OPTIMUM®
Asset Management

# Financial Outlook September 2022

By Martin Delage, Canadian Chief Investment Officer

## The Virtue of Patience

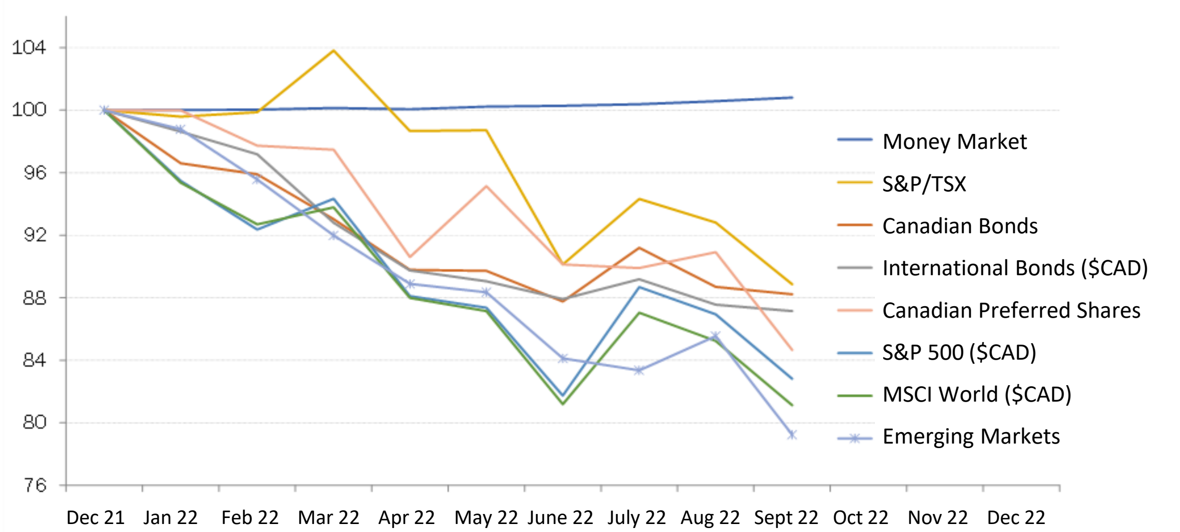
In our previous Financial Outlook, we discussed inflation and recession at length. Even though inflation is still high, the economic indicators are increasingly pointing to a recession. That being said, we think it will be moderate.

As you can see from the table below, all the markets are down on a year-to-date basis. It is highly unusual to see the stock and bond markets lose ground at the same time. Amid these declines, the typical 60-40 balanced portfolio has had the worst performance in 40 years.

Nevertheless, we must keep in mind that the best investment opportunities and the largest increases in value occur as a result of such declines. For any investor, selling after a sharp market decline is tantamount to giving up on the economy's ability to recover.

The Optimum team is monitoring market events not only to position the portfolios so that they can derive maximum benefit from the market rebound, but also to control risk. Don't hesitate to contact your representative if you have any questions about the markets and your portfolio. We're here for you. This is what Optimum Asset Management's Elite Experience is all about.

**Financial Markets' Performance**




Source: Bloomberg

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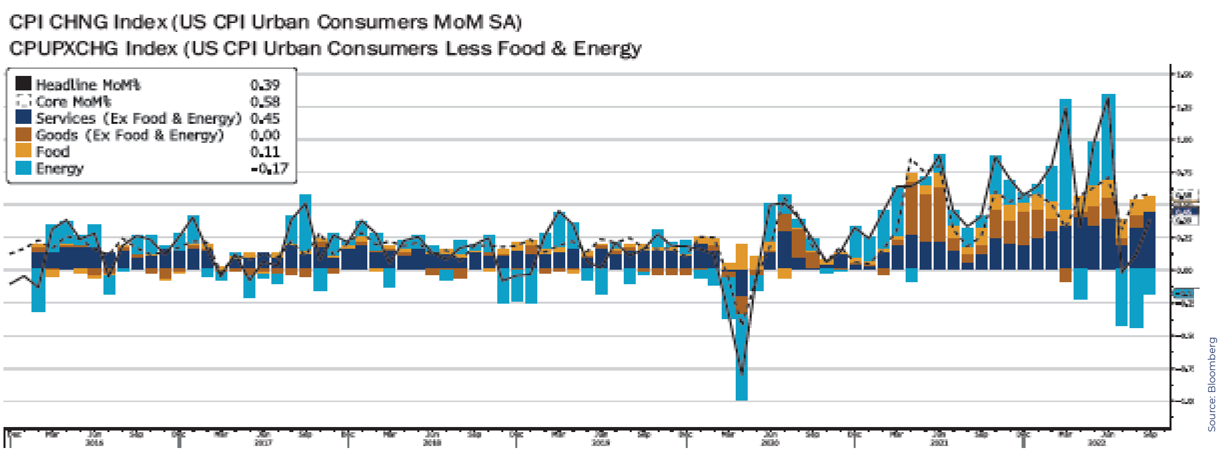
The third quarter failed to reverse the trajectory that the economy has been on since the start of the year. At this point, tougher financial conditions are leading to an economic slowdown. Even so, the impact of the slowdown is mitigated by the job market, which has cooled in recent quarters but remains generally robust. The strong job market is allowing the U.S. Federal Reserve to focus on price stability and to act confidently to prevent inflation from becoming entrenched.

