October 29, 2020

Update on the IA Clarington Strategic Funds

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The following is a summary of a webcast held on October 29, 2020.

Key takeaways

- Key indicators suggest an increasingly favourable macroeconomic environment.
- Higher-paying dividend equities and high-yield bonds are poised to benefit from the broad economic recovery.
- We expect the U.S. dollar to weaken regardless of who wins the U.S. presidential election.

The past vs. the future: The economy, markets and the Strategic Funds

- Today the U.S. announced that Q3 GDP was up over 33% (annualized).
- Underneath this number, you're seeing a lot of good things happening.
  - E.g., durable goods orders were up 45% in Q3 and non-durable goods were up 80%.
- I think this GDP number is a really good indicator of what we can expect going forward.
- Keep in mind that three months ago, the experts were saying Q3 GDP growth would come in at around -3.7%.
- My estimate is that the U.S. needs about 2.7% GDP growth next quarter to break even relative to last year, and I think this is completely doable.
- The savings rate is extremely high, so the consumer is in good shape.
  - The consumer is solvent and is deleveraging.
  - This sets us up for strong growth potential over the next number of years.

U.S. Personal Savings as a % of Disposable Personal Income

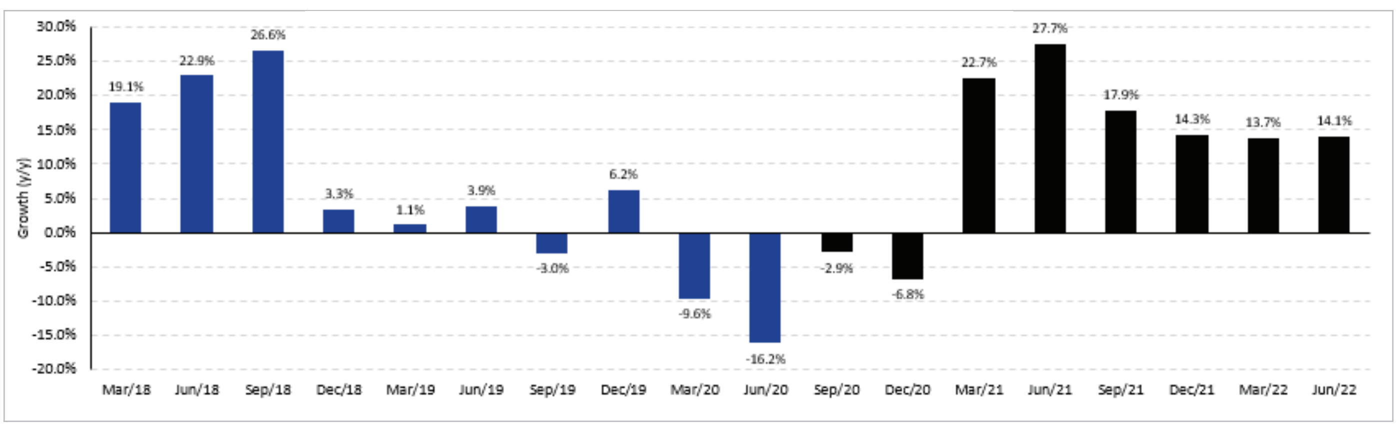
Source: IA Clarington Investments, Bloomberg LP. As at October 17, 2020.

- Some key catalysts we can't ignore:
  - o More fiscal stimulus no matter who is in the White House.
  - o Good prospects for a COVID-19 vaccine relatively soon.
  - o Weaker U.S. dollar, which will be a major catalyst for specific sectors and companies going forward.
- Over 75% of Purchasing Managers' Index surveys are showing continued strength and broad-based growth.

Opportunities in equites and fixed income

- It was pretty clear that the trough for the markets would come in the second quarter, and that going forward we're likely to see better earnings, grinding towards break-even in the next quarter or so.

