CHARTBOOK

Market Comment

Prepared by Ocean Front Wealth Management

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OCEANFRONT WEALTH MANAGEMENT

iA Private Wealth™

Portfolio Managers

Scott Keast, B.Comm, CIM®, CFP®

Shane McMahon, CIM®, CFP®

Matthew Cameron, CFA®, CIM®

Head of Senior Private Client Relations

Bruce Lindsay, CFP®, CH.F.C.®, CLU®

Investment Advisors

Brendan Leathem, CFP®, CLU®

Adam Carris, CIM®, CFP®

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Market Comment

North American markets were down in January, as the TSX fell 0.6% and the S&P500 fell 1.1%. We saw a unique scenario where the news was dominated by Reddit message board groups battling hedge funds to drive up the price of heavily sold short stocks like GameStop and AMC Entertainment. During the month, GameStop's price rose from around $20 in mid-January to an astonishing high of **$483**. Other than being an interesting story, it seems unlikely this has any broader implications for markets other than perhaps being a sign of some speculative sentiment.

A story that we expect to become more and more important this year, and next year, is inflation. The pandemic has had numerous effects on society, many of which could align to create a scenario where we see significantly higher than average inflation. This would have significant effects on asset prices and investment portfolios for which it is prudent to prepare.

Source: Ocean Front Wealth Management, Yahoo Finance, stockcharts.com

“Are we in a bubble?”

Past performance does not guarantee future results.

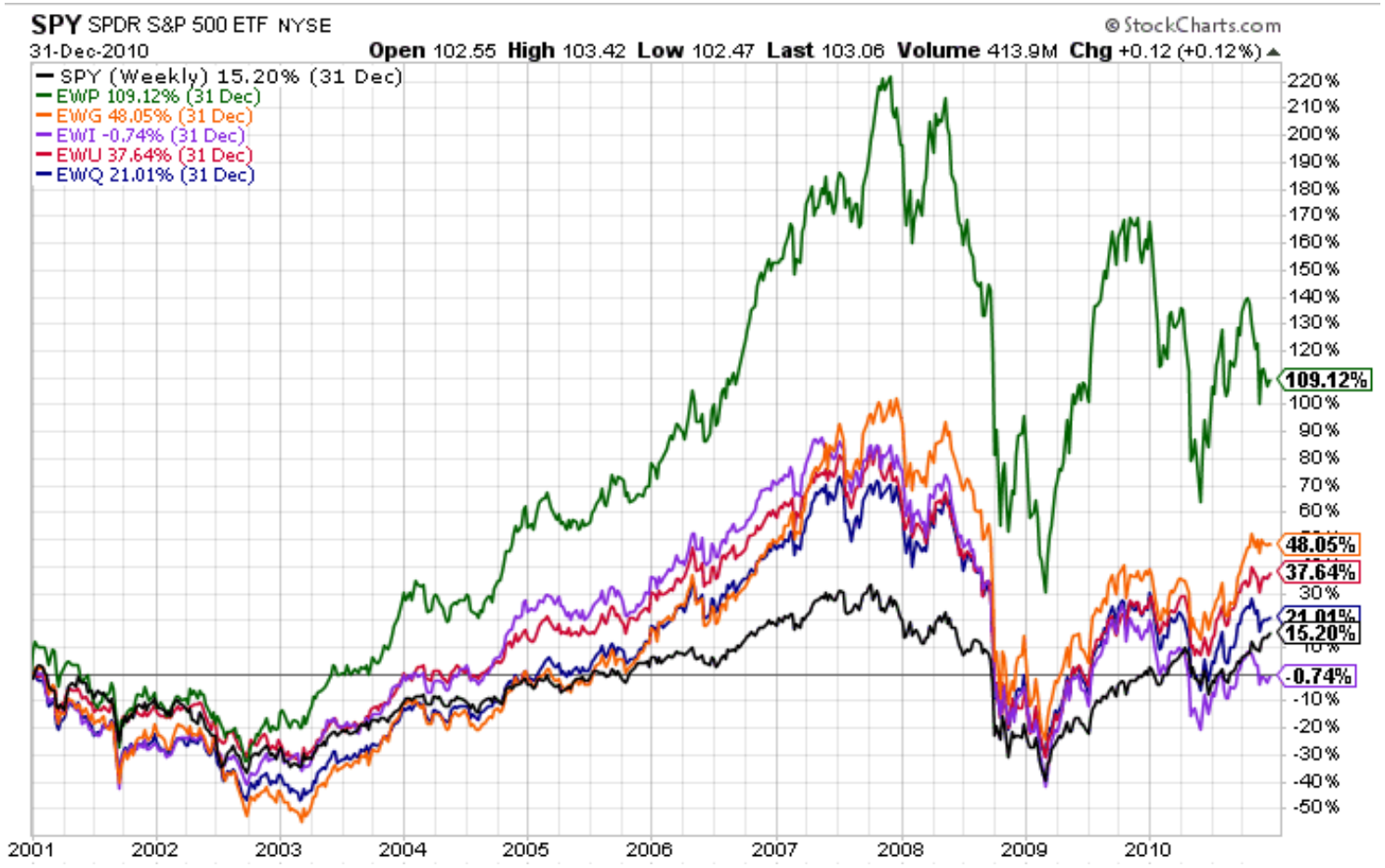
If you watch financial news you may hear this type of discussion often; *Are we in a bubble? Is a crash coming?*

