SEI Investments Canada Company

Q1 2022

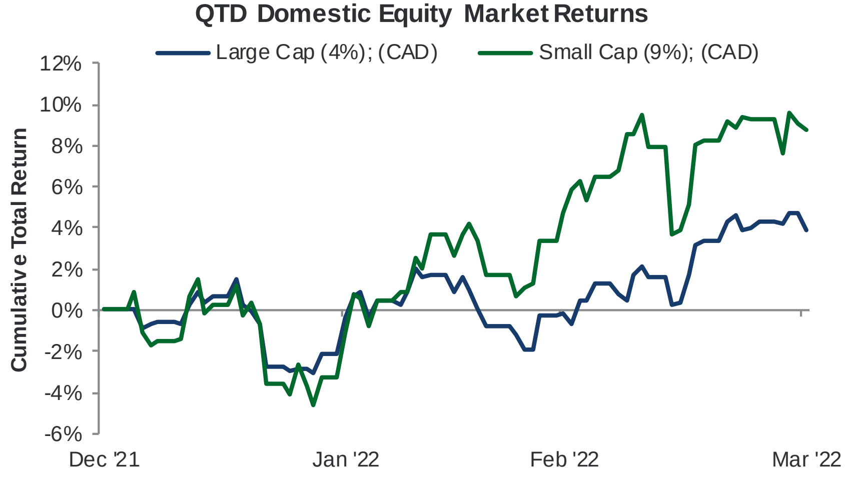
Market performance overview.

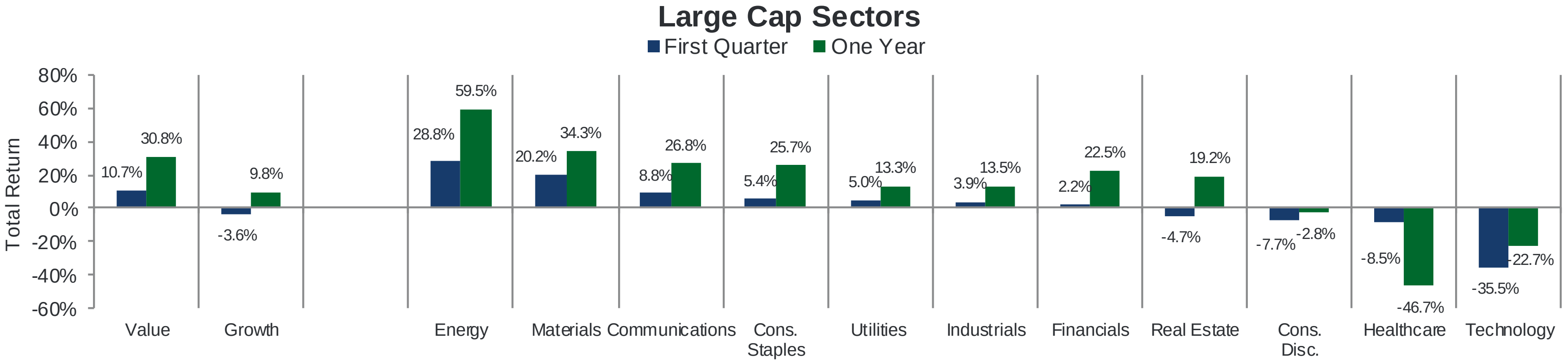
- It was a challenging quarter for most asset classes with the notable exceptions of domestic equities, thanks to a war-related spike in commodities prices that pushed energy and materials issues higher.
- Bond markets were hard-hit as persistent inflation pressures and firm central bank commitments to further monetary tightening pushed yields higher. The rapid global spread of the omicron variant in January, and Russia's invasion of Ukraine at the start of March, weighed on risk appetite and pushed inflation expectations even higher. As a result, three-month returns for many asset classes ended in the red and one-year returns were flat to negative outside of commodities, Canadian equities and US large caps.
- US high yield returns were negative for the quarter as spreads widened modestly. However, lower sensitivity to long-term interest rate changes provided some cushion relative to higher-quality debt over the quarter.
- Commodities returned to their winning ways after a lackluster fourth quarter, as Russia's invasion of Ukraine put renewed upward pressure on the prices of many raw materials.
- The Canadian dollar strengthened modestly on higher energy prices and a continuing trade surplus.

Canadian Dollar = CAD USD Exchange Rate, Commodities = Bloomberg Commodity Total Return Index (CAD), Canada Inflation Linked = FTSE Canada Real Return Bond Index (CAD), High Yield = ICE BofA US High Yield Constrained Index, 100% Hedged (CAD), Canada Long Duration Govt = FTSE Canada Long Term Government Bond Index (CAD), Canada Long Duration Overall = FTSE Canada Long Term Overall Bond Index (CAD), Canada Fixed Income = FTSE Canada Universe Bond Index (CAD), Emerging Markets Equity = MSCI Emerging Markets Index (Net) (CAD), International Equity = MSCI EAFE Index (Net) (CAD), U.S. Small Cap = Russell Custom 2500 Index (Net 15%) (CAD), U.S. Large Cap = Russell Custom 1000 Index (Net 15%) (CAD), Canada Small Cap = S&P/TSX Small Cap Index (CAD), Canada Equity = S&P/TSX Composite Index (CAD). Sources: SEI, index providers. Past performance is no guarantee of future results. As of 03/31/2022.

Canadian equity market review

- Both large and small caps were relatively subdued until March, when another move higher in commodities prices following the invasion of Ukraine gave a strong boost to the important energy and materials sectors.
- Relatively stable areas like staples and utilities performed well despite higher rates, while other rate-sensitive areas like technology, discretionary and real estate struggled. Cannabis names pulled healthcare lower.
- Within large caps, value outperformed growth by a wide margin thanks to outperformance of the energy and materials sectors and the steep decline in technology.

