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MARKET COMMENTARY Q4 2021

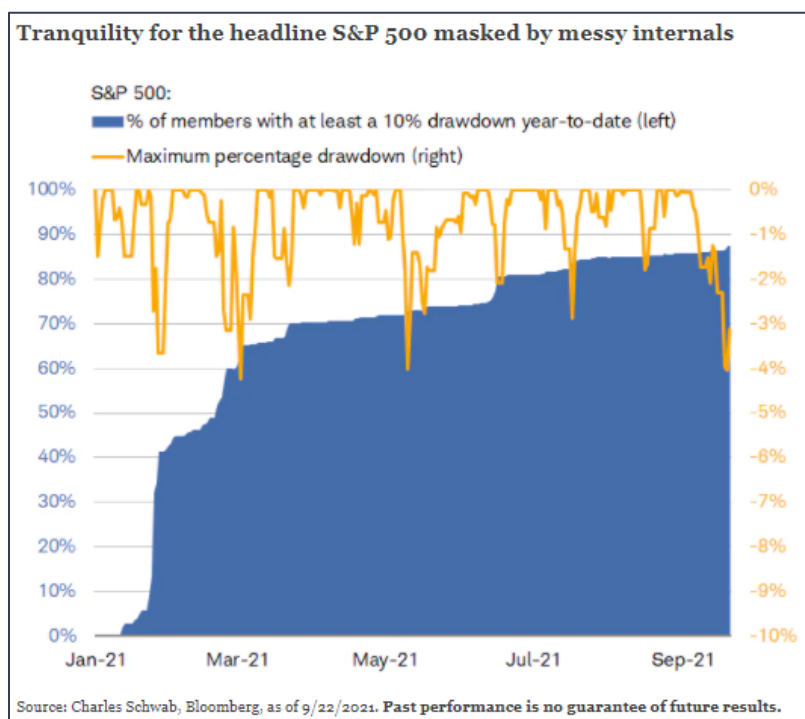
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Mandeville Market Perspective – Fall 2021

Although North American equity indices have steadily climbed year-to-date, index performance hides much of the choppiness that lies beneath its surface. Last quarter, we cautioned investors about the risks of normalizing economic growth & above-average inflation, and are now beginning to see softness appear in broad-based economic data. Market jitters last quarter surrounding Evergrande, global supply chain bottlenecks, the Central Bank's dilemma and multiple spending bills on the desk of US Congress, have all added to the level of implied volatility in the financial markets.

That said, while these may act to moderate the explosive global growth seen YTD, a combination of government stimulus, ultra-low interest rates (relative to history), successful vaccination campaigns in advanced economies bolster our belief that common equities will remain the highest returning asset class over the long term. Said differently – the TINA thesis for equities (there is no alternative) should remain intact over the long run.

As is most often the case, headline index returns rarely provide the full picture – to date, almost 90% of S&P 500 constituents have experienced a drawdown of at least 10%, despite the index continuing on its upward trajectory.



With Global stocks now facing a multitude of near-term pressures that will likely keep volatility elevated through year-end, we recommend investors maintain a certain amount of cash on the sidelines to take advantages of the opportunities said volatility presents.

Central Banks' Inflation Dilemma

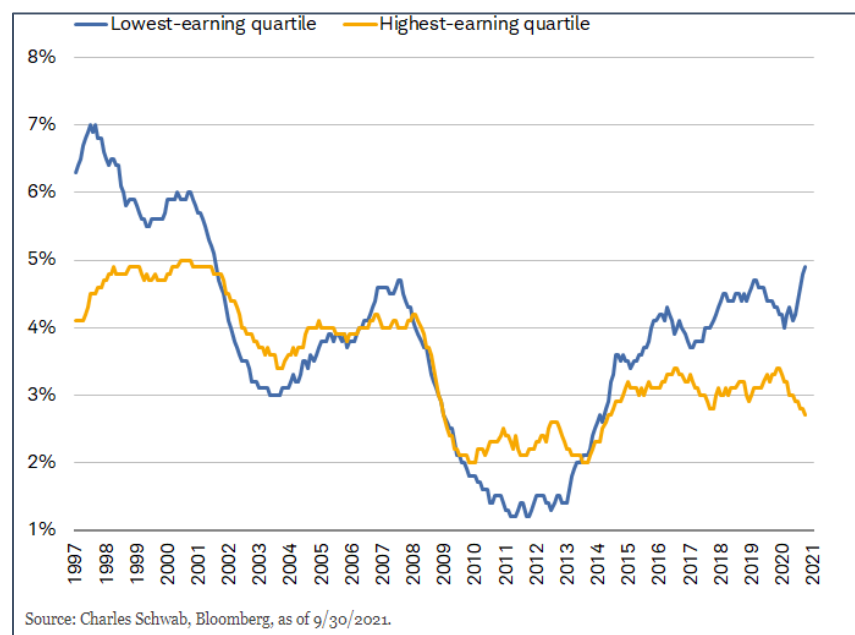
The US Federal Reserve has indicated that it is prepared to begin tapering its bond-buying program, and is on pace to raise short-term rates by the end of 2022. As the Fed Chair Jerome Powell broadcasts an eventual end to the central bank's dovish policy stance, both bond and equity markets are pricing in the prospects that economic growth (and inflation) are likely to normalize over the longer-term.

