

Q4 2024

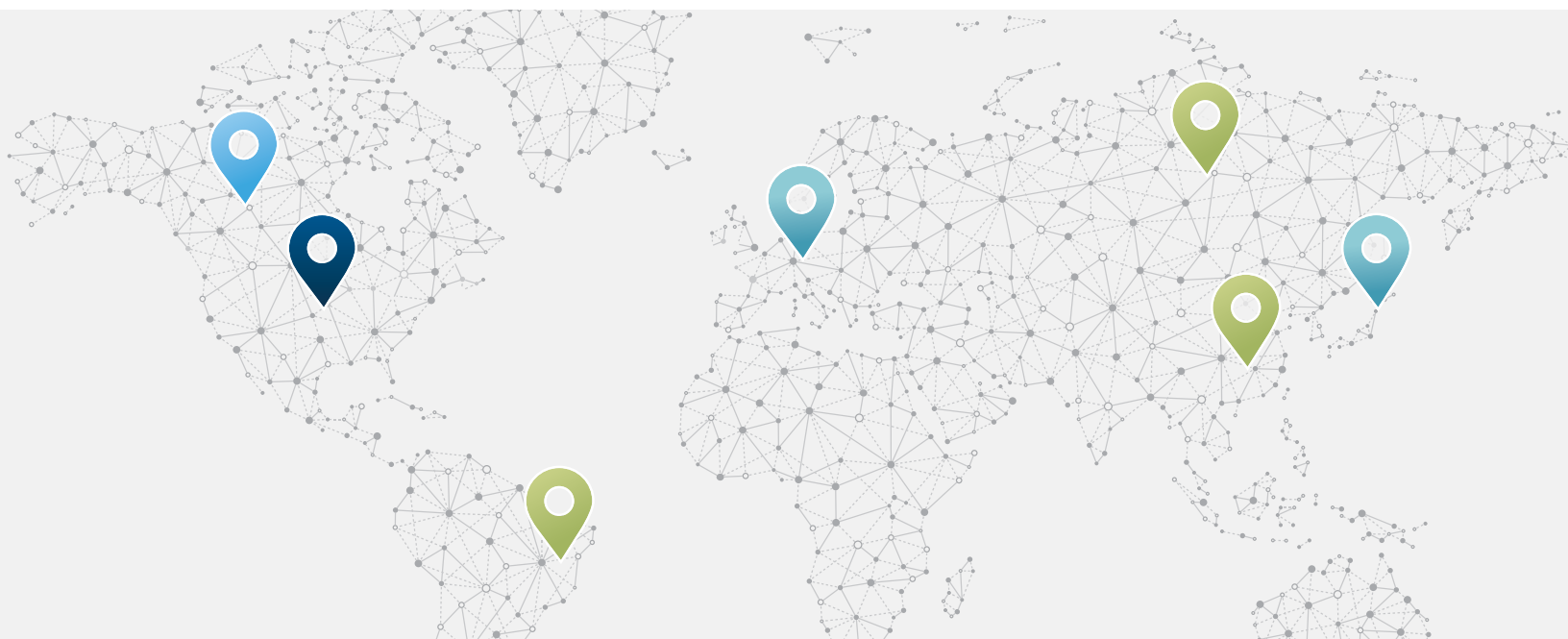
Investment Outlook  
and Portfolio Strategy



# Macroeconomic Landscape

## Global

With the last trace of the global inflation shock showing more encouraging signs of fading and signs that economic growth is cooling, the pivot towards an easier monetary policy stance has taken hold across advanced economies.



### Canada

The Canadian economy is running at an anemic pace, with growth slowing to below the economy's potential rate as the impact of cumulative rate hikes weighs on heavily indebted households that are more sensitive to higher borrowing costs. With inflation back at the 2% target, rapidly waning price pressures have prompted the Bank of Canada to adopt a more aggressive pace of easing versus its major peers as officials place greater emphasis on arresting the economic slowdown following lacklustre performance in the third quarter.

### United States

The US economy continues to operate above its potential rate. The labour market has moved back into a better balance, while inflation has commenced a convincing descent towards the Federal Reserve's 2% target. With inflation judged to be on a more sustainable path downward, policymakers have indicated that the upside risks to inflation have declined at the expense of the downside risks to growth. That saw the Federal Reserve proceed with a jumbo 50 basis point rate cut in September in a pre-emptive move to avoid a hard landing.