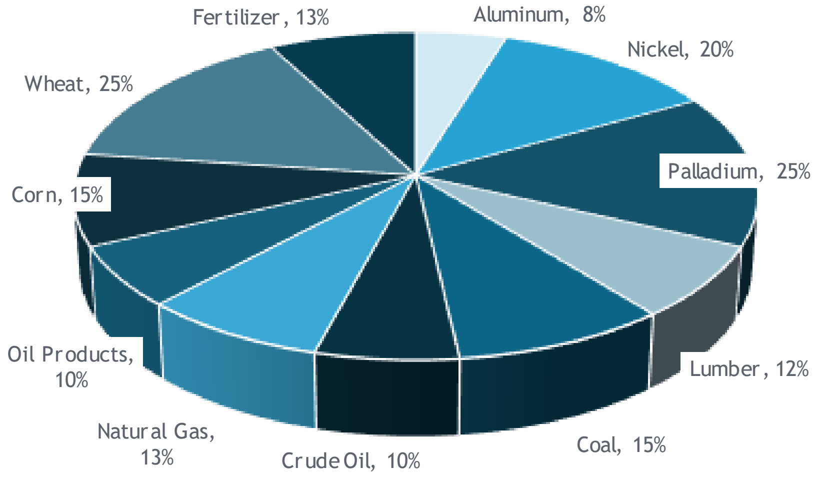


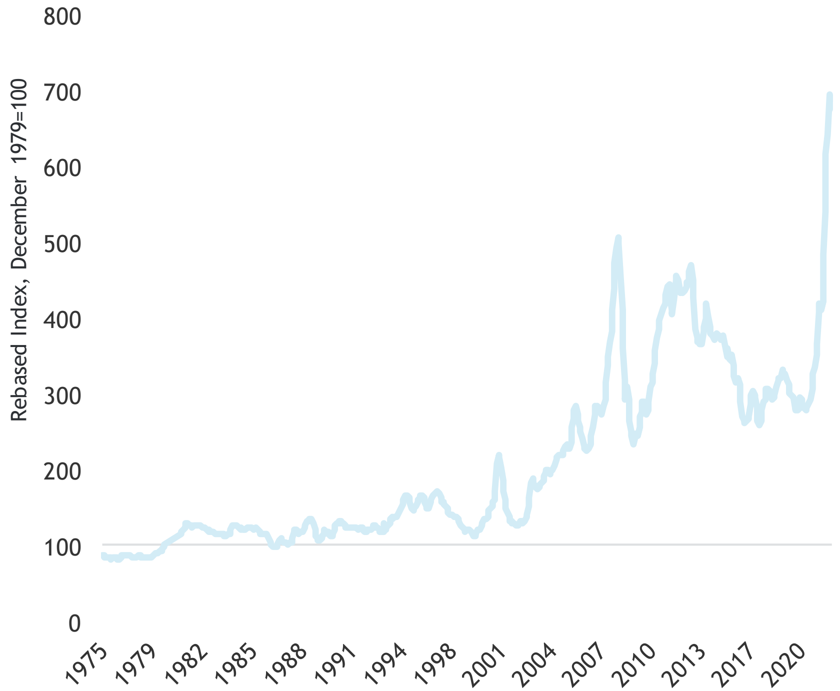


Sources: Factset, MSCI, Standard & Poor's. Large Cap = Canada S&P/TSX Composite, Small Cap = S&P/TSX Small Cap. Value and Growth represented by MSCI Canada Value Index and MSCI Canada Growth Index, respectively. Sectors represented by respective S&P/TSX Composite sector indexes. As of 3/31/2022. Past performance is not a guarantee of future results.

War, shortages, inversions - time to panic yet?

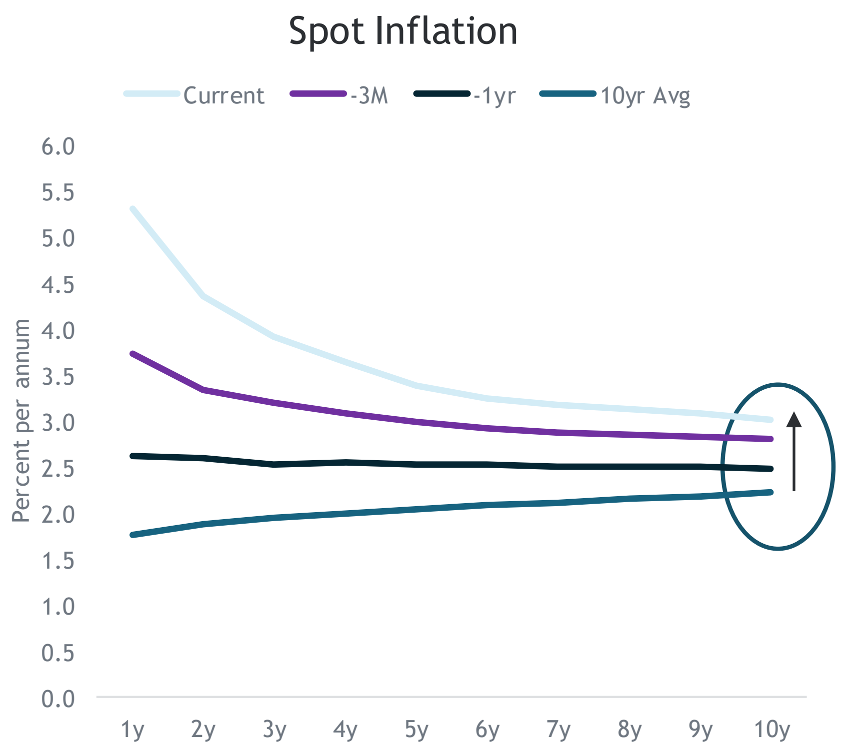
Ukraine: small demand impact, serious supply shock.

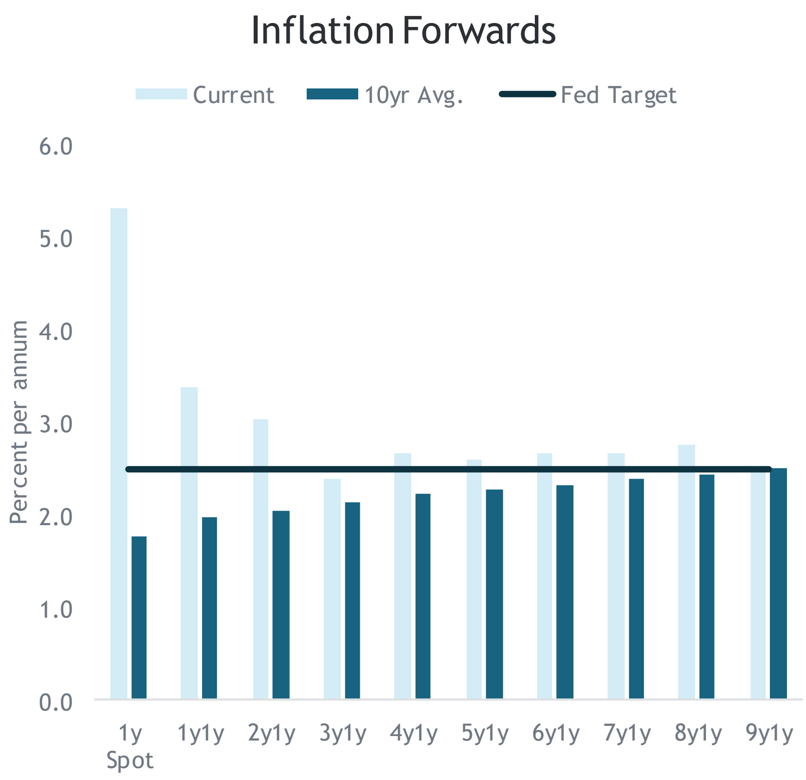




Left chart shows Russian and Ukrainian exports of selected commodities as percentages of world totals. Data as of 12/31/2021. Source: Capital Economics. Right chart shows US Producer Price Index for nitrogenous fertilizer manufacturing indexed to December 1979=100, monthly data from December 1975 through March 2022. Source: US Bureau of Labor Statistics.

