iA Clarington

2021 Market Outlook

iA Wealth

Year Ahead 2021

This past year will be remembered as the "year of the virus". Daily life changed in ways we never could have anticipated, and the longest business cycle on record came to an abrupt end, bringing with it unprecedented economic uncertainty. As we now turn our sights towards the year ahead, it is clear that 2021 will be the "year of the vaccine".

While considerable uncertainty remains, a number of positive developments are taking shape. First, the immense amount of fiscal stimulus that was pumped into the global economy – totalling more than 10% of GDP, on average, within developed countries, and 16% in Canada[1] – should act as a significant tailwind in 2021. A large part of this stimulus money has been saved by households, which are likely to spend more once the economy reopens.

Second, central banks are likely to keep interest rates low and continue to pump liquidity into the global economy through their quantitative easing programs. The U.S. Federal Reserve (Fed), in particular, has indicated that it will be at least a couple of years before the punch bowl gets taken away.

Third, we cannot imagine a stronger form of fiscal stimulus than a global vaccination campaign. As the economy gradually reopens, we should see an unwinding of pent-up demand and a few quarters of above-potential growth in both developed and emerging countries.

In the U.S., the labour market rebounded sharply during the summer, but began to lose steam in the closing months of 2020. Additional fiscal stimulus will likely be necessary in 2021 to prevent long-term damage to the workforce. With the appointment of former Fed Chair Janet Yellen as Treasury Secretary, it appears that this much-needed help will soon be on the way.

At home, the Canadian economy is performing very well heading into 2021, with the labour market about 80% of the way back to its pre-pandemic peak and no talks of pulling the plug on fiscal support. We anticipate good things from the Canadian economy in 2021 and expect it to outperform the U.S. Importantly, the likelihood of an improved relationship with our main trading partner to the south will also be a significant positive going forward.

Finally, even though global equity markets have rebounded at the swiftest pace ever since the lows of March, and are again sitting at or near all-time highs, we are optimistic about the return outlook for 2021. The broad underlying market rotation should support further gains in equities throughout the year, although continued pandemic-driven unpredictability will likely bring a healthy dose of volatility. The year ahead should be a good one for active portfolio managers and those willing to take on a bit more risk than they normally would.

– Clément Gignac

First Vice-President, Diversified Funds & Chief Economist
iA Investment Management Inc.

[1]Source: Statista (https://www.statista.com/statistics/1107572/covid-19-value-g20-stimulus-packages-share-gdp/).

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Dan Bastasic MBA, CFA

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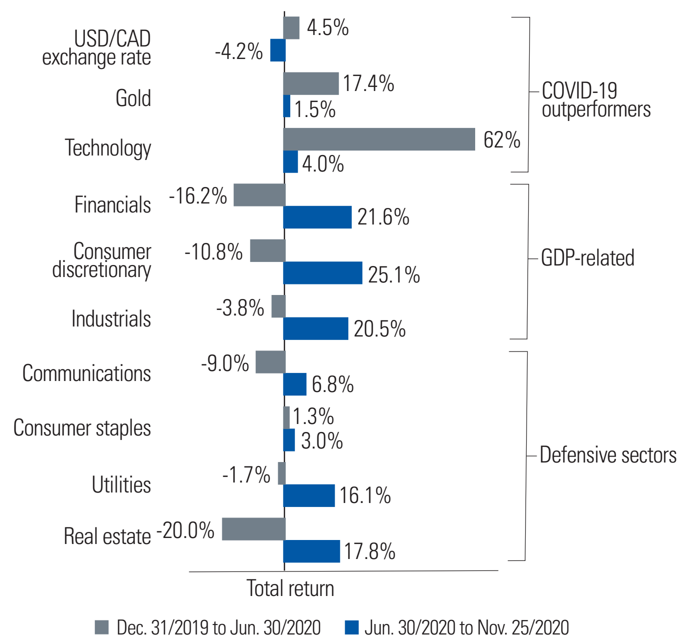
Where are the opportunities?

From COVID-19 and millions of lost jobs to a highly contentious U.S. presidential election, this past year has been like no other in recent memory. Yet the markets have managed to set new highs in the U.S., with Canada closely following suit. Unprecedented fiscal and monetary policy measures backstopped both Main Street and Wall Street, giving investors the time and confidence to endure the pandemic. This stimulus will likely be with us for years to come, and central banks have indicated that they intend to keep short-term rates at historically low levels.

Sector returns after the mid-year point gave us a glimpse of our possible future and the potential investment opportunities that lie ahead. Within equities, seven sectors drove returns – compared to just two in the first half of the year (see chart). We expect economic growth and corporate earnings to accelerate over the course of 2021, creating tailwinds for equity and higher-yielding bond returns.

Asset class and TSX sector returns in 2020



Source: Bloomberg, as at November 25, 2020. TSX = S&P/TSX Composite Index.

Sectors that will benefit from accelerated earnings growth and attractive valuations will likely include financials, consumer discretionary, and cyclically related stocks. High-dividend-yielding equities will likely see gains from the lack of yield available from government bonds. The U.S. Federal Reserve has promised to keep rates low for the foreseeable future, which will be a major contributing factor to a depreciating U.S. dollar. Global markets, including Canada, will likely benefit from this over the next year.

What are the challenges?

Despite unprecedented fiscal and monetary support, current valuations in parts of the equity and fixed-income markets leave them vulnerable to shocks, whether it be a rotation away from what drove returns in the first half of 2020 – technology and gold – or an unexpected lift in inflation expectations due to liquidity in the economy.

This year could truly shape up to be a market of individual stocks instead of a stock market. Security selection and allocation will be key to managing risk-adjusted returns during the year. While we are confident that global economies will accelerate in 2021 and market returns will follow, there are ingredients of uncertainty and doubt, which may produce a more stair-stepped advance in place of the V-shaped recovery seen during 2020.

How are you positioning the Funds?

Our overall positioning – broad exposure to equities complemented by an allocation to higher-yielding bonds – has not materially changed during the past three months. Our exposure in the second half of 2020 has tilted towards financial, consumer and industrial-related securities that offer attractive valuations and have higher operating leverage to a reopening of global economies. Within fixed income, we see the best opportunities in higher-yielding bonds that benefit from corporate earnings improvements and have lower sensitivity to interest rate increases. Since the beginning of Q3, we have hedged the majority of our U.S. dollar exposure to mitigate currency risk.

Why is this the right approach for 2021?

