

## QUARTERLY MARKET UPDATE

AS AT June 30, 2021

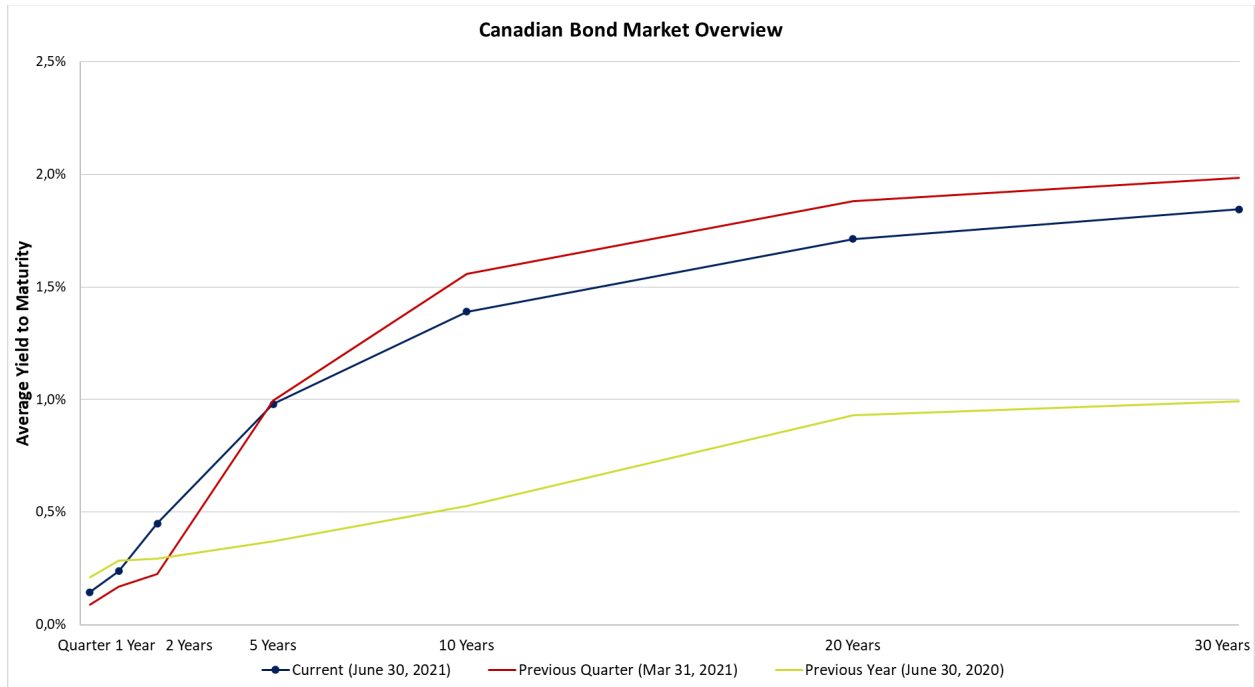
*The following information is being provided as an overview of Vestcor Inc.'s (Vestcor) investment activities and the general financial market conditions experienced during the noted reporting period.*

*Please note that the following material is specific to Vestcor activities and is presented for information purposes only. It does not constitute investment advice in any way, and no guarantee is provided as to its completeness or appropriateness. We recommend that readers consult a professional advisor with respect to their own specific financial matters.*

