NCM PENSION PORTFOLIOS MONTHLY UPDATE

Pension Style Investing for ALL CANADIANS

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For capital markets, the first month of 2022 was a rough ride. There were few places to hide across the spectrum of investment markets. Bonds continued to react negatively to higher inflation reports and the imminent central bank tightening. While we don't like the volatility and certainly don't like lower prices in our portfolios, we do feel that our tactical positioning has prepared us for the current market conditions.

The Road to Policy Change

A heavier tilt to shorter-dated and less interest-rate-sensitive fixed income has helped our relative performance as central banks finally begin their tightening cycle. The only questions now are if the first rate hike in the US will be 25bps or 50bps, and to what degree Canada will follow. The Canadian bond market unsurprisingly has already been anticipating the well telegraphed policy changes. For example, Canadian 10-year bond yields bottomed after the first wave of COVID in May of 2020 and have doubled to over 2% today. Since then, long provincial bonds (ETF: ZPL) have shown losses of over 8%, but a similar ETF tracking short-term provincial bonds (ETF: ZPS) is lower by only 1.5%. Higher interest rates are bad for all bonds, but short maturities clearly are impacted less. The Pension Portfolios' short-term fixed income is concentrated in the short-term provincials.

Canada Remains Key

Over the past year, we have repeatedly presented our opinions concerning Canadian stocks. Our central thesis is quite simple: we firmly believe that Canada enjoys a relative value advantage. This view has resulted in a significant tilt into our Canadian NCM Funds. This means that a quarter of our equity holdings are dedicated to Canadian companies. Relative to the average global balanced fund this is a significant tilt to our home equity market. While our reasons for owning more Canada have been based on valuation and growth, the advent of tensions in Eastern Europe has not hurt. Russia threatening on the Ukrainian border has supported both energy prices and gold, two significant, "made in Canada" sectors.

Asset Allocation

The table below shows how regional performance stacked up during January. The performance aligns well with our tactical positioning. Canadian indices performed the best, second was international indices that exclude North America, and in third place is the struggling US, defined by an S&P 500 ETF. Canada and Non-North American investments both figure prominently in the Pension Portfolios. Another interesting take-away from this table is the degree that higher dividend Canadian companies have performed. As measured by the Dividend Aristocrats ETF, high dividend payers avoided a negative month and turned in significant positive returns. Dividends are an important attribute among our NCM funds and are also an important attribute for the Pension Portfolios in general.

Performance January 2022

iShares S&P/TSX Canadian Dividend Aristocrats Index ETF	1.7%
iShares Core S&P/TSX Capped Composite Index ETF	-0.4
Vanguard FTSE Developed All Cap ex North America Index ETF (CAD-hedged)	-3.1
SPDR S&P 500 ETF Trust	-5.3

Source: S&P capital IQ

As we move through the first quarter of 2022, our asset mix in expected to remain relatively unchanged. Minor changes to move to less volatile and more defensive positions should be expected but the major regional equity allocations and our fixed income profile will be static. Importantly, neither the short position in fixed income nor our tilt to Canada is scheduled to see any changes for the foreseeable future.

Volatility Will Be Sticking Around

We have been anticipating significant central bank policy changes for quite a while and we are now on the cusp of less fiscal and monetary accommodation. No one can anticipate how capital markets will react in the near term. Heightened volatility in capital markets will almost certainly be a result. We have already seen the volatility spike and some of the daily swings in stock prices have been astonishing. The S&P 500 recorded the second largest point swing since 1967 last month. On January 24th the index traded lower by almost 5%, only to retrace this loss to close flat - a day trader's dream and a risk manager's nightmare.

We often guide investors to look to the longer term. We also think that investing in quality companies with great growth prospects is a good cushion in uncertain times. Volatility is no fun while it is happening, but it is fact of equity markets. We have also learned that reacting to capital market volatility is dangerous. In our opinion, the elevated volatility that comes with heightened uncertainty is simply a distracting nuisance.

We believe we are positioned defensively given the looming policy shifts, COVID irritations and now geopolitical tensions. At this point in the cycle, we hope that policy change comes sooner rather than later. We are also praying for negotiated resolutions in Europe and, finally, feel that post-COVID societal normalization cannot come too soon.

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