We strive to deliver the best possible risk-adjusted returns over time, and while 2021 is shaping up to deliver historically high corporate earnings and economic growth, we believe there is more risk in following the return drivers of the first half of 2020 (technology and gold) than in allocating capital to securities with a yield advantage and the potential to benefit from synchronized global growth.

In 2021, we believe it will be important to hedge foreign currency, have outsized exposure to higher-yielding stocks and bonds, and reduce overall volatility through a healthy complement of undervalued defensives.

Jean-Pierre Chevalier CFA

iA Investment Management Inc.

IA Clarington Global Value Fund

IA Clarington Global Value GIF

IA Clarington Thematic Innovation Class

Where are the opportunities?

U.S. equity markets recovered quickly following the downturn in the first quarter of 2020. Fiscal and monetary policies were effective, while a large part of the economy was able to use technology to adapt to the pandemic. In fact, one could argue that the economy, at the most fundamental level, is powered today by data, bandwidth and processing technologies. Science also came to the rescue with massive efforts that led to a vaccine breakthrough towards the end of the year.

As we move into 2021, consensus expectations are for a gradual reopening of the economy as the vaccine is made available globally. Equity markets are already pricing some of this in, with significant outperformance of cyclical industries since last summer and especially in November.

We think there are still outperformance opportunities in companies that were disrupted by COVID-19, such as airlines and restaurants. But we view these opportunities as very tactical in nature, since the market will quickly price in the upcoming reopening well in advance.

The 2020 recession was one of a kind on many fronts. One thing that is different is the fact that savings levels have risen quite significantly, a result of stimulus payments and months of discretionary spending cutbacks. Thus, we are of the view that post-vaccine, we could see a very strong consumer boom in the U.S. This could mean positive earnings revisions for domestic-exposed companies.

What are the challenges?

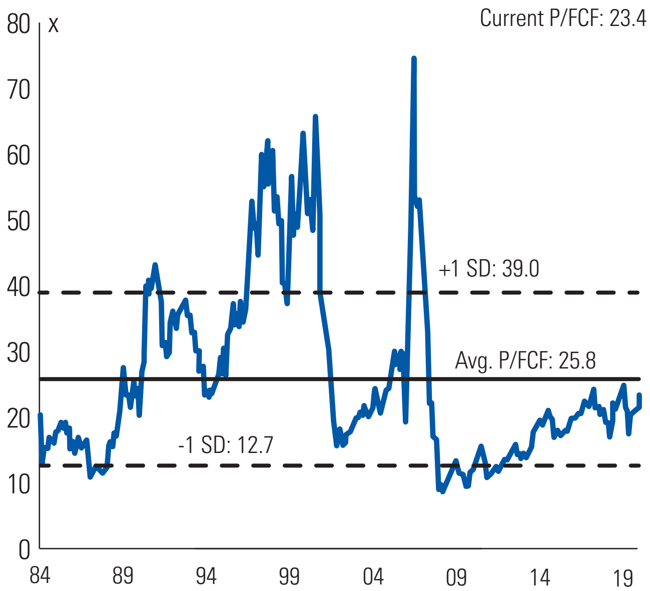
It appears we are heading towards a tough winter with the second wave of COVID-19. There is some potential for increased volatility, but we think the market will remain focused on the upcoming benefits of the vaccine.

The U.S. presidential transition seems to be going relatively well considering the context, but this could also bring uncertainty if tensions rise from here. Control of the Senate has still not been decided, as Georgia's two seats will not be filled until the run-off elections in January. We believe there is a low probability that the Democrats prevail and complete the blue sweep, but this is a risk factor at the start of the year. If the Republicans are able to hold the Senate, it could result in political gridlock, which is historically positive for U.S. stocks.

The U.S. equity market's valuation is elevated on an historical price-to-earnings ratio (P/E) basis. But it is important to remember that the equity market valuation is inversely correlated to the level of interest rates on a non-linear basis. That makes the P/E multiple very sensitive to any significant move in interest rates. So far, central banks have signaled a willingness to be patient before raising rates.

We believe COVID-19 has permanently accelerated the growth of intangible assets and their deflationary pressures. We will continue to monitor this closely. We also think U.S. companies will benefit from an enhanced ability to convert earnings into free cash flow. In fact, when you look at valuation on a free-cash-flow basis, it is a more positive story – and we will take real free cash flow over accounting-based earnings any day.

2021 outlook getting back to normal



Source: Credit Suisse, Standard and Poor's, Thomson Financial and FactSet. Data as at November 21, 2020. P/FCF = price-to-free cash flow ratio; SD = standard deviation.

How are you positioning the Funds?

IA Clarington Thematic Innovation Class is a U.S. equity fund that invests in companies from all sectors benefitting from technological advances and a perpetually changing environment. This is a well-diversified strategy, making it possible to have a strong focus on risk management while benefitting from a deep understanding of long-term innovation themes.

We construct the portfolio using a barbell strategy. On one side, we like to have exposure to innovators and keep between 5–15% in small- and mid-cap stocks. On the other end, we go with dominant firms that provide more exposure to the reopening of the economy.

We think the recovery will be more targeted towards productivity than new capacity. To take advantage of this, we are currently invested in themes including smart cities, building efficiency and industrial automation.

The pandemic brought attention to the importance of investing in the future of health care. We think the confluence of connectivity and genomics is resulting in many opportunities from a stock selection point of view.

In our view, artificial intelligence, genomics and smart energy technologies will be driving U.S. equity returns over the next decade in the same way that digital advertising, e-commerce and cloud computing explained most of the returns in the last decade. We live in a world of technology-driven change and COVID-19 is further accelerating this theme. The impact is broad and affects all sectors and industries. How companies deal with this is central from a stock selection perspective.

Why is this the right approach for 2021?

Our focus is on risk management and stock selection. Position sizing is very important for us; we apply strict guidelines to keep a strong discipline and we do not let emotions get in the way. We think investing is about the future and we will continue to refine our unique thematic style while incorporating our differentiated view of what lies ahead.

A possible pitfall is to have a narrative that fails to adjust for the significant rerating of cyclicals following the first vaccine announcement. There is a good chance that very early in the new year, the markets will be pricing in a full reopening of the economy. We think it will be important to be nimble tactically and reinvest in other parts of the market.

It is also important to keep an open mind, because if there is one thing we learned in 2020, it is that an outlook can change very rapidly. As a famous boxer once said, "Everybody has a plan until they get punched in the mouth."

Clément Gignac MESc

iA Investment Management Inc.

iA Wealth Managed Portfolios
IA Clarington Global Yield Opportunities Fund
IA Clarington Monthly Income Balanced Fund
IA Clarington Monthly Income Balanced GIF
IA Clarington Yield Opportunities Fund
IA Wealth Enhanced Bond Pool

Where are the opportunities?