At the Federal Open Market Committee (FOMC) meeting earlier in November, Powell announced the start of its balance sheet tapering at a pace of \$15bn per month (of which \$10bn is Treasuries and \$5bn is mortgage-backed securities), while holding interest rates steady.

Rhetoric from central banks around the world shows a willingness to tolerate a higher degree of inflation, at least in the short-to-mid term – a dramatic policy shift from prior cycles where central banks moved to pre-emptively counteract overheating inflation. Bankers are justifying the move with the fact that the prior decade was characterized by lower-than-targeted inflation, coupled with the fact that decision makers believe much of today's inflation is transitory.

While certain pockets of inflation may well be transitory, others are likely more lasting. Wage growth, for example, is historically very sticky – meaning once employers decide to raise wages, it's very difficult to subsequently reduce them.

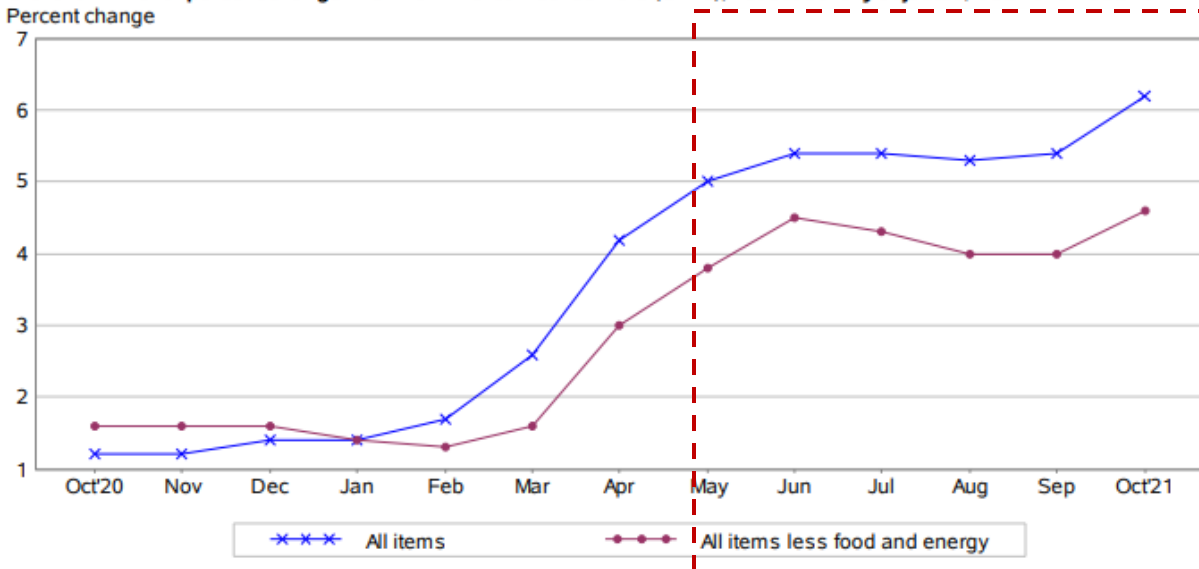
Today, the economy is experiencing levels of wage growth that nears the upper-bound of its decade long average. Bottom line: wages are growing quickly, yet much of the growth is still being driven by lower income-earning workers, which indicates a very strong labour market and potentially irreversible price increases to follow.



