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Fall 2021

Hunter
Team

Stay Invested

As recovery continues from the COVID-19 pandemic in the first half of 2021, the economy has made significant progress and the equity markets have advanced remarkably higher.

The current investment environment presents many challenges. Investors are wary of potential reduced governmental support, a possible new wave of COVID infections, more aggressive regulatory and tax policies, along with many other worries.

We still view equities as more attractive long-term investments relative to fixed income. This is due to:

- An incredible amount of stimulus and government spending.
- Global central bank commitment to keeping interest rates low.
- A large amount of uninvested cash built up on the sidelines.
- Extremely strong earnings growth for publicly listed companies.
- Significant new investment in the technological infrastructure for a COVID and work at home economy.
- Lower inventories, underproduction of goods, and delayed capital investment during the last year-and-a-half has kept costs down and the prices for goods high.
- Greater online traffic and ecommerce.

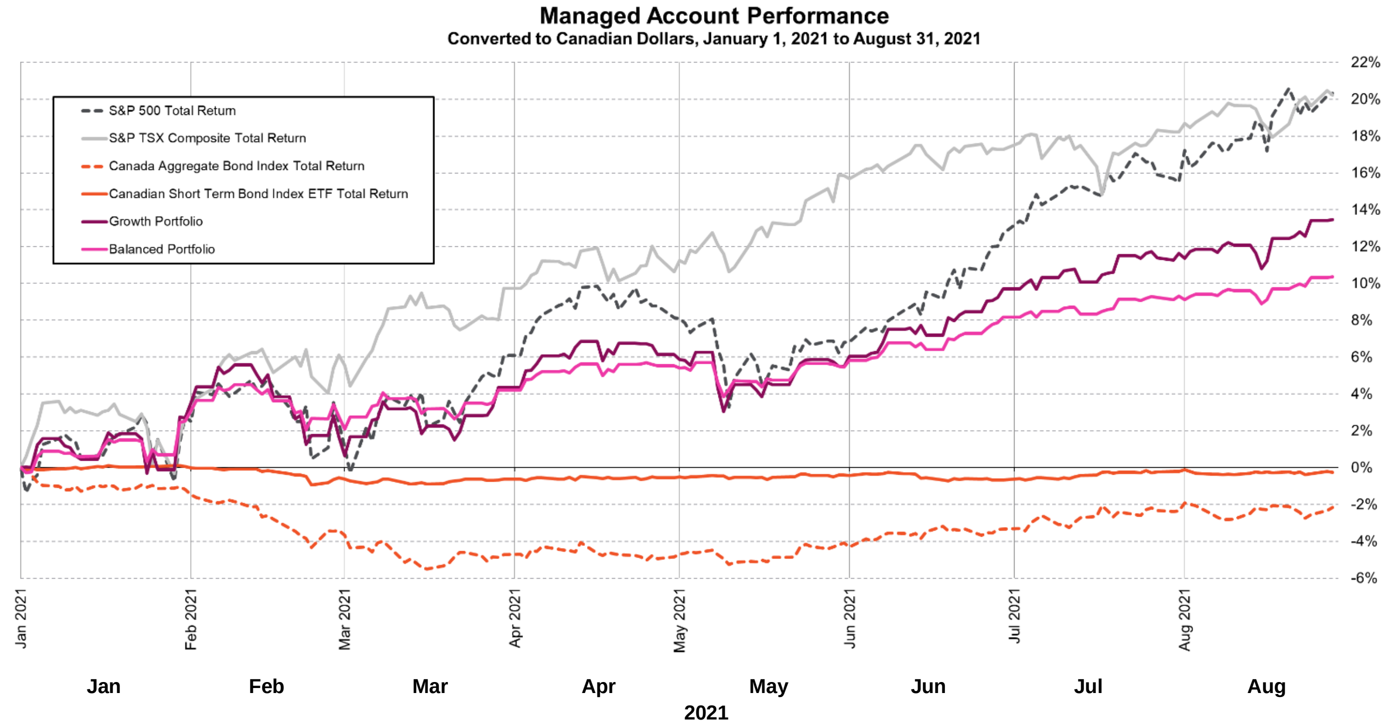
Our fixed income and alternative investment securities have performed very well over the past year, particularly when compared to negative returns from most fixed income year-to-date benchmarks. Our clients may consider more equity to take advantage of current levels of stimulus and avoid low government guaranteed rates. But this change increases risk and volatility. We are pleased that by providing the option to hold more creative fixed income and alternatives solutions to complement equity allocations, we can still achieve strong and consistent returns for our clients along with the option for more equity.

