QUARTERLY MARKET UPDATE

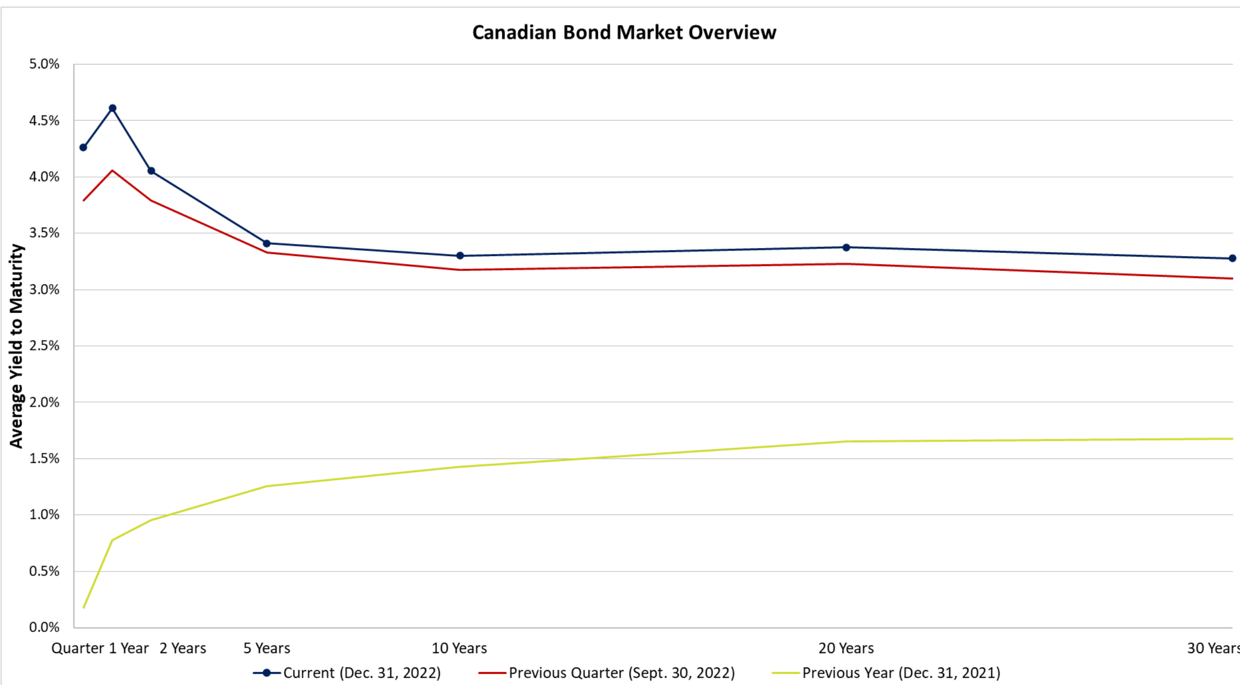
AS AT DECEMBER 31, 2022

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.

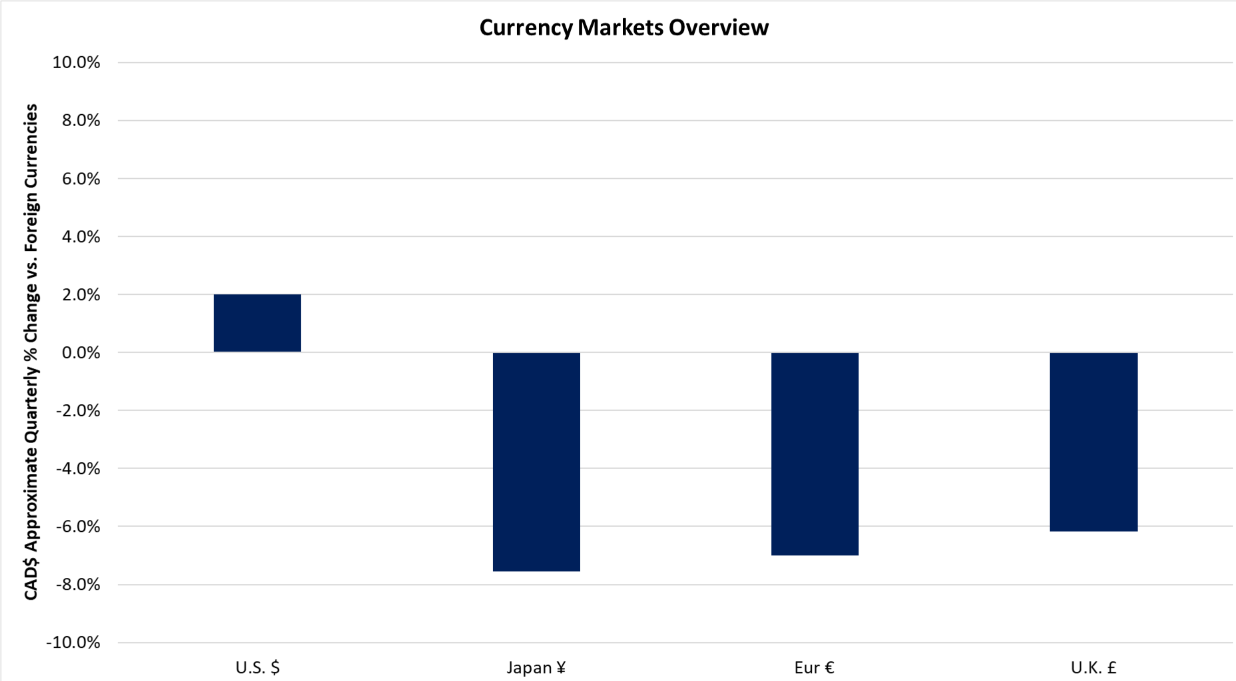
Please note that the following material is specific to Vestcor activities and is presented for information purposes only. It does not constitute investment advice in any way, and no guarantee is provided as to its completeness or appropriateness. We recommend that readers consult a professional advisor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

