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Strategic Outlook — July 2020

Despite the global stock market rally observed in recent months, we believe we're not out of the woods yet. The damage inflicted by the COVID-19 pandemic, on both a human and an economic level, will continue to be felt for a long time. For now, we are maintaining a cautious outlook as we closely monitor the latest developments on the capital markets.

Short-term outlook (6 to 24 months)

It goes without saying that key interest rates should remain at rock-bottom levels over the next several quarters. Any alternative scenario seems unlikely given that the impacts of the recession will certainly be felt over the next two years. Central banks will probably opt to keep rates low to stimulate the economic recovery.

We now find ourselves in a situation where real interest rates are negative. Imagine you bought a Canadian government bond with a 10-year maturity, and inflation rises from 1.9% to 3%. The only reason you might want to hold this type of investment is to retain its **nominal** value, notwithstanding your loss of purchasing power. (*)

In equity, and particularly shares of publicly traded companies, we're at risk of seeing short-term fluctuations in market value. For now we're maintaining a neutral stance in terms of allocation. If the markets see further declines, we'll switch to an opportunistic tactic in order to take advantage of the attractive dividends on offer. We believe that equity remains an essential component of a long-term investment strategy and offers the most promising returns.

(*) For example, at the time of writing, a Canadian government bond maturing in August 2022 offers a yield of 0.288% (you read that correctly—less than 1%!) From this paltry yield, you'd need to subtract the inflation rate for the holding period. Assuming a rate of inflation of 1.9% (as measured by Statistics Canada's 2019 Consumer Price Index), the inflation-adjusted return on this investment would amount to -1.62% per year.

Medium-term outlook (2 to 5 years)

It is possible that central banks may "accept" an inflation rate slightly higher than 3% before raising key rates and reintroducing a more restrictive monetary policy. If this occurs, yields on bonds with maturities over 2 years would be reduced. Again, a losing scenario for investors.

In equity, we believe there's a strong chance that returns will resume a moderate growth path thanks to attractive dividends. Certain sectors and regions also offer moderate growth potential.

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Long-term outlook (5 to 15 years)

The crisis caused by the coronavirus pandemic has shed light on the interconnectedness of our economies, human health and the environment. Now more than ever, it's imperative for us to respond to the challenges that are set to shape future risks and influence returns. We believe that these challenges will continue to impact us and have repercussions on the performance of investors' portfolios. These challenges include:

- *Climate change*. Time is running out to prevent some of the potentially catastrophic consequences of climate change. In more traditional economic sectors, it will be important to identify players that are at risk and those that are taking measures to successfully transition to a low-carbon economy. For example, many promising opportunities are emerging in renewable energies.
- *Unbridled capitalism.* This model of economic organization, which focuses solely on profit and ignores impacts on stakeholders, the environment and human capital, will end to failure unless we transition to a more responsible paradigm. The actions of some companies during this pandemic are a good indicator.
- *Major geopolitical trends.* They will influence the markets and economies for better or for worse. In particular, observers will need to closely watch US-China relations given their current toxic state. Another movement to monitor is the backlash against globalization as we knew it concurrent with the rise of nationalist sentiment in places like the United States, the United Kingdom and Brazil.

These are all major challenges and they need to be factored in when managing your investment portfolio. We are currently working on ways to improve our decision-making process by incorporating a rigorous and methodical evaluation of environmental, social and governance criteria, with a particular focus on reducing the carbon footprint of your portfolios.

We'll have the opportunity to discuss these changes with you in future discussions and publications. Announcements will be made in the fall.

Until then, on the behalf of the entire team, I wish you a safe and enjoyable summer!

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