Our Investment Philosophy

We are long-term, goal-focused, planning-driven portfolio managers. We firmly believe in formulating an individual financial plan for each family, and to build investment strategies that focus on achieving goals set out in that personalized plan.

This newsletter provides an understanding of the building blocks we use in building solid, goals-based portfolios for our clients.

Managed Accounts



Source: Richardson Wealth Limited, net of fees, unaudited

Growth Portfolio is one specific growth-oriented managed account. The asset mix averaged approximately 77½% equity, 2½% fixed income, 17½% alternatives, and 2½% cash.

Balanced Portfolio is one specific balanced managed account. The asset mix averaged approximately 41% equity, 32% fixed income, 25% alternatives, and 2% cash.

Selected accounts are considered representative of growth and balanced portfolios across most managed client accounts. The level of cash varied throughout the quarter. Individual managed accounts vary in results due to customization. Deposits or withdrawals to portfolios, and the resulting implementation of changes in securities held represents the largest cause for differences in accounts. Client-directed and non-model securities held in managed accounts can also result in a significant performance difference from the average experience.

Most managed portfolios have already earned solid double-digit growth this year. Growth oriented portfolios have started to pick up a sizeable gain on top of more conservative or balanced mandates due to the strong performance of equity markets.

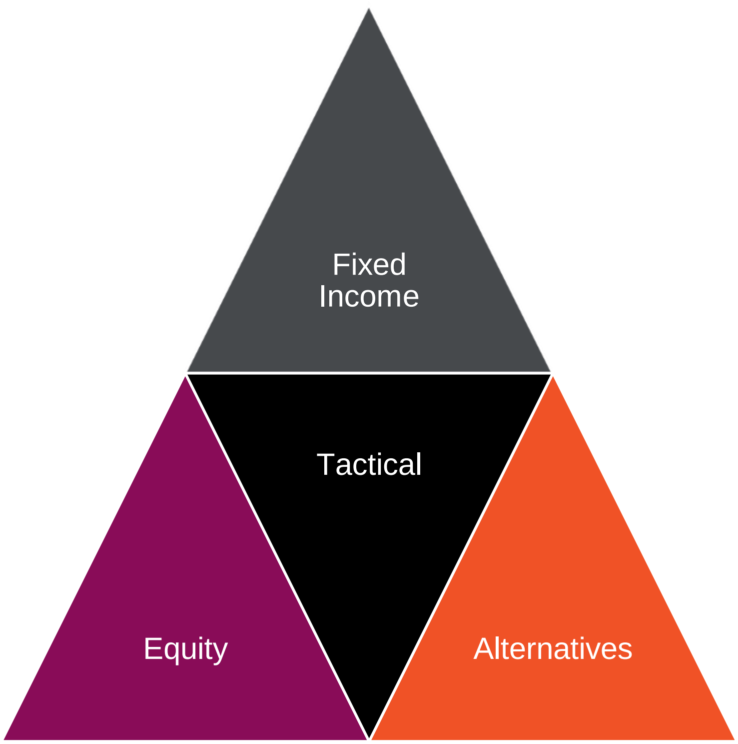
Both Canadian and US stock markets have provided incredibly strong results for equity investors. At the same time investing in bond averages has lost money. Even staying in very short-term bond issues provided returns less than break-even. After accounting for inflation and taxes, pursuing safety has been a losing strategy.

Fixed income and alternative investments in our managed portfolios have not suffered the fate of the negative bond benchmarks. Our managed portfolios hold higher yielding corporate bonds as well as private credit through alternatives as well as asset backed lending. Owning a creative suite of fixed income products with more aggressive credit lending than government-backed securities has allowed fixed income to provide a positive contribution. Alternative investments have also provided a great absolute return with results largely uncorrelated to what is happening in either the equity or fixed income markets

Owning more equity has been the obvious choice in 2021 to enhance performance. However, we are pleased to see that our fixed income and alternative allocations provided a reasonable result with much less risk and volatility. **This allows our clients to chose whether they would like the higher potential gains from moving more investments into equity, or retain allocations in fixed income and alternatives to pursue a more consistent result.**

Portfolio Design

The Building Blocks:



Fixed Income

- Stability and income
- Dependent on interest rates
- Increase during economic weakness/falling rates

Equity

- Tax effective growth and income
- Provides most return but highest variability
- Increase during economic strength

Alternatives

- Absolute return and reduced portfolio volatility
- Enhanced diversification, uncorrelated to economies and interest rates
- Often private, complex, unique, less liquidity

Tactical

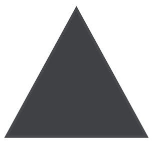
- Provides risk management through timing
- Favours cash during uncertainty and weakness
- Focuses on leadership sectors demonstrating outperformance

Money is fuel. It allows you to either do the things you want to do, or prevents you from doing them when you don't have enough.