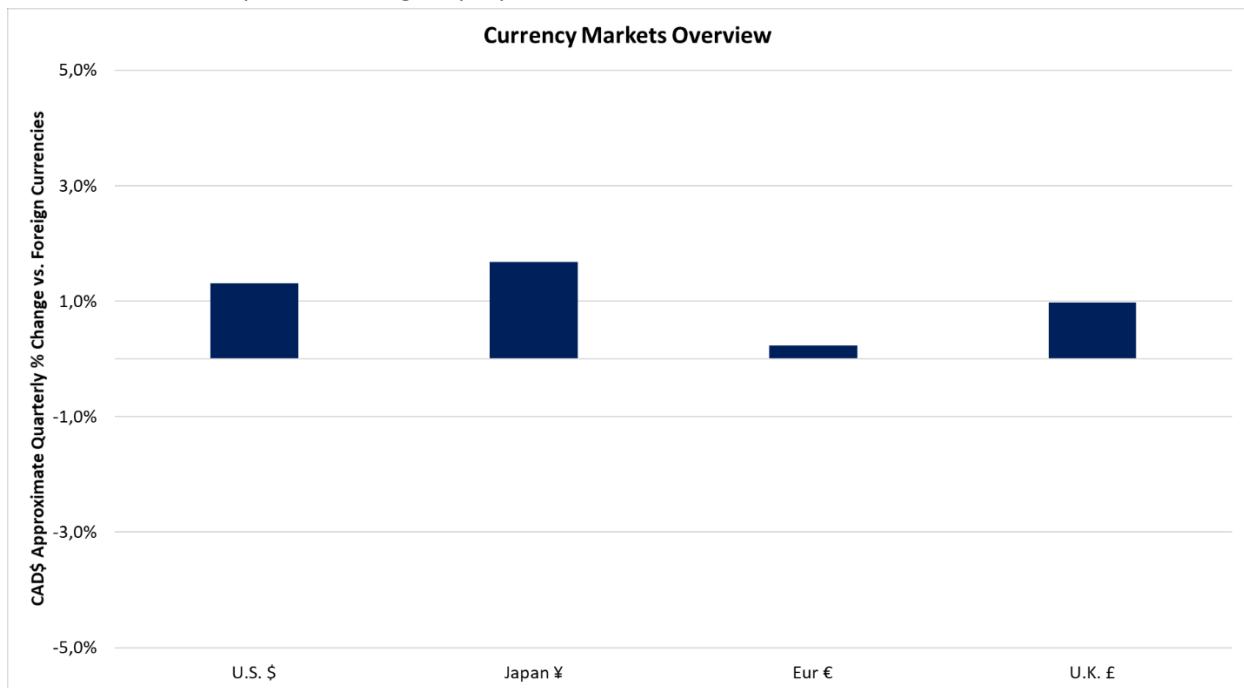
### Performance Overview

---

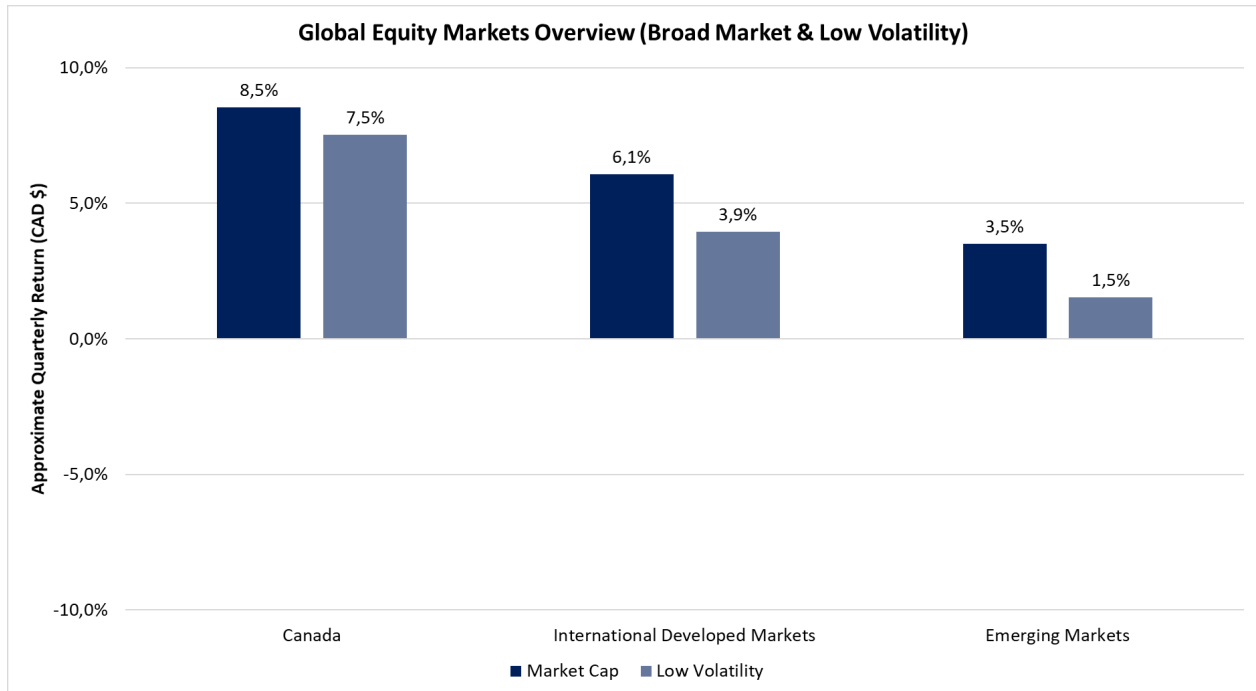
- Performance was broad based during the quarter with positive returns across all asset classes with Equities posting the strongest returns during a period of positive risk sentiment. Other areas of strength include inflation sensitive Real Estate and Real Return Bond asset classes. Fixed Income investments posted solid gains in the current quarter, following losses in the previous period.
- The yield curve flattened somewhat over the period with longer-term yields falling and short-term yields rising. Over the quarter the Bank of Canada kept interest rates unchanged while reducing the quantitative easing bond purchase program, beginning the process of removing extraordinary monetary stimulus provided during the pandemic. Fixed income indexes experienced gains with the Canadian All Government Bond index up 1.80%. The Corporate Bond index underperformed government bonds, gaining 1.28% due to a lower sensitivity to falling longer-term yields as credit spreads remained stable.
- Real Return bonds had a strong quarter gaining 3.53% and outperformed Canadian nominal bonds due to a high sensitivity to falling long term yields.