### International

Whether the US economy can achieve the elusive soft landing remains at odds with challenges facing the euro area and the United Kingdom, where efforts to sustain their nascent recoveries following recent signs of stagnation are coming up against the need to tame services-driven inflation. Specifically in the euro area, the German locomotive remains plagued by prolonged malaise in the factory sector and a bleak consumer backdrop. Manufacturers have been struggling for over a year amidst sluggish external demand and households are proving hesitant to spend.

### Emerging Markets

The Chinese economy is facing dual headwinds. Property market woes and deteriorating private sector sentiment have limited the scope for domestic-driven growth, while weak external demand conditions are constraining export growth and factory activity. That points to the mounting risk of underperforming the government's 5% annual growth target and underscored the urgency for Beijing to act. After the People's Bank of China unleashed a slate of stimulative measures in late September, Politburo authorities pledged to take actions towards stabilizing the housing market and to support fiscal spending.

# Economic Outlook

## Sticking A Soft Landing

The evolution of our closely monitored Key Policy Variables suggests that achieving a soft economic landing seems much more conceivable. After stalling out earlier this year, the downtrend in inflation has reasserted itself. The Federal Reserve's preferred gauge of underlying inflation is running at 2.1% on a three-month annualized basis. With inflation judged to be moving sustainably to 2%, policymakers have shifted their focus to potential downside risks to the labour market. That prompted the Federal Reserve to cut interest rates by 50 basis points in September, while setting the stage for another 150 basis points of rate cuts by the end of 2025.

Still, while the labour market is rebalancing and slack is building, conditions are not consistent with an economy on the cusp of a recession. Unemployment remains low and the economy is running just above its potential rate. Taken together, the Federal Reserve's determination to prevent further weakness in the labour market and avoid falling behind the curve is keeping the soft landing scenario very much in play.

| KEY POLICY VARIABLES:<br>UNITED STATES                   | Federal Reserve Target | Current | Soft Landing |
|--|------------------------|---------|--------------|
| Gross Domestic Product Growth (Q/Q, Annualized)          | 2.0%                   | 2.0%    | **           |
| Unemployment Rate (%)                                    | 4.4%                   | 4.1%    | **           |
| Nonfarm Payrolls (3 Month Average)                       | 150k                   | 186k    | **           |
| Average Hourly Earnings (Y/Y)                            | 3.0%                   | 4.0%    | **           |
| Employment Cost Index (Y/Y)                              | 3.0%                   | 4.1%    | **           |
| Job Openings To Unemployed Ratio                         | 1.20                   | 1.10    | **           |
| Core Personal Consumption Expenditures Price Index (Y/Y) | 2.2%                   | 2.1%    | **           |
| Long-Term Inflation Expectations (%)                     | 2.5%                   | 3.0%    | **           |
| FEDERAL RESERVE POLICY RATE                              | 3.50%                  | 5.00%   | LOWER        |

Source: Bloomberg as of September 30, 2024.

## Scenario Overview & Investment Strategy

**Soft Landing (55%):** Our high-probability scenario assumes that central banks prove successful in taming inflation with little in the way of damage to the economy. An environment of non-recessionary rate cuts is unambiguously positive for stocks and warrants a moderate overweight allocation over our cyclical time horizon. We maintain an underweight allocation to bonds, with the potential for a less-dovish Federal Reserve versus market expectations leaving little in the way of upside for bond prices. While the prospect for further rate cuts have been fully priced into bond markets, equity markets still have room to run, in our view.

The risks to our bullish thesis and the path to a soft landing are two-fold:

**Inflation Revival (25%):** Should an economy that remains "too hot" prompt policymakers to reconsider their easing plans and refrain from pursuing the magnitude of rate cuts discounted in the market, investors would need to recalibrate their expectations for interest rates higher. This would act as a powerful headwind for both stock and bond markets.

**Shallow Recession (20%):** An outright recession stemming from the lagged impacts of cumulative tightening cannot be ruled out. While rates would undoubtedly be slashed aggressively in response, a recessionary environment and the implications for corporate earnings would outweigh the stimulative impacts from rate cuts and sap both risk appetite and equity markets alike.

