GLOBEINVEST
CAPITAL MANAGEMENT INC.

INVESTMENT NOTES

MARCH 2022

UPCOMING 2022 BNN SHOWS

Christine: April 14 @ 12pm

Christine: May 17 @ 12 pm

Christine: June 14 @ 12 pm

Russia called NATO's bluff and invaded Ukraine on February 24. The associated spike in commodity prices means inflationary pressures will intensify and persist for longer. While excluded by central banks in measuring inflation, higher energy and food costs will erode growth in real income, which will likely lead to slower growth in overall consumer spending.

Performance amongst industry sectors diverged this past quarter with commodity-based industries such as Energy and Base Metals posting double-digit price percentage gains while Consumer Discretionary and Technology stocks retreated, dragged down by the prospect of weaker consumer spending and higher interest rates.

Of note, bonds (as measured by the Canadian Bond Universe Index) were the worst performing asset class this quarter as yields rose sharply in anticipation of interest rates increases. Bonds have also lagged the S&P/TSX Composite Index over the past decade with a 10-year CAGR of 2.5% versus 9.1% for the broad equity index.

Geopolitical Crises

History shows that geopolitical crises often have a modest impact on U.S. equities. Typically, stocks track earnings, not wars. While these events exact a terrible human toll, they tend not to affect equity valuations over the long term. A review of 22 major nonfinancial shocks, from the Pearl Harbour attack onward revealed that these events on average led to a one-day loss of about 1.1%, with the total retracement from the geopolitical event date averaging 4.8%. It typically took 20 days for equities to bottom and 43 days to bounce back.

In the case of the Russia/Ukraine war, March 8 may have been the bottom, 12 days after the invasion started. On that day, the S&P500 Index was down 2.8% over the 12 days and 13.0% from its closing high on January 3. By the end of the quarter, the Index rallied to finish up 8.6% from its trough. Granted, it may be premature to draw any conclusions while the conflict is ongoing.

The geopolitical climate has shifted dramatically and has far-reaching implications for global trade. No matter how the war in Ukraine ends, it is unlikely the global economy will remain as tightly integrated as it once was. The world looks increasingly bifurcated as most Western countries have imposed aggressive sanctions against Russia while other nations such as China, India, and United Arab Emirates have not.

The Economy

The economic impact of this war will vary across geographies depending on a country's proximity and reliance on Russian exports. From a global perspective, Russia's GDP is relatively small, only 1.7% of global GDP (comparable to Canada) so an abrupt slowdown of its economy will have minimal direct impact. Russian exports consist primarily of fossil fuels, base metals, agricultural products, and fertilizer. It is the collateral impact resulting from the price spike in these products, due to sanctions on Russian goods, that will weigh on global economic growth and increase inflation this year.

The North American economy is relatively insulated from Russian trade activity compared to the European Union (EU) which relies on Russia for 40% of its natural gas and 25% of its oil consumption. The United States has banned all Russian oil and gas imports and the U.K will phase out Russian oil imports by the end of 2022. On March 8th, the EU announced a new plan called REPowerEU to seek alternative supplies with the goal to reduce EU's purchase of Russian gas by two-thirds before the end of 2022 and to be independent of Russia energy well before 2030.

The risk of stagflation has risen since the invasion, which has exacerbated the rise in food and energy prices. Three conditions typically exist in stagflation: (1) rising inflation (2) slowing economic growth and (3) high unemployment. Presently, two of the three conditions have been met.

The job situation in both Canada and the United States is healthy and has recovered to pre-pandemic levels. However, with the unemployment rate falling back to the pre-COVID level, wage inflation starts to become worrisome. Encouragingly, the labour participation rate in the United States, which had been stagnant for most of 2021, has

been steadily climbing since the fall, thereby expanding the labour pool (Chart 1). The Great Resignation looks to be reversing the course. Reasons behind the improvement include receding worries about catching COVID, schools reopening allowing parents to return to work full-time, and for some, a realization that retirement happened too early. In Canada, a renewed focus on increasing immigration to compensate for reduced levels during the health crisis has resulted in a historically high number of newcomers arriving in 2021, with even higher targets set by the federal government through 2024. Immigration accounts for almost 100% of Canada's labour force growth.