Other sources of inflation have been well documented— a surge in demand for goods and services is outstripping the pace of supply. Supply chain congestion at critical global shipping ports has led to shortages of items ranging from computer chips to household goods. Layered on top of that is rapidly rising commodity prices and wage expectations, which has led analysts to revise inflation assumptions – consensus now is that it will remain elevated much longer than markets originally anticipated.

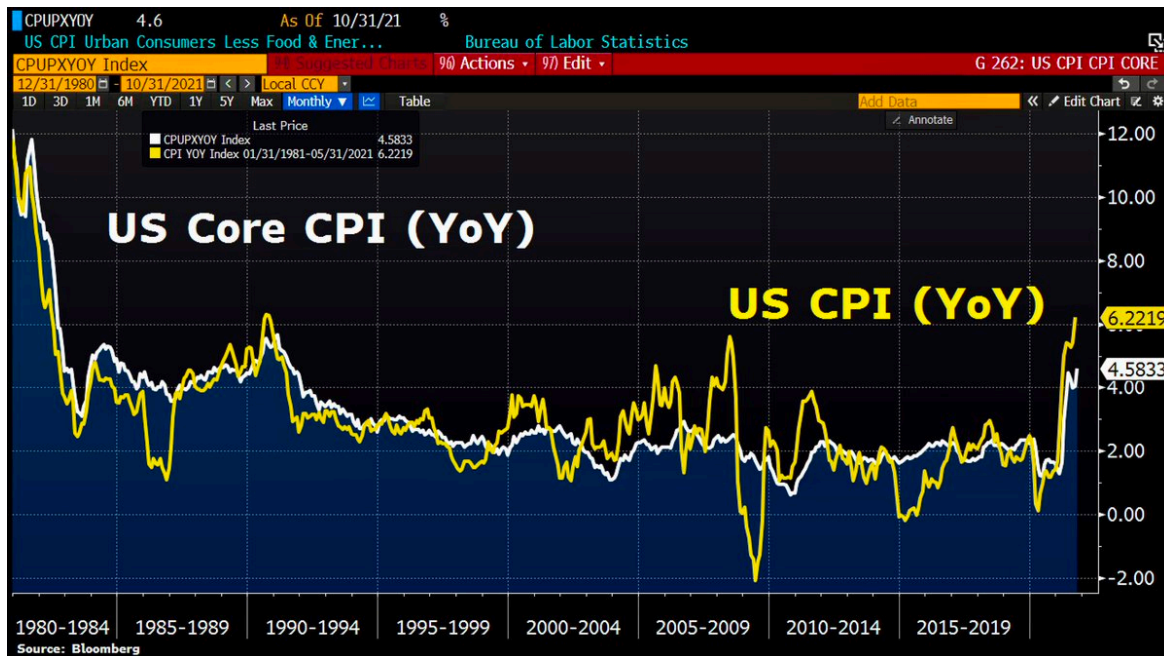
US inflation hit a 3-decade high in October, delivering significant increases in price for everything from food to cars to fuel. The US Consumer Price Index (CPI) – a measure of what consumers pay for a standardized basket of goods and services – increased 6.2% in October from its prior year. This was the fastest 12-month change since 1990, and the 5th consecutive month above 5%.

Chart 2. 12-month percent change in CPI for All Urban Consumers (CPI-U), not seasonally adjusted, Oct. 2020 - Oct. 2021



Source: US Department of Labour

The current struggle for the market, however, is that the Fed adopted a policy of “flexible average inflation targeting” amidst the COVID-19 pandemic – a move aimed at combating persistently low inflation in the years prior to 2020. The Fed signaled that instead, it would allow inflation to run “hot” for some period of time, to ensure its objectives of maximum employment are met and that growth would not be curtailed. Today, with inflation running well above the Fed’s ~2% target, the market is at odds with whether the Fed should (or will) raise rates to bring inflation levels back to 2%-2.5%.



Source: Bloomberg

North of the border, the Bank of Canada adjusted its forward guidance at its October meeting to account for Canada's hot economy. While the BoC held its policy rate steady at 0.25%, it pulled forward its guidance for when they expect enough economic "slack" will be absorbed to warrant a raise in rates – this is now expected to occur in the middle of 2022, but could occur as early as April. Interestingly, the BoC guided that it didn't anticipate inflation to normalize until 2024 – and no, that's not a typo.

Key implications for investors is that analysts now forecast 3 rate hikes from the BoC in 2022, taking the overnight rate to 1% by the end of next year – a substantially more hawkish outlook than our US peers.