# Economic Scenarios

## Main Scenario | Soft Landing

Probability 55 %

In this optimistic scenario, the world's major central banks prove successful in engineering a so-called soft economic landing, thanks to a persistent downtrend in inflation that comes with very limited deterioration in the economy. The disinflationary impulse prompts central bankers to transition from an on-hold monetary policy stance towards aggressive interest rate cuts and inflation is contained without a recession or a significant cost to employment. Central banks achieve the soft landing by cutting rates at early signs of economic weakness, keeping the economy not-too-hot or not-too-cold, but just right. Consequently, the economy averts a hard landing and a new economic cycle begins.

## Scenario 2 | Inflation Revival

Probability 25 %

In the "inflation revival" scenario, both growth and inflation surprise to the upside, which brings into question the ability of central banks to reduce policy rates by the magnitude that is discounted in the market. Should persistent economic resilience, tighter than expected labor market conditions, and the recent easing of financial conditions spark a second wave of inflation, central banks would undoubtedly abandon their plans to cut interest rates further and instead prioritize bringing inflation back to 2% by leaving interest rates at restrictive levels for an extended time. Indeed, cutting interest rates while the economy is operating above its potential and at a time when labor market conditions remain relatively tight risks slowing or even reversing the disinflation process. Amplifying the upside risks to inflation would be an unwelcome escalation in the geopolitical conflicts in Ukraine and/or the Middle East that would create an oil shock and add to the inflationary impulse.

## Scenario 3 | Shallow Recession

Probability 20 %

In the "shallow recession" scenario, consumer-led tailwinds that acted as a buffer to the sharp increase in interest rates through 2023 morphs into headwinds that inevitably pushes the economy into a mild recession. Cumulative central bank tightening begins to weigh more meaningfully on both consumers and businesses given the long lags in the monetary transmission mechanism and weighs more prominently in the data. Specifically, household finances deteriorate under the weight of a cooling jobs market and dwindling excess savings. Meanwhile, tight monetary policy and credit conditions exerts more pain on businesses, manifesting itself into a surge in bankruptcies of vulnerable businesses. Inflation slows by much more than expected in response to the loss of economic momentum. Central banks slash interest rates aggressively in response, but not soon enough to avert a rise in unemployment and a mild recessionary outcome.

# Portfolio Strategy

## Matrix of Expected Returns (CAD)

| SCENARIOS                                   | SOFT LANDING | INFLATION REVIVAL | SHALLOW RECESSION |
|---|--------------|-------------------|-------------------|
| <b>PROBABILITY</b>                          | <b>55%</b>   | <b>25%</b>        | <b>20%</b>        |
| <b>TRADITIONAL INCOME</b>                   |              |                   |                   |
| Money Market                                | 3.6%         | 3.9%              | 3.4%              |
| Canadian Bonds                              | -2.1%        | -8.6%             | 1.5%              |
| <b>NON-TRADITIONAL INCOME</b>               |              |                   |                   |
| Diversified Credit                          | 7.0%         | 8.0%              | 7.0%              |
| Diversified Real Estate                     | 8.0%         | 9.0%              | 6.0%              |
| Infrastructure                              | 7.0%         | 8.0%              | 6.0%              |
| Agriculture                                 | 7.0%         | 8.0%              | 6.0%              |
| <b>TRADITIONAL CAPITAL APPRECIATION</b>     |              |                   |                   |
| Canadian Equity                             | 6.7%         | -12.5%            | -24.2%            |
| U.S. Equity                                 | 2.6%         | -19.8%            | -31.0%            |
| International Equity                        | 0.9%         | -19.4%            | -24.9%            |
| Emerging Market Equity                      | 5.9%         | -24.2%            | -29.6%            |
| <b>NON-TRADITIONAL CAPITAL APPRECIATION</b> |              |                   |                   |
| Private Equity                              | 15.0%        | 12.0%             | 8.0%              |
| CAD/USD                                     | 0.76         | 0.78              | 0.70              |

Source: Fiera Capital, as of September 30, 2024.