Elevated food and energy costs will erode growth in real household income and dampen overall economic growth. Even before the war, GDP growth in most countries was expected to slow this year from the elevated levels recorded last year by the global economy emerging from the recession. Notwithstanding recent downward revisions, real GDP growth in Canada and the United States is expected to be in the 3% to 4% range this year, with Canada outpacing the United States, before growth rates moderate further in 2023.

Central Banks

North American central banks appear to be satisfied that maximum sustainable employment has been achieved, so now the focus is price stability. Inflation is running significantly above the stated target of averaging 2% and is projected to continue to do so through to 2023. Less accommodative monetary policy is necessary to assuage both short-term and long-term inflation concerns. While current inflation is high at 5.7% in Canada and 7.9% in the United States, expected inflation over the longer-term is anchored with the U.S. 10-Year Breakeven Inflation Rate at 2.84% (Chart 2).

Commodity prices have spiked up, but supply-induced price shocks do not generally persist for a prolonged period of time. As the old adage goes, "the cure for high prices is high prices." When prices keep going up, demand destruction and an increase in supply follow, both of which eventually leads to lower prices. For reference, the futures curves for various commodities are all in backwardation (charts 3-8), meaning financial markets do not believe that today's high prices will persist over the medium-term.

Presently, the U.S. Federal Reserve projects that the Federal funds rate will be 1.9% by the end of this year and 2.8% by the end of 2023 compared to 0.5% now. The pace of the interest rate increases has become murkier as inflation has recently been revised upwards. Market pundits opine aggressively front-loading monetary tightening may be most effective to rein in inflation expectations. Financial markets are projecting a quicker pace of increases than the Federal Reserve, estimating that the Federal funds rate will reach 2.5% by year-end and 3.0% in 2023.

The shift from quantitative easing (QE) to quantitative tightening (QT) is also being closely monitored. Last time around, following the financial crisis, the pace of the run-off was very gradual, and QT did not start until three years after QE ended in 2015. This time the Fed's balance sheet is almost double the size at $8.5 trillion, economic growth is higher, and inflation is higher. Accordingly, Fed officials have signaled QT may start in May, just two months QE ended and at a much faster pace.

GLOBEINVEST
CAPITAL MANAGEMENT INC.

The Fed hopes to tame inflation through interest rate hikes and QT while holding unemployment steady and avoiding a recession. History shows that a soft landing is difficult to achieve, but there are some unusual features in today's economy that are more supportive of that outcome. In addition to higher interest rates, a shift from demand for goods to services may further reduce demand for durable goods and when combined with improved supply as bottlenecks are resolved, result in lower prices for items such as cars, appliances, and electronics. Secondly, as the U.S. labour force bounces back, employment can continue to grow without putting significant upward pressure on wages for companies.

The U.S Treasury yield curve has flattened significantly since the last quarter. The 10-Year/2-Year spread went negative last week, albeit briefly, also known as "inverting". This is a cause for concern as an inverted curve remains one of the best leading indicators of a recession. Bear in mind, recessions do not typically start ahead of the curve inverting and the lead time could be as long as two years, with the average lead time of 16 months based on the last seven recessions. Furthermore, the S&P 500 historically peaked an average of eleven months after an inversion, gaining 15% over this timeframe. Nonetheless, the flattening yield curve is flashing a warning sign and signals an increased probability of a recession over the next few years.

The FOMC is committed to being data dependent so its path is not set in stone. Its actions are influenced and adjusted depending on incoming data and financial market stability. In the near-term, a more flexible inflation range may be required as the pendulum swings towards less globalization.

Trend to Deglobalization or More Onshoring

Over the past thirty years, the global economy has benefitted from globalization which is considered deflationary as corporations sought to manufacture goods in lowest cost regions around the world. Consumers in developed countries benefitted through low priced products contributing to low inflation, while workers in developing countries benefitted from the jobs provided by manufacturing the goods.

The supply chain disruptions arising from the global healthcare crisis highlighted the problems that can arise from sourcing goods from far away countries. More recently, the Russia/Ukraine war highlighted the vulnerabilities that come with relying on autocratic countries for key goods and materials. There is a recognition amongst countries and corporations that the lowest cost source may not always be the optimal solution.

The semiconductor industry is one that has recognized the importance of increasing local sourcing. Major semiconductor manufacturers have announced new foundry facilities to be built in the United States.