Portfolio management involves matching your current investment strategy and future earnings to the things you want to spend on over your lifetime. A financial plan maps this out. It helps you confidently live your life, knowing you have planned out the "fuel" to do it.

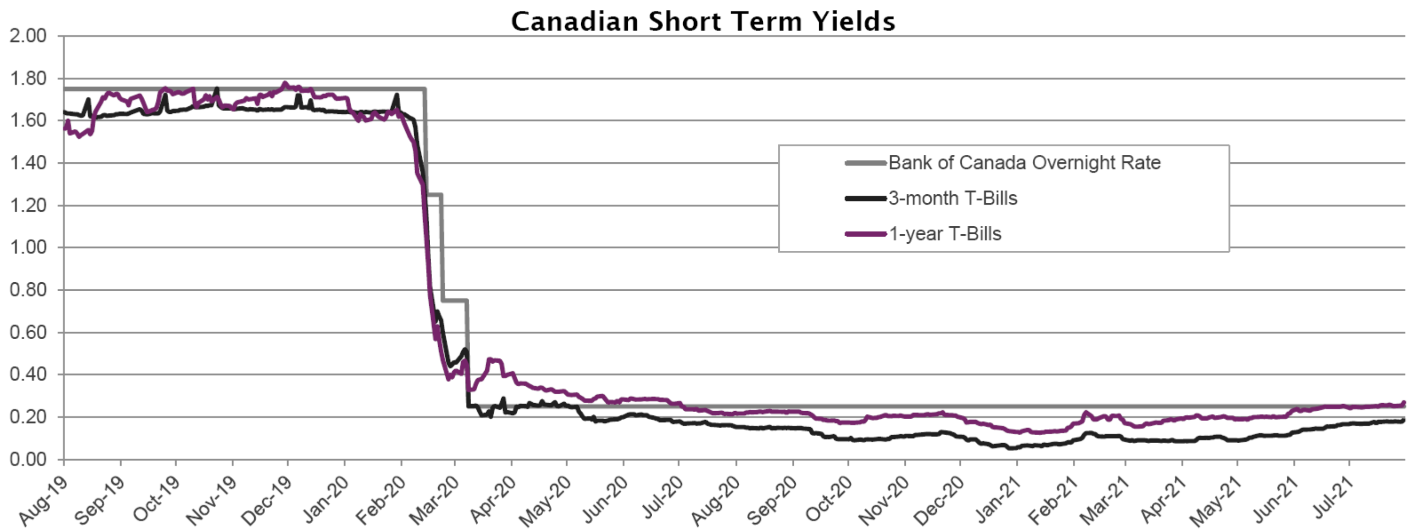
Building a portfolio isn't about knowing the future and somehow owning only the highest performing investment. It involves understanding the characteristics of each building block, and fitting them together in a way that achieves the growth rate, cash flow, and tax minimization needs, while reducing the effects of negative surprises and losses. It is balancing the need for growth and returns against the consistency of those returns and potential for loss.

A portfolio is well constructed when its owner is comfortable with amount of fluctuation in the portfolio (in particular the negative variances) *and* the longer-term rate of return meets the goals in the financial plan. Periods of market weakness are often the best test of whether asset mix is right. However, investor attitudes change over time. As we age, consistency, safety, and cash flow become more important. Changes in employment (particularly unemployment), moving, significant expenses, health changes, and retirement also affect attitudes about asset mix.



