

# **Vancity** Investment Management



## **2021 Market Outlook**



## Where are the opportunities?

Positive vaccine announcements support our view for continued economic recovery in 2021. Conquering the COVID-19 health crisis with vaccines that are broadly distributed and widely accepted will be a critical driver of releasing pent up economic demand and a return to more normalized consumption trends. In this environment, corporate earnings growth is set to improve significantly and support equity valuations.

Companies in the renewable energy space are well positioned to benefit from the global imperative to combat climate change. Governments world-wide have incorporated a green focus in their economic recovery plans. For example, the incoming US Biden administration has announced a \$2T climate agenda that focuses on achieving a carbon pollution-free power sector by 2035 and a target to net zero carbon emissions by 2050.

Canadian finance minister, Chrystia Freeland set a positive tone in her August throne speech by saying, “I think all Canadians understand that the restart of our economy needs to be green. It also needs to be equitable. It needs to be inclusive, and we need to focus very much on jobs and growth.”

In fixed income, we prefer corporate bonds for their attractive yield carry over similar term government of Canada bonds, whose yields continue to hover near historical lows. With bond markets showing an improved risk tone, we also see opportunities in longer term provincial bonds that were not included in the Bank of Canada’s quantitative easing bond purchase program.

## What are the challenges?

2020 global events highlighted the widening inequity and discrimination faced by marginalized groups. The Black Lives Matter Movement increased broader awareness of the injustices faced by the Black Community. COVID-19 disproportionately affected minority groups who faced higher rates of infection, death, COVID-related job losses, and Indigenous communities continued to feel the impacts of historic and systemic oppression. Racial equity and systemic racism will continue to be areas of investor and company focus.

The Canadian government’s support programs played a major role in assisting the recovery but came with a very large price tag in the form of a massive budget deficit. Recent estimates from the International Monetary Fund (IMF) project Canada’s budget deficit as a percentage of GDP to come in at 19.9% this year, the largest amongst developed nations. While Canada entered the pandemic with a relatively good fiscal position, the country lost one of its ‘AAA’ credit ratings when it was downgraded by Fitch Ratings in June. Canada maintains the highest “AAA’ rating from the three other major rating agencies, but could face other downgrades if policymakers don’t take effective action to reduce fiscal deficits after the economy begins a sustained recovery.

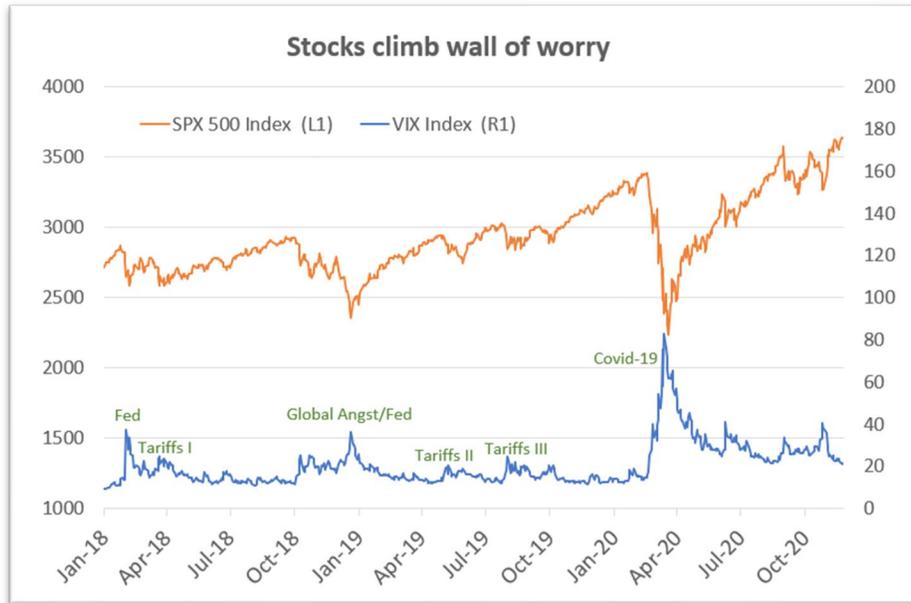
Investors will continue to face a wall of worry to climb in 2021. The impacts of the global pandemic will take time to fade. The massive fiscal and monetary stimulus that has been



deployed globally to combat the lockdown induced recession will be in place for an extended period.

## Chart

Source: Bloomberg



S&P 500 Index – a stock market index that measures the stock performance of 500 large companies listed on stock exchanges in the United States.

VIX Index – a measure of the stock market's expectation of volatility based on S&P 500 options. A ticker symbol and popular name for the Chicago Board Options Exchange's CBOE Volatility Index.





## How are you positioning the Funds?

Following the short but sharp pandemic-induced recession, the equity funds are positioned for the early stages of an economic recovery by increasing exposure to cyclical sectors such as financials, industrials and materials. Equity markets are also contending with a rotation from the high-flying work-from-home names to deep value and recovery names as vaccine news has emerged. We are not immune to market swings, but our focus on high-quality and long-term growth has minimized the fund's exposure to many speculative situations that are whip-sawing traders.

The Bond Fund is slightly short duration positioned vs. the benchmark, with an underweighting to the long end of the curve. We expect bond yields to slowly grind higher through 2021 alongside a steady economic recovery. Central banks will continue to scale back their QE programs, but will maintain their extremely accommodative monetary policies well into the future. Yield curves will likely continue to steepen, as the front end of the curve remains pinned by near-zero policy rates.

## Why is this the right approach for 2021?

Our fixed income strategy targets an overweight to corporate bonds and an underweight to federal bonds. In this ultra-low bond yield environment, credit spreads as a percentage of the total all-in yield remain at attractive levels relative to historical averages, despite the significant tightening of credit spreads in 2020. Reflecting the rising corporate leverage levels and the continued uncertainty over the economic recovery, our bond portfolios are biased towards higher credit quality corporates.

We believe security selection will continue to be an important contributor to portfolio returns in 2021. Both the equity and bond portfolios delivered successful results as fossil fuel free strategies. We will continue to apply our four-element climate risk strategy of divestment, decarbonization, reinvestment and engagement.

VCIM's collaborative approach integrates ESG analysis with traditional financial analysis, and we only invest in companies that meet both sets of criteria. The result is a portfolio of sustainable businesses that have earnings growth rates and return on shareholder equity we expect to exceed market levels.



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Vancity Investment Management is located on the unceded territories of the Coast Salish territory, represented today by the Musqueam, Squamish and Tsleil-Waututh Nations. They have been custodians of this land for thousands of years and I would like to pay my respect to the elders both past and present.

