

Economic Outlook

Summer 2022

Summary

- The outlook has shifted drastically over the last six months, with the general optimism at the year's outset now replaced with growing pessimism, as increased cost pressures more than offset the quality of life benefits associated with record low unemployment and easing public health restrictions. It is not a coincidence historically low consumer sentiment comes as gas prices, perhaps the most visible variable cost to most households, touched their own highs.
- This creates a challenging environment for policymakers. The rapid stimulus-supported recovery has resulted in economies operating with excess demand that needs to be tempered in order to rein in price pressures and limit the longer-term demand destruction posed by high inflation. There is reason to believe that households and businesses have the capacity to absorb this impact.
- That said, global growth momentum is slowing, and there remains an abundance of headwinds combining with the pervasive negativity to create a fragile backdrop, materially raising the risk of an economic downturn materializing sooner rather than later; aggressively tightening policy would only serve to exacerbate the slowdown.
- The bottom line is that the outlook remains highly uncertain, and the months ahead will see policymakers weigh each datapoint carefully to determine whether the odds favour the upside risks to inflation, the downside risks to growth or the baseline scenario of a soft landing.
- For financial markets, while there are clear and present downside risks, the magnitude of the damage done to this point, combined with the abundant pessimism that is pricing in an increasingly dour outlook, arguably shifts the balance of risk in favour of potential upsides. "Bad" outcomes may not end up being "as bad as feared" as the backstop provided by underlying strength of consumer and business finances and a general lack of material imbalances could limit the overall economic fallout.

Walking a fine line

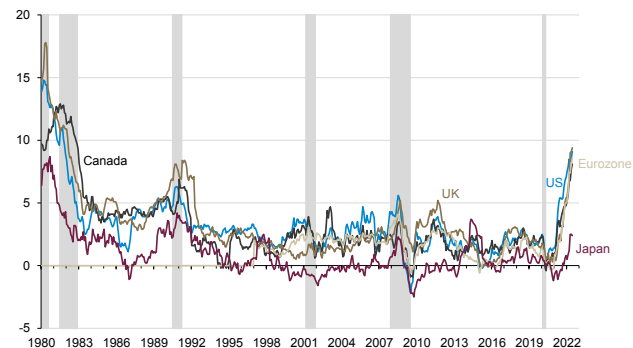
The broad expectation at the start of the year was that the global economy would slow from last year's elevated pandemic recovery-boosted rate of growth, but that the ongoing reopening would still support a pace of expansion that remained above that of the pre-crisis period.

As 2022 began, however, there were successive shocks to the system (a new pandemic wave and resultant lockdowns, as well as Russia's invasion of Ukraine), that hindered the ability of economic activity to continue to normalize, instead making the already evident imbalances between supply and demand even worse.

The result was that nascent price pressures that were hoped to be "transitory" — set to fade as a fully functioning supply side was able to catch up to demand — were not only persisting but intensifying and broadening out.

CHART 1: THE COSTS OF LIVING

Consumer price inflation
(year-over-year percent change in consumer price index)

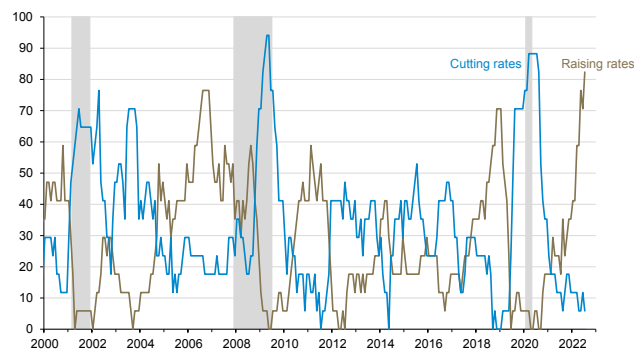


Source: Guardian Capital based on data from Bloomberg to June 2022; shaded regions represent periods of US recession

Concerns over the destructive nature of inflation (households and businesses forced to spend ever more on fewer goods & services, weighing on "real" activity), spurred global central banks into action, first with caution and then greater impetus.

