INVESTMENT FUNDS

DIVIDEND GROWTH & U.S. DIVIDEND GROWTH

MONTHLY COMMENTARY

February 28, 2021

February was another positive month for equities on both sides of the border, with both the S&P/TSX and S&P500 continuing to make new all-time highs. However, the recovery in the economy and the stock market has started to cause a sharp rebound in interest rates from all time lows hit last summer during the worst of the COVID crisis, which could present a risk for some equities. For context, the 10-year government bond in the U.S. and Canada traded down to a yield of about 0.50% last summer. After the initial vaccine announcement, this rate moved up to about 0.90% at year end, and since then has shot up to over 1.50%. The move in rates is also partially responsible for some of the sector rotation we have seen in the market since the vaccine announcement in November. As investors, the value of a company can be calculated as the present value of future cash flows that the company will generate. With risk-free rates at close to 0%, these benefits high-growth companies that trade at a high valuation, as low interest rates can be used to justify very high valuations. As rates move higher, this becomes a headwind for these companies, and a tailwind for others. For example, we are seeing the technology sector suffer on a relative basis, while we are now seeing outperformance in Financials, which usually trade at far lower valuations.

On the vaccine front, we continue to see positive news that are ahead of prior expectations. The Johnson & Johnson vaccine is the latest one that has been approved in both the U.S. and Canada, and when added to our existing approved vaccines, full vaccination of adults is expected to occur a few months quicker than previous forecasts at the beginning of the year. Besides being great news for humanity, it is also contributing to the strength seen in equities and interest rates.

February is always a busy month with many companies reporting their Q4 2020 results, and one of the more interesting set of results came from the Canadian Banks Q1 2021, which encompasses the November to January time period. This is a great time to make a year-over-year comparison as their Q1 2020 reporting period ended just before the COVID pandemic hit. As a group, earnings were estimated to be down roughly 5% year over year, but actual results blew away estimates and were up 12% on a combination of organic growth, lower provisions on loans, and improving margins. As a result, earnings for the group should surpass 2019 levels this year, rather than in 2022 which is what was estimated previously. Bank stocks have performed very well to start 2021, and have a few things going in their favour in addition to their earnings growth. First, as discussed, the recent rise in interest rates is generally good for bank margins, so to the extent that rates stay at current levels or continue to rise it should be a tailwind. In addition, bank valuations remain fairly inexpensive, and they should capture some interest from other expensive parts of the market as the sector rotation continues. And lastly, there is still a regulatory restriction on dividend increases and share buybacks as a result of the pandemic. If we continue to see excellent financial results this restriction could be lifted later this year, and we believe banks would respond by raising dividends substantially and repurchasing their own shares. We have great exposure to banks in both Canadian and U.S. mandates and are excited to see their recovery occurring ahead of our expectations.

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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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