Performance Overview

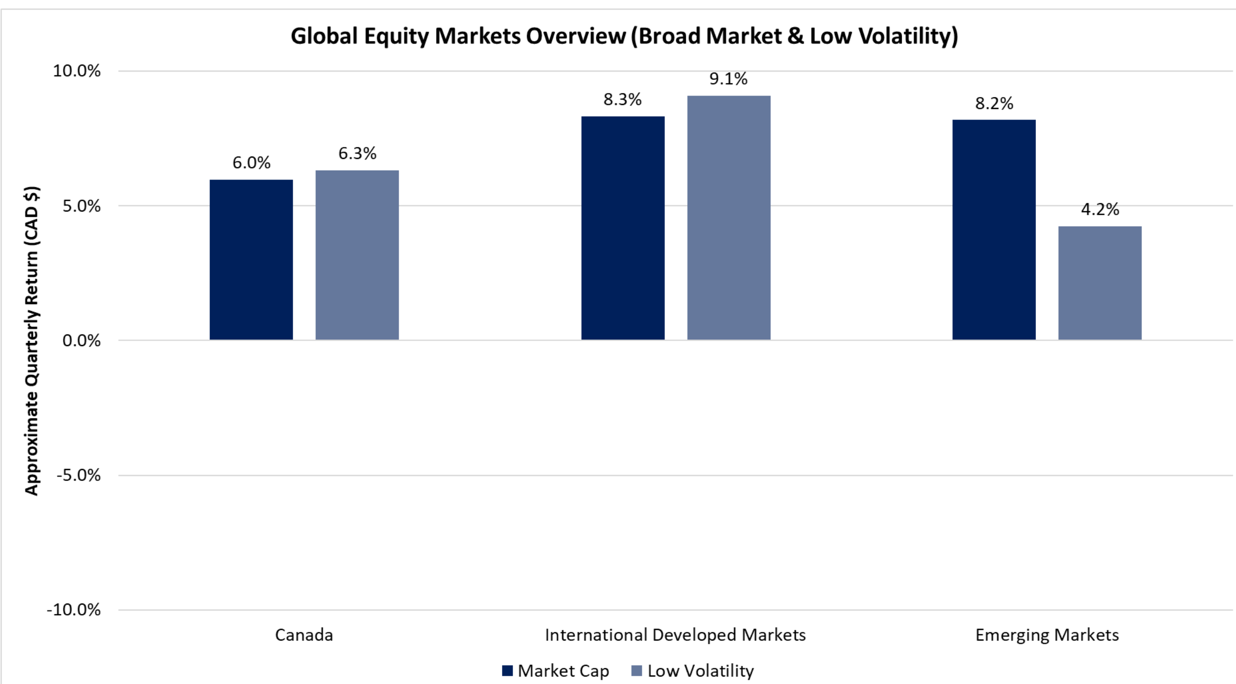
- Performance was strong during the quarter with most asset classes having positive performance. Equities produced the highest returns during the period with broad-based positive performance across all regions and strategies including private equity.
- Yields moved higher over the quarter while the curve continued to invert with the one-year rate rising 0.55% while the 30-year bond yield rose 0.18%. Short-term rates increased as the Bank of Canada continued rising interest rates, 50 bps at the October meeting and 50 bps in December and have signaled further increases may be necessary to return inflation to target.



- Given this backdrop, the Canadian All Government Bond index declined modestly, down 0.21% due to rising yields. Corporate bonds outperformed government bonds over the period with index returns of 1.00% due to higher overall yield levels and more exposure to short-term debt. The Real Return Bond index rose 2.81%, outperforming other bond sectors due to earning higher inflation linked income and higher investor demand for inflation protected securities.
- In currency markets, the Canadian dollar appreciated relative to the US dollar while experiencing strong depreciation against other major currencies. This resulted in a negative portfolio impact on US dollar denominated assets and a positive portfolio impact for assets denominated in other major currencies.