What tends to be overlooked in this type of comment is that it is most often directed at the US market. As you can see on the chart of the MSCI regional ETF returns from 2011-2020, the US has dramatically out-performed these European markets over this period. Investors in the iShares MSCI Spain ETF would likely not consider it to be in a bubble, having earned a cumulative return of 4% over ten years.

This isn’t a call on whether the US or any other market is in a bubble or not, it’s just a reminder of what has happened around the globe in the past decade.

Source: Ritholtz Wealth Management, awealthofcommonsense.com, ycharts.com, Ocean Front Wealth Management

2001-2010 Returns



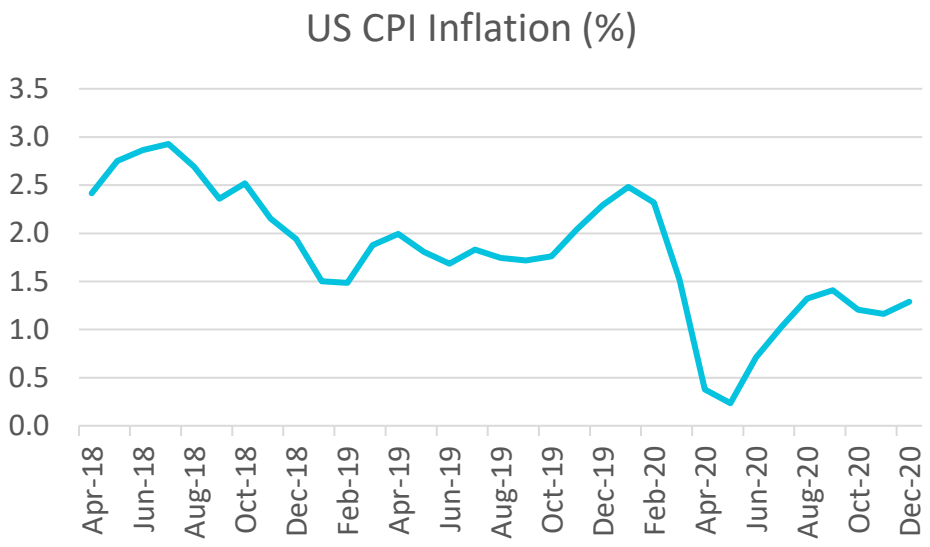
Past performance does not guarantee future results.

This is a chart of the same ETFs shown on page 5. This chart shows their returns from 2001-2010 instead of 2011-2020. It was the MSCI Spain ETF with the best return (109% cumulative), while the US S&P500 ETF (15% cumulative, the black line) was only better than the Italian ETF.