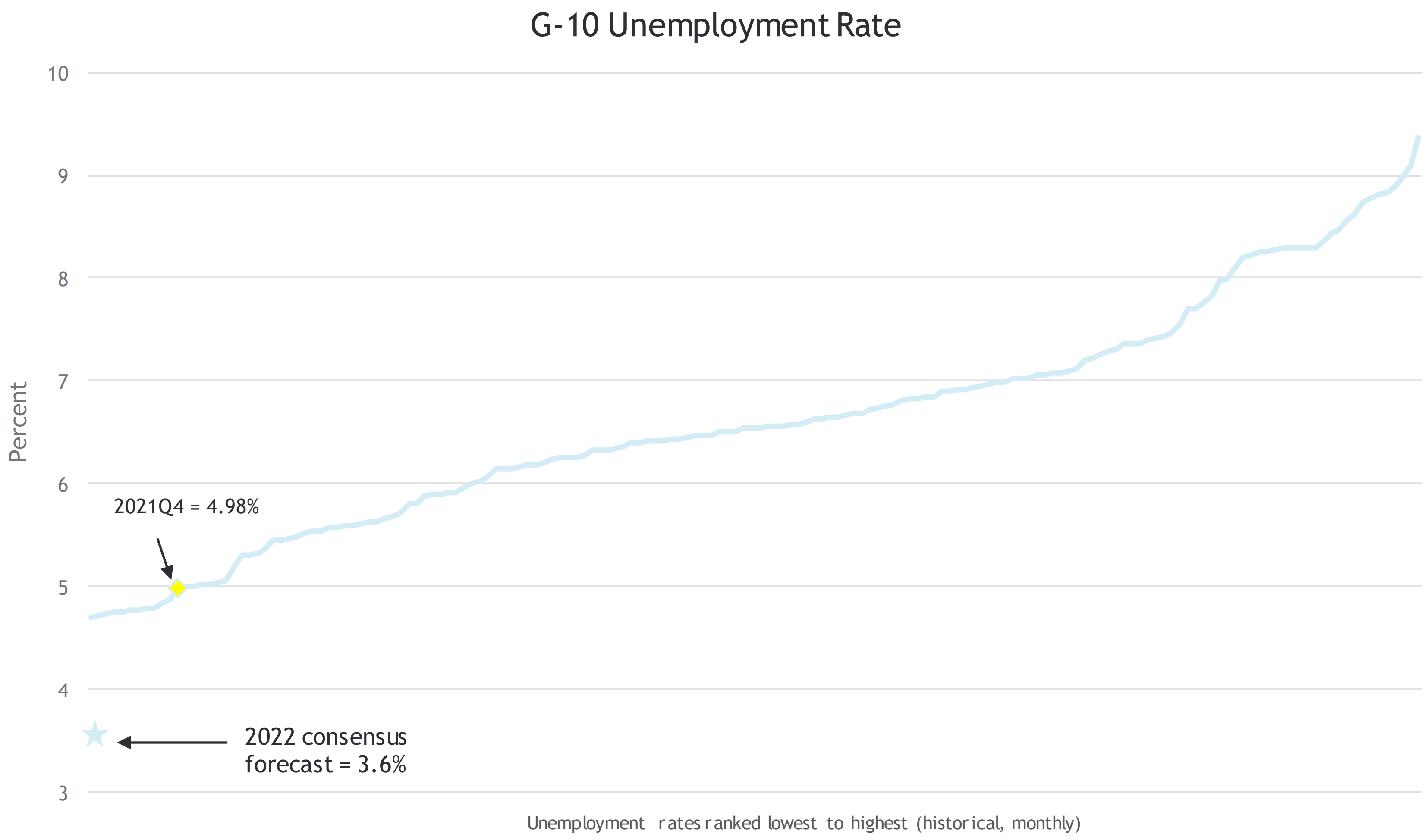
Markets have come around to the higher-inflation view.





