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Global Asset Management

Financial Outlook September 2024

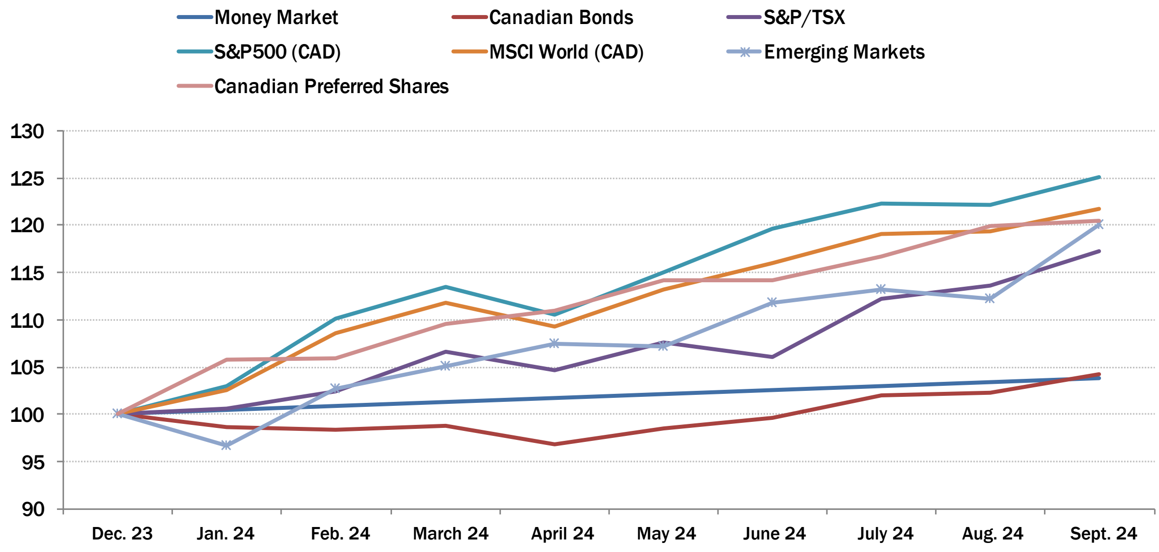
By Martin Delage, Canadian Chief Investment Officer

The Market Makes a New Peak Despite Economic Concerns

The third quarter of 2024 at a glance:

- The U.S. Federal Reserve cut its key interest rate by 50 basis points and the market is expecting another cut of at least 50 basis points by the end of the year
- The Canadian key rate remained at 4.25%, contributing to the pressure on borrowers and indebted sectors
- Emerging markets performed well, supported by China’s new stimulus measures
- The Canadian stock market (S&P/TSX) advanced more than 10.5%, led by the financials sector

Monthly Financial Market Returns



Source: Bloomberg

Monthly economic video
Stay abreast of the economy and financial markets: Watch our videos by clicking on this link (*French only*).

Economy

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

During the quarter, inflation and the labour market continued to weaken, reducing the need for central banks to keep interest rates above the range of 2.25% to 3.25%. As a result, they adopted a more accommodative monetary policy, leading to significant rate cuts. This shift increased the likelihood of a soft landing for the economy and boosted the equity markets.

The U.S. economy has solid momentum, with second-quarter real GDP growth clocking in at 3.0%, and GDP Now's estimate for the third quarter is similar. Even though the labour market is slowing slightly, it remains resilient with low initial jobless claims, a high participation rate and rising unemployment due to the entry of new workers (see graphs below).

In this context, the Federal Reserve's recent decision to cut its key interest rate by half a point is surprising, as are the expectations of more cuts, because we think the risk that inflation will tick up is underestimated.

U.S. Labour Force Participation Rate

Source : Bloomberg

Contribution to the Change in the U.S. Unemployment Rate since February 2023

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Economy (cont'd)