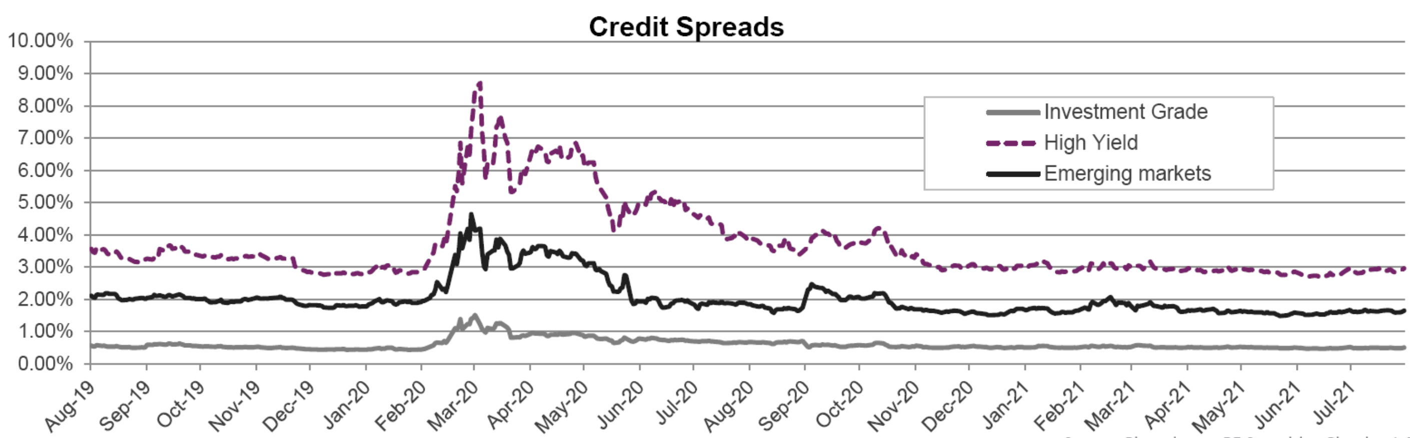
Fixed Income forms the starting point of portfolio construction. It represents lending money in return for interest and future principal repayment. It is the portion that is generally the safest, providing a base level of income and cash flow. This asset class has the least variability in results, but is dependent on global interest rates. Credit quality can vary significantly depending on the securities owned.

Providing a greater measure of predictability comes at the cost of a lower return. Governments and central banks have set interest rates at close to their lowest level in history. Stimulating the economy means making it painful to savers who want guarantees. After taxes and inflation, government and investment grade bonds guarantee a loss in purchasing power because the yields they offer are so low. Where these securities are marketable, they also risk short-term drops in their market value should rates rise going forward.



Source: Bloomberg

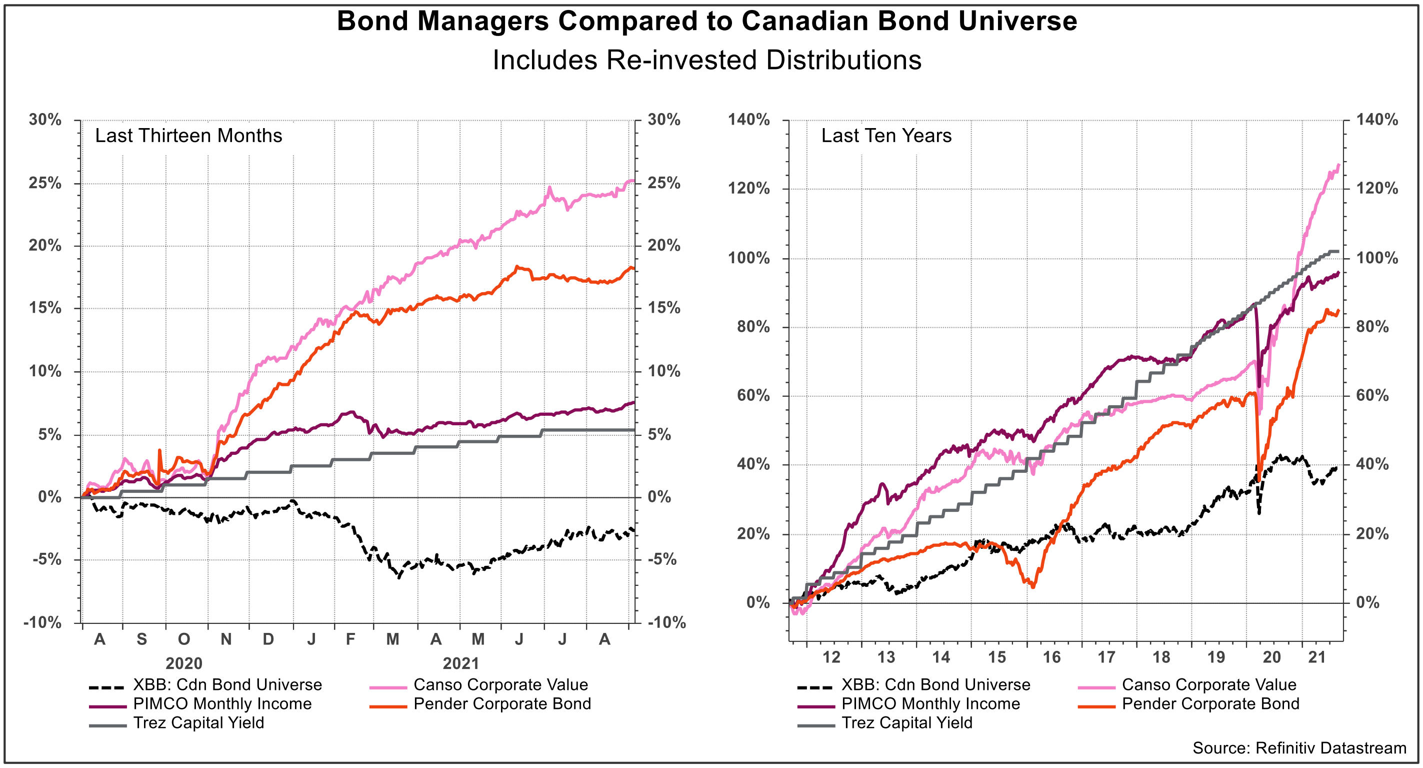
Increasing yields on fixed income products can be done by increasing the credit risk of the bonds, mortgages, or loans you hold. This means lending to companies rather than governments and possibly owning bonds or debt instruments of potentially riskier companies in order to pick up a higher yield.