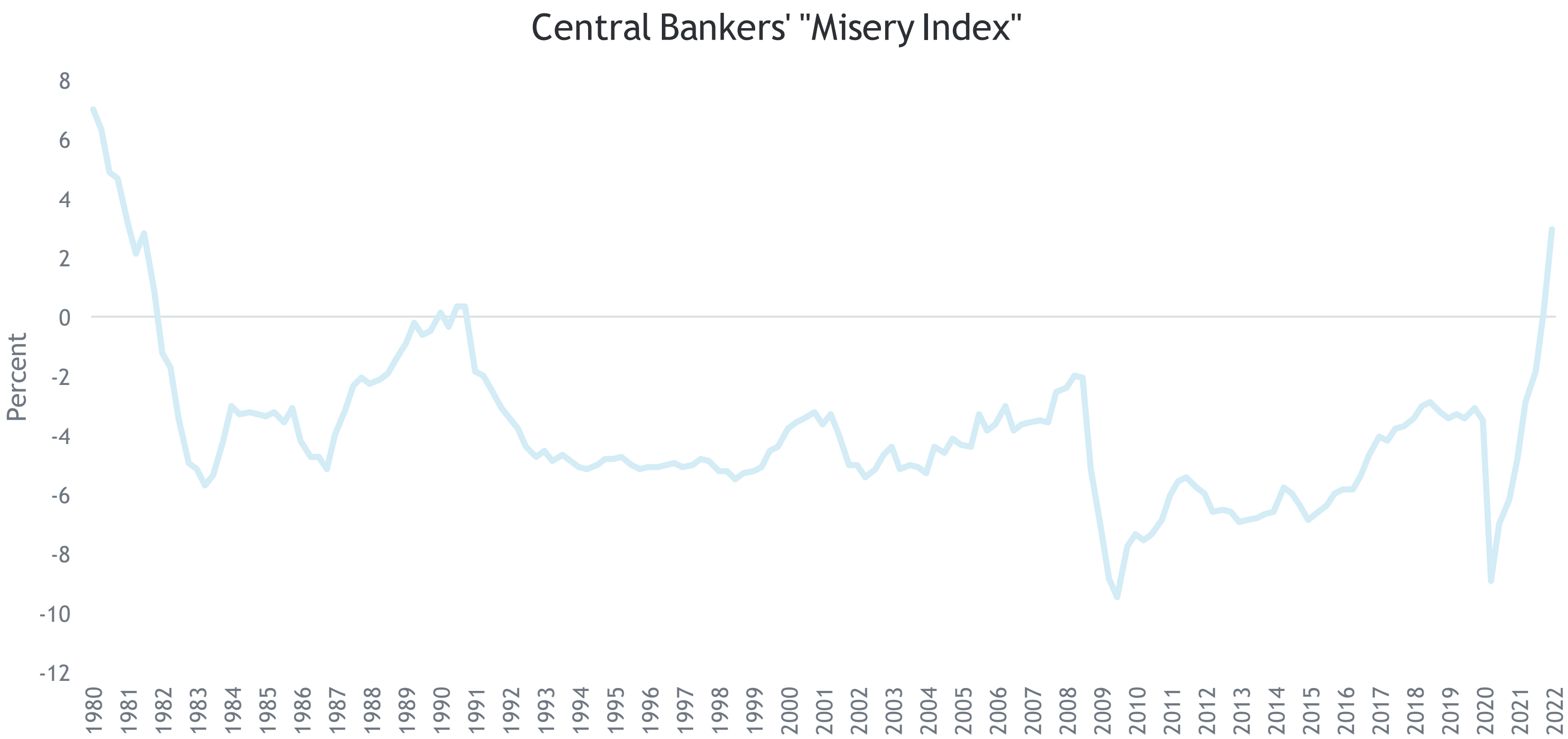
Left chart shows US inflation expectations reflected in zero-coupon inflation swap as of 3/31/2022, 12/31/2021, 3/31/2021 and the 10-year average as of 3/31/2022. Sources: Bloomberg, SEI. Right chart shows US one-year zero coupon inflation swaps of various tenors as of 3/31/2022. ‘1y spot’ represents the inflation rate expected over the next year, ‘1y1y’ - the inflation rate expected for the one-year period beginning one-year from today, ‘2y1y’ - the inflation rate expected for the two-year period (annualized) beginning one-year from today, and so on. Sources: Bloomberg, SEI.

However you measure it, labour markets are tight.



Historic monthly unemployment rates, ranked in ascending order, for the Group of Ten (G-10). G-10 constituents include the United States, Euro Area, Japan, United Kingdom, Canada, Australia, New Zealand, Switzerland, Denmark, Norway and Sweden, weighted by current prices GDP. 2022 consensus forecast as reported by Bloomberg. Quarterly data from 1980Q1 through 2021Q4 as at 19 April 2022. Sources: Bloomberg, SEI.

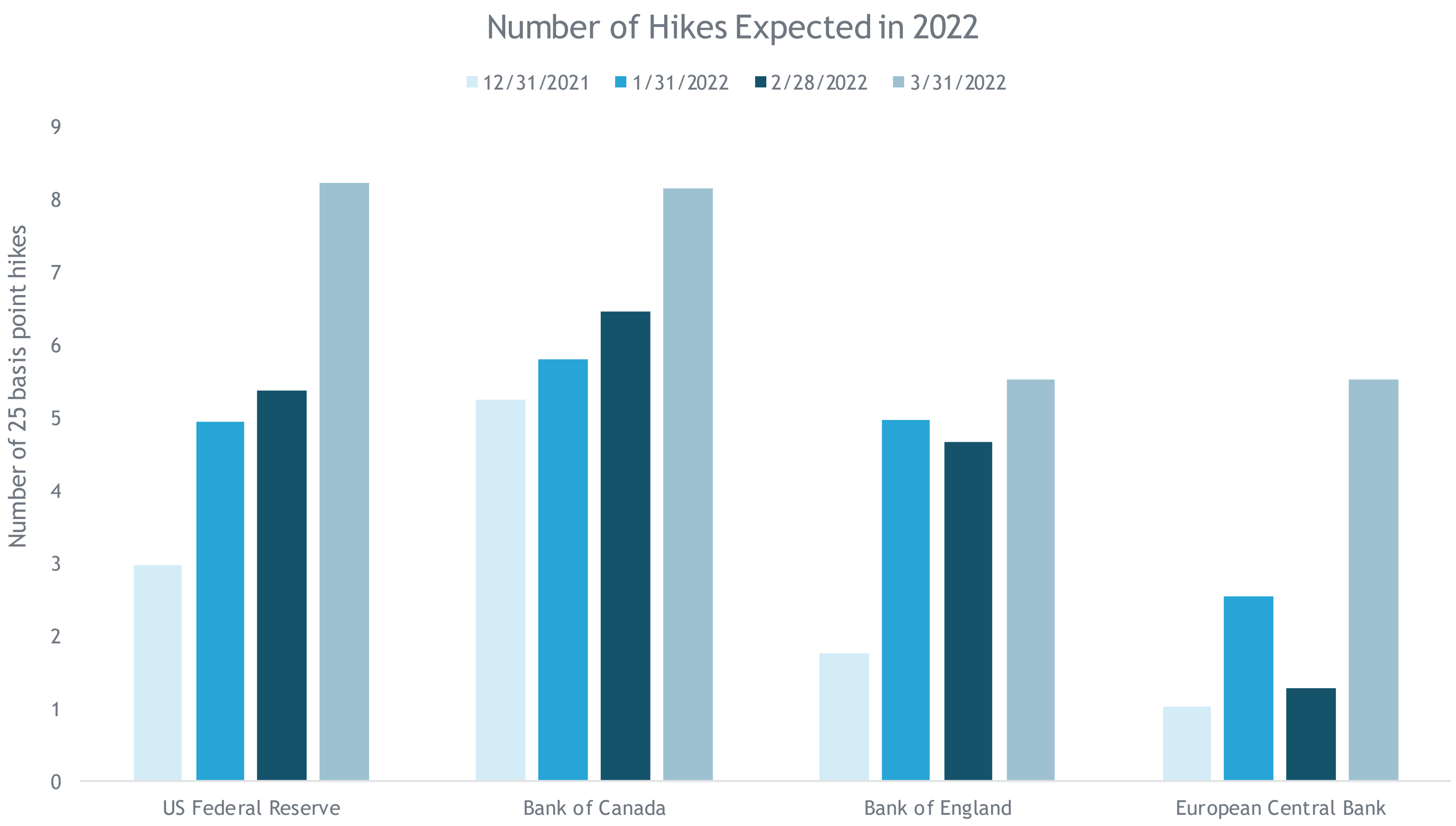
Central bankers find themselves in a difficult position.