\$1.2 Trillion Infrastructure Bill Signed into Law

As Central Banks begin to ease off the stimulus accelerator, the White House continues to charge full speed ahead.

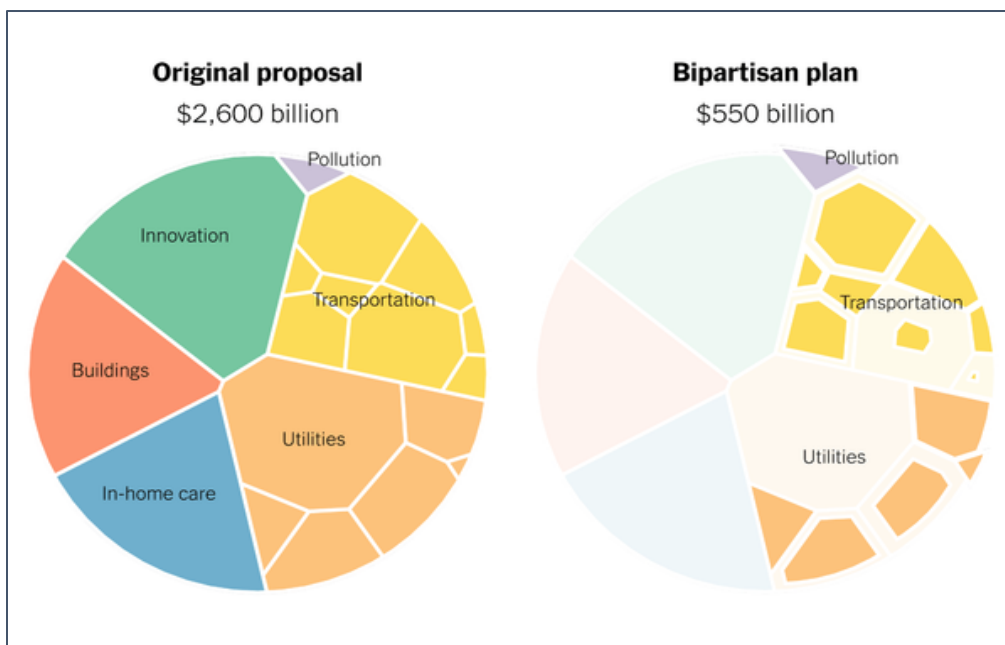
This month, President Biden signed a \$1.2 trillion infrastructure bill into law, finalizing a key part of his economic agenda. The bill will deliver \$550bn of new federal investment in America's infrastructure over the next 5 years, spanning everything from bridges to roads to broadband to energy infrastructure.

Notable aspects of the bill are plans for the largest federal investment in public transit in history and in passenger rail since the creation of Amtrak, a \$65bn commitment to improving the nation's broadband infrastructure, \$42bn to upgrade port infrastructure and airports, \$15bn for low-

emission buses and electric vehicle infrastructure, \$65bn to rebuild the electric grid, and \$110bn for roads, bridges and other major infrastructure upgrades.

Surprisingly, amongst a multitude of measures proposed to pay for the spending, raising taxes was not cited as an option. Rather, it is expected to add \$256bn to the federal budget deficit over the next 10 years.

In terms of economic impact, these investments are likely to have more of a long-term impact on job creation than immediately. The benefits of infrastructure spending take longer to trickle through the economy than does easing monetary policy, however the impacts are very long-lasting. According to S&P Global, the Bill will lead to 883,600 new jobs by 2030, indicating a substantial runway for continued economic strength.