CHART 2: POLICY TURNAROUND

Central bank policy rate direction, G20
(six-month rolling percent of G20 central banks)



Source: Guardian Capital based on data from Bloomberg and the Bank for International Settlements to July 22, 2022; shaded regions represent periods of US recession

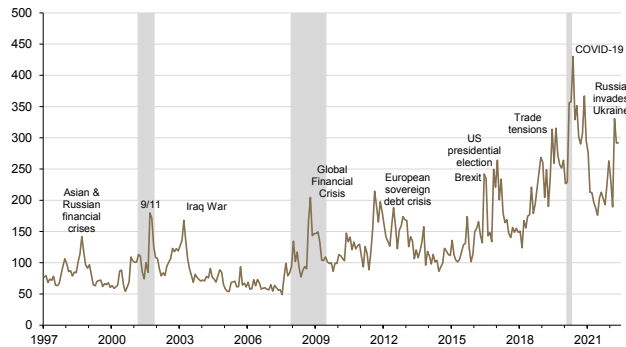
Yet, while a shift away from highly stimulative policy is warranted, such adjustments take time to filter into the real economy (though financial markets react much more swiftly), which makes them difficult to appropriately calibrate. This is a key reason that policymakers, historically, have erred by doing too much to rein in surplus demand, instead pushing into deficit and the economy into recession.

The risk of such a policy error looms even larger in the current environment, given issues on the supply side — largely insulated from the impact of monetary policy in the short-term (central banks cannot do anything to immediately pump more oil, grow more grains, produce more microchips or clear port traffic) — share the blame for the current pricing predicament.

So the moderation that comes, part and parcel, with the normal evolution of the economic cycle from "recovery" to "expansion" is being compounded by the impact of high inflation and tighter financial conditions, not to mention the ongoing pandemic and geopolitical tensions.

CHART 3: HIGHLY UNCERTAIN TIMES

Economic Policy Uncertainty Index¹, world
(index; 1985 to 2019 average = 100)

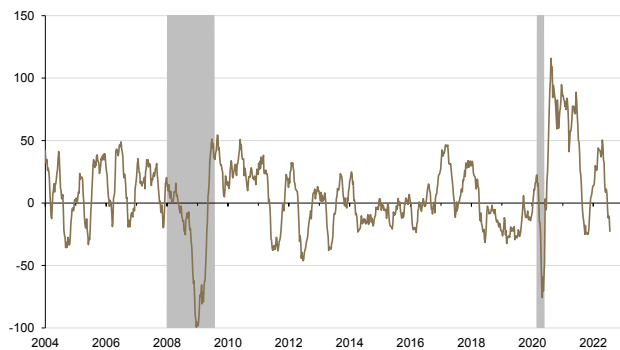


Source: Guardian Capital based on data from PolicyUncertainty.com to May 2022; shaded regions represent periods of US recession

Against this backdrop, the global economic dataflow has generally underperformed through the last few months (and financial markets with it), as sanguine expectations have proven too optimistic.

CHART 4: AN UNPLEASANT SURPRISE

Citi Economic Surprise Index², world
(diffusion index; >0 denotes “better than expected” dataflow)

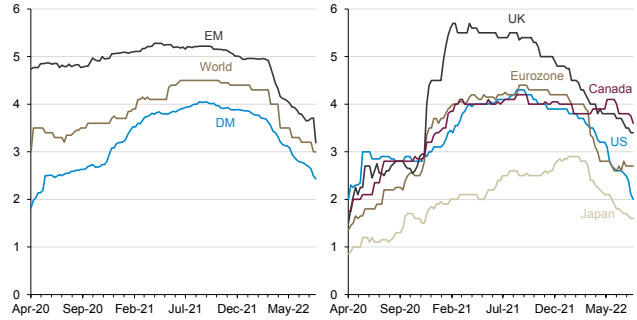


Source: Guardian Capital based on data from Bloomberg to July 22, 2022; shaded regions represent periods of US recession

In response, and factoring in a more challenging road ahead, forecasters have slashed their growth outlooks, with earlier expectations for above-trend growth giving way to much more tepid rates.

CHART 5: A LITTLE MORE OFF THE TOP

Consensus real GDP growth forecasts, 2022
(percent)



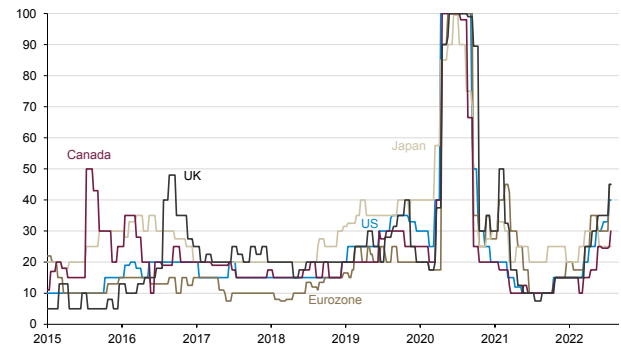
Source: Guardian Capital based on data from Bloomberg to July 22, 2022

The combination of lowered expectations and widening confidence intervals around the forecasts suggests that the risks of an outright contraction have increased markedly.