- The traditional “misery index” adds the unemployment and inflation rates, providing a measure of consumer or household discomfort.
- *Subtracting* the unemployment rate from the inflation rate gives an indication of how uncomfortable central bankers might be.
- Given falling unemployment and rising inflation, this measure shows just how precarious a position central banks find themselves in.

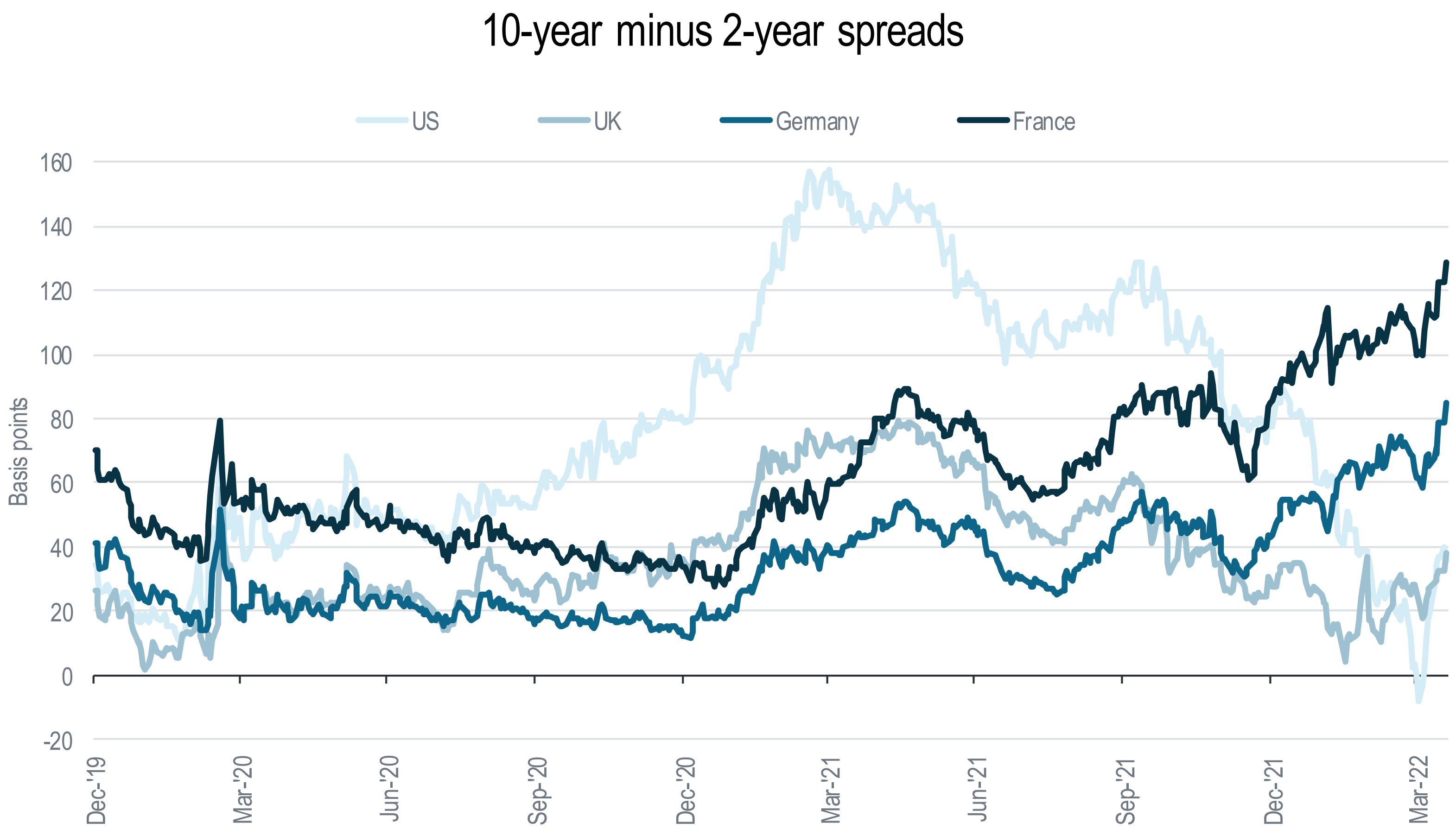
Group of Ten (G-10) unemployment and inflation rates measured quarterly from 3/31/1980 to 3/31/2022. Constituents include United States, Euro Area, Japan, United Kingdom, Canada, Australia, New Zealand, Switzerland, Denmark, Norway and Sweden, weighted by current prices GDP. Sources: Bloomberg, SEI.

High inflation, tight labour markets mean tightening ahead.



Expected number of 25 basis point rate hikes implied by interest rate forward curves for each country. Sources: Bloomberg, SEI.

Yield curves have responded in different ways.



Charts depict spread or difference between 10-year and two-year (10Y2Y). Daily data from 31/12/2019 through 4/12/2022. Source: Bloomberg.

Yield curves have responded in different ways.