Discussions regarding potential future events and their impact on the markets are based solely on historical information and Fiera Capital's estimates and/or opinions, and are provided for illustrative purposes only. General Market projections are hypothetical estimates of long-term returns of economic asset classes based on statistical models and do not represent the returns of an actual investment. Actual results could vary substantially. Models have limitations and may not be relied upon to make predictions of future performance of any account. Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

## Current Strategy<sup>1</sup>

### Traditional and Non-Traditional Portfolios

|                        | MINIMUM | BENCHMARK | MAXIMUM | STRATEGY | +/-  |
|------------------------|---------|-----------|---------|----------|------|
| Money Market           | 0%      | 5%        | 30%     | 5%       | 0%   |
| Canadian Bonds         | 5%      | 25%       | 45%     | 5%       | -20% |
| Canadian Equity        | 10%     | 20%       | 40%     | 35%      | +15% |
| U.S. Equity            | 0%      | 10%       | 20%     | 5%       | -5%  |
| International Equity   | 0%      | 10%       | 20%     | 0%       | -10% |
| Emerging Market Equity | 0%      | 5%        | 15%     | 10%      | +5%  |
| Non-Traditional Income | 5%      | 25%       | 45%     | 40%      | +15% |

### Traditional Portfolios

|   | MINIMUM    | BENCHMARK  | MAXIMUM    | STRATEGY   | +/-        |
|---|------------|------------|------------|------------|------------|
| <b>TRADITIONAL INCOME</b>               | <b>20%</b> | <b>40%</b> | <b>60%</b> | <b>35%</b> | <b>-5%</b> |
| Money Market                            | 0%         | 5%         | 30%        | 5%         | 0%         |
| Canadian Bonds                          | 5%         | 35%        | 55%        | 30%        | -5%        |
| <b>TRADITIONAL CAPITAL APPRECIATION</b> | <b>40%</b> | <b>60%</b> | <b>80%</b> | <b>65%</b> | <b>+5%</b> |
| Canadian Equity                         | 5%         | 25%        | 50%        | 40%        | +15%       |
| U.S. Equity                             | 0%         | 15%        | 30%        | 10%        | -5%        |
| International Equity                    | 0%         | 15%        | 30%        | 5%         | -10%       |
| Emerging Market Equity                  | 0%         | 5%         | 15%        | 10%        | +5%        |

## Evolution of Value-Added<sup>1</sup>



Source: Fiera Capital, as of September 30, 2024.

<sup>1</sup> Based on a 100 basis point value added objective. The benchmark employed here is based on a model portfolio and for illustrative purposes only. Individual client benchmarks are employed in the management of their respective portfolios. Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

# Fixed Income Outlook

## Fixed Income Review

Fixed income markets generated positive results in the third quarter as traders braced for aggressive rate cuts from major central banks. Yield curves steepened in a bullish fashion, with the policy-sensitive short-end falling by much more than longer-dated yields. For the quarter, the FTSE Canada Bond Universe gained 4.7%.

Lingering worries about inflation have given way to concerns about the health of the economy and prompted a dovish shift from major central banks.

The Federal Reserve joined its peers and cut rates by 50 basis points to a target range of 4.75% to 5.0% in September. Officials believe that risks to the economic and employment outlook are now every bit as important as inflation risks. The updated forecasts suggest that a soft landing is still very much in play. Gross domestic product (GDP) growth is estimated at 2.0% between 2024 and 2027, inflation is seen as moving back to target in 2025, and the "dot plot" of rate projections implies a further 150 basis points of rate cuts by the end of next year.

The Bank of Canada is among the most dovish leaning of its central bank peers and the case for further easing remains strong. With inflation melting away more prominently and an ailing economic backdrop, the bank has lowered rates by 75 basis points since June to 4.25%. Officials' emphasis on excess supply conditions and building slack underpins their dovish stance and has tipped the scales towards a jumbo 50 basis point rate cut in October—particularly after the Federal Reserve's outsized move.