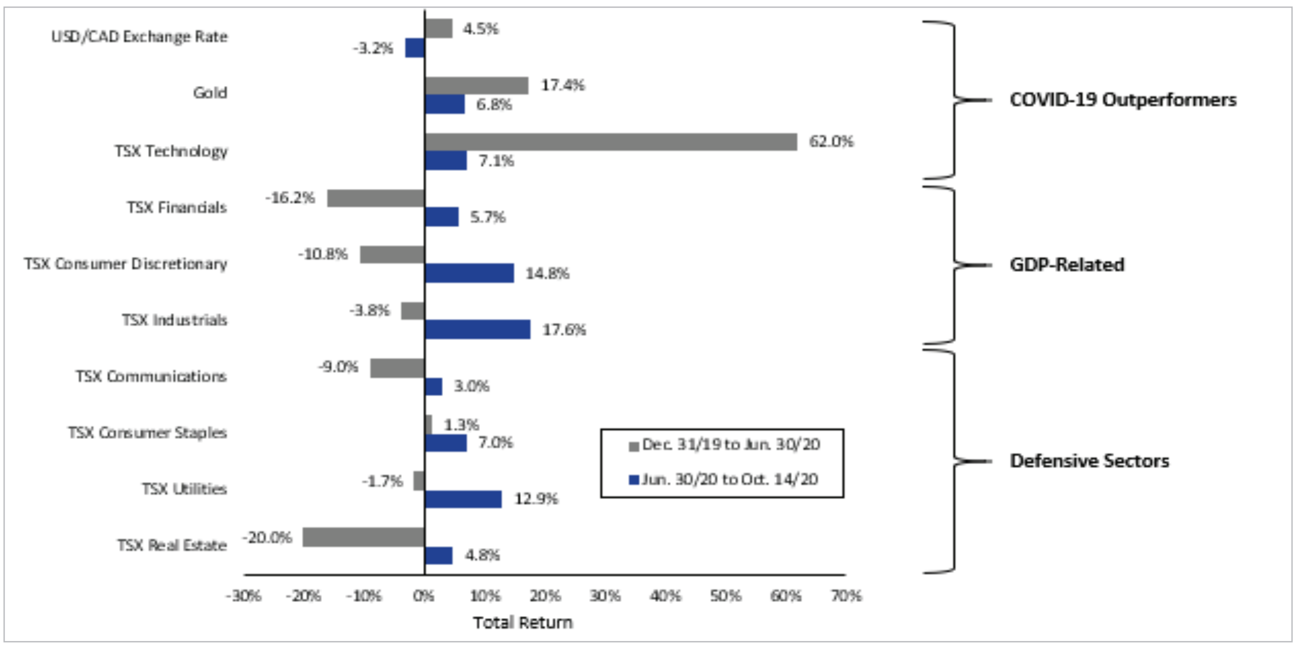
S&P 500 Positive Earnings Per Share Growth Over Time



Source: iA Clarington; Bloomberg LP as at October 14, 2020.

- According to the analysts – and I'm not disagreeing with them – you should expect to see some pretty healthy growth within equities for the next couple of years.
- Within that growth picture, financials, consumer stocks, health care, and some cyclicals are driving future earnings expectations.
  - o It's not gold and technology, as we saw in the first six months of the year; they'll be there, but the real growth will likely come from these other sectors going forward.
  - o In other words, areas that did really well in the first half of 2020 are likely not going to be the market leaders going forward.
- With rates expected to stay low for the next couple of years and with more stimulus on the horizon, I think that within equities there is really no alternative to the more defensive, higher-yielding dividend stocks.
- I think Q3 has given us a glimpse of what the next several years are going to look like:
  - o Instead of gold and technology dominating, as they did in the first half of the year, there has been a broadening out of the rally across other sectors with the reopening of the economy.
  - o We expect this rotation to continue.
  - o We've been deploying cash and adding to these other sectors, as well as to high yield, for the last three months.