- All Public equity regions and strategies had positive performance during the quarter as investors became hopeful that inflation may have peaked, easing concerns about the economic implications of higher price pressures and the furthering of aggressive monetary tightening. Low volatility strategies outperformed market-capitalization weighted indexes in developed regions while underperforming in Emerging Markets.



- Private market investments including, real estate, infrastructure, and equity underperformed their public market counterparts. Caution is still warranted as private markets tend to lag public markets in terms of valuation impacts.

Market Environment & Outlook

Summary:

- Markets mostly reversed course in Q4, with equity markets broadly stronger and medium-term interest rates changed little by the end of the quarter.
- Except for weakness in the tech heavy NASDAQ index, most equity markets posted solid single digit percent gains in the fourth quarter. International developed markets were significantly stronger than North American and emerging markets indexes.
- While year-over-year consumer price indexes appeared to have peaked by mid-2022, central banks generally maintained a bias toward tighter policy in Q4.
- The significant adjustments in financial markets throughout 2022 may present opportunities for investors with sufficient liquidity to improve both return and liquidity profiles going forward.

Equity markets showed significant strength in Q4, with Canadian, U.S., International Developed Markets, and Emerging Markets showing gains of approximately 6%, 6%, 15%, and 8% respectively for the final three months of 2022. Despite this, global equity investors finished the year with significant declines in value, with those same four indexes showing declines of approximately -6%, -12%, -9%, and -15% for the full calendar year, respectively. Canadian equities, composed of a relative overweight position in stronger performance energy companies matched with a relative underweight in globally underperforming technology companies, provided a modest measure of protection for investors, despite also dropping 6% for the year.

While equities had gains only in the fourth quarter, bond investors could more neatly split the year in half from a performance perspective. The first half saw benchmark 10-year Canadian yields spike nearly 2% (resulting in a -12% return for bond investors) as investors digested the rapidly changing inflation and monetary policy outlook. In contrast, while interest rates were not completely stable through the second half, in general benchmark 10-year yields finished the year at a similar level to June 30, and domestic bond investors earned roughly flat returns in each of Q3 and Q4.

Ultimately, with similar losses for both bonds and stocks for the full calendar year, the median diversified investor holding a portfolio of global stocks and domestic bonds likely earned total returns of approximately -12% in Canadian dollar terms for 2022. In general, 2022 was likely the third weakest year on record for a 60/40 stock/bond investor.

While traditional diversification from bonds did not provide downside protection for investors, less traditional investments provided meaningful diversification. While Canadian, Global, and Emerging Market equities experienced losses of -6%, -12%, and -15% in 2022, low volatility versions of these indexes experience much smaller losses of -1%, -4%, and -8%, respectively. In total, global low volatility equities earned a return of approximately -3% in Canadian dollar terms, compared to -12% for standard indexes. Investors in absolute return strategies also likely experienced relatively strong returns for the year, with downside risk hedges offsetting losses in traditional investments.

Inflation was a significant concern for investors throughout 2022, and as such, central banks remained biased toward relatively tighter monetary policy throughout the year. The Bank of Canada raised short term rates twice in the fourth quarter alone for a total increase of 1%, while the Federal reserve raised by 1.25% over the same period. By year-end short-term rates in Canada and the U.S. had reached 4.25% and 4.5%, respectively, significantly higher than the extended period of 0.25% policy rates following the original COVID-19 economic turmoil in 2020. Although inflation remains above target for both economies, year-over-year consumer price index (CPI) values appeared to have peaked by mid-year and showed continuing declines toward the end of 2022, and markets are now forecasting limited further short-term rate hikes in North America, with the potential for rate declines as soon as the second half of 2023.

In terms of external sources of risk, while global supply chains have not completely normalized, measures of activity show that as import volumes have declined somewhat, delays in shipment processing at most container ports have declined significantly. Additionally, while COVID continues to be a concern, and business travel will likely remain impaired, measures of leisure travel show strong activity in most markets, including the progressively reopening domestic Chinese market, demonstrating a continuing – if uneven – recovery from the dislocations of the 2020-2022 period.

Overall, investors have faced a challenging environment in recent years. Significant volatility spikes throughout COVID made active management a challenge and showed the value of maintaining strong liquidity within investment portfolios, and traditional diversification failed significantly in 2022. Despite this, investors like Vestcor with portfolios that provided effective downside protection in recent years are likely well positioned to take advantage of several opportunities going forward.

Bond yields have increased significantly, and for the first time in recent memory will contribute meaningfully to medium term expected returns for diversified investors. While compensation for credit risk is not at all time highs, higher overall yields, combined with relatively lower interest rate risk, allowed corporate bonds to modestly outperform in 2022 and contribute to their attractiveness going forward, at least in certain segments of the market. For investors who prioritize liquidity, the relatively higher level of shorter-term interest rates provides at least a transitory opportunity to maintain exposures while reducing risk and improving the liquidity profile of the combined portfolio. Overall, a diversified portfolio today has a much-improved expected return profile when compared to two years ago, and bonds in general can potentially play an improved role in pension fund portfolios going forward from both a return generating and risk management perspective.