- In currency markets, the Canadian dollar advanced versus all major currencies which somewhat moderated positive foreign equity returns.



- Strong equity market performance continued from the previous quarter with all strategies producing positive results. Canadian equities outperformed other markets due in part to negative foreign currency translation. Low volatility strategies lagged broad equity markets across all regions as expected during periods of strong risk sentiment.



## Market Environment and Outlook

### Summary:

- Global equity markets finished the first half of 2021 in strongly positive territory, with the MSCI World Index up 9.9% in Canadian dollar terms, while the equivalent emerging markets index gained 4.4% over the same period.
- Market risk levels also continued a recovery toward more normal levels during the first part of the year. The VIX Index, a proxy for market implied equity market volatility, moved steadily lower in the first half to close the month of June at just 15.8.
- While interest rates had moved significantly higher in the first quarter, benchmark government bond yield declined in the May-June period, with the Canadian Government 10-year yield ending the first half at 1.39%.

Equity markets continued the COVID-19 rebound in Q2, with most global markets posting strong gains to close the first half. In general, Canadian markets led the gains in the January-June period, with the TSX Composite Index gaining 17%, comparing favourably with the rest of the developed markets (+9.6%) as well as emerging markets (+4.4%). Significant equity market gains in 2021 have been concentrated in higher risk and lower quality securities, with small cap names in both Canada and the U.S. outperforming larger capitalization peers by about 2-2.5% for the first half.

Although Low Volatility portfolios have also contributed strongly to total returns in 2021, the post-COVID trend of lower risk names underperforming higher risk peers continued. From a global perspective, low

volatility indexes underperformed market capitalization weighted benchmarks by -2%, -4.9%, and -1.5% in the Canadian, World ex Canada, and Emerging markets. Underperformance was particularly acute in the U.S., with lower volatility portfolios lagging market cap portfolios by nearly 6% for the six months ended June 30.

Energy markets continued to recover in 2021, with a generic 1<sup>st</sup> month futures contract for WTI crude oil closing out June at \$73.47 after opening 2021 at \$48.52. With the Canadian market's significant sensitivity to energy and other commodity markets, higher oil prices contributed strongly to the S&P/TSX Index outperformance over the S&P 500 in 2021, with nearly 2% of the Canadian outperformance in 2021 coming from energy companies.

After moving higher in early 2021, bond yields began a modest retreat in the second quarter. After reaching a high of about 1.6% in January, the Canadian 10-year benchmark yield has now dropped to closer to 1.3%, reflecting continued uncertainty among investors about the future path of interest rates. At the same time, credit spreads for more marginal issuers continue to compress, and overall expected returns for diversified bond portfolios have continued to decline in recent months.

While overall the economic and market recovery from the depths of the COVID-19 pandemic and its associated recession has continued strongly thus far in 2021, there are several warning signs on the horizon that suggest continued caution is warranted. In general, while the Federal Reserve has strongly indicated that the current inflation spike is expected to be transitory, investors will be watching the evolution of monetary policy closely in the coming months, and markets will likely react strongly to any perceived changes in the path of interest rates from the current expectations.

In addition to general policy conditions, the ongoing vaccination effort continues to be the primary driver of economic reopening globally. Countries with greater percentages of vaccinated individuals have produced admirable reductions in infection rates so far, but global differences in vaccination rates mean the global recovery will continue to be uneven in the near term. At the same time, ongoing concerns with COVID-19 variants have resulted in a rise in cases even in areas with strong vaccination records, with the vast majority of U.S. states showing an increase in COVID infections in recent weeks, concentrated for the most part among the unvaccinated. Looking forward, investors are facing similar conditions as in prior updates, with stretched valuations, continued economic uncertainty in certain segments of the economy, and a significant disparity in the success of vaccination programs globally.