COVID-19 brought the record-long business cycle and bull market to an abrupt end in early 2020, meaning we are now officially in an early cycle market environment. We expect a few years of strong economic growth with limited inflationary pressures as the massive output gap created during the pandemic-induced recession gradually closes. In our view, the investment implications are clear: equities should outperform bonds, the yield curve should gradually steepen, small- and mid-cap stocks should outperform large caps, cyclicals should outperform technology and, finally, value should outpace growth.

We favour an overweight equity position that is globally diversified. The U.S. stock market has dominated all other major markets over the last decade and is now relatively expensive. With the ongoing rotation towards value and cyclicals, we expect the U.S. market to underperform in 2021, with emerging markets, EAFE (Europe, Australasia and the Far East) and Canada having a good year.

What are the challenges?

There is still significant uncertainty surrounding COVID-19, and it could be argued that equities may already be pricing in a lot of good news as we move into 2021. Although we are optimistic about the reopening of the economy and earnings growth over the next few years, we remain fully committed to our prudent approach to risk management.

There is also some risk that the economic recovery becomes a bit too strong and inflation rears its head, as the massive quantities of stimulus in 2020 translate into a strong and swift rise in interest rates. Such a scenario could create the fear that central banks will tighten monetary conditions earlier than expected, which would weigh on risk appetite.

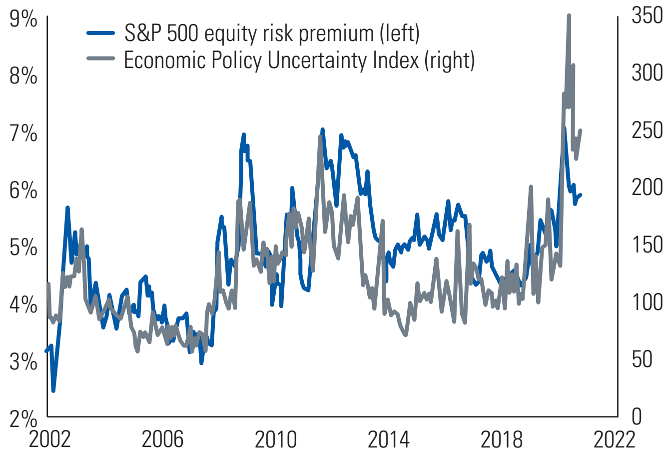
Our overall view is that the current environment calls for prudence and caution in the face of unprecedented macro-level uncertainty.

How are you positioning the Funds?

As noted above, our strategy is to overweight equities relative to bonds and diversify this overweight globally. The equity risk premium – the portion of equity returns that exceeds the risk-free rate – is still sitting at historically elevated levels (see chart), even though typical valuation measures such as the price-to-earnings ratio suggest the market is expensive. The equity risk premium is helpful for highlighting the fact that asset allocation deals with the relative valuation of assets. Currently, with interest rates still sitting near all-time lows, equities as an asset class are quite attractive compared to bonds.

S&P 500 Index equity risk premium and economic policy uncertainty

Monthly as of October 31, 2020



Source: PolicyUncertainty.com, Goldman Sachs Global Investment Research. Equity risk premium calculated by subtracting the 10-year U.S. rate from the earnings yield on the S&P 500 Index.

While we acknowledge that it is always risky to underweight the U.S. stock market, we are positioning our Funds so that the equity overweight is spread across regions that have underperformed over the last few years and are now ripe for a revaluation. We thus favour emerging markets, EAFE and Canada, as all three are well positioned to benefit from the underlying market rotations from growth to value and cyclicals.

On the fixed-income side, we prefer to keep duration low, as interest rates are likely to move progressively higher in 2021. We are also favouring corporate bonds over government bonds to benefit from the additional yield.

We expect the global economic recovery to push the Canadian dollar higher relative to the U.S. dollar. Accordingly, we will continue to actively hedge our U.S. dollar exposure over the course of the year.

Finally, we are still holding a small position in gold. It acts as a good diversifier in periods of geopolitical uncertainty and should benefit from the low-rate environment we expect over the next few years.

Why is this the right approach for 2021?

We see 2020 as the year of the virus, and 2021 as the year of the vaccine. This means that the world will slowly get back to normal, to an economy swimming in liquidity. This environment should be supportive of risk assets, but diversification will remain key, as the lingering uncertainty will likely create bursts of volatility throughout the year.

Reduced economic uncertainty in 2021 relative to 2020 will likely push the equity risk premium lower, which should come through a combination of gains on equities and rising interest rates.

Alexandre Morin CFA

iA Investment Management Inc.

IA Clarington Bond GIF
IA Clarington Money Market Fund
IA Clarington Money Market GIF
IA Clarington Real Return Bond Fund
IA Wealth Core Bond Pool

Where are the opportunities?

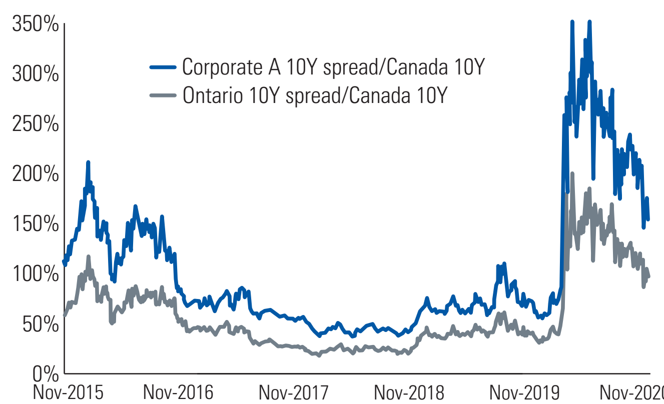
While 2020 was marked by an extraordinary event that had a major impact on the markets and life in general, we believe 2021 will bring with it a return to a certain normality. To cope with the damage caused by the COVID-19 pandemic, governments have had to rapidly and significantly increase their indebtedness. After having borrowed urgently with very short terms to maturity, they now want to take advantage of historically low rates to extend the duration of their debt.

For their part, central banks continue to buy large quantities of government bonds to prevent a rapid and disorderly rise in long-term interest rates, which would slow the economic recovery. In addition, it will take a long time for them to begin a cycle of overnight rate normalization given the low level of inflation we have had for several years.

Overall, we believe the significant borrowing needs of governments combined with overnight rates near zero should result in additional yield curve steepening in 2021. We will position our portfolios opportunistically to take advantage of this.