Source: Bloomberg

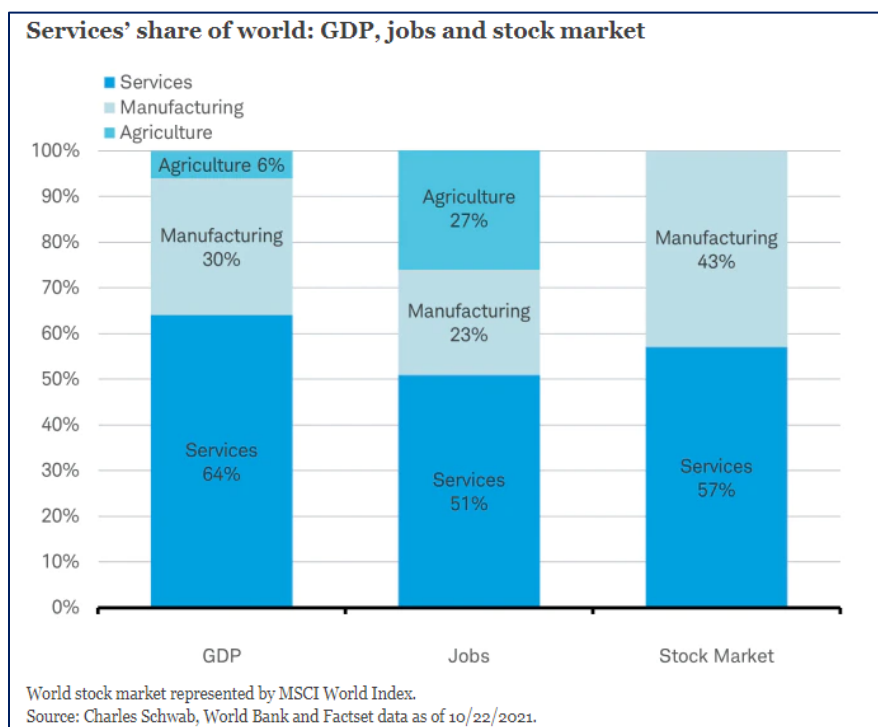
Longer-Term Economic Conditions Remain Favourable Despite Near-Term Volatility

Last quarter, our asset allocation guidance reflected our view that shorter-term economic data was poised to cool-off over the next two years – we have seen this appear in economic data of late. Recent PMI data suggests that purchasing managers have slowed their expenditures, which is likely a result of product & labour shortages.

A global energy supply crunch has reared its head in recent weeks, exacerbating the upward trend in natural gas spot prices and spilling over into other commodity prices. This has raised

concerns around economic output and inflation, particularly in the European and Asian economies. European benchmark natural gas prices have soared over 500% in 2021 alone – a similar story in Asia as well. Most recently, North American natural gas prices have joined the rally, with futures reaching some of their highest levels since 2014. The meteoric supply/demand imbalance across the global natural gas complex has added another layer of downside risks to near-term economic growth. For example, China's PMI fell into contractionary territory in early October.

Thinking longer-term, a major bright spot for equity markets is that the global services sector is still experiencing explosive growth – we define services to include healthcare, law, entertainment, hospitality, education, among others. In fact, services' share of world GDP has now far surpassed that of manufacturing or agriculture, despite most economic data releases reporting activity in the manufacturing sector. Said differently, despite soft economic readings from traditional indicators (i.e. PMI), Services comprise over half of the MSCI World Index and should continue to drive further market momentum through the end of the year.



Earnings Revisions Strong, Though Normalizing from Peak

Year-over-year corporate earnings growth has also begun to stabilize off of inflated levels earlier this year. As supply chain bottlenecks increase companies' costs for materials and labor, near-term profit margins are likely to contract. The level of upward analyst earnings revisions has turned negative, reflecting a consensus view that near-term corporate earnings are unlikely to continue

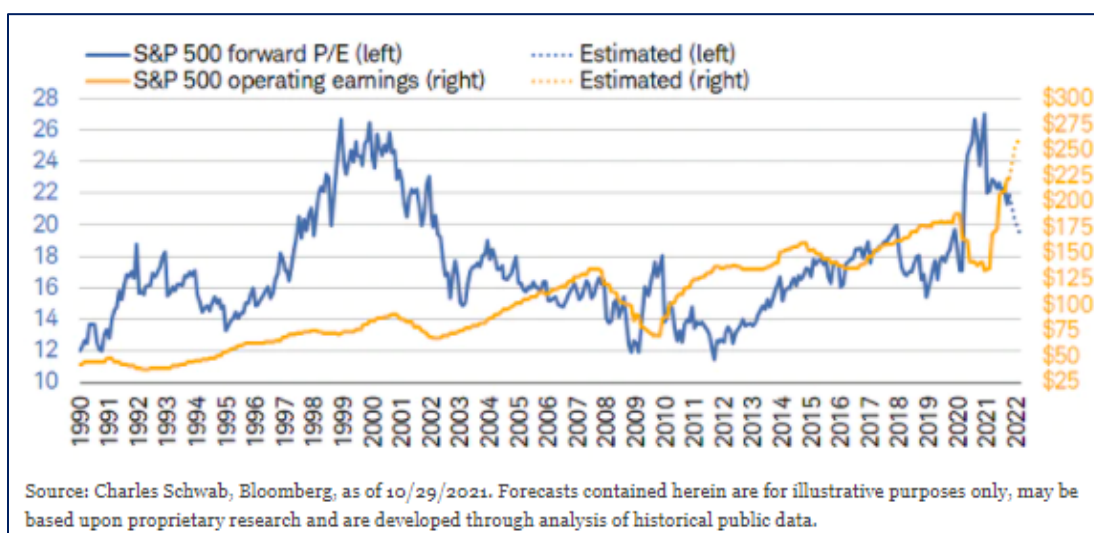
beating expectations. Since the end of the summer, the level of positive analyst earnings revisions has lost momentum, broadly speaking. The aforementioned supply chain bottlenecks, increase in input costs and elevated wages is beginning to weigh on corporate earnings.