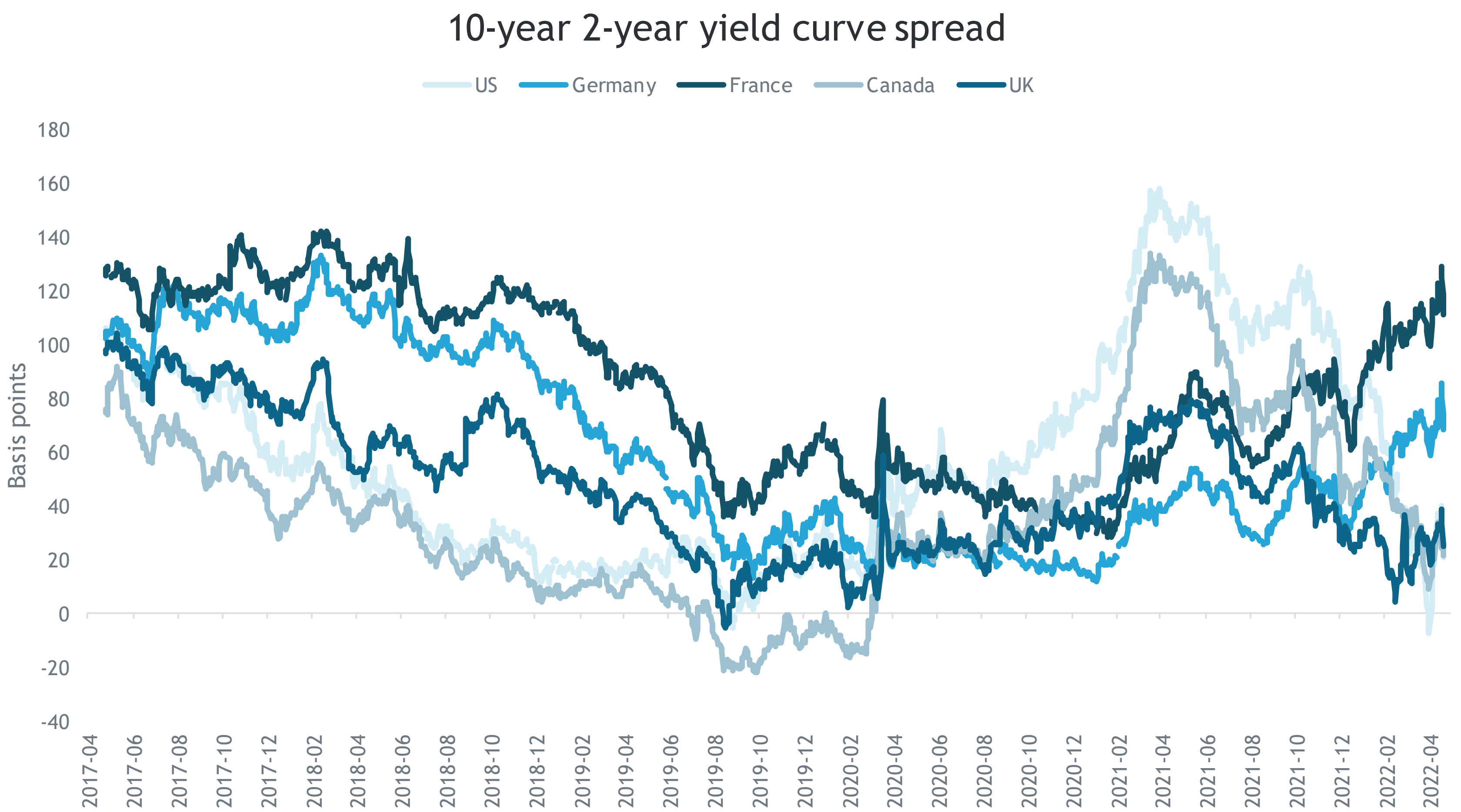
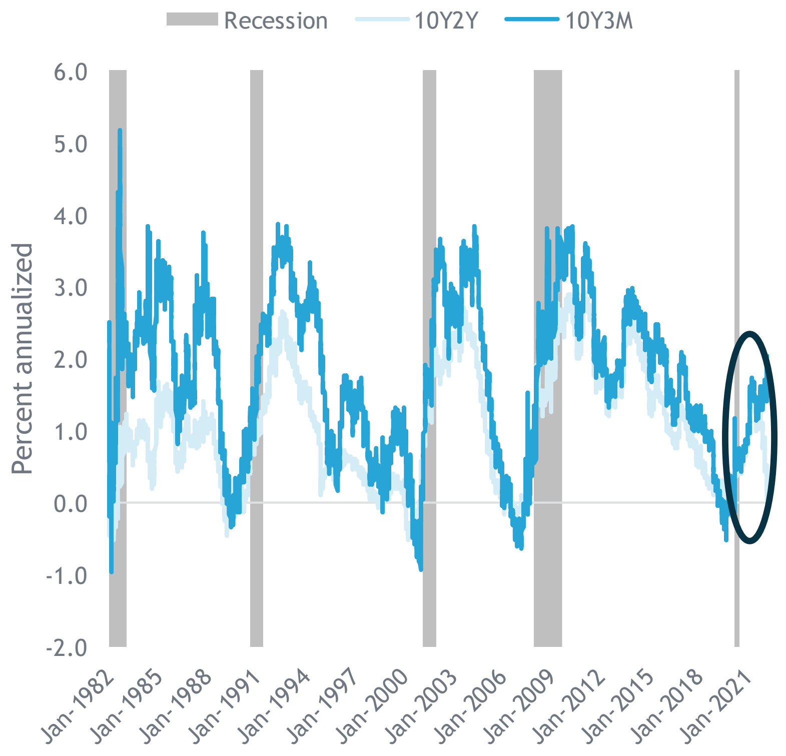
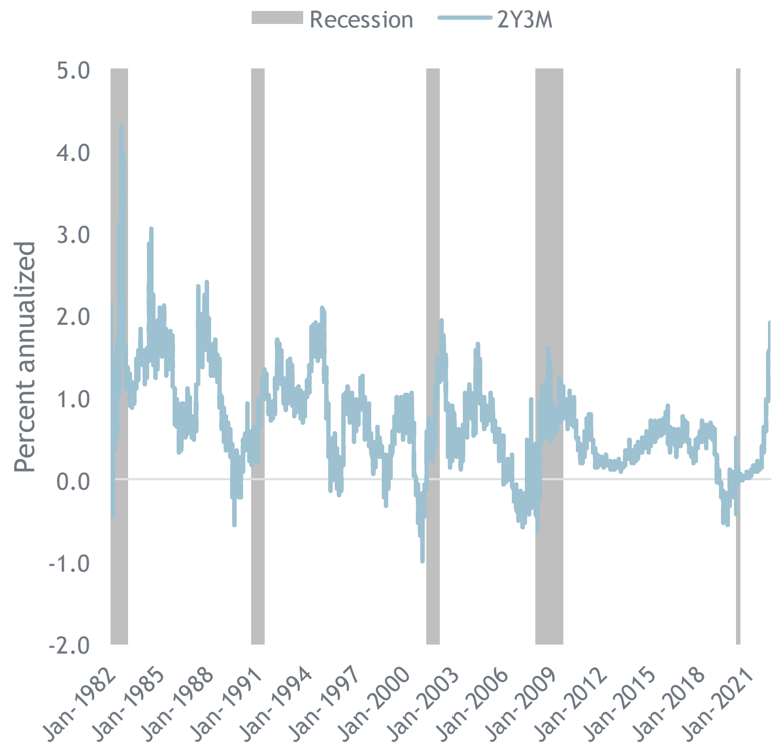


Chart shows difference between 10-year and two-year government bond yields for each country. Daily closing values from 24 April 2017 through 22 April 2022.
Source: Bloomberg.

Yield curves have responded…with an unusual divergence.