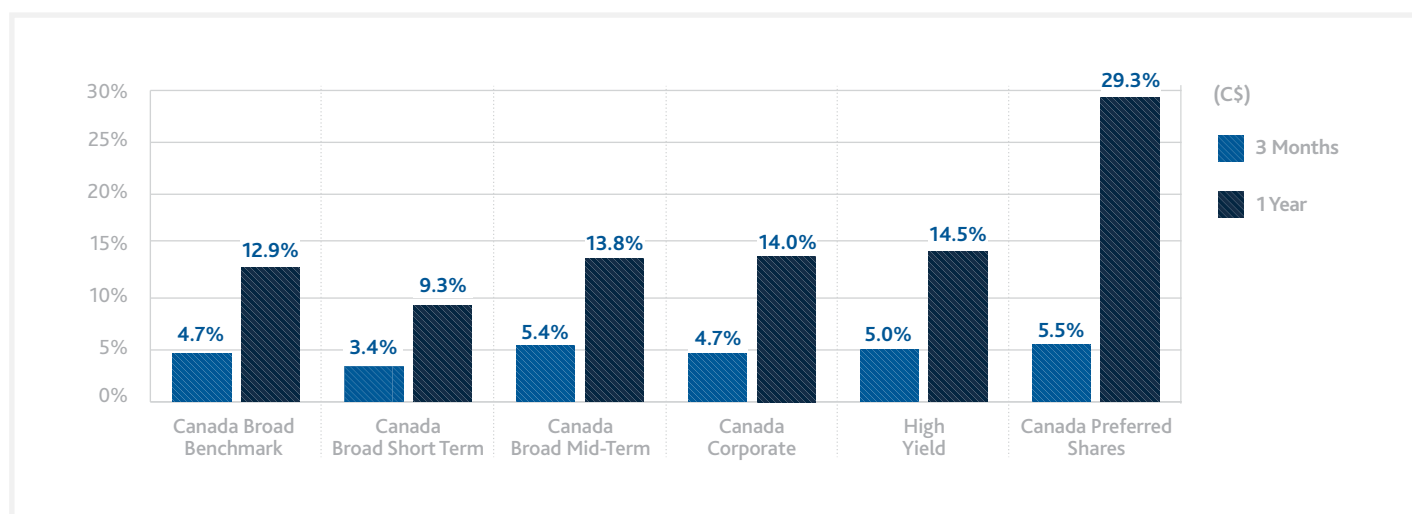
The European Central Bank reduced rates in June and September, bringing the deposit rate to 3.5%. Underlying price pressures are abating and the economy is losing steam. That has set the stage for further easing, particularly given that inflation has slowed to below 2% for the first time since 2021.

In contrast to other major central banks, the Bank of England has yet to shift its focus from inflation to growth. While the central bank lowered rates by 25 basis points to 5.0% in August, stubbornly elevated wages and services inflation prompted the central bank to remain on hold in September, while Governor Bailey has cautioned against cutting rates "too much or too quickly."

## Investment Strategy

Our high probability scenario that is calling for a soft landing assumes less rate cuts than are currently discounted in the bond market (which is already discounting the most aggressive easing cycle on record). Barring a recessionary outcome that would validate those expectations, bond yields are more likely to rise than fall from here. The looming risk of a second inflation wave adds to the upside risk. Given these unattractive risk-reward prospects, we maintain an underweight allocation to bonds.

## Canadian Fixed Income Market Returns



Source: Fiera Capital, as of September 30, 2024.

Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

# Equity Outlook

## Equity Review

The soft landing narrative extended throughout the third quarter and catalyzed a market rally that saw many global indices breach new highs. The MSCI All Country World posted a quarterly gain, with developed market equities underperforming their emerging market peers. The S&P 500 breached a fresh high but underperformed as mega cap technology stocks lost some of their shine as the rotation out of these high-flying stocks took hold. Meanwhile, the S&P/TSX pushed above 24,000 for the first time, closing out its best quarter in more than four years thanks to solid performance in the heavyweight financials and materials sectors that comprise nearly half of the index. The MSCI EAFE also advanced, while the MSCI gauge of emerging market stocks led the global charge after Beijing unveiled a massive round of stimulus that saw Chinese equities surge higher towards quarter-end.

Despite the impressive gains this year, we expect the uptrend in equities to extend thanks to an environment of monetary policy easing (positive for valuations) and a soft economic landing (positive for earnings). We assign a 55% probability to this optimistic scenario.