Strong earnings have resulted in the broad-based Price-to-Earnings multiple of the S&P 500 down from levels not seen since the dotcom bubble. Last year, investors questioned whether the market was doomed for a repeat of 1999-2000, as the forward P/E of the S&P 500 reached 27x.

What many fail to understand, however, is that the Earnings of corporate America were trending at artificially depressed levels – said differently, the Earnings (denominator) component of the P/E ratio compressed while the Price (numerator) component was left unchanged as investors looked beyond the COVID-19 pandemic.

Today, the forward P/E ratio remains elevated but is declining as corporate Earnings play catch-up. Nevertheless, the market is expensive relative to history by any traditional metric, which is often a leading indicator of heightened volatility for the quarters/years to come.

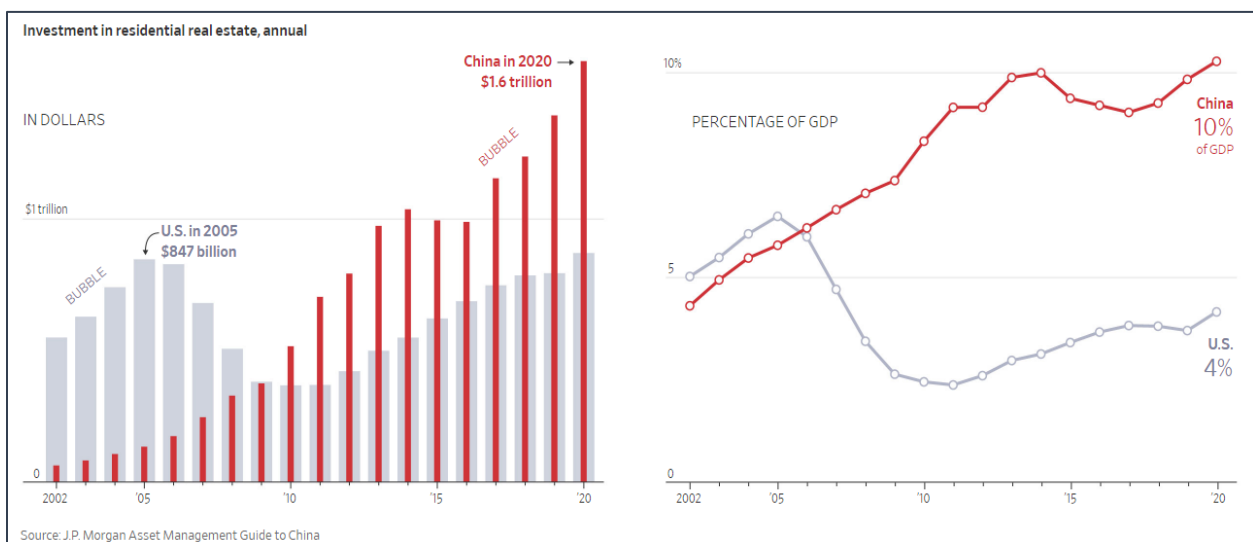


China's Embattled Evergrande

We feel it's important to acknowledge the Evergrande debacle which caused a broad-based global equity market selloff in late September/early October and was the subject of many client questions/concerns— although no longer front-and-centre in the financial press, we feel it's important for investors to keep a close eye on.

Chinese property development giant Evergrande was (and still is) on the brink of collapse, and analysts caution that the potential fallout from its bankruptcy could have implications that extend far beyond China's borders. According to Capital Economics' chief Asia economist, the "Evergrande collapse would be the biggest test that China's financial system has faced in years."

