INVESTMENT FUNDS

NORTH AMERICAN EQUITY

MONTHLY COMMENTARY

January 31, 2022

The setup for 2022 is one that is more likely to bring a higher level of volatility versus last year, which was quite below average from a historical standpoint. January showed that, with negative returns to start the year with the S&P 500 returning -4.5% in Canadian dollars and -5.2% in U.S. dollars. The difference is explained by the Canadian dollar weakness, which tends to depreciate whenever the stock markets start to go down.

This increased volatility is caused by many reasons, the main one being the Fed's hawkish pivot signalling the start of quantitative tightening this year. This move follows quite a swift change in tone from the Fed since Powell was renamed for another term late last year. This has caused market expectations for rate increases to move from basically none somewhere last summer to currently four or five during 2022. During this pivot, there has been real turbulence underneath the indexes. As of January 25, while the S&P 500, the Nasdaq composite and the Russell 2000 (small capitalization index) were down 11.0%, 17.3% and 20.0% respectively, the average stocks within those indexes were down 18.7%, 46.6% and 39.6%. From here, it's important to realize that, for a large part of the market, this has already been brutal.

Starting now, we think the risk is higher at the index level where many big stocks have simply refused to go down meaningfully. We don't have a crystal ball, but an analogy we would make is that in a war, the generals are usually the last to fall. Thus, we see better opportunities in stocks that have already gone down a lot and are opportunistically adding new positions in the portfolio. We approach the first half of 2022 as "hunting season" and have identified many opportunities for long-term alpha. This setup is very similar to the start of 2016 where many stocks were sold off quite heavily on a hawkish pivot from the Fed.

We think that at some point the market will focus on the many derivative impacts from the labour and capacity shortages which are mostly pointing towards the need for increased investment in productivity enhancing initiatives. We also think that in a world of higher wage growth, companies with a higher ratio of profits per employee are better positioned. That's what differentiates the U.S. market today, especially the technology sector, versus other higher inflation eras like the 70s. Coming back to productivity, we see three reasons that might be the source of sustainable upside on a broader level. First, momentum was accelerating at the end of last decade and we think it might come back after two years of pandemic. Second, we see recent evidence of technological acceleration with increased investments in intellectual property products. Lastly, there has been increased economic dynamism with rising new business formations and U.S. patent applications. In short, we think that with supply chain problems gradually being resolved and demand moving away from goods to services (as we finally reopen economies), the debate might evolve from rising inflation and Fed hawkishness to one where we talk about declining inflation with rising productivity starting to help.

For the energy complex, the standoff between Russia and NATO is affecting global oil and natural gas prices. If Russia moves ahead, Western allies are seeking tougher penalties than those imposed after the invasion of Crimea back in 2014. The European Union would target the banking and energy sectors to hurt Russia at the risk of worsening the energy crisis on the old continent. Interestingly, the U.S. became the world's largest exporter of natural gas (LNG) in December for the first time. Even if Canadian E&Ps continue to benefit from high commodity prices, they continue to focus on shareholder returns, and we expect very modest production growth across the industry, which should support the oil price.

Within the fund, we recently added a real estate company, H&R. After spinning off Primaris, there is a visible path to get 100% exposure to multi-family and industrial within the next five years. The current multi-family portfolio is mostly in the Sunbelt, currently the fastest rent growth market in the U.S. H&R is one of the cheapest REITs in Canada (~25% discount to NAV) with strong upcoming catalysts to close the discount.

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Main funds managed by the team

✓	Canadian Equity Growth
✓	Real Estate Income
✓	Global True Conviction
✓	Canadian Equity Growth Hybrid 75/25
✓	Global True Conviction Hybrid 75/25
✓	IA Clarington Canadian Leaders Class

iAIM snapshot

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- Major player in the asset management industry
- Manages $97 billion in general portfolios and segregated and mutual funds
- A team of 184 people, including 108 investment professionals (including 44 CFA charterholders)
- Composed of experienced managers who emphasize fundamental analysis, identification of value and long-term investing

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