In Canada and the United States, the central banks have been aggressive in raising their short-term rates (+1.75% in Canada and +1.50% in the United States) to bring inflation down to an acceptable level. But because the successive rate hikes have been faster than expected, market volatility has risen sharply.

It is generally accepted in economic circles that central bank policies take effect with a lag of several quarters. Moreover, the combination of lower demand due to rate hikes and unblocking of supply chains should eventually bring inflation down despite rising prices for services. The following chart shows how inflation has shifted from goods to services, which are represented by the dark blue bars. A significant portion of the inflation in services is due to the cost of housing, which economists say will slowly decline.

**CPI Month on Month**




In the international arena, the U.S. economy continues to enjoy a solid position, particularly in terms of its job market, with a 3.5% unemployment rate. Europe is still under pressure and heading for a recession, mainly because of the energy crisis caused by the Ukrainian conflict. As for the Chinese economy, despite various stimulus measures, it is at a standstill owing to the chaotic real estate market and the containment measures still in place in cities with Covid cases.

# Bond Market

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

**FTSE Russell Index Returns/
Third Quarter of 2022 (%)**

| | Federal | Provincial | Municipal | Corporate | Total |
|---|---|---|---|---|---|
| **Short** | -0.38 | -0.20 | -0.19 | -0.27 | -0.31 |
| **Medium** | 0.93 | 1.00 | 0.99 | 0.35 | 0.84 |
| **Long** | 1.77 | 1.57 | 1.23 | 1.22 | 1.51 |
| **Universe** | 0.27 | 0.99 | 0.75 | 0.23 | 0.52 |

Source: FTSE Russell

The Canadian bond market saw bifurcated returns in the third quarter. Short-term notes had negative returns because of central bank rate hikes, whereas medium- and long-term maturities performed better. The Universe Index, which includes all maturities, was up 0.52% on the quarter.

According to our analysis, the Canadian bond market's outperformance relative to that of the United States is symptomatic of our fragile domestic demand, compounded by global commodity weakness. Even so, we think this outperformance will be difficult to maintain in the current context. We expect the Canadian dollar to weaken further in order to offset any new adverse events that may affect the Canadian economy.

Even though the market's decline has been fairly orderly, volatility is very high and liquidity is diminishing. We have flirted with a financial debacle several times (Credit Suisse, United Kingdom and Italy), and, with the U.S. dollar's uptick (+5%), we expect things to get worse before they get better.

## STRATEGY

For our Canadian bond strategy, we are maintaining a slightly long duration bias. Our position is protected by tight stop losses to limit downside risk in a highly volatile market.

We also continue to overweight high-quality credit because we think the current spreads offset the risk of recession. As for lower-quality credit, we are still taking a cautious approach and will wait until credit spreads reach recession levels before adding to this position in the portfolios. Finally, we are maintaining our overweight in real return bonds as a hedge against inflation.

# Equities

By Nicolas Poirier, Director, Equities

The third quarter of 2022 was negative for the Canadian market, with the S&P/TSX Index returning -1.41%. The same was true for the MSCI World Index, which returned -0.07% in Canadian dollars. Even so, the U.S. S&P 500 Index had a positive return of 1.32% in Canadian currency.

On the Canadian market, the communication services, health care, real estate and energy sectors all declined by more than 5% in the third quarter.

Notably, the health care and information technology sectors have lost more than half of their value since the start of the year, with declines of 56.89% and 57.39%, respectively.

| Canadian Stock Market | | |
|---|---|---|
| Sector Returns | | |
| | 3rd Quarter | YTD 2022 |
| Energy | -5.27% | 19.57% |
| Consumer Staples | 2.62% | 1.48% |
| Health Care | -6.44% | -56.89% |
| Utilities | -4.63% | -3.39% |
| Real Estate | -6.44% | -26.71% |
| Financials | -1.24% | -12.33% |
| Industrials | 4.23% | -5.51% |
| Communication Services | -7.33% | -7.99% |
| Materials | 2.52% | -5.96% |
| Information Technology | -4.69% | -57.39% |
| Consumer Discretionary | 4.18% | -13.65% |
| Index | -1.41% | -11.14% |

Source: Bloomberg

The market downturn has taken price-to-earnings ratios on the U.S. and Canadian markets down to levels not seen since the 2008 crisis. As a result, we see buying opportunities for investors who have a longer investment horizon and can tolerate the current volatility on the financial markets.

**Price-to-Earnings Ratio – Canadian Stock Market**


Source: Bloomberg

## STRATEGY – OPTIMUM CANADIAN EQUITY FUND

The Optimum Canadian Equity Fund focuses on high-quality companies with excellent profitability, low leverage and substantial cash flows. Over the long term, these companies increase their top-tier intrinsic value and maintain a resilient financial performance, regardless of the macroeconomic context.

In the third quarter, our overweight in industrials and consumer staples contributed to the strategy's outperformance vis-à-vis the index. With no energy sector holdings, the strategy also benefited, as this sector declined amid lower oil prices.

The high-quality companies we added to our portfolio during the quarter included Aritzia, WSP Global and Loblaw. Aritzia is a design house and high-end fashion boutique that has been offering exclusive brands since 1984. WSP Global is an international advisory services and technical expertise firm that has nearly 55,000 employees and operates on a growth-by-acquisition model. Loblaw is one of Canada's largest food, pharmacy and health-care retailers with nearly 220,000 employees.

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# Our Team

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## WHO ARE WE?

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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