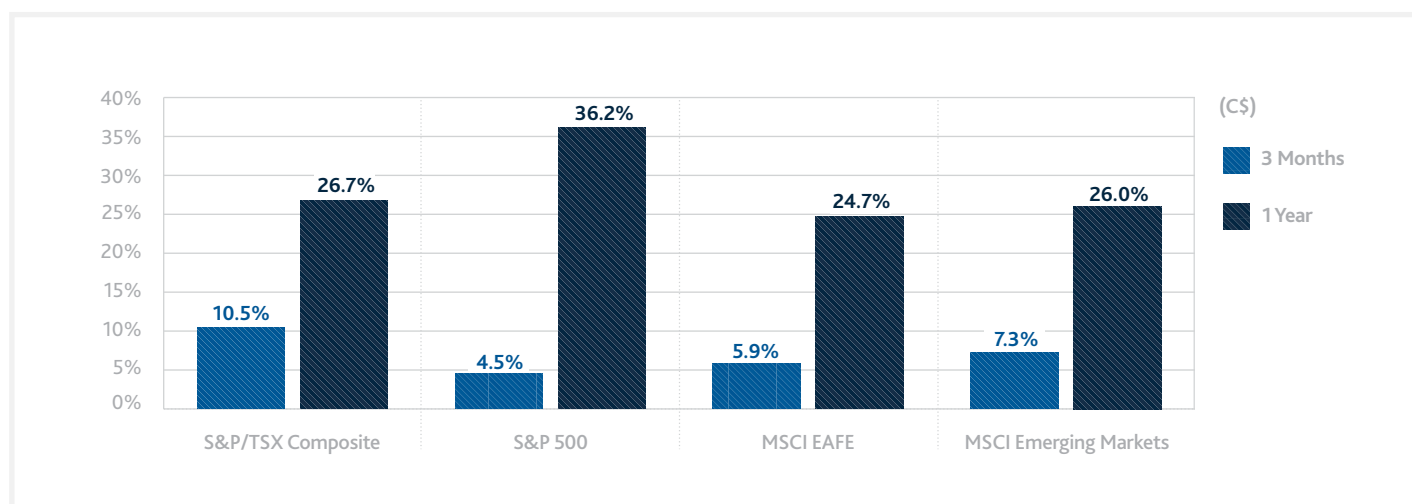
Still, there are some notable risks to the outlook, and recent stock market gains would undoubtedly be vulnerable should investors move to price-in an alternative scenario that includes either a restrained liquidity backdrop (“Inflation Revival” = 25%) and/or a deteriorating growth and earnings backdrop (“Shallow Recession” = 20%). On the former, the risk of a second wave of inflation

that would prompt a “hawkish” policy response and the need for interest rates to remain higher for longer than investors currently expect. In this scenario, bond yields would revert higher and equity market valuations would contract. On the latter, economic growth deteriorates more meaningfully as the cumulative impact of past rate hikes begins to take its toll. While central banks would certainly step in and slash interest rates, it would not be soon enough to avert a recessionary outcome and a bear market in stocks.

## Investment Strategy

With a majority of our scenarios favouring risky assets, we have assumed a moderate overweight stance on stocks over our tactical 12-18 month horizon. Indeed, an environment of disinflationary growth is decidedly positive for stocks. So long as the economy holds up and inflation doesn’t roar back to life, lower interest rates and strong earnings growth are expected to drive stocks higher. With conviction in the bullish soft landing scenario increasing, there’s room for the rotation trade to gain further ground. Regionally, we have a preference for Canadian and Emerging Market stocks, where relatively attractive valuations should allow for further upside should the market rally broaden out towards previous laggards in a pro-cyclical, risk-on environment.

## Equity Market Returns



Source: Fiera Capital, as of September 30, 2024.

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# Private Markets Outlook

## Inflation, Interest Rates and the Case for Non-Traditional Income

While inflation has made some notable progress in subsiding over the last year, there are growing reasons to believe that we are embarking on a period of structurally higher inflation over the next 5 years given secular forces including demographic trends (aging populations) and labour shortages, deglobalization (onshoring), rising debts/deficits, lingering geopolitical conflicts, and the imbalances associated with the green energy transition.