Given historically low interest rates, we believe that a large overweight to credit will be a good approach for 2021. We expect to be overweight corporate bonds, as their shorter duration makes them an attractive investment in an environment where long-term interest rates are rising moderately (see chart). This past year saw record volumes of new corporate bond issues, resulting in significant cash on hand. In addition, no less than US$17 trillion worth of bonds outside of North America are trading at negative interest rates, which means that North American corporate bonds offer attractive yields to maturity.

Excess yield of credit bonds as a percentage of federal 10-year yields



Source: Bloomberg, as at November 26, 2020. Canada 10Y = Government of Canada 10-year bond yield; Corporate A 10Y spread = Canadian Corporate A-rated bond spread; Ontario 10Y spread = Province of Ontario 10-year bond spread.

We expect to be overweight municipal bonds. In particular, we like non-rated bonds from municipalities in the province of Quebec, as their short maturities (generally less than five years) make them an attractive investment in a context of rising long-term interest rates.

We anticipate that interest rates could increase less rapidly outside of North America because fiscal stimulus measures are less expansive than they are here and central banks buy more bonds in proportion to the size of their respective markets. As a result, we plan to invest part of our portfolios outside of North America to take advantage of this desynchronization in the movements of different interest rate markets. We also plan to dynamically manage exposure to exchange rate fluctuations between the Canadian dollar and a number of foreign currencies.

Finally, central banks appear more determined than ever to support a sustainable return of inflation after almost never hitting their targets since the Great Financial Crisis. With this in mind, we will consider opportunistically investing a portion of our portfolios in bonds whose values fluctuate according to the level of inflation, such as real return bonds in Canada and Treasury inflation indexed bonds in the U.S.

What are the challenges?

The first half of 2021 will be challenging. Changes in interest rates will be intimately linked to the severity of the COVID-19 crisis and the possibility of large-scale distribution of one or more vaccines to counter the pandemic. Currently, most strategists and analysts are expecting long-term interest rates to go up in 2021. But we must always remain cautious about the consensus view, because if events do not unfold in line with expectations, the market may react violently. Therefore, we will remain nimble in managing duration and yield curve positioning. It is not certain that the evolution of long-term interest rates in 2021 will translate into a continuous and uninterrupted rise. Also, the attractiveness of the relatively high level of North American interest rates for foreign investors should mitigate this increase.

The various levels of government have resorted to unprecedented fiscal measures, which have helped alleviate the severity of the crisis and support a strong economic recovery. Central banks, for their part, have bought a lot of bonds in order to balance supply and demand. The future of this balance will be important. Although they are readjusting their level of involvement, central banks will play a critical role in containing a significant rise in long-term interest rates stemming from a glut of securities in the market. As for the various levels of government, they could pump more oxygen into the economy through additional spending and investment programs, resulting in even greater borrowing needs.

Politics and geopolitics played a significant role in 2020. They could very well continue to complicate the current economic recovery if, for example, additional fiscal stimulus is slow to materialize in the U.S. Also, the markets will be on their guard regarding how Joe Biden and the Democrats govern. Plus, we must not forget that before the shock of the pandemic, some major issues were still unresolved, including trade relations between the U.K. and Europe, trade tensions between the U.S. and China, and the situation with Iran.

How are you positioning the Funds?

In line with the opportunities outlined above, our portfolios have a substantial allocation to quality corporate credit securities. After undergoing a dramatic widening last spring, credit spreads have tightened significantly. Strong government support for the economic recovery should favour companies that were able to weather the 2020 crisis. In addition, central banks are providing significant support through corporate bond buying programs. Finally, investors' search for yield should continue to favour corporate bonds.

We also have exposure to various U.S. credit products, such as corporate securities with a maturity of less than five years and high-yield corporate bonds. The aim is to benefit from their excess returns and the depth and diversity of issuers in these markets.

As mentioned earlier, we like municipal bonds and intend to maintain an overweight to this asset class throughout 2021.

We will remain nimble when it comes to duration, which we will manage via Canadian, U.S. and other interest rate markets.

Finally, we expect that the anticipated rise in long-term interest rates, combined with an overnight rate anchored by central banks, should lead to a steepening of the yield curve. As is the case with our duration management, we will remain nimble in our yield curve positioning to take advantage of opportunities as they present themselves.

Why is this the right approach for 2021?

Agility, liquidity and the pursuit of value are among the main factors guiding our investment process. Portfolio strategy is driven by multiple actions taken simultaneously based on our most likely scenario, and we have the ability to tactically adjust certain parameters to modify the portfolio's risk level and improve its expected return. Calling on multiple positions at the same time gives us flexibility with the desired level of risk as well as the ability to quickly adjust if necessary.

Finally, our approach for 2021 will be to protect our portfolios against possible long-term interest rate hikes while taking advantage of the risk premium offered by credit securities.

Donny Moss CFA

iA Investment Management Inc.

IA Clarington Canadian Conservative Equity Class
IA Clarington Canadian Conservative Equity Fund
IA Clarington Canadian Conservative Equity GIF
IA Clarington Canadian Dividend Fund
IA Clarington Dividend Growth Class
IA Clarington Dividend Growth GIF
IA Clarington U.S. Dividend Growth Fund
IA Clarington U.S. Dividend Growth GIF
IA Clarington U.S. Dividend Growth Registered Fund

Where are the opportunities?

In 2020, excess returns were concentrated in a few areas, particularly technology, gold and stocks that benefitted from the pandemic. We expect that in 2021 returns will become more evenly dispersed, and with the encouraging vaccine data that has recently been released, we have already seen some rotation into previously underperforming sectors, such as financials and energy. We think financials can perform better in 2021, as bank loan losses will be contained at lower levels than first estimated, while interest rates have bounced off lows and consumers sit on excess cash levels.

We also think Canadian multifamily real estate is interesting and should perform better as immigration resumes. Finally, consumer retail remains an important area to watch, as companies providing a good online and brick-and-mortar experience should continue to outperform and grow without needing to expand their physical footprint.

What are the challenges?

One of the main challenges for equities as we move into 2021 is valuations. We have witnessed a massive rebound from the March lows to new all-time highs; however, it is important to remember that we are still recovering from a major economic recession. There continues to be a large amount of government support in the economy, and there is potential for volatility if this support is dialed back as we move through 2021.

In addition, while we have multiple vaccines becoming available in the near future, the rate at which countries will be able to vaccinate their citizens will vary. This may have an impact on how quickly we can resume 'normal life', with follow-on implications for the sectors that were most negatively affected in 2020.

How are you positioning the Funds?