Source: Bloomberg, RF Securities Clearing L.P.

A modestly higher yield can also be obtained by owning longer-term fixed income instruments. However, the longer the term, the greater a marketable bond's value will fluctuate in the near term. Where interest rates rise, existing low yield fixed income becomes less attractive, and the value of those fixed income holdings decreases.

We have been particularly pleased with how we've been able to achieve returns for fixed income investors over the last year. The below chart on the left shows how our core fixed income managers have posted fantastic results recently, in an environment where the broader bond index has lost money. The below chart on the rights confirms how these managers have consistently added significant value over the last ten years.



Our use of private lending, global lending, and other loan types through these mutual funds and private offering memorandum managers has offered a means of picking up yield. Each of these methods has unique risks related to their credit.

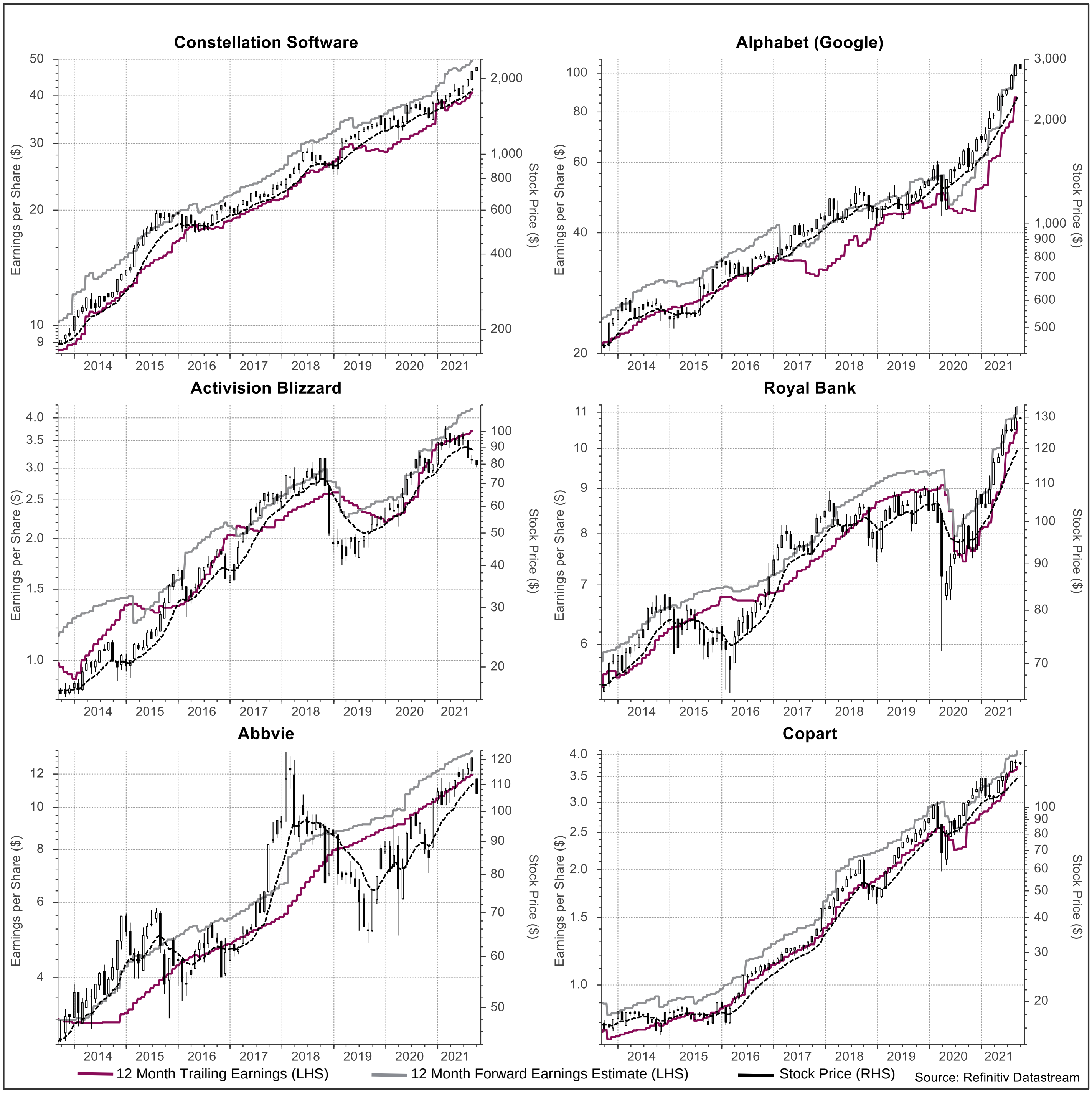
Equity allows participation in the ownership of a variety of businesses and growth in the economy. It is the primary source of making your capital grow. Many securities, particularly in Canada, also pay dividends that often exceed the yield received from fixed income in today's environment. Owning equity is one method of protecting against inflation on a tax-effective basis.