- Flattening and brief inversion of the 10-year, two-year yields spread has caused some observers to warn of recession or stagflation.
- However, the 10-year, three-month spread has been steepening, and the two-year, three-month spread has widened dramatically.
- All else equal, that spread will flatten or invert if the Fed tightens sufficiently – at that point the recession signal will be stronger.

Charts depict spread or difference between 10-year and two-year (10Y2Y), 10-year and three-month (10Y3M) and two-year and three-month constant maturity Treasurys. Grey bars indicate recession periods. Daily data from 1/4/1982 through 4/12/2022. Sources: Board of Governors of the Federal Reserve System, Federal Reserve of St. Louis, NBER.

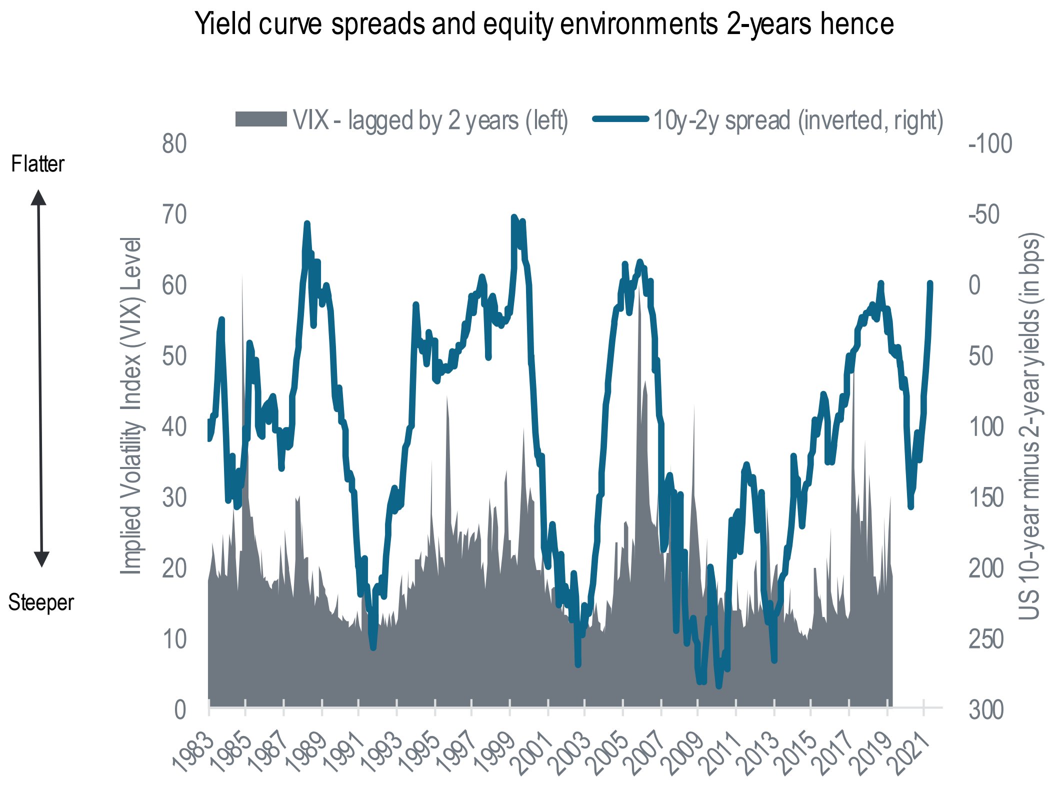
Time to recession varies substantially.

Date of inversion		Preceded recession?		Months until recession	
10y-2y	10y-3m	10y-2y	10y-3m	10y-2y	10y-3m
12/'56	no inversion	✓	no inversion	8	n/a
09/'59	no inversion	✓	no inversion	7	n/a
12/'65	01/'66	✓	✓	48	47
03/'73	06/'73	✓	✓	8	5
08/'78	11/'78	✓	✓	17	14
09/'80	10/'80	✓	✓	10	9
12/'88	05/'89	✓	✓	19	14
05/'98	07/'00	✓	✓	34	8
12/'05	08/'06	✓	✓	24	16
08/'19	05/'19	✓	✓	6	9
			Average:	18 months	15 months
			Range:	**6 to 48 months**	**5 to 47 months**

'10y-2y': yield on US Treasury Securities at 10-year constant maturity minus yield on US Treasury Securities at 2-year constant maturity from 6/1/1976 to 3/31/2022; prior to 6/1/1976, yield on US Treasury Securities at 10-year constant maturity minus yield on US Treasury Securities at 1-year constant maturity. '10y-3m': yield on US Treasury Securities at 10-year constant maturity minus 3-month Treasury Bill rate. Prior to 4/1/1962, frequency of data used in determining dates of inversion was based on averages of business days, monthly; daily data used thereafter. Source: Federal Reserve Bank of St. Louis, NBER, SEI.

Inversion adds to uncertainty, but not a market-timing tool.

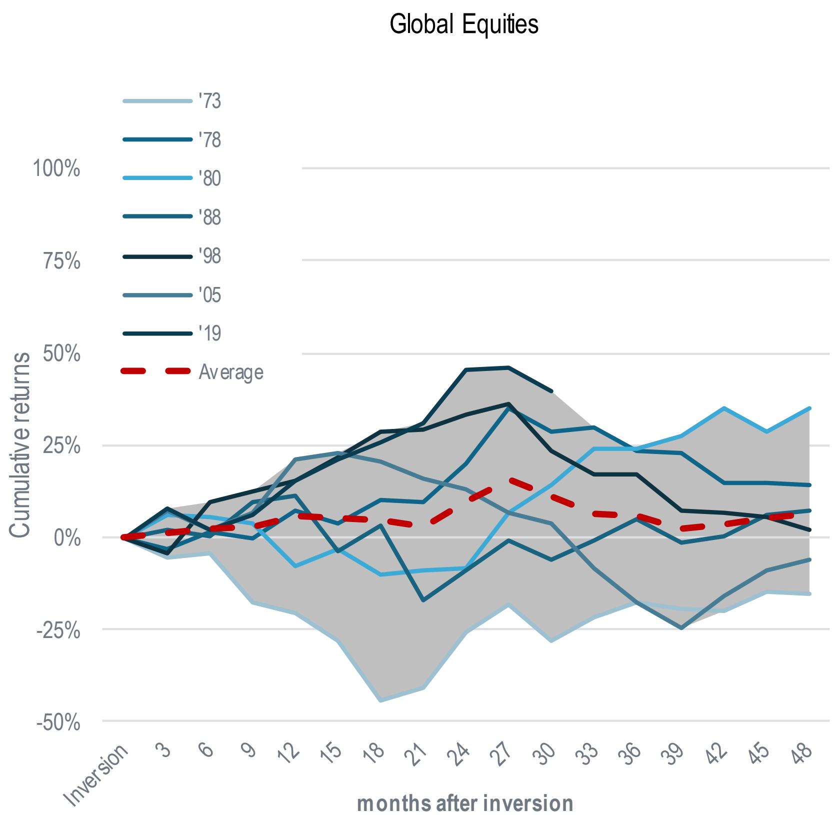
When 10y-2y spread is...	# of occurrences (monthly, since 1983)	VIX (average level), 2-years post-inversion
Negative	30	29
0 to 50 bps	108	24
50 to 100 bps	67	20
100 to 150 bps	70	17
150 to 200 bps	54	15
200+ bps	84	16