The consensus of modelled and subjectively assigned odds of a recession across developed markets (DM) have risen sharply over the last few months, with the assumed likelihood of a downturn in the next 12 months amounting to a coin flip.

CHART 6: RISING RECESSION RISKS

Consensus expected probability of recession in 12 months
(per cent)



Source: Guardian Capital based on data from Bloomberg to July 22, 2022

Importantly, though, just because something is viewed as increasingly likely does not mean that it will materialize — after all, a time-tested rule of markets is “*when all the experts and forecasts agree, something else is going to happen.*”

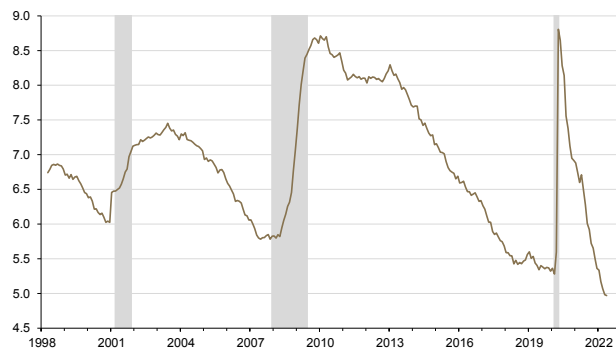
Indeed, it is easier to avoid (or at least mitigate) accidents that can be seen coming — it is those unexpected shocks, that seemingly come out of nowhere and are, thus, inherently unpredictable, that tend to do the most damage.

Another material economic downswing will inevitably occur, but trying to predict such an event with any sort of lead-time is a mug's game — a recession is typically well underway before the data reflect that fact, and by then a bulk of the financial market fallout has already taken place.

For the here and now, despite the growing concerns and numerous headwinds, growth momentum appears to remain broadly in place (albeit at a lower rate than a year ago), which is keeping global labour markets historically firm.

CHART 7: SCARCITY OF LABOUR

Unemployment rate, OECD*
(percent)



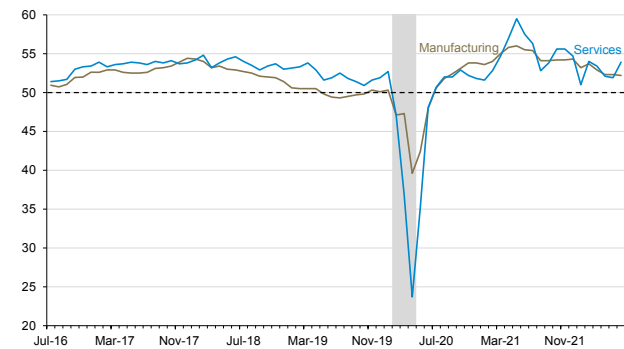
*OECD= Organisation for Economic Co-operation and Development³
Source: Guardian Capital based on data from OECD to May 2022; shaded regions represent periods of US recession.

Goods producers are still working through supply chain constraints and related order backlogs, while easing public health restrictions and pent-up consumer demand for more intangible life experience, after two years of social bubbles, underpin activity at service providers.

The global purchasing managers' indexes for the manufacturing and services sectors remain comfortably in expansionary territory, indicating the economy, in aggregate, is still continuing to expand at the halfway point of the year.

CHART 8: MAINTAINING MOMENTUM

Purchasing Managers' Indexes⁴, world
(diffusion index; >50 denotes expansion)



Source: Guardian Capital based on data from Bloomberg to June 2022; shaded region represents period of US recession

That said, there are a rising number of forces acting upon the global economy that are likely to temper the momentum — and serve to complicate the job of policymakers seeking to walk a fine line in their efforts to balance addressing the long-term negatives of inflation without generating significant cost to the global economy in the short term.

What could go right?

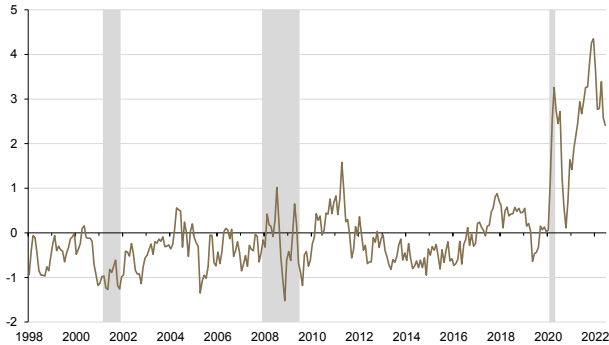
Clearly one of the best possible things to happen in the near term would be a moderation in inflation that eases cost pressures on households and businesses alike and takes the pressure off central banks to use the blunt instruments in their toolbox to tamp down demand. There are some positive developments on this front.