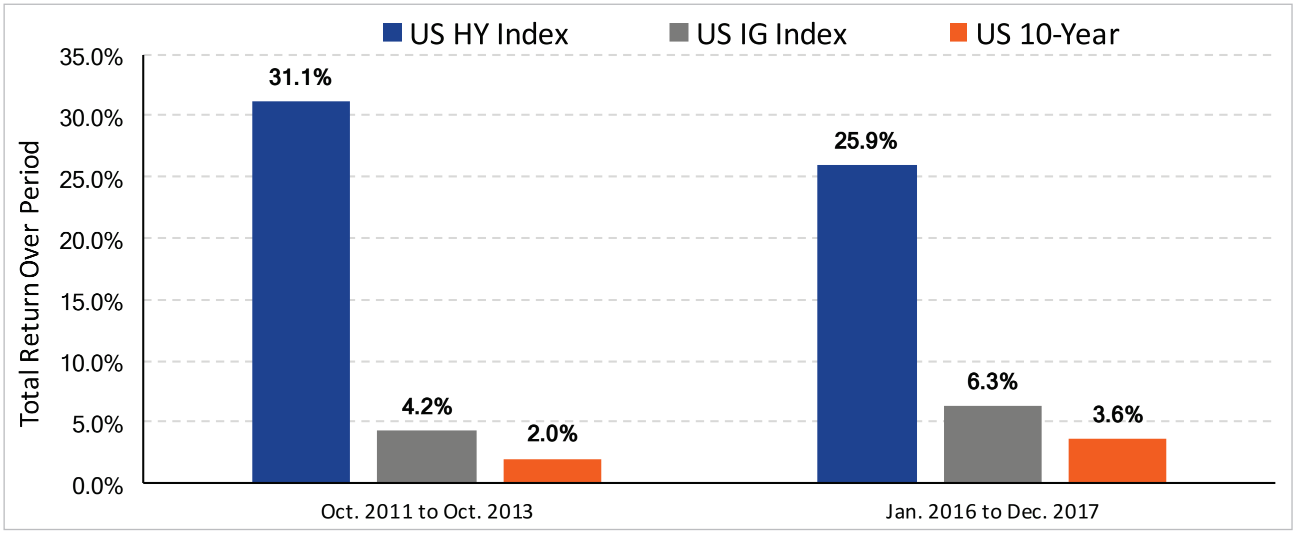
Asset Class & TSX Sector Returns Over Time



Source: iA Clarington; Bloomberg LP as at October 14, 2020.

- We expect the U.S. dollar to weaken regardless of the election's outcome, though we may see a bit more weakness if Biden wins.
  - o We went fully hedged about a month ago (from about 70% hedged for most of the summer), and unless something dramatically changes over the next couple of months, we expect to stay at that level for the next several years.
- Negative real yields have been the driving issue for performance this year, impacting different asset classes differently.
  - o When real yields go down, gold and technology do well, while value, high-paying dividend stocks and high-yield bonds get hit.
- But as powerful as this is to the downside, historically it's even more powerful to the upside for high yield when real yields trend towards positive (or break even).

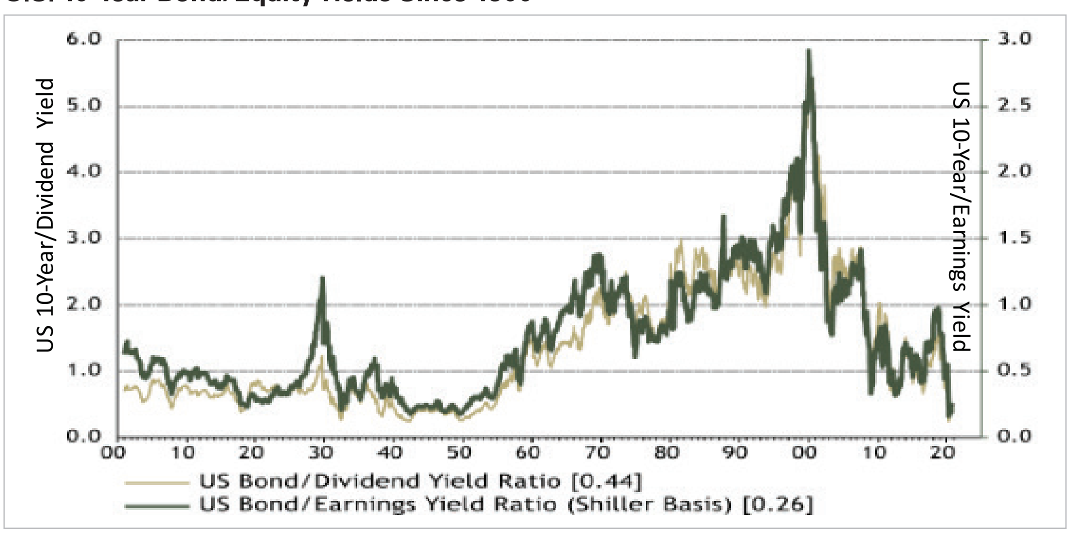
Historically, high yield outperforms coming out of negative rates



Source: iA Clarington; Bloomberg LP as at October 14th, 2020, US HY Index refers to the Barclays US Corporate High Yield Index; US IG Index refers to the Barclays US Aggregate Bond Index; US 10-Year refers to the Barclays US Government 10-Year Term Index.