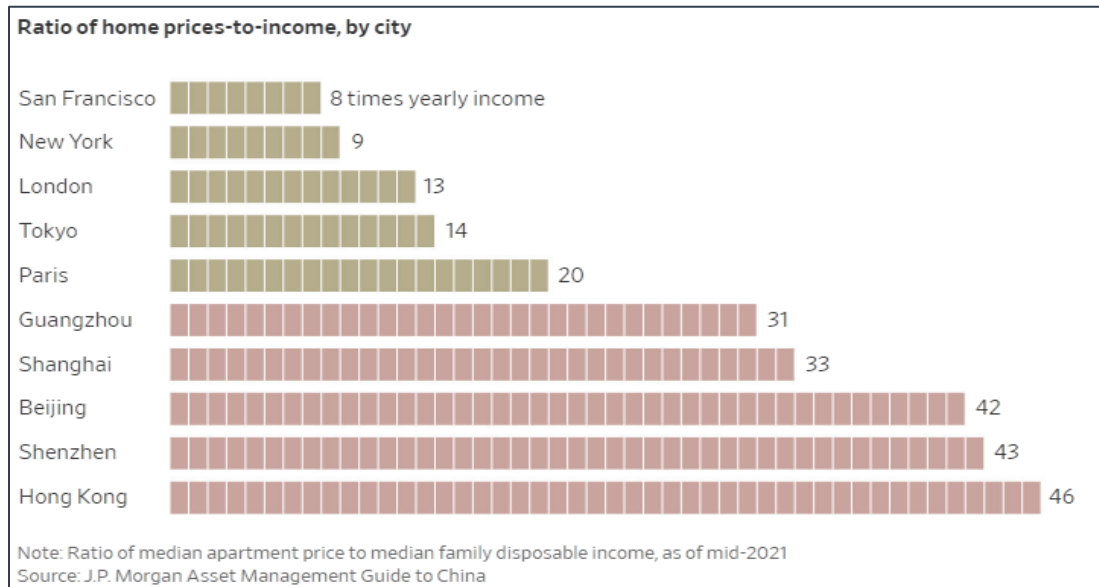
After its rapid, multi-decade expansion in China, Evergrande for years had purchased real estate assets as China's economy thrived. An aggressive expansion agenda, coupled with accommodative debt markets, allowed Evergrande to amass a crushing debt burden north of \$300bn. A recent policy shift from the Chinese government imposed tougher limits on indebtedness of corporations and has left Evergrande scrambling to pay down \$300bn in liabilities. Analysts worry that if the developer defaults on this debt, there would be far reaching implications for the overall Chinese real estate sector.



Evergrande and the broader real estate sector in China are significant drivers of GDP, and the latest Evergrande debacle has shed light on the scale of the real estate bubble that has been building for years in the country's residential property market.

From 2002 to 2020, Chinese investment in residential real estate as a percentage of GDP has dwarfed the U.S. housing bubble of the 2000's. At roughly 10% of Chinese GDP, a deterioration or slowdown in the housing market would cause significant knock-on effects for the broader Chinese economy.

To further put into perspective the sheer scale of China's housing boom, one can look at the median home prices to family disposable income. Today, a median apartment in San Francisco or New York costs roughly 8.5x annual income of a family; in Hong Kong, Shenzhen and Beijing, this figure is north of 40x.



Thus far, Evergrande has averted default by selling off assets at deeply discounted prices. For example, its recent sale of Dutch electric motor maker e-Traction, was sold earlier this month at a staggering 97% discount to Evergrande's 2019 purchase price.

As the firm continues its fight to meet interest payments, investors still grapple with many unknowns, including what the Chinese government response to the crisis might be. Beijing has signaled it is preparing to protect the interests of property owners for the benefit of protecting national interests. As it stands today, Evergrande remains a going concern, however the prices of its stock & bonds indicate that investors expect the company to fail and eventually restructure.