For starters, there are growing indications that the pressures on the links within the global supply chain are easing. Production is increasingly able to run at a higher capacity as public health restrictions are scaled back globally, and goods are flowing more freely as shipping bottlenecks subside and transportation hubs face less congestion.

The aggregated gauge of global supply chain pressures compiled by the Federal Reserve Bank of New York, while still materially above its long-term averages, has moderated notably in recent months.

CHART 9: PRESSURE RELEASE

Global Supply Chain Pressure Index⁵, world
(standard deviations from the series' average)



Source: Guardian Capital based on data from Federal Reserve Bank of New York to June 2022; shaded region represents period of US recession

Relatedly, shipping costs have come off the boil as well, with the global benchmark freight rate for major east-west trade routes down 33% from its earlier peak. The resultant reduction in costs of production should be felt in goods prices in months to come.

CHART 10: REDUCED SHIPPING

Drewry World Container Index⁶
(thousands of US dollars per 40-foot container)

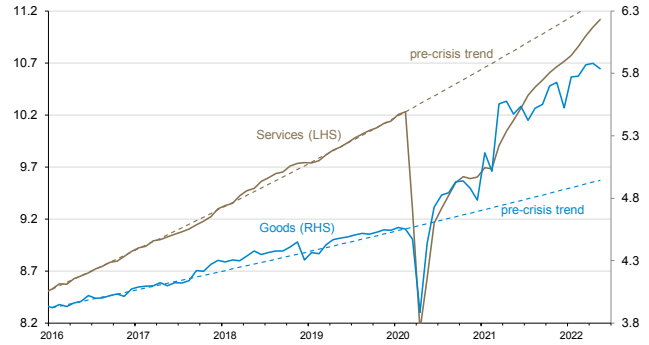


Source: Guardian Capital based on data from Bloomberg to July 22, 2022; shaded region represents period of US recession

Further, consumer goods demand is ebbing from its blistering pace over the last two years, as spending transitions back in favour of the previously restricted services that dominated the household budget prior to the pandemic.

CHART 11: A SHIFT TO SERVICES

Nominal personal consumption expenditure, US
(trillions of US dollars)

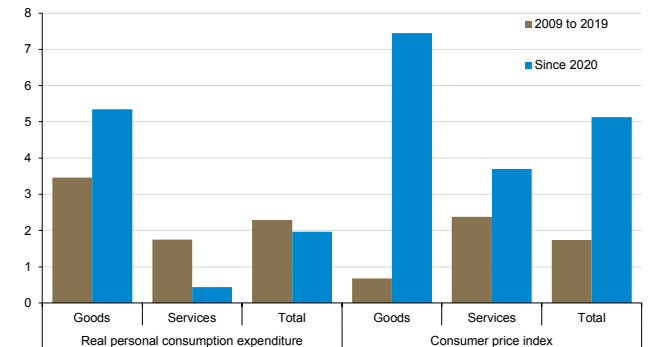


Source: Guardian Capital based on data from the Bureau of Economic Analysis to May 2022

This eases pressure on suppliers, while also shifting the consumer spending basket toward expenditure areas that have seen more modest inflation.

CHART 12: TREND REVERSALS

Real consumer spending & inflation, US
(annualized per cent)



Source: Guardian Capital based on data from the Bureau of Economic Analysis & the Bureau of Labor Statistics to May 2022

Additionally, while commodity prices remain elevated — particularly for energy products, thanks to the sanction-induced constraints on Russian supplies — they have come off the boil thanks to a combination of expectations for increased supply and the downgraded growth outlook. Any progress with respect to the ongoing war in Ukraine would be a welcome development here as well.

CHART 13: A LESS HOT COMMODITY

S&P Goldman Sachs Commodity Price Index⁷
(index)



Source: Guardian Capital based on data from Bloomberg to July 22, 2022; shaded regions represent periods of US recession

Given the impact on real spending and investment is greater the longer excessive price pressures persist, any indication of a sustained downtrend in inflation is very welcome — such progress on central banks’ price stability mandates would mean that more extreme policy prescriptions would not necessarily be warranted.