- Our base case return for high yield as an asset class over the next 12 months is about 12.5% (only two weeks ago it was about 9.5%).
- We're expecting a very favourable two-year cycle for high yield, and for a number of reasons:
  - o The economic picture is getting better.
  - o Spread levels today relative to where they'll likely be at the end of the cycle.
- Equity valuations are near 100-year lows relative to government bonds.
  - o Against the macroeconomic backdrop discussed above, this makes us very confident about how we're positioned for the next couple of years.

U.S. 10-Year Bond/Equity Yields Since 1900



Source: Bloomberg, ASR Ltd., Refinitiv Datastream/Shiller.

Performance overview

- The table below shows that we've outperformed peers about 85% of the time.
  - o The other 15% has generally provided a very attractive buying opportunity.
- This reflects how we invest – we're trying to be right 85% of the time over a 12-month horizon.
- Historically, when we've had a period of weaker performance, it has generally been followed by top decile results every year for the next five years.

IA Clarington Strategic Income Fund

Total Return	2012	2013	2014	2015	2016	2017	2018	2019	YTD	3Q20
Fund	10.57%	13.81%	9.04%	-4.59%	15.45%	6.86%	-2.07%	14.69%	-3.73%	5.37%
+/- Category	4.30%	2.66%	0.75%	-4.48%	7.57%	0.83%	2.19%	1.78%	-5.05%	1.95%
Quartile Rank										
Percentile Rank	**2**	**22**	**32**	**92**	**1**	**35**	**11**	**17**	**94**	**4**
# of Funds in Cat.	516	563	592	591	592	611	665	607	473	602

Source: iA Clarington; Morningstar data as at October 16th, 2020. IA Clarington Strategic Income Fund has outperformed the peer group in 85% of calendar years.

Q&A

What is the exposure to energy sector debt in the IA Clarington Strategic Corporate Bond Fund?

- Direct exposure to energy exploration and production names is about 4.5–5%, with about another 8% in energy infrastructure.
  - o These bonds are due to mature in 2–3 years, and I don't think energy is going to be in trouble from a cash flow perspective, so these companies should be able to meet their obligations to bondholders.
  - o In 15 years it may be a different story, but in the nearer term, it's unlikely we'll see any cash flow problems.
  - o There are some very positive micro-catalysts for energy.
  - o If global growth ticks upward, and if the U.S. economy delivers 2.5% GDP growth next quarter, with a 3.5–4% year in 2021 (which I think is very possible), energy would definitely stand to benefit.
  - o I think oil could be trading in the mid-$50 range next year.
  - o But if there's a Democratic Party sweep, and if they keep their word, there's going to be some pressure year after year on oil and energy in general.
  - o You could see a situation where you don't get any positive sentiment on any energy stocks, no matter what global growth looks like.

What's something that you're not currently anticipating, but if it were to occur, would lead you to consider changing the way you're positioning the Funds?

- Lower negative real rates would be the big one.
- If real rates continue to stay low or even trend a bit lower for the next six or seven months, the clear implication would be that you need to up your technology exposure, and here at iA Clarington we do have mandates that can provide that exposure.
- I think the Strategic Funds would still do well in that environment, but if you want to focus in on what will outperform under those conditions, it's technology as well as gold.

- In this scenario, I don't think the divergence between technology and gold on the one hand, and the other parts of the market on the other, would be as significant as it was in the first part of this year; but if you didn't want to be exposed to as much volatility, you would need to move into these two very high-priced areas of the market.
  - o But again, this is not the scenario we're anticipating as our base case.

Visit iaclarington.com to learn more about Dan Bastasic and the IA Clarington Strategic Funds.

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