It can be difficult to predict what will happen over the next decade, which is a good example of why diversification can be valuable. Investors do not want to find themselves overexposed to one geographical area when it under-performs, nor do they want to miss out on the out-performers. Having a globally diversified portfolio can help prevent both of those problems.

Source: stockcharts.com, Ocean Front Wealth Management

Higher Inflation on the Horizon?



Past performance does not guarantee future results.

After the initial COVID shock in Q1 of 2020, inflation has been on the rise. Some of the key factors that may affect inflation are:

1. Monetary policy
   - Money printing is inflationary
   - Low interest rates are inflationary
2. Fiscal policy: higher government spending is inflationary
3. Velocity of money *(how quickly money changes hands through spending)*
4. Supply and demand effects *(ex. a decrease in demand for certain goods due to lockdowns was deflationary)*

It is expected that most, if not all, of the above factors either currently are, or are likely to soon be inflationary, which should push inflation higher in the coming years.

Source: US Federal Reserve Bank of St. Louis, Ocean Front Wealth Management

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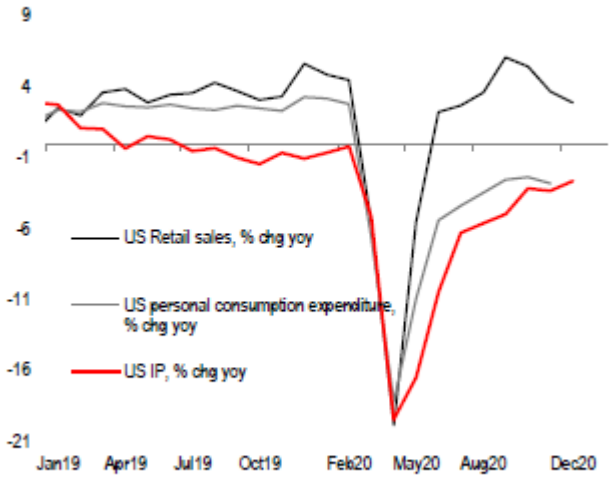
The Case for Inflation

Figure 2: Goods consumption has held up much better than production, potentially creating supply shortages

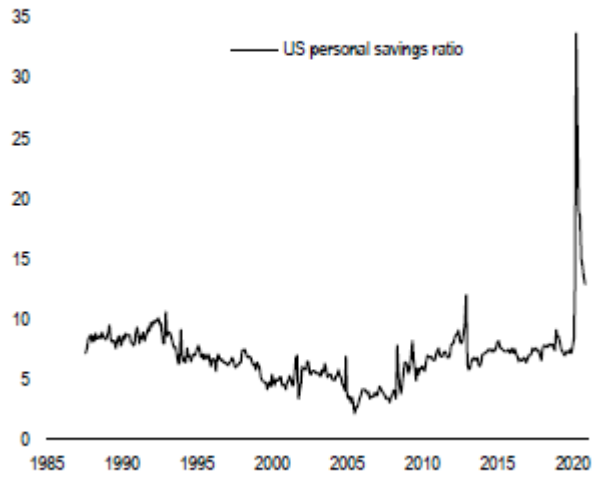


Source: Refinitiv, Credit Suisse research

Figure 23: M2 growth is at record levels and loan growth has held up, this is in sharp contrast to the GFC

Source: Refinitiv, Credit Suisse research

Figure 20: The savings ratio is likely to fall...



Source: Refinitiv, Credit Suisse research

The first chart above on the left shows a potential supply and demand imbalance, as production has lagged consumption and retail sales. This can potentially create a supply shortage which could push prices higher. Money supply growth (M2) has been huge, as seen in the second chart. In the third chart, we see the US personal savings rate spiked in early 2020 *(due in part to lockdowns)* and has since decreased. Are you planning any trips or expenditures for after the pandemic? We expect there is pent-up demand from delayed purchases which could cause a spending boom post-pandemic. That would be highly inflationary.