With that said, there is already a hefty shift in policy rates that is pretty much baked in right now, and that raises the specter of recessions past.

In general terms, aside from exogenous shocks (such as pandemics or wars), recessions typically come about due to the presence of significant financial imbalances and excesses.

In these scenarios, central bank-induced increases in costs of capital make overextended financial positions untenable and force an unwind that creates negative spillovers — and the extent of the hit is a function of the magnitude of the imbalance.

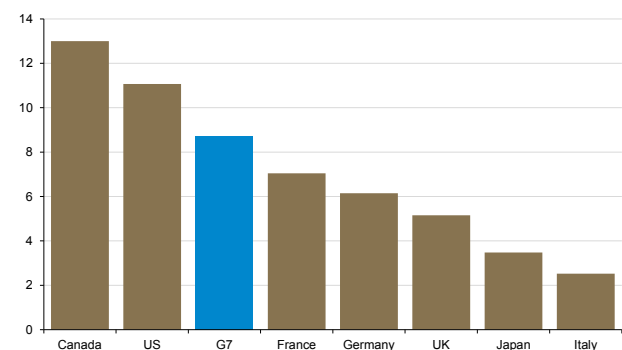
As things stand, there are limited indications of significant financial imbalances — there were absolutely pockets of excess (blank cheque “special purpose acquisition companies” being able to raise billions of dollars on the open market and the variety of cryptocurrency-related entities are good examples), but no signs of the type of systemic misallocations of capital like the kind that preceded the tech wreck and global financial crisis.

Household finances are currently in historically good shape despite the impact of the pandemic. The combination of an unprecedented transfer of funds from the government to households, pandemic restrictions that constrained spending (especially on services, which accounted for two-thirds of household budgets prior to the pandemic) and a rapid recovery of labour markets amid re-openings have resulted in a global savings glut.

Since the start of 2020, households across the G7 have cumulatively socked away nearly US\$4 trillion in savings over and above pre-crisis trends — that is a stockpile equivalent to almost 9% of the value of the output of these key DM economies, though Canadians and Americans benefitted more than their peers overseas from their governments’ comparatively generous supports.

CHART 14: SAVING GRACE

Excess* personal savings, G7
(trillions of US dollars)



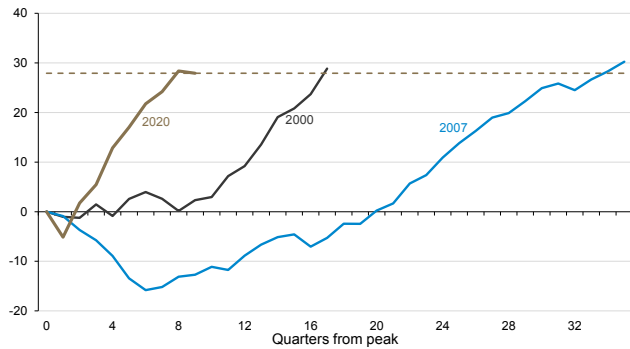
*Cumulative personal savings from Q1 2020 to Q1 2022 in excess of 1999 to 2020 trend savings rates; source: Guardian Capital based on data from Bloomberg & the OECD to Q1, 2022

That “excess saving” has been amplified by the monetary policy-supported strength in global financial and residential real estate markets over the last two years.

Indeed, even with the year-to-date weakness in financial markets, US consumer wealth, for example, is 30% above its pre-crisis peak, a threshold it took four years to hit after the tech wreck at the turn of the millennium, and eight-and-a-half years following the global financial crisis.

CHART 15: A WORTHY INCLUSION

Household net worth, US
(per cent change from pre-recession/crisis peak)

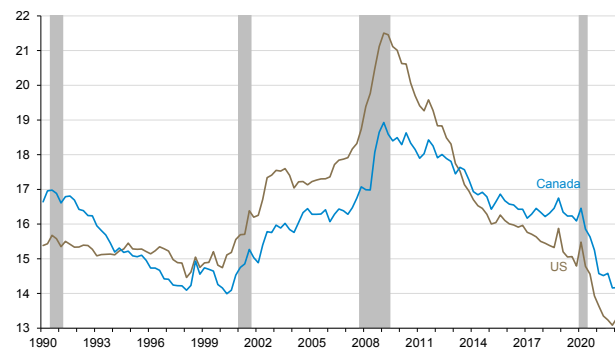


2000 peak = Q3 2000; 2007 = Q3 2007; 2020 = Q4 2019; source: Guardian Capital based on data from the US Federal Reserve Board to Q1 2022

The improvements on the asset side of the ledger have outpaced more modest increases in debt, meaning that household solvency is actually at generational bests, providing a sizable cushion against broader declines in asset prices.