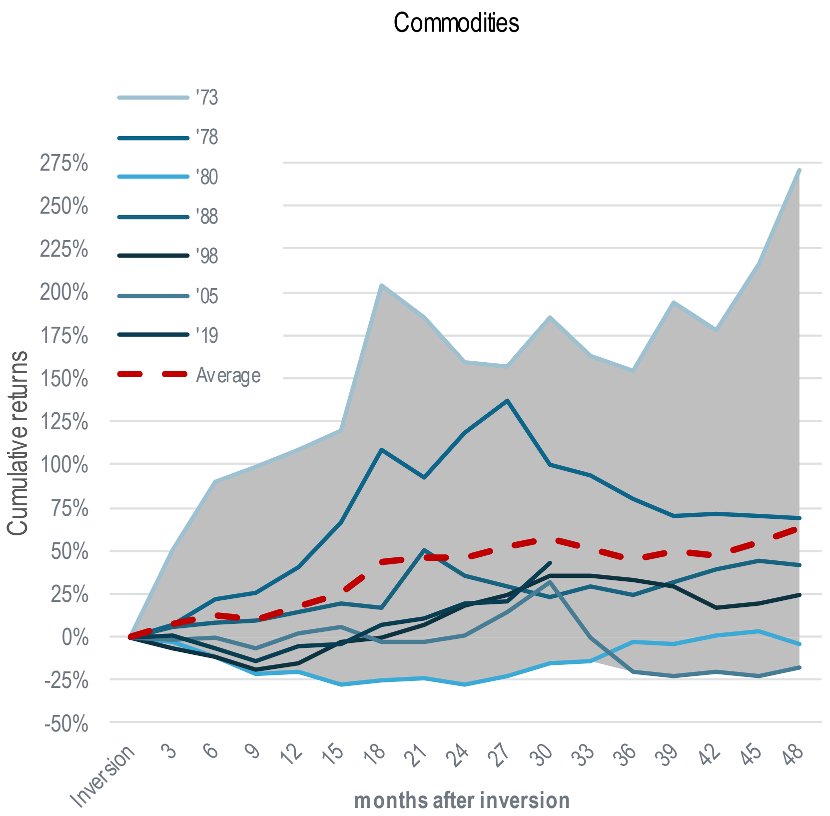


Source: Federal Reserve Bank of St. Louis, CBOE. VIX: CBOE Volatility Index (VIX) from 1/1/1990 to 3/31/2022 and CBOE S&P 100Volatility Index (VXO) from 1/1/1986 to 12/31/1989. VIX levels were lagged by two years. ‘10y-2y’: yield on US Treasury Securities at 10-year constant maturity minus yield on US Treasury Securities at 2-year constant maturity from 1/31/1984 to 3/31/2022; data is inverted. Monthly data. Past results are not indicative of future results.

Curve inversion hasn't been a death knell for risk assets.

Cumulative returns after inversion



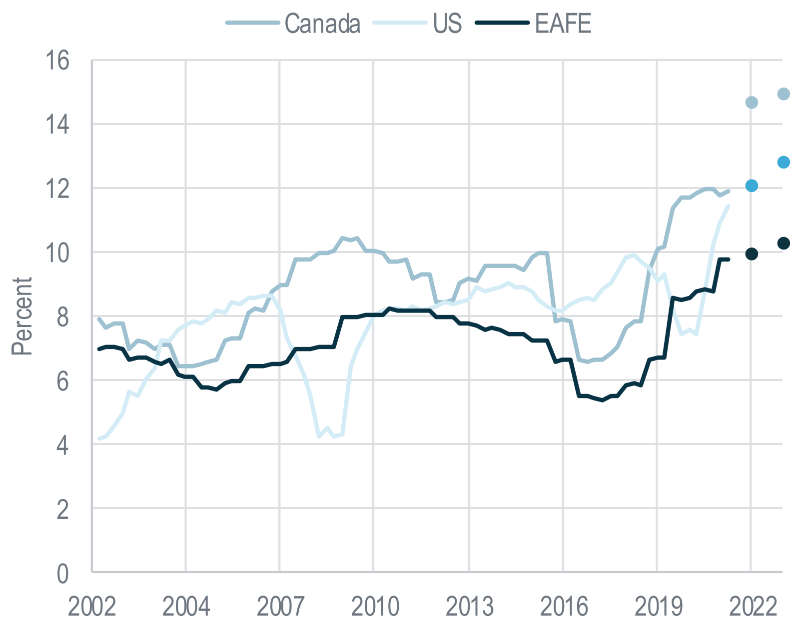


Source: Bloomberg, MSCI, S&P. Shaded areas represent maximum and minimum cumulative results at each three-month interval. 'Global Equities': MSCI World Index Total Return - Net (CAD). 'Commodities': Bloomberg Commodity Total Return Index (CAD). Index returns are for illustrative purposes only and do not represent actual investment performance. Index returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index. Past performance is not a guarantee of future results.

Believe it or not, there are still reasons for optimism.

- Strong balance sheets outside central governments:
  - Businesses
  - Households
  - State & local governments
- Corporate profit margins and earnings remain solid.
- Mobility and related measures continue to improve.
- Pent-up demand for travel, dining, services, etc.
- Labour markets remain very healthy.
- Financial conditions remain easy.
- Recession probability models remain well-behaved.
- Significant planned investment:
  - Military expenditures
  - Infrastructure, including supply chains
  - Residential real estate
  - Continued pandemic support

Healthy corporate profit margins are expected to remain strong



Canada: S&P/TSX Composite, US: Russell 3000 Index, EAFE: MSCI EAFE Index. Quarterly data from 3/31/2001 to 12/31/2021. Dots are forward estimates provided by FactSet for calendar years 2022, 2023, and 2024 as of 4/13/2022. Source: FactSet, MSCI, Russell, S&P.

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