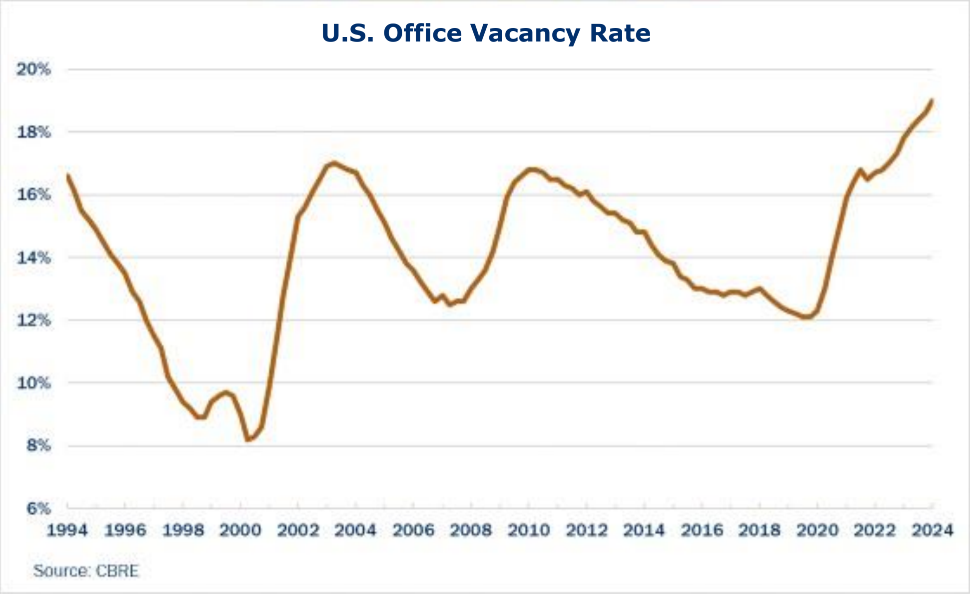
By Hugues Sauvé, FVP, Fixed Income and
Executive Assistant to the Canadian Investment Officer

A Look at the Real Estate Sector

Since the 2020 pandemic, a number of trends have profoundly changed commercial real estate. The rise of remote work, the modernization of corporate functions, changing tenant preferences and higher interest rates have redefined the market, leading to a higher office vacancy rate (see graph below). In fact, Moody's predicts that the rate could reach 24% by 2026, with landlords potentially losing $250 billion. Regional banks, which hold about 70% of the $2.9 trillion in loans to the sector, are especially vulnerable because of unrealized losses in their loan portfolios.

In Canada, concerns are emerging because many residential mortgages taken out in 2020 at historically low rates will have to be renewed in 2025. In addition, the expected slowdown in immigration and in the U.S. economy could weaken some growth drivers. That being said, despite high valuations and low affordability, the housing market is expected to continue supporting the economy, thanks to a structural imbalance between supply and demand, reinforced by government stimulus measures, longer-term mortgages and construction programs.

At the same time, China has announced a stimulus package that includes rate cuts, an easing of regulations in the property sector and bank interventions to support its stock market. Even so, the effectiveness of these initiatives is uncertain because structural reforms are needed to boost domestic demand, strengthen the social safety net and address confidence and inequality issues.



PRI Principles for Responsible Investment

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Bond Market

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

Returns on FTSE Russell Indexes / Third Quarter 2024 (%)

Maturity	Federal	Provincial	Municipal	Corporate	Total
Short	3.10	3.48	3.39	3.77	**3.39**
Medium	5.30	5.45	5.44	5.60	**5.40**
Long	6.31	5.51	5.61	5.98	**5.75**
Universe	4.33	5.05	4.97	4.67	**4.66**

Source: FTSE Russell

Global bond markets began the third quarter cautiously amid renewed concerns about inflation in the United States, prompting a reassessment of the schedules for interest rate cuts. At the start of the quarter, the central banks held rates steady, with the exception of Canada, where a 25-basis-point cut led to a strong bond market performance (see graph above).

It wasn't until September that other central banks joined in. The U.S. Federal Reserve cut rates by 50 basis points in response to an unexpectedly large decline in inflation and employment. This decision weakened the dollar and caused bond yields to fall, especially two-year Treasury notes.

The European Central Bank also cut rates by 25 basis points. German and French 10-year government bonds saw their yields decline and their prices rise but they underperformed in relation to Italy and Spain, which were the best performers in Europe.

As for our Canadian bond strategy, all our biases performed well during the quarter. We took profits on our long-duration bias when the 10-year yield reached 3.0%. We also went back to real return bonds, which offer a favourable option on inflation.

In credit, our stance is defensive owing to the limited potential for gains, which has prompted us to focus on identifying idiosyncratic securities. Despite recent increases, we still consider preferred shares attractive because we think they offer an adequate return in the current market.

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Equities

By Nicolas Poirier, Director, Equities

In the third quarter, global stock markets rose sharply, taking a number of indexes to new all-time highs. Investor confidence got a boost from rate cuts by the U.S. Federal Reserve and a number of other central banks around the world, the Chinese government's measures to revitalize its economy and strong U.S. corporate earnings. A significant advance by the Canadian banking sector enabled the Canadian market to outperform the global markets. The main risks we are monitoring are the lagged effect of rate hikes on the job market and geopolitical risks.