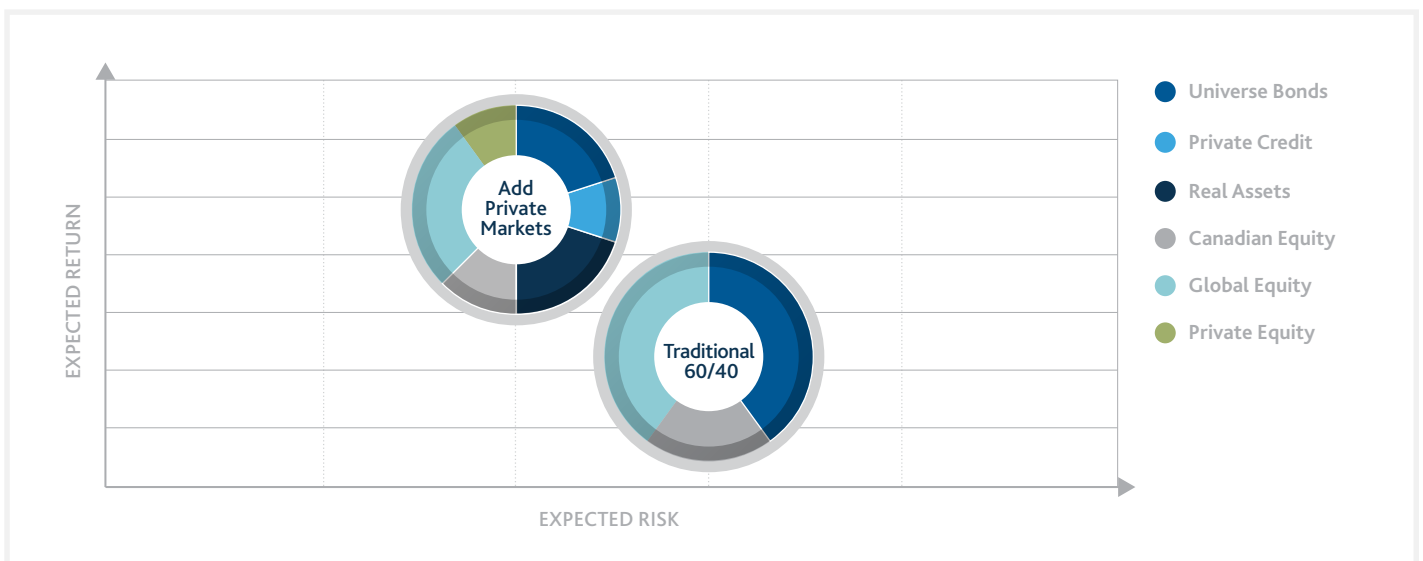
Structurally higher inflation (and accordingly, interest rates) suggests that traditional fixed income may fall short of what investors have grown accustomed to over the last several decades and reinforces the case for non-traditional sources of income in the portfolio setting.

From a portfolio construction perspective, these developments argue for an allocation to private credit and real assets as an alternative to traditional fixed income. Private credit is a viable option for those looking for stability, downside protection, and predictable yield. The opportunity is particularly compelling given that banks are retrenching from lending activities at a time when interest rates are elevated, which has allowed private lenders to fill that financing gap left by traditional banks and originate loans at attractive risk-adjusted yields. Meanwhile, in a world where

inflation is higher than it has been for the past four decades and is set to remain elevated, real assets should play a critical role in protecting purchasing power. Specifically, farmland and the underlying produced agricultural commodities tend to generate value in real terms as prices rise, while infrastructure has the potential to yield predictable cash flows that are uncorrelated to the economic cycle with contracts that frequently include built-in protections against inflation. Meanwhile, real estate is often considered a good inflation hedge because it is a tangible asset whose replacement costs rise with inflation, benefiting from the appreciation in value. From a valuation perspective, the opportunity is particularly compelling given that the monetary tightening cycle has reached a peak and interest rates have begun to decline, setting the stage for a recovery in the coming years.

In addition to the attractive investment attributes above, their low correlation to traditional asset classes and their differentiated sensitivities to the economic cycle provide diversification benefits and a reduction of overall portfolio risk, underscoring the merits of allocating to non-traditional income and enhancing the risk-reward proposition in the portfolio setting.

### Portfolio Resiliency and Private Market Strategies



Private Market strategies continue to be instrumental in the construction of a resilient and well-diversified portfolio. Optimizing a portfolio to include private credit, real assets, and private equity may enhance both the performance and durability of a total portfolio, including maximizing the potential for an increase in its reward per unit of risk.

Source: Fiera Capital, for illustrative purposes only.

# Commodities and Currencies

## Currency Markets



The US dollar (-4.8%) retreated in the third quarter, driven by a profound pivot in the policy stance of the Federal Reserve that saw rate differentials move against the dollar. After spending much of 2024 firmly on hold, the Fed joined a host of global central banks in the easing cycle as the disinflationary impulse reasserted itself and prompted officials to reduce borrowing costs. The greenback was weaker versus all of its Group-of-10 trading peers, with the Canadian dollar (+1.2%), euro (+3.9%), pound (+5.8%), and yen (+12.0%) all strengthening over the last three months. Looking forward, the US dollar could come under further pressure as the Fed ramps up more aggressively into easing mode, while investor appetite for risk may dampen demand for the safe haven currency.