Asset Allocation and Portfolio Guidance

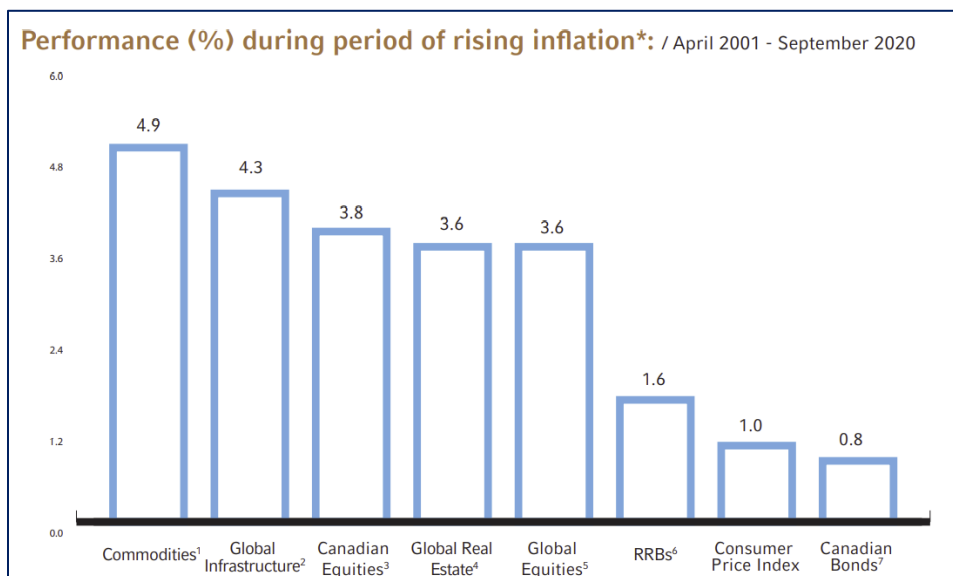
While last quarter certainly lived up to its volatile reputation, we still believe that equities offer investors the best risk-reward relative to other asset classes. In our last note, we adjusted our factor guidance for equities in favour of Quality over Value, which continues to perform strongly amidst a volatile macro backdrop.

We reiterate our Quality factor preference for the time being – these are generally companies exhibiting high returns on capital, stable year-over-year earnings growth, low financial leverage and the ability to pass along heightened input costs to its consumers – the last point being especially relevant in today's environment. At this stage in the economic cycle, we favour stable compounders over more cyclically oriented businesses, which should help investors weather the current volatile market conditions.

Gross Performance as of 10/29/2021 in USD									
Index Name	1D	1W	1M	3M	YTD	1Y	3Y	5Y	10Y
MSCI ACWI Index	-0.2%	0.4%	4.5%	2.6%	17.2%	36.3%	19.0%	15.3%	11.6%
 MSCI ACWI Minimum Volatility Index	-0.2%	-0.4%	2.1%	0.8%	10.4%	20.1%	11.4%	10.4%	10.2%
 MSCI ACWI High Dividend Yield Index	-0.4%	-0.4%	1.4%	-1.4%	10.3%	29.2%	11.4%	10.3%	8.5%
 MSCI ACWI Quality Index	0.3%	1.1%	5.6%	2.1%	19.0%	35.4%	25.1%	19.7%	14.8%
 MSCI ACWI Momentum Index	-0.1%	1.5%	6.0%	5.5%	11.7%	24.5%	22.9%	19.9%	15.1%
 MSCI ACWI Enhanced Value Index	-0.6%	-0.8%	-1.0%	-1.8%	12.2%	38.3%	9.9%	9.2%	7.9%
 MSCI ACWI Equal Weighted Index	-0.4%	-1.1%	1.6%	0.9%	10.4%	30.2%	14.6%	10.7%	8.1%
 MSCI ACWI Growth Target Index	-0.4%	-0.1%	3.8%	2.1%	15.6%	32.2%	19.0%	16.3%	12.7%

Source: MSCI

We remain underweight fixed income in light of recent Central Bank commentary, although appreciate the fact that an allocation to fixed income can act as a buffer through periods of equity market volatility. While keeping mindful of investors' risk profiles, alternative assets - including private credit and private real estate - can be used as additional sources of income where appropriate. Many alternative assets have historically exhibited low correlations to traditional asset classes, providing substantial diversification benefits. Moreover, investments such as real estate and infrastructure have also historically performed well during periods of rising inflation and thus can act as a hedge against more inflation-sensitive areas of one's portfolio.



Source: Refinitiv, Russell Investments

Of course, understanding the nuances of private & alternative products is difficult for many individuals – a qualified and professional advisor can assist in this process, working with individuals to determine how alternative assets can fit within one's long-term wealth objectives.



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