Our investment strategy is bottom-up and focuses on finding well-managed companies with durable competitive advantages and the ability to grow dividends over the long term without using excessive leverage. To achieve this, we use an in-house valuation model that focuses on cash flow and gives us the ability to forecast several scenarios over a longer time horizon.

We run a concentrated portfolio of 45–55 stocks, with generally low turnover. In terms of positioning, we aim to keep our sector exposure close to neutral where possible and attempt to add value through stock selection. Our

Canadian and U.S. mandates have a large-cap dividend focus, which means our Funds will usually be positioned as slightly defensive and conservative versus the index.

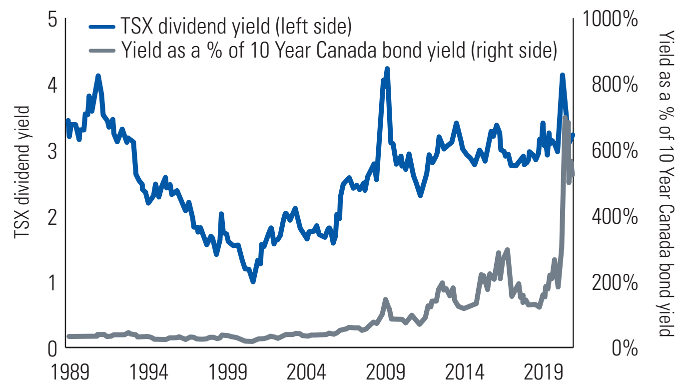
Within our Canadian and U.S. mandates, we have a healthy weighting in financials and believe this sector should perform better in 2021. In addition, within our Canadian portfolio, we continue to use the U.S. market to gain better exposure to sectors where Canada lacks suitable investment opportunities, such as health care and technology. As these sectors grow, more companies are introducing dividends and increasing them regularly, which expands our investable universe. We are seeing something similar in the materials sector, which has traditionally been a tough place to find dividend growth stocks. For both mandates, we believe there is continued opportunity within consumer discretionary, specifically in well-managed retailers with an outperforming online channel.

Why is this the right approach for 2021?

Our mandate and stock selection process tilts towards a conservative stance that is close to sector neutral. However, it is important to note that we have a long time horizon, with the majority of stocks in our Canadian mandate being held for over 15 years. Therefore, our overall positioning does not change much from year to year, as we aim to buy good companies and hold them for a very long time.

We believe that with interest rates at all-time lows, the income received from dividends is more important than ever – a point that is often overlooked by investors. If rates stay low for an extended period, it should provide an additional tailwind for stocks that pay a growing dividend.

Dividends an increasingly important source of income



Source: CIBC, data as at October 27, 2020. TSX = S&P/TSX Composite Index.

Matthew J. Eagan MBA, CFA
Daniel J. Fuss MBA, CFA, CIC
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Eileen N. Riley MBA, CFA
David W. Rolley CFA
Lee M. Rosenbaum MBA
Elaine M. Stokes

Loomis, Sayles & Company, L.P.

IA Clarington Loomis Global Allocation Class
IA Clarington Loomis Global Allocation Fund
IA Clarington Loomis Global Equity Opportunities Fund
IA Clarington Loomis Global Equity Opportunities GIF
IA Clarington Loomis Global Multisector Bond Fund
IA Clarington Global Opportunities Class
IA Clarington Global Opportunities Fund

Where are the opportunities?

In equities, we have found opportunities in the technology sector, including electronic payments and semiconductor equipment companies, consulting firms with technological expertise, and software companies with a significant value-add proposition for clients.

We have found a number of opportunities in health care, specifically in companies offering products and services geared towards higher growth areas and manageable reimbursement risk.

We also have a diverse group of companies within the financials sector, including fee-based businesses, banks, and insurance companies. Our consumer exposure captures the strong demand for e-commerce and at-home connected fitness, as well as best-in-class physical retailers with a compelling value proposition.

In fixed income, we still see room for credit spreads to continue to tighten and generate excess returns, despite retracing to near pre-COVID levels. Corporate credit offers an attractive yield advantage and our base case is for the credit cycle to transition from the credit repair phase to the recovery phase. Key factors pointing to a solid recovery include the aggregate health of the consumer, a strong outlook for housing, low inventories in many goods that will have to be replenished, and the fact that the small business sector seems to be holding up relatively well with fiscal supports. The U.S. consumer looks to be in its best financial shape in decades, with $1.25 trillion of excess savings compared to pre-COVID levels.

Credit spreads are well supported as corporate earnings are expected to improve, and technicals remain favourable with support and backstops from developed market central banks. Subdued inflation will permit policy rates to stay lower for longer. We intend to remain overweight corporates given strong asset class support, investor focus on attractive yield alternatives to government bonds, and a potential vaccine rollout in 2021.

Within U.S. fixed income, we are finding specific opportunities in pharmaceuticals, health care, technology, financials and communications. The emphasis has been primarily on sectors with defensive characteristics and companies that have stable to improving fundamentals and the liquidity profile to survive the downturn. In non-U.S. fixed income, we are finding attractive opportunities in banking, consumer non-cyclicals, communications and REITs. A slow global recovery and lagging emerging market economies create attractive net-of-inflation yield potential and selective term premium opportunities where central bank reactions are favourable.

What are the challenges?

The shape of the economic recovery depends on the trajectory of COVID-19, which will largely be determined by the emergence of an effective antiviral therapy, development of a successful vaccine, and widely accessible and accurate testing capabilities. While progress has been made in all of these areas, particularly on the vaccine front, outcomes are still very difficult to predict with certainty. A recovery is also reliant on the scope of continued fiscal and monetary support, as well as other relief packages, in the U.S. and globally.

A significant economic risk for bonds is a faster-than-expected recovery in global growth, accompanied by a rise in inflation once labour markets tighten. Emerging markets would likely benefit from improved terms of trade, while long-dated Treasuries could sell off. The largest geopolitical risk at this point is the possibility of Chinese military posturing towards Taiwan. Either risk would be a catalyst for volatility during a period of potential market complacency.

While we do monitor the macro environment, for us what has always been most important is company fundamentals. We believe our deep expertise in fundamental research will enable us to continue to provide investors with consistent potential for attractive excess returns.

How are you positioning the Funds?

IA Clarington Loomis Global Allocation Fund continues to have a majority equity allocation, reflecting our view that valuations are more attractive in equities than fixed income.