Our focus is to own companies with earnings. Currently, companies involved in technology, infrastructure, consumer communications, and financial services are where we see the strongest and most consistent earnings growth. The portfolio is active, and although individual companies owned are often hoped to be held for years, the proportion of each of them held can actively vary as news and results become available.

This asset class has the greatest return expectation. Each year there can be significant variability in results. Diversifying, having an active approach, owning mid- to larger-sized companies with significant and consistent earnings, and having a discipline for buying and selling can reduce overall variability and narrow the band of probable results.

We believe that as companies make money, they are worth more money. This concept has held true for our largest positions in client portfolios. Over the past eight years, these companies have consistently grown their earnings and their share prices followed. Highlighted below are six of our largest stock holdings, compared against their earnings.

The largest holding in our managed portfolios (as well as one of the longest held) is Constellation Software. It shows a nearly perfect correlation between earnings growth and stock price appreciation. Abbvie's stock price appreciation occasionally deviates from its earnings growth rate. Periods of overvaluation and undervaluation allow trading opportunities. Abbvie's long-term earnings growth is fairly consistent even if the stock's price hasn't been, which has ultimately lead to a higher stock price over time.



Alternative investments in our managed portfolios are divided into three broad groups:

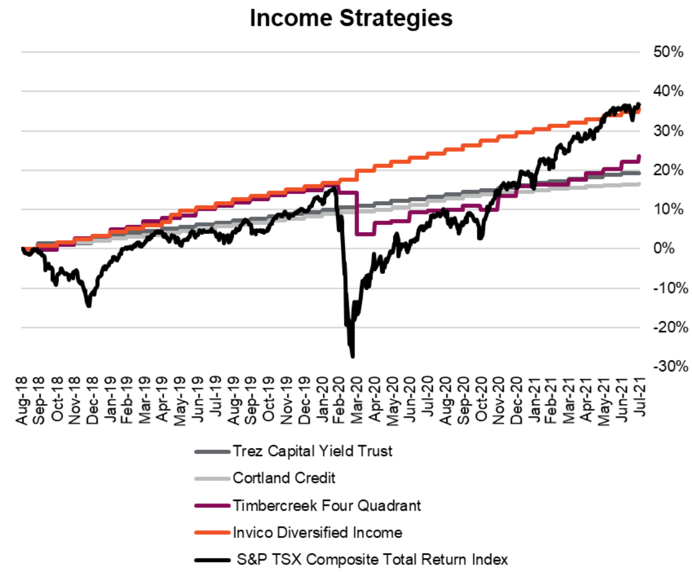
Income alternatives issue private credit or loans, lend against or manage real estate, or own receivables. Occasionally they will also have private equity ownership or royalty interests.

