A Smooth Start (For Now)

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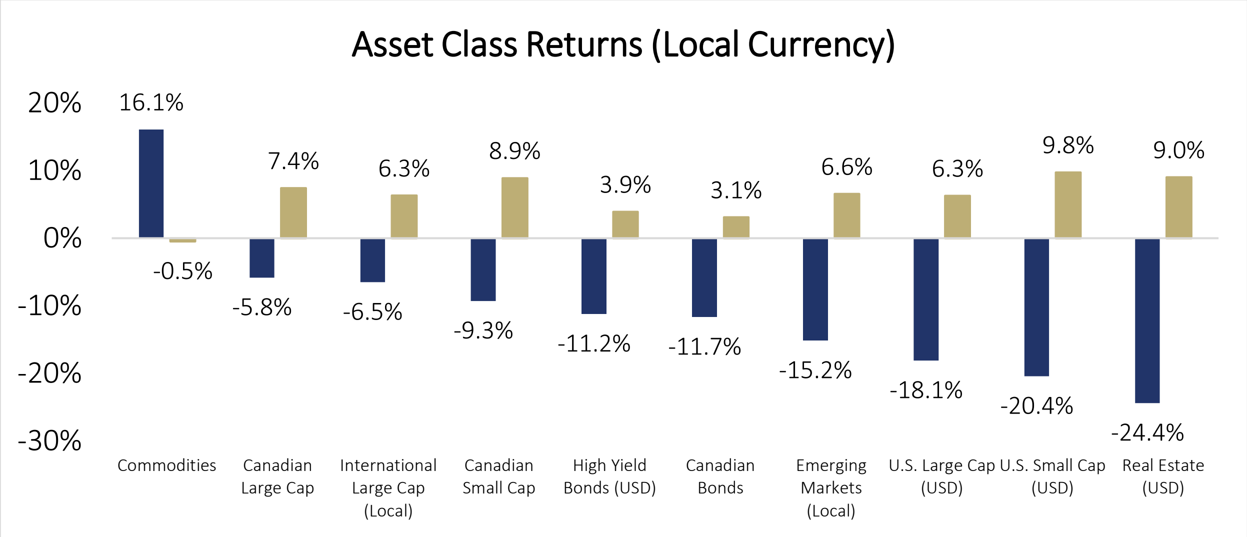
Investors' appetites have increased as we entered 2023. Generally, at asset class level, the larger the loss in 2022, the larger the gain (recovery) in 2023, though this is only the data for January (see chart below). We recognize investors are feeling reassured by progress on several issues: First, China exited their zero-COVID restrictive policy and is now fully reopened. Second, inflation is cooling and there is confidence it will gradually decline to 3% in 2023. As a result, central banks will at least pause hiking rates in the coming months. Third, the Russia/Ukraine situation, while unresolved, is also not getting worse. Last but not least, Europe was able to maintain healthy natural gas inventory as the winter was warmer than usual, hence lower drawdown.



Source: Morningstar Research Inc., Bloomberg Finance LP, as of January 31, 2023. Asset class returns are based on the following: Commodities: Bloomberg Commodities Index TR USD; U.S. Large Cap: S&P 500 TR USD, High Yield: ICE BofAML U.S. High Yield TR USD, U.S. Small Cap: Russell 2000 TR USD, Canadian Bonds: FTSE Canada Universe Bond, U.S. Bonds: Bloomberg US Aggregate Bond TR USD, Real Estate: FTSE EPRA NAREIT Developed TR USD, Intl Large Cap: MSCI EAFE GR LCL, Canadian Large Cap: S&P/TSX Composite TR, EM Equity: MSCI EM GR LCL, Canadian Small Cap: S&P/TSX Small Cap TR, Global Large Cap: MSCI World GR LCL.

The gains have been impressive considering the very short time frame. Our portfolios have had a similar experience: "recovery ratio" and performance were enhanced due to stronger performance in equity driven by an overweight allocation to China, small caps, and real estate. Hedging a portion of our USD exposure also added value. On the other hand, an overweight energy position was a detracting factor in January.

We do not expect the next 11 months to be as smooth as January. Some of the good news has been baked into asset prices, as we've seen from recent market rallies. We have made some adjustments including raising cash (which now has a yield of 4%), trimming bonds, and reducing Chinese and U.S. equity exposure. Cash will be re-deployed when opportunities arise, but must at least beat the 4% return hurdle. This means we will probably return to purchasing equity before bonds, bearing in mind a 10-year Canadian bond only yields 3.1% today (Feb 9, 2023).

1. Canadian Natural Resources Limited 2. Suncor Energy Inc. 3. Royal Bank of Canada 4. Toronto-Dominion Bank 5. Brookfield Corporation	6. Microsoft Corporation 7. Alphabet Inc. Class A 8. Alibaba Group Holding Ltd. 9. WSP Global Inc. 10. Enbridge Inc.	11. Prologis, Inc. 12. Amazon.com, Inc. 13. Element Fleet Management Corporation 14. Tencent Holdings Inc. 15. Canadian Pacific Railway Limited

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