In equities, we believe investing in companies with the alpha drivers of quality, intrinsic value growth and valuation can help deliver long-term outperformance. Targeting these alpha drivers allows us to capture two market inefficiencies: mispricing, through our valuation alpha driver, and a 'duration effect' through our quality and intrinsic value growth alpha drivers. We define the duration effect as a high-quality company's ability to add value over time through the compounding of cash flows.

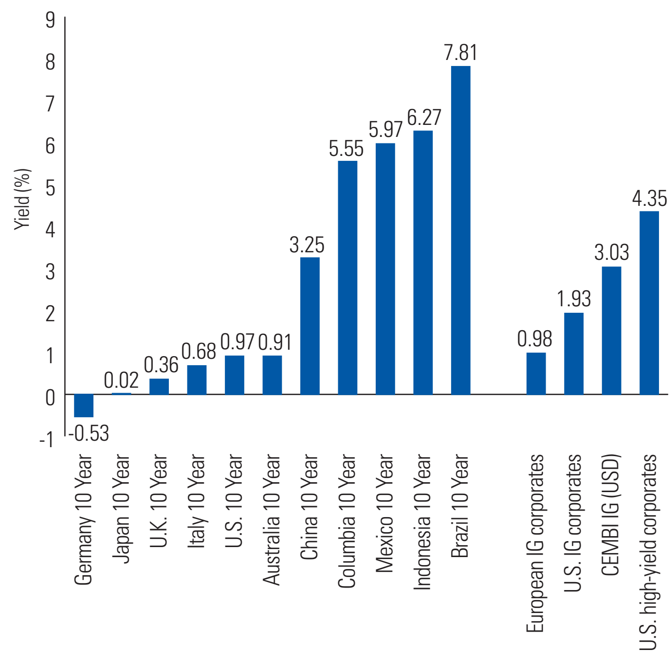
Portfolio positioning continues to be driven by our best ideas. We currently have significant exposure to the information technology, consumer discretionary and health care sectors. Conversely, we do not have any exposure to the utilities and energy sectors.

Within fixed income, we have a larger allocation to non-U.S. securities, as we are finding more opportunities in this part of the market.

In U.S. fixed income, we have a risk barbell with cash/reserves (U.S. Treasury debt) balanced against higher-conviction ideas in high yield and investment grade debt, plus a small allocation to convertible securities. The overall duration is neutral to the benchmark, reflecting our view that yields are likely to be rangebound over the near term.

The non-U.S. component is broadly underweight duration relative to global government bonds. With negative-yielding issues prevalent in Europe and Japan, the portfolio is decisively positioned away from bonds in these markets. The portfolio holds overweight duration positions in the U.S., Canada, and select emerging market countries with favourable yield and fundamental characteristics (see chart).

Select global yields



Source: Bloomberg, as at November 12, 2020. All currencies local unless otherwise indicated. European IG corporates = Bloomberg Barclays Euro Aggregate Corporate Index; U.S. IG corporates = Bloomberg Barclays US Corporate Bond Index; CEMBI IG (USD) = JPM CEMBI Diversified Broad High Grade Blended Spread Index; U.S. high-yield corporates = Bloomberg Barclays US Corporate High Yield Index.

Why is this the right approach for 2021?

We believe asset allocation shaped by our best global alpha opportunities can generate attractive long-term risk-adjusted returns. We allocate capital by leveraging our core competency in fundamental research – a more effective approach, in our view, than trying to correctly predict macroeconomic variables, which may be backward looking and uncorrelated with returns.

In 2021, we anticipate an increasingly volatile market environment to create opportunities for us to allocate capital on an individual security basis across both equity and credit.

Joe Jugovic CFA
Clement Chiang MBA, CFA
Darren Dansereau CFA
Mathew Hermary CFA
Ian Cooke CFA

QV Investors Inc.

IA Clarington Canadian Balanced Class
IA Clarington Canadian Balanced Fund
IA Clarington Canadian Balanced GIF
IA Clarington Canadian Small Cap Class
IA Clarington Canadian Small Cap Fund
IA Clarington Canadian Small Cap GIF
IA Clarington Global Equity Fund
IA Clarington Global Equity GIF
IA Clarington U.S. Equity Class
IA Clarington U.S. Equity Currency Neutral Fund

Where are the opportunities?

Unparalleled monetary stimulus is now having its impact on the real economy. More than half of the jobs lost at the depth of the recession have been recouped and global manufacturing data continues to improve. Recent company earnings releases have also been constructive, showing signs of normalizing consumer spending and bottoming industrial activity.

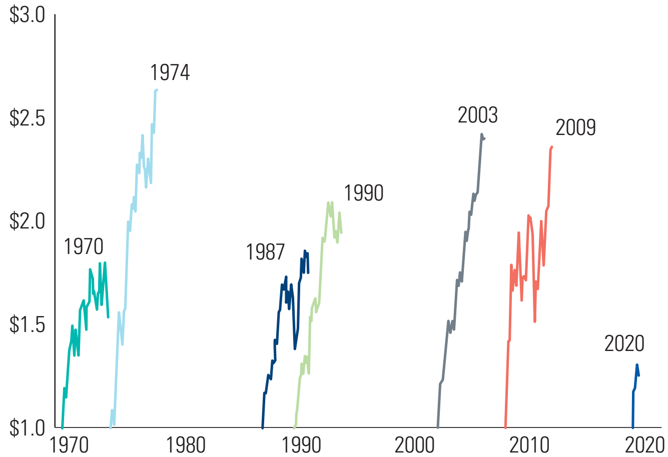
Although equity markets have continued to advance, it has been on the back of a select few goliaths, with the largest technology companies making up an outsized portion of the gains. In Canada, gold stocks dominated performance from the lows of March through the end of Q2. Ignited by the pandemic, these themes have created significant divergences within the market. It feels a lot like 1999, when old economy stocks, despite sound fundamentals, underperformed more "exciting" growth stories by a sizeable margin.

The companies in our portfolios have demonstrated remarkable resilience while navigating uncharted waters through the pandemic. Many of the industry leaders we own are making investments today that will drive attractive return potential going forward. The resulting improvement to free cash flow (cash available for shareholder-friendly initiatives) has led to debt reduction, dividends and share buybacks for many of these businesses.

The most interesting long-term opportunities appear to be businesses facing near-term neglect while maintaining ample franchise and balance sheet strength to flourish over an entire business cycle (see chart). Our equity mandates continue to selectively take advantage of these opportunities.

Value stocks rocket in recoveries

Growth per $1 invested, gains after the bottoming in seven crashes



Source: Kenneth French, via Norman Rothery/The Globe and Mail (chart by John Sopinski). Data as at September 30, 2020. The chart depicts a portfolio of large U.S. value stocks with the lowest 30% of price-to-book-value ratios. The portfolio was rebalanced annually, weighted by market capitalization, and includes dividend reinvestment.