Past performance does not guarantee future results.

Source: Refinitiv, Credit Suisse, Ocean Front Wealth Management

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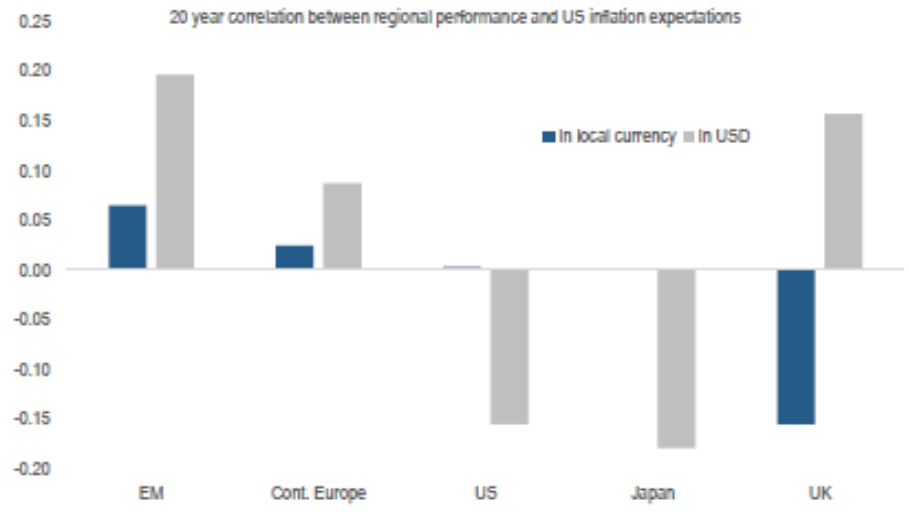
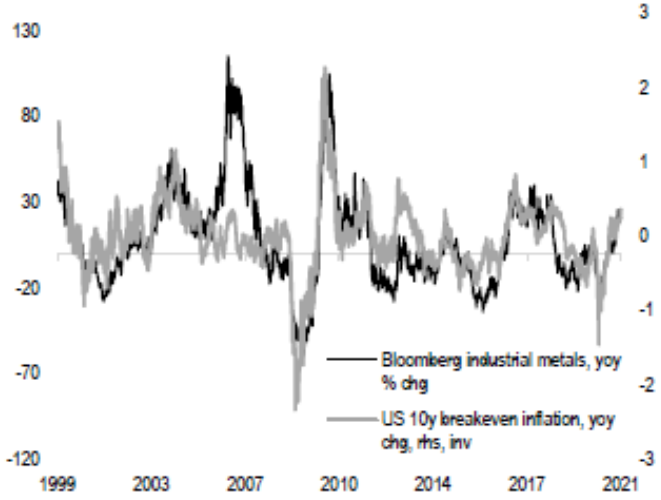
Implications for Investors

Figure 78: A rise in inflation expectations is good for GEM



Source: Refinitiv, Credit Suisse research

Figure 69: Commodity benefits from higher inflation expectations...



Source: Refinitiv, Credit Suisse research

Historically, two asset classes that have shown positive correlation with inflation expectations are commodities and emerging market stocks. This means they tend to perform relatively well in periods where inflation expectations are increasing. Owning stock in emerging market companies and commodity producers like miners can be beneficial in an inflationary environment. Another implication is that inflation is often met with higher interest rates, which is a challenging environment for income producing securities like bonds and dividend paying stocks.

Past performance does not guarantee future results.

Source: Refinitiv, Credit Suisse, Ocean Front Wealth Management

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Source: Ocean Front Wealth Management

References

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- U.S. Bureau of Labor Statistics, Consumer Price Index for All Urban Consumers: All Items in U.S. City Average [CPIAUCSL], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CPIAUCSL, February 2, 2021.
- Credit Suisse Global Equity Strategy, January 29, 2021.

Source: Ocean Front Wealth Management, Wiley, CMT Association

Disclaimer

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