## Gold



Gold (+12.7%) hit a fresh high on the back of rate-cut optimism, robust central bank purchases, and lingering conflicts in the Middle East and Ukraine that have driven haven demand. Looking forward, gold prices should receive some support in an environment of lingering geopolitical tensions, while the path of least resistance for real interest rates remains lower and should increase the allure of the non-interest-bearing metal over the next 12-18 months.

Source: Bloomberg, as of September 30, 2024.

## Oil



Crude oil (-16.4%) posted a steep quarterly decline on expectations that OPEC+ will ease their voluntary supply curbs at the same time that output from outside of the cartel is increasing. An underwhelming economic backdrop in top importer China also weighed on the outlook for demand. We remain bullish on oil prices given favourable supply-demand dynamics. On the supply side, ongoing tensions in the Middle East (which accounts for about a third of global supplies) risks prompting an oil shock. On the demand side, China's slate of new monetary and fiscal stimulus measures aimed at buttressing the world's top consumer may also drive a resurgence in demand and help to reinvigorate prices in the coming year.

## Copper



Copper (+3.7%) notched a quarterly gain, rallying late in September after China's top leaders stepped up efforts to revive economic growth for the world's largest metals consumer. Looking forward, copper stands to benefit in the global effort to scale-up in green infrastructure spending. Renewable energy capacity expansion and a growing electric vehicle market underscores that healthy demand is expected to persist and buttress prices for the red metal.

# Forecasts for the Next 12-18 Months

| SCENARIOS                                   | SEPT 30,<br>2024 | SOFT<br>LANDING | INFLATION<br>REVIVAL | SHALLOW<br>RECESSION |
|---|------------------|-----------------|----------------------|----------------------|
| PROBABILITY                                 |                  | 55%             | 25%                  | 20%                  |
| <b>GDP GROWTH</b>                           |                  |                 |                      |                      |
| Global                                      | 3.00%            | 3.00%           | 4.00%                | 2.00%                |
| Canada                                      | 1.50%            | 1.50%           | 2.00%                | -1.00%               |
| U.S.  | 2.00%            | 2.00%           | 2.50%                | -0.50%               |
| U.S. Output Gap                             | 0.50%            | 0.50%           | 1.00%                | -1.50%               |
| <b>INFLATION (HEADLINE Y/Y)</b>             |                  |                 |                      |                      |
| Canada                                      | 2.00%            | 2.25%           | 3.00%                | 2.00%                |
| U.S.  | 2.50%            | 2.25%           | 3.00%                | 2.00%                |
| <b>SHORT-TERM RATES</b>                     |                  |                 |                      |                      |
| Bank of Canada                              | 4.25%            | 3.00%           | 3.50%                | 2.50%                |
| Federal Reserve                             | 5.00%            | 3.50%           | 4.00%                | 2.50%                |
| <b>10-YEAR RATES</b>                        |                  |                 |                      |                      |
| Canada Government                           | 2.96%            | 3.50%           | 4.50%                | 3.00%                |
| U.S. Government                             | 3.78%            | 4.00%           | 5.00%                | 3.50%                |
| <b>PROFIT ESTIMATES (12 MONTHS FORWARD)</b> |                  |                 |                      |                      |
| Canada                                      | 1622             | 1600            | 1500                 | 1400                 |
| U.S.  | 267              | 270             | 250                  | 215                  |
| EAFE  | 162              | 160             | 150                  | 135                  |
| EM  | 83               | 85              | 72                   | 65                   |
| <b>P/E (12 MONTHS FORWARD)</b>              |                  |                 |                      |                      |
| Canada                                      | 14.8X            | 16.0X           | 14.0X                | 13.0X                |
| U.S.  | 21.6X            | 22.5X           | 19.5X                | 17.5X                |
| EAFE  | 15.3X            | 16.0X           | 14.0X                | 13.0X                |
| EM  | 14.0X            | 15.0X           | 13.0X                | 12.0X                |
| <b>CURRENCIES</b>                           |                  |                 |                      |                      |
| CAD/USD                                     | 0.74             | 0.76            | 0.78                 | 0.70                 |
| EUR/USD                                     | 1.11             | 1.08            | 1.05                 | 1.00                 |
| <b>COMMODITIES</b>                          |                  |                 |                      |                      |
| Oil (WTI, USD/barrel)                       | 68.17            | 85.00           | 95.00                | 70.00                |
| Gold (USD/oz)                               | 2636.10          | 2400.00         | 2200.00              | 2500.00              |

Source: Fiera Capital, as of September 30, 2024.

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