What are the challenges?

Despite these positives, many businesses, particularly those in the services industry, continue to face unprecedented challenges. Headlines contain telling signs of the fragility beneath the surface of the market and economic recovery, which is still very much at the mercy of the pandemic and our collective response to it. Even with promising vaccine trials and a U.S. political backdrop that suggests more stability going forward, narrow market strength during the rebound thus far may continue to result in added volatility.

For over 40 years, the U.S. Federal Reserve (Fed) has maintained a dual mandate of price stability and maximum sustainable employment. However, after a decade of persistently undershooting its 2% inflation target, the Fed announced in August that it would shift towards inflation averaging over time, allowing inflation to move beyond 2% for a period before considering increases in interest rates. This is an important policy shift that investors should not ignore.

On the one hand, U.S. government interest rates provide a benchmark from which all other assets are valued. By signaling that it will continue to keep rates low (and bond prices high) for an extended period, the Fed runs the risk of further inflating asset prices – perhaps to levels without modern precedent. Although most central banks are much more worried about deflation than inflation, a policy of allowing inflation to run above 2% for a period to compensate for past shortfalls, if successful, raises the probability that inflation may become a problem at some point while fueling further separation between the haves and have nots. As the market discounts this adjustment in Fed policy, investors may find that the recent past provides poor context for how the next decade unfolds.

How are you positioning the Funds?

Our equity strategies continue to exhibit what we view as an attractive valuation and risk-return profile, as well as sound risk management characteristics. With measured cyclical exposure, they are well positioned to benefit from a gradual economic recovery. The dividend yields offered by our equity portfolios are reasonable on an absolute basis while representing a significant advantage over bond yields. We remain active in our bond portfolios, seeking additional high-quality corporate investments with considerable spreads to government bonds.

With yields as low as they are, few fixed-income investments are competing with equities. Although stocks are typically more volatile than bonds, we expect an equity portfolio with stable and growing dividends to generate appreciably more income than bonds over the medium term. As such, we remain overweight equities relative to bonds in our balanced strategy while maintaining sufficient liquidity to rebalance if another market drawdown unfolds.

Why is this the right approach for 2021?

We remain committed to QV's investment philosophy and have not blindly chased recent preferences of the market. Pockets of opportunity are available where valuations remain undemanding for what have traditionally been good businesses. These are the companies we expect will see the greatest lift when the tide eventually turns, and we have been positioning our portfolio in their favour. Despite lingering uncertainty in the current environment, we expect our consistent and patient approach to risk-managed investing to continue to generate attractive long-term return potential in the years ahead.

Shelly Dhawan Head of ESG
Jeffrey Lew CFA
Andrew Simpson CFA

Vancity Investment Management Ltd.

IA Clarington Inhance Bond SRI Fund
IA Clarington Inhance Balanced SRI Portfolio
IA Clarington Inhance Canadian Equity SRI Class
IA Clarington Inhance Conservative SRI Portfolio
IA Clarington Inhance Global Equity SRI Class
IA Clarington Inhance Growth SRI Portfolio
IA Clarington Inhance Monthly Income SRI Fund
IA Clarington Inhance Monthly Income SRI GIF

Where are the opportunities?

Positive vaccine announcements support our view that 2021 will see a continuation of the economic recovery. Conquering the COVID-19 health crisis with vaccines that are broadly distributed and widely accepted will be critical for releasing pent-up economic demand and returning to more normalized consumption trends. In this environment, corporate earnings growth is set to improve significantly and support equity valuations.

Companies in the renewable energy space are well positioned to benefit from the global imperative to combat climate change. Governments worldwide have incorporated a green focus in their economic recovery plans. For example, the incoming Biden administration in the U.S. has announced a $2 trillion climate agenda that focuses on achieving a carbon pollution-free power sector by 2035 and a target of net-zero carbon emissions by 2050. Canadian finance minister Chrystia Freeland also set a positive tone in her August throne speech, stating: "I think all Canadians understand that the restart of our economy needs to be green. It also needs to be equitable. It needs to be inclusive, and we need to focus very much on jobs and growth."

In fixed income, we prefer corporate bonds for their attractive yield carry over similar-term government of Canada bonds, whose yields continue to hover near historical lows. With bond markets showing an improved risk tone, we also see opportunities in longer-term provincial bonds that were not included in the Bank of Canada's quantitative easing bond purchase program.

What are the challenges?

Global events in 2020 highlighted the widening inequality and discrimination faced by marginalized groups. The Black Lives Matter Movement increased awareness of the injustices faced by the Black community, and Indigenous communities continued to feel the impact of historic and systemic oppression. COVID-19 disproportionately affected minority groups, which faced higher rates of infection, death, and pandemic-related job losses. Racial equity and systemic racism will continue to be areas of investor and company focus.

The Canadian government's support programs played a major role in assisting the recovery, but came with a very large price tag in the form of a massive budget deficit. Recent estimates from the International

Monetary Fund (IMF) project Canada's budget deficit as a percentage of GDP to come in at 19.9% this year, the largest among developed nations. While Canada entered the pandemic with a relatively good fiscal position, the country lost one of its AAA credit ratings when it was downgraded by Fitch Ratings in June. Canada maintains its AAA rating with the three other major rating agencies, but could face other downgrades if policymakers do not take effective action to reduce fiscal deficits after the economy begins a sustained recovery.

Investors will continue to face a wall of worry in 2021, as the impact of the global pandemic will take time to fade (see chart). The massive fiscal and monetary stimulus that has been deployed globally to combat the lockdown-induced recession will be in place for an extended period.

Stocks climb wall of worry

Source: Bloomberg, as at November 27, 2020. VIX Index = Chicago Board Options Exchange CBOE Volatility Index. Fed = U.S. Federal Reserve action (interest rate hikes, market moving policy speeches, etc.).

How are you positioning the Funds?

Following the short but sharp pandemic-induced recession, the equity mandates are positioned for the early stages of an economic recovery through increased exposure to cyclical sectors such as financials, industrials and materials.

Equity markets are also contending with a rotation from the high-flying work-from-home names to deep value and recovery names as positive vaccine news has emerged. We are not immune to market swings, but our focus on high-quality companies and long-term growth has minimized our exposure to speculative situations that are whipsawing traders.