In Canada:

- The S&P/TSX Index rose 10.50% on the quarter
- Best sectors: real estate, financials and utilities
- Worst sectors: energy, industrials and consumer staples
- The rise in the price of gold benefited the materials sector
- The technology sector's underperformance was due to declines in Open Text (-21.2%) and Shopify (-13.5%)

Optimum Canadian Equity (10.02% gain in Q3 and 19.65% for 2024)

During the third quarter, the strategy benefited from its absence from the energy sector and its overweight in the consumer staples and consumer discretionary sectors. That being said, it suffered from an overweight in industrials and an underweight in financials. One of the portfolio's holdings, Sleep Country, received a takeover bid at a 34% cash premium, and the proceeds of the disposition were reinvested in the portfolio. Our companies continued to report solid results and stood out from the more cyclical companies in the natural resource sectors. Canadian banks' lower loan-loss provisions suggest the economic environment will improve in the coming months.

Optimum Low Volatility Canadian Equity (8.68% gain in Q3 and 14.78% for 2024)

The third quarter was somewhat difficult for the Low Volatility Canadian Equity strategy, given the strong performance by the Canadian stock market. The strategy captured about 83% of the market's upside, which is in line with its history in a rising market. The underweight in the energy sector and the overweight in the real estate sector were beneficial, but the overweight in industrials and materials subtracted value during the quarter. The investor enthusiasm sparked by central bank easing may abate; thus, we think it is wise to stay invested in the most defensive companies in the Canadian stock index in the coming months.

Equities (cont'd)

By Nicolas Poirier, Director, Equities

Optimum Canadian Equity Multifactor (11.06% gain in Q3 and 17.46% for 2024)

During the quarter, the strategy benefited from an underweight in the energy sector as well as an overweight in the real estate sector. Even so, it suffered from underweight positions in the financials sector, especially Canadian banks, and the technology sector. The momentum portion of the strategy stood out during the quarter with its stock selection in industrials and consumer staples. A rising market is ideal for such a strategy because it overweights stocks with the best recent performance. The equal-weight portion also benefited from the strong performance by smaller caps, notably by underweighting energy and industrials.

In the United States:

- The S&P 500 gained 4.50% in Canadian currency during the quarter
- Best sectors: real estate, industrials and utilities
- Worst sectors: technology, communications and energy
- Smaller-cap companies stood out, with the S&P 500 Equal Weight Index outperforming the S&P 500 Index by 3.71% during the quarter
- The energy sector's underperformance was due to the lower oil price

MSCI World Index:

- The index returned 5.01% in Canadian currency during the quarter
- Top sectors: real estate and utilities
- The Canadian stock market outperformed the MSCI World with its strong weighting in financials

Optimum Global Equity (6.76% gain in Q3 and 14.93% for 2024)

Global stock markets ended the third quarter higher on rate cuts by a number of central banks, including the U.S. Federal Reserve, as well as sustained growth of U.S. corporate earnings. The strategy benefited from stock selection in the consumer discretionary, industrials and financials sectors. Even so, it suffered from its stock picking in the technology sector and its absence from the utilities and real estate sectors, which performed well. The strategy benefited from the outperformance of smaller-cap companies in relation to larger caps. The S&P 500 Equal Weight Index outperformed by 3.71% relative to the S&P 500 Index, which had its worst quarterly relative performance since 1990. We are convinced these companies will tend to outperform the indexes over the long term, particularly given their size.

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Who are we?

The three asset management firms are subsidiaries of Optimum Financial Group, a diversified, global and privately owned group whose mission since 1969 has been to ensure its clients' financial security.

With a track record of more than 35 years in asset management, we have brought together a team of highly qualified professionals from various areas of the financial and technology sectors.

The firms stand out with their client proximity and excellence. Optimum Asset Management in Canada combines its talents with those of its sister companies, Optimum Gestion Financière in France and Optimum Quantvest in the United States. With teams in three countries, we have privileged access to various markets. The subsidiaries had a combined CA$8.7 billion in assets under management for institutional and private clients as at September 30, 2024.

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The performance is shown in Canadian dollars, before management fees and is annualized for all periods over one year.

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The indexes used in the present document are indexes which are widely recognized benchmarks used to measure investment performance for their respective asset classes and were chosen based on their degree of comparability and similarity with the investment strategies presented.

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