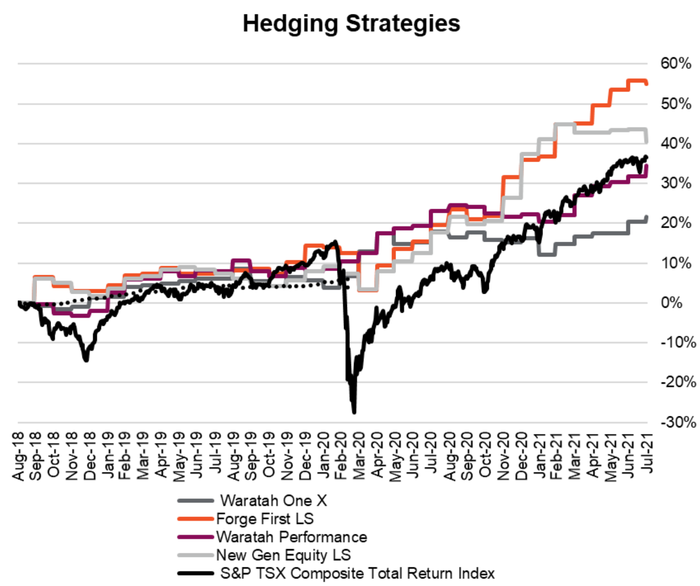
Hedge funds own stocks and other securities both long while holding others short. The intention of hedge funds we own is to reduce the market risk of holding stocks long only. Instead hedge funds make their money on the spread growing between the quality companies they own and the lower quality companies they think might fall or underperform which they short. The result for the funds we continue to hold is less variability, and significantly reduced correlation with the markets, yet with an overall return competitive with equities.

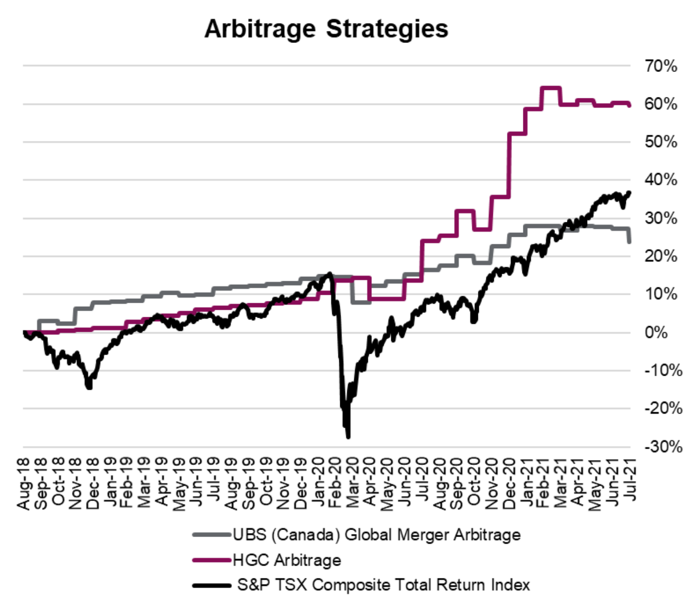
Arbitrage funds focus on takeovers and events where one security converts to something else at a set price, yet trades at a discount from that price. When a takeover is announced, for example, the acquired stock converts to the acquiror's stock (or to cash) at some defined rate in the future. Often the acquired stock will trade at a discount to that conversion rate, gradually approaching the set value as the deal date gets near. The risk is that the relationship breaks, such as a failed merger. For this reason, most arbitrage managers tend to have analysts and lawyers who assess the regulatory, governmental approval, financial and other risks of a deal going through. Holding several arbitrage securities in a portfolio produces a return stream that tends to be uncorrelated to most other securities and aims to provide a fairly robust absolute return.

Increasingly, we've suggested holding alternative investments in place of fixed income, particularly income focused alternative strategies. However, the private nature of some of these securities means that it can sometimes take weeks or months before cash is received as settlement from sell instructions.

Alternatives are a great building block to a portfolio, providing it with uncorrelated results to stock markets, greater consistency, and often good long-term returns.