CHART 16: PULLING THE LEVER

Household debt-to-asset ratio*
(per cent)



*Data made comparable following [Statistics Canada's guidelines](#)⁸
Source: Guardian Capital based on data from the US Federal Reserve Board & Statistics Canada to Q1 2022; shaded regions represent periods of US recession

The wealth cushion has been constructive for spending growth to this point and looking forward, they can help offset the impact of higher costs of living, as households have the capacity for savings rates to fall after two years of “over-saving.”

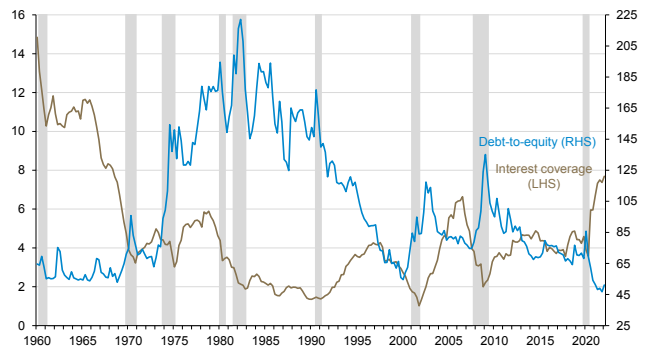
There are few indications of significant disparities in the business sector either.

Corporate balance sheets are also in fairly pristine shape with high liquidity, low leverage and negligible interest burdens — a product of firms taking advantage of market conditions over the last decade

to raise funds at low rates for extended terms.

CHART 17: BUSINESSES ARE NOT BURDENED

Nonfinancial corporate interest coverage & leverage, US
(times interest earned) (percent)



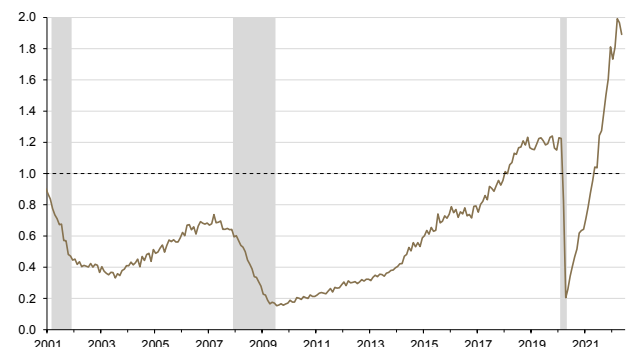
Source: Guardian Capital based on data from the US Federal Reserve Board & Statistics Canada to Q1 2022; shaded regions represent periods of US recession

The positive aggregate fundamentals suggest that there is scope to weather a potential hit to profitability without setting off a particularly harsh downswing in the credit cycle that causes firms to scale back investment intentions or headcounts.

On the potential job market impact, it remains the case that there is still an abundance of excess demand for labour as economies hit capacity constraints — as noted, unemployment rates are at historically low levels while, for example, there are still more than 11 million vacant job openings in the US or nearly two for every person currently among the ranks of the unemployed.

CHART 18: LOTS OF JOBS, FEW WORKERS

Job openings per unemployed person, US
(number)



Source: Guardian Capital based on data from the U.S. Bureau of Labor Statistics (BLS) to May 2022; shaded regions represent periods of US recession

What could go wrong?

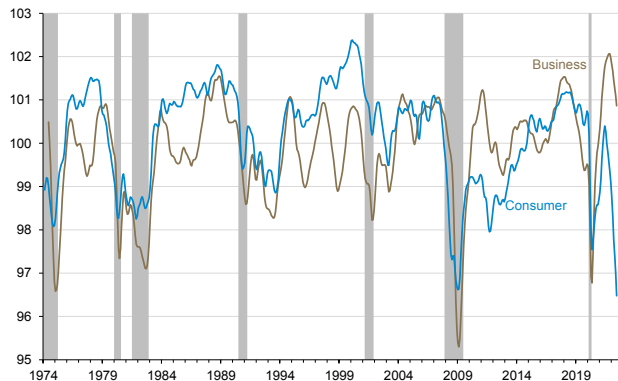
The apparent absence of significant imbalances serves to limit the likelihood of things going truly off the rails, triggering a deep and long-lasting hit to activity. At the same time, this does not mean that any downswing can be completely averted.

The cost-driven growing pessimism among consumers and businesses of late