INVESTMENT FUNDS

DIVIDEND GROWTH & U.S. DIVIDEND GROWTH

MONTHLY COMMENTARY

September 30, 2020

The third quarter of 2020 has seen the world economy rebound from the worst quarter in modern history as Q1 2020 was severely impacted by the Covid-19 pandemic. In the quarter, major stock exchanges added to their accumulated gains since the troughs of last March, supported by a massive injection of liquidity from central banks and a brighter economic outlook for the coming year.

The global recovery is going much better than expected and signs of economic surprises are reaching record levels worldwide. Two things are at play: the expectations of economic analysts were probably too pessimistic, and the compound effects of the monetary and fiscal stimulus are more massive than expected.

However, we must remain cautious and not raise our expectations too quickly, since at the time of writing, a second wave of the spread of COVID-19 is emerging in Spain, France and, unfortunately, at home in Canada.

The good news, if there is any, is that governments around the world seem to believe that a return to a complete shutdown of the economy in the event of a marked resurgence of the virus in the coming quarters is not desirable and is therefore highly unlikely. So, it's reasonable to think that economically, second wave or not, the worst is behind us.

On the financial markets side, August and September have been hectic and most likely indicators of the quarters to come.

Dividend Growth Performance Comment

The S&P/TSX 60 had a positive third quarter, nine of its eleven sectors of the index realizing a positive return, with Industrials and Materials returning above 10% return. In terms of relative performance over the third quarter, the fund outperformed its index. Successful stock selection was the main driver of outperformance. Most of the outperformance in the stock selection was driven by stock picking in the health care sector with exposure to Thermo Fisher in the United States that had big tailwind from the testing and research for a Covid-19 vaccine. In Materials, an overweight in Nutrien was positive as it returned above 20% during the quarter.

U.S. Dividend Growth Performance Comment

The S&P 500 also had a positive third quarter, nine of its eleven sectors posting a positive return, with Materials, Consumer Discretionary and Industrials being the best performers. Information technology, which represents more than a quarter of the index was the fourth-best performer with close to double digit positive return during the quarter. In terms of relative performance, the fund outperformed the index during the quarter. Great stock picking was the main driver of performance. In Health Care, an overweight in Thermo Fisher was positive, and Abbott also contributed from their exposure to COVID testing with their new 15-minute test. In Consumer Discretionary, an overweight in McDonald's and Domino's was a positive as they saw an increase in same store sales following the COVID-19 situation.

iA Financial Group

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iA Investment Management

Looking forward, we are preparing for increased volatility and are monitoring two significant items. First is the second wave of COVID-19, and the second is the U.S. election, where there seems to be a clear leader in the polls. However, we know from experience that it will be important to wait for the result before declaring a winner. With the projected number of mail-in ballots to be cast in this election, it is possible that we will need to wait some time after election day in order to know the winning party. In general, the stock market does not like uncertainty, so there is downside risk if the outcome takes time to determine. On the positive side, we have numerous COVID-19 vaccine candidates that are in trial, and while we do not expect to see a vaccine in this calendar year, as we move closer to a potential announcement this should be a tailwind for stocks. Coupled with a definitive election result, there is potential for a better outlook as 2020 ends and we move into 2021.

While these items almost guarantee a noisy Q4, our investment strategy has not changed. We continue to favour companies with durable competitive advantages, great management teams, conservative balance sheets, and pay a growing dividend. Putting these attributes together gives us a portfolio that should perform well regardless of the direction of the stock market or economy. In addition, we feel it's a great time to focus on dividend stocks. Given the steep drop in yields to generational lows, the yield from dividend stocks looks more attractive than ever. Furthermore, our focus on finding stocks that can grow the dividend sustainably means that this income stream should grow every year. One example of this type of company in Canadian our portfolio is Fortis, who have increased their dividend for the past 47 consecutive years. On top of that, they have recently announced that they will increase the dividend 6% per year for the next 5 years. Currently the stock yields over 3.5%, which compares very favourably to a 10-year GoC bond at 0.50%. Fortis has outperformed the S&PTSX over every long-term time horizon – 5, 10, 15 or 20 years. We believe the future is bright for Fortis and other similar companies, as they slowly attract capital away from lower-yielding alternatives. Another example from our U.S. Fund is Johnson & Johnson, who have increased their dividend for the past 57 consecutive years. Currently the stock yields 2.8% which compares very favourably to a 10-year Government bond at 0.70%, especially when you consider that the dividend will continue to grow yearly.

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DONNY MOSS, CFA

— Principal Portfolio Manager, North American Equities
— Joined iAIM in 2008
— More than 15 years of investment experience
— Bachelor's degree in commerce, Dalhousie University

Main funds managed by the team

✓	Dividend Growth
✓	U.S. Dividend Growth
✓	Dividend Growth Hybrid 75/25
✓	IA Clarington Canadian Dividend Fund
✓	IA Clarington Dividend Growth Class
✓	IA Clarington U.S. Dividend Growth Fund
✓	IA Clarington Canadian Conservative Equity Fund

iAIM snapshot

— Principal asset manager for iA Financial Group
— 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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