The bond mandate is slightly short duration with an underweight to the long end of the curve. We expect bond yields to slowly grind higher throughout 2021 alongside a steady economic recovery. Central banks will likely continue to scale back their quantitative easing programs, but maintain their extremely accommodative monetary policies well into the future. Yield curves will likely continue to steepen, as the front end of the curve remains pinned by near-zero policy rates.

Why is this the right approach for 2021?

Our fixed-income strategy targets an overweight to corporate bonds and an underweight to federal government bonds. In this ultra-low bond yield environment, credit spreads as a percentage of the total all-in yield remain at attractive levels relative to historical averages, despite significant credit spread tightening in 2020. Reflecting rising corporate leverage levels and continued uncertainty over the economic recovery, our bond portfolios are biased towards higher-quality corporates.

In our view, security selection will be an important driver of returns in 2021, and we will continue to apply our four-element climate risk strategy of divestment, decarbonization, reinvestment and engagement.

Our collaborative approach integrates environmental, social and governance (ESG) analysis with traditional financial analysis, and we only invest in companies that meet both sets of criteria. The result is a portfolio of sustainable businesses that we view as having attractive potential for earnings growth rates and return on shareholder equity that exceed market levels.

Amar Dhanoya MBA, CFA
Jeff Sujitno HBA, CPA, CIM

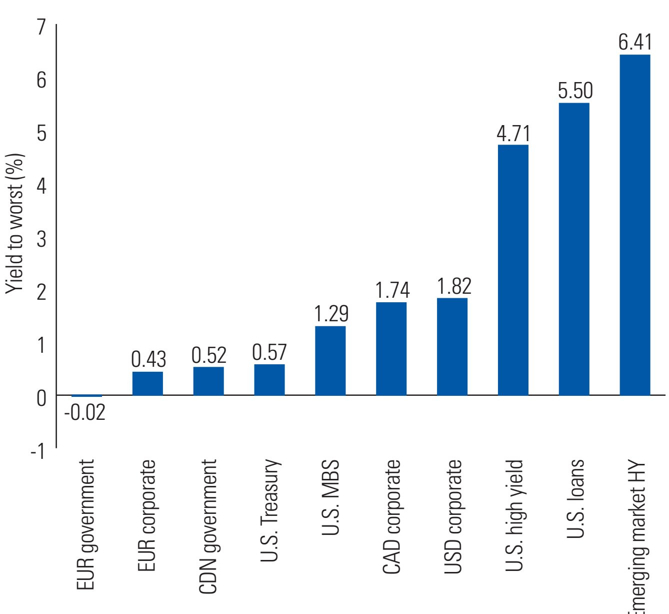
Wellington Square

IA Clarington Core Plus Bond Fund
IA Clarington Core Plus Bond GIF
IA Clarington Floating Rate Income Fund
IA Clarington U.S. Dollar Floating Rate Income Fund

Where are the opportunities?

We believe the best opportunities are in non-investment grade credit, such as loans and high-yield corporates (see chart). As of November 27, the Credit Suisse Leveraged Loan Index had a yield of 5.5% (3-year) and the Bloomberg Barclays U.S. Corporate High Yield Index had a yield of 4.7% (yield to worst). We expect continued capital flows into these asset classes as investors search for higher-yielding opportunities.

Yields across fixed-income segments



Source: Bloomberg, as at November 27, 2020. See disclaimer for index information.

Within investment grade, we favour BBB-rated corporates based on the additional spread and yield relative to higher-rated segments. Pandemic-disrupted credit sectors such as airlines, gaming, leisure, and restaurants have lagged the recovery in the equity markets, and while we believe there are opportunities in these areas, security selection will be critical to success.

What are the challenges?

A key challenge is the historically low-yield environment driven by central bank actions for accommodative conditions. We do not expect policy rates to increase in at least the next three years, but we do expect the yield curve to steepen, with longer-term rates rising on an improving economy and fiscal support.

Yields across fixed income are near historical lows, and this is forcing investors to recalibrate their return expectations. In addition, capital gain potential is more limited as credit spreads have rebounded across investment grade and non-investment grade markets since the March sell-off. There are still opportunities for capital appreciation, but the beta trade is over, making sector, rating, and security selection critical to generating alpha.

We expect a steepening yield curve with short-term rates pinned down by central banks, while longer-term rates will react to an improving economy and fiscal support.

How are you positioning the Funds?

We will take advantage of any pandemic-driven volatility that may arise, and expect to be fully invested with a minimal cash weighting across the Funds.

We plan to add measured risk into our floating rate income mandate by reallocating capital from lower-yielding positions to higher-yielding ones.

Within our core plus bond mandate, we will maintain duration at the higher end of our range (about 3.5 years) to maximize spread exposure. We will also stay at the higher end of our range in our allocation to non-investment grade holdings (about 25%). Yield curve steepening is certainly a concern, but primarily for areas with maturities of over five years. We will also maintain our focus on BBB-rated securities within investment grade. Finally, the highest-rated parts of this Fund will be invested in floating rate collateralized loan obligations (CLOs) to minimize interest rate sensitivity.

Why is this the right approach for 2021?

In our view, full credit exposure within fixed-income portfolios is the right approach for 2021 because it provides investors with potential to earn higher yields and gives them exposure to capital appreciation from spread compression. The successful rollout of a COVID-19 vaccine will allow for a full economic recovery, which would bode well for credit markets.

We believe governments and central banks will continue to backstop credit markets, significantly reducing the risk of a violent sell-off similar to the one we witnessed in March 2020. Confirmation that credit support programs, including the secondary market corporate credit facility in the U.S., will expire at the end of 2020 had virtually no impact on credit spreads. This reinforces our view – and that of the market – that support will be there if necessary, even if no official program is in place.

Wellington Square refers to Wellington Square Capital Partners Inc. (sub-advisor) and Wellington Square Advisors Inc. (sub-sub advisor). EUR government = Bloomberg Barclays Pan-European Aggregate Treasury Index; EUR corporate = Bloomberg Barclays Pan-European Aggregate Corporate Index; CDN government = Bloomberg Barclays Canada Aggregate Treasury Index; U.S. Treasury = Bloomberg Barclays U.S. Treasury Index; U.S. MBS = Bloomberg Barclays U.S. Mortgage Backed Securities (MBS) Index; CAD corporate = Bloomberg Barclays Canada Aggregate Corporate Index; USD corporate = Bloomberg Barclays U.S. Corporate Bond Index; U.S. high yield = Bloomberg Barclays U.S. Corporate High Yield Bond Index; U.S. loans = Credit Suisse Leveraged Loan Index; Emerging market HY = Bloomberg Barclays EM USD Aggregate High Yield Index.

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