a second quarter as difficult as the first, with the Universe Index recording a year-to-date decline of more than 12.2%. All components of the FTSE Canada Index performed negatively during the quarter.

Interest rates rose sharply during the quarter, as shown in the following graph. This increase, combined with wider credit spreads for risk assets, caused the value of such assets to decline.

Canada Yield Curves



Data as at June 30, 2022
Source: Bloomberg

STRATEGY

Our bond strategy seeks to benefit from a reversal of negative bond sentiment and a reassessment of central bank robustness in the face of the rapidly deteriorating economic landscape. As a result, we have shifted our portfolios' duration bias upward slightly to benefit from these changes. We also continue to overweight real return bonds to take advantage of their inflation option, their value relative to traditional bonds and their attractive yield.

In our Optimum Public Market Income Core+ Fund, we are maintaining the preferred share component at levels similar to those of the first quarter because we continue to think this asset class has attractive return potential in the current economic environment, even though it is subject to greater volatility than the bond portion of the portfolio.

As for the Optimum Private Market Income Fund, we are deploying new amounts to private debt managers. As the weight of this component of the fund increases, so will its sources of return. It will be recalled that the fund's private debt investments are generally variable-rate. As a result, the fund benefits from the higher interest rates in the current market, which partially offsets the impact of these rates on the value of the bond portion of the portfolio.

Equities

By Nicolas Poirier, Director, Equities

The second quarter of 2022 was negative for the Canadian (S&P/TSX), U.S. (S&P 500) and global (MSCI World) markets. Concerns about the global economic slowdown combined with the crisis in Ukraine caused all sectors of the global index (MSCI World) to decline, despite a better performance by the energy sector and the defensive sectors (consumer staples, health care and utilities).

The U.S. and Canadian markets performed in similar fashion in the second quarter with declines of more than 13%, even though, in the first quarter, the Canadian market advanced 3.8% and the U.S. market declined 5.9% (in Canadian currency). We think the stock markets have priced in the bad news of recent months.

As for emerging markets, they outperformed the other markets in the second quarter thanks to China (+6.75% in Canadian currency), whose government made reassuring comments about new economic stimulus measures.

With the significant declines in the various markets, we took advantage of buying opportunities to increase our exposure.

Stock Indexes

Sector Returns (CAD$) in the Second Quarter

	MSCI World	S&P 500	S&P / TSX
Energy	-4.9%	-2.3%	-1.9%
Consumer staples	-6.2%	-1.6%	-6.2%
Health care	-7.1%	-3.0%	-49.6%
Utilities	-7.2%	-2.1%	11.7%
Real estate	-14.6%	-12.1%	-17.8%
Financials	-15.9%	-14.9%	-13.1%
Industrials	-16.5%	-12.1%	-12.7%
Communication services	-19.3%	-18.2%	-8.8%
Materials	-19.6%	-13.3%	-23.6%
Information technology	-21.7%	-17.8%	-30.7%
Consumer discretionary	-23.7%	-23.9%	-10.2%
Index	-16.1%	-13.5%	-13.2%

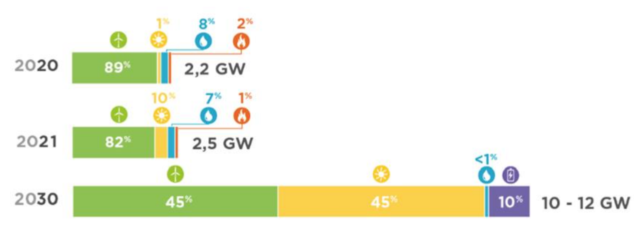
Source: Bloomberg

STRATEGY – LOW VOLATILITY CANADIAN EQUITY FUND

The strategy of Optimum's Low Volatility Canadian Equity Fund is to focus on the most defensive securities in the S&P/TSX Index to ensure better preservation of capital in down markets. Absorbing a smaller portion of a decline generates better returns over the long term. The logic is simple: A 50% loss on an investment requires a 100% return to recover the initial value.

To cite an example of a defensive stock, the renewable energy provider Boralex is part of the Optimum Low Volatility Canadian Equity Fund. The company, which has been in operation for more than 30 years, is a leader in the Canadian market and France's largest independent producer of onshore wind power. The company's revenues are highly predictable, with nearly 98% of its electricity generation subject to prices that are predetermined and indexed over the long term. This visibility allows Boralex to take advantage of growth opportunities and to pay an attractive dividend, and helps support its share price in times of uncertainty. Boralex plans to increase the share of solar in its portfolio of assets and projects significantly by 2030.

Targeted Technological Breakdown of Installed Capacity (in GW)



Source: Boralex

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Asset Management

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WHO WE ARE?

Combined, our asset management subsidiaries manage $7.3 billion Canadian dollars globally for an institutional and private wealth clientele. These subsidiaries are held by Optimum Group, which employs over 600 employees across Canada, the United States and in France.

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