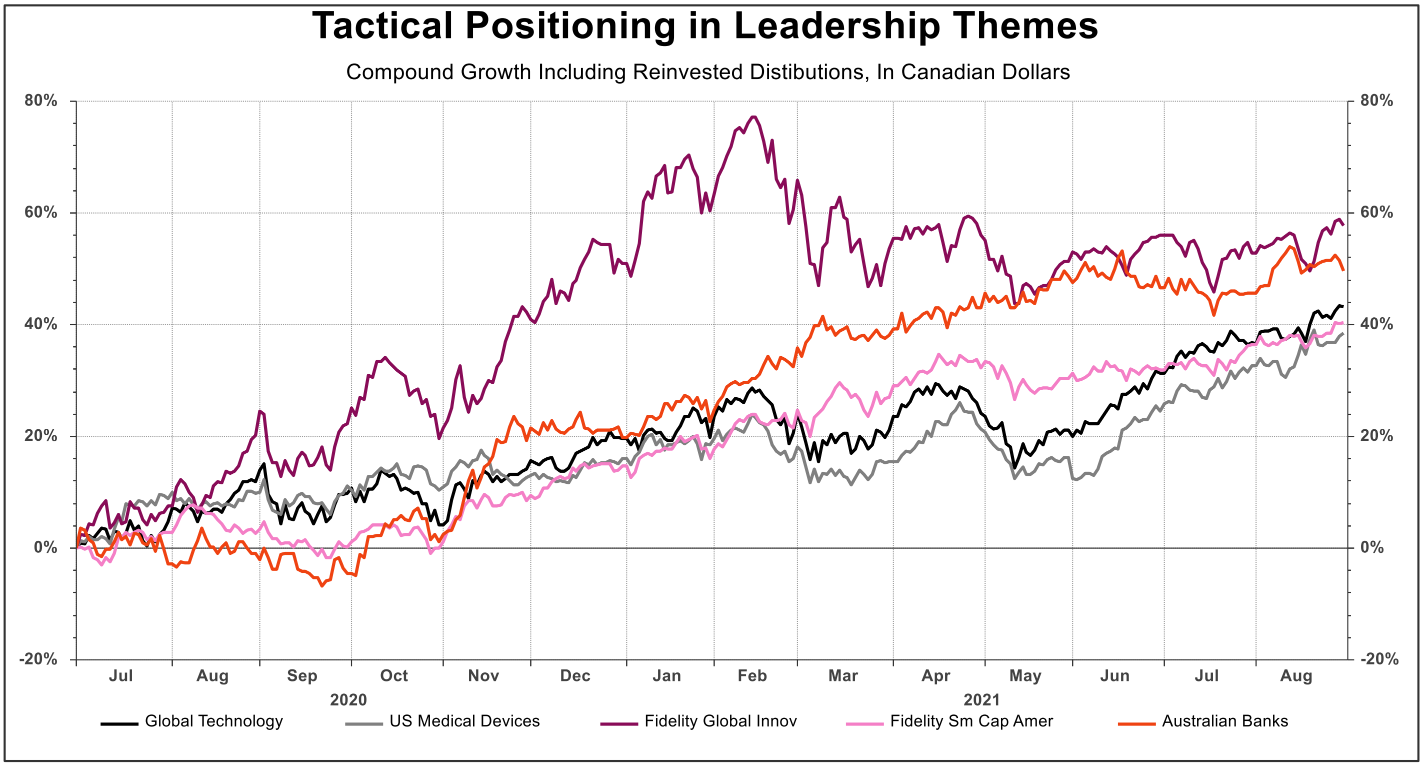






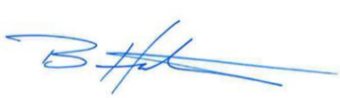
The Tactical portion of the portfolio may contain any of the other three asset groups as well as cash. It is the portion of the portfolio dedicated to timing and leadership.

Exchange traded funds are one of the primary instruments we use to capture market trends and timing. They offer liquidity in large baskets of themes that make it easy to enter and exit. Currently global technology, medical devices, small cap US companies, and several Australian banks are examples of equity trends owned in the tactical models. Fidelity's Global Innovators fund offers us a tactical manager who very actively rotates between industry sectors and individual stock names.



The most significant weighting in the tactical model is currently equity, composing around 65% of the tactical model. Another roughly 20% of the tactical model directs the current alternative investment holdings to be slightly larger than target levels. The final portion is currently in cash and a small amount of fixed income.

Regards,



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