REPowerEU is a step towards deglobalization, putting energy security above cost and proximity. Stop gap measures include the release of strategic oil reserves and delaying the decommissioning of coal powered plants. Longer-term solutions include sourcing supply from less autocratic countries, while accelerating growth in renewables such as hydro, wind, solar and potentially nuclear. The focus on energy security in conjunction with climate change goals will require capital investment to build out the necessary

infrastructure and represent a positive development for exporting nations that are politically friendly.

Corporate Profits

Corporate profits will be the key driver for stock price appreciation. Stock valuation is influenced by future earnings growth and interest rates. The latter is going up, so multiple expansion is unlikely to play the same role over the next decade as it did in the last.

Earnings per share for the TSX/S&P Composite Index and S&P500 Index are expected to be up 12.7% and 9.1%, respectively this year. For next year, forecasts call for profit growth of 3.6% and 9.9%, respectively. Profit margins, which are at historical highs, are expected to be maintained, indicating companies should successfully offset higher input costs by implementing price increases and productivity improvements.

Many companies have commented on an already improving supply chain which is expected to get better as the year unfolds. Management commentary on this topic in light of China's rolling shutdowns to contain COVID-19 will be a good indicator if profit margins will hold.

Share buybacks for S&P500 companies reached a record level in 2021; so far, 2022 is on pace to be even higher still. Companies typically repurchase their shares when they are confident of the future. A lower share count is also supportive for reported earnings per share.

Conclusion

The global economy has experienced two extreme events over the past two years which has made forecasting even more difficult than usual. Frankly, we do not know when the next recession will occur, nor does anyone else.

The geopolitical landscape is changing, potentially leading to a realignment of alliances and a restructuring of global trade. It is human nature to adapt to change and that is already underway. Change can present both challenges and opportunities. We will focus on the opportunities and companies that will benefit from them.

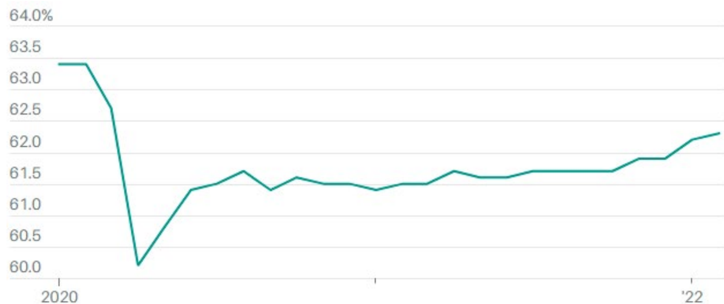
The security selection process for our client portfolios remains unchanged, adhering to our basic tenets of buying both reasonably valued (1) income stocks with attractive dividend yields and stable, visible future cash flows to fund annual dividend increases and (2) growth stocks with sound balance sheets, industry tailwinds, and pricing power.

Once again, we will be mailing out our Investment Policy Statements shortly for you to review. It is very important to let us know if there are any changes that would affect your financial objectives, risk tolerance or time horizon. We would appreciate your attention to this matter to ensure that your personal information is up to date.

Christine Poole, MBA, CFA

GLOBEINVEST
CAPITAL MANAGEMENT INC.

CHART 1: Labor-force Participation Rate
-U.S. Bureau of Labor Statistics, accessed via the St. Louis Federal Reserve



Note: Percent, seasonally adjusted

CHART 2: 10 Year Breakeven Inflation Rate
- Federal Reserve Bank of St. Louis

Note: Shaded areas indicate U.S. recessions

CHART 3: NYMEX Light Sweet Crude Oil Futures Curve
- Refinitiv Datastream

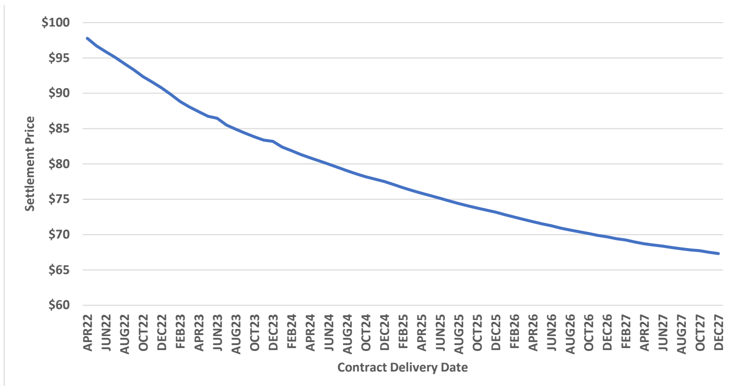
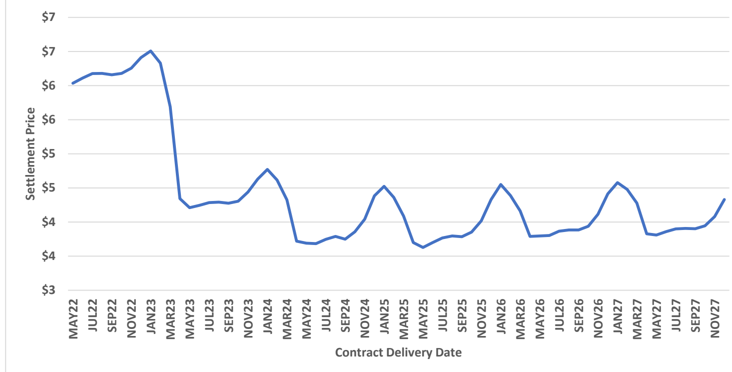


CHART 4: NYMEX Henry Hub National Gas Futures Curve
- Refinitiv Datastream



GLOBEINVEST
CAPITAL MANAGEMENT INC.

CHART 5: CBOT SRW Wheat Futures Curve
– Refinitiv Datastream

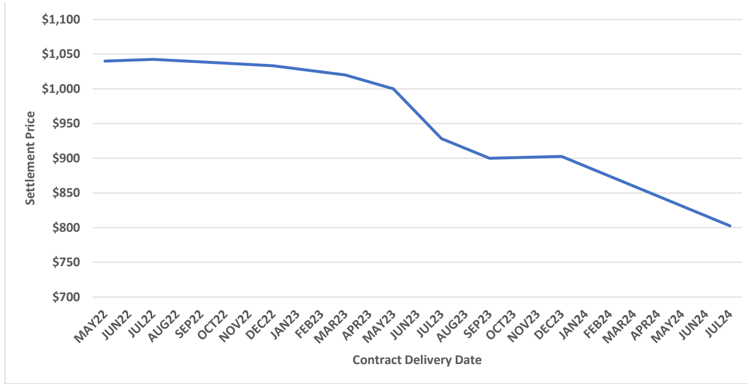


CHART 6: CBOT Corn Futures Curve
– Refinitiv Datastream

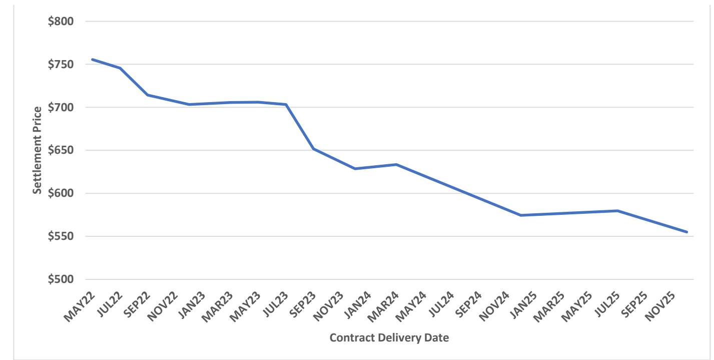


CHART 7: LME Aluminum Official Prices Curve
– The London Metal Exchange

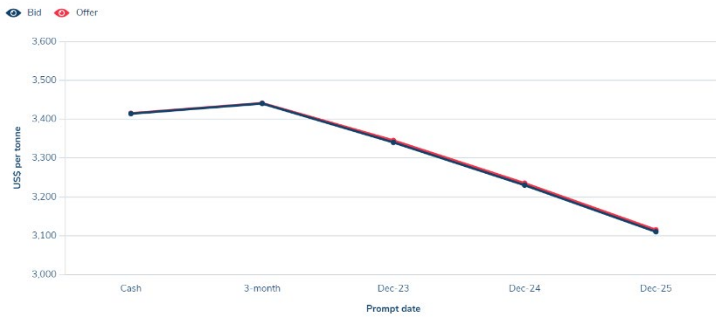
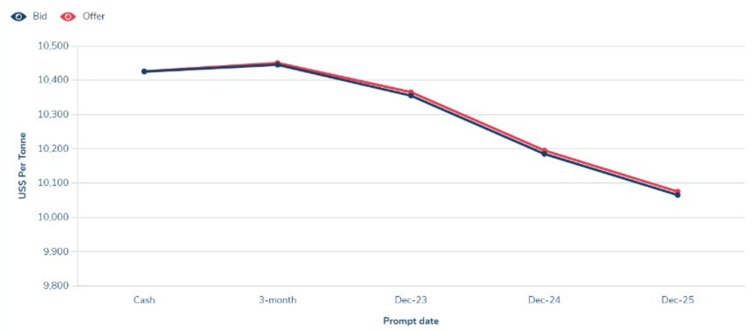


CHART 8: LME Copper Official Prices Curve
– The London Metal Exchange



RECENT BNN SHOWS

Christine: March 15, 2022

Christine: February 15, 2022

Christine: January 18, 2022

Christine: December 14, 2021

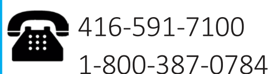
Christine: November 16, 2021

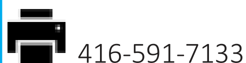
Christine: October 13, 2021

Christine: September 14, 2021

20 Queen St. West, Suite 3308 Toronto, ON M5H 3R3

www.globe-invest.com


416-591-7100
1-800-387-0784


416-591-7133

info@globe-invest.com

MARCH 31, 2022 STATISTICAL SUMMARY

STOCK MARKETS	QTD	YTD
S&P TSX COMPOSITE TOTAL RETURN (CAD)	3.8 %	20.2 %
S&P 500 TOTAL RETURN (CAD)	-5.6 %	15.1 %
S&P 500 TOTAL RETURN (USD)	-4.6 %	15.6 %
DJIA TOTAL RETURN (USD)	-4.1 %	7.1 %
NASDAQ COMPOSITE PRICE RETURN (USD)	-9.1 %	13.3 %
MSCI WORLD INDEX PRICE RETURN (CAD)	-6.5 %	8.1 %
CANADIAN UNIVERSE BOND INDEX	-7.0 %	-4.5 %

COMMODITIES	QTD	YTD
GOLD	5.7 %	14.2 %
SILVER	7.4 %	2.6 %
COPPER	6.4 %	18.0 %
NATURAL GAS (NYMEX)	51.3 %	116.3 %
WTI	33.3 %	69.5 %
BRENT	35.1 %	65.8 %

TREASURY BONDS	3/31/22	12/31/21	3/31/21
2 YEAR (CAD)	2.27 %	0.98 %	0.22 %
2 YEAR (US)	2.28 %	0.73 %	0.16 %
5 YEAR (CAD)	2.39 %	1.28 %	0.99 %
5 YEAR (US)	2.42 %	1.26 %	0.97 %
10 YEAR (CAD)	2.40 %	1.45 %	1.55 %
10 YEAR (US)	2.32 %	1.52 %	1.72 %
30 YEAR (CAD)	2.37 %	1.72 %	1.97 %
30 YEAR (US)	2.44 %	1.90 %	2.35 %
CPI (CAD)	5.70 %	4.80 %	2.20 %
CORE CPI (CAD)	4.70 %	4.00 %	1.10 %
CPI (US)	7.90 %	7.00 %	2.60 %
CORE CPI (US)	6.40 %	5.50 %	1.60 %

GlobeInvest Capital Management Investment Notes is a statement of opinion based on information which GlobeInvest Capital Management Inc. ("GCMI") believes, but does not warrant, to be reliable. It contains assessments of market conditions at a specific point in time and is not intended to be a guarantee of future results. It is intended solely for the use of GCMI clients. The reader should not rely on or act upon the information contained herein without first obtaining the advice of a registered investment adviser.

GCMI is registered with the Ontario Securities Commission, the British Columbia Securities Commission, the Alberta Securities Commission, the Saskatchewan Securities Commission, the Manitoba Securities Commission, Autorite des marches financiers and the Nova Scotia Securities Commission as Portfolio Manager ("PM"). In GCMI's role as PM it acts as an investment manager for private and institutional investors on a discretionary basis.

GLOBEINVEST
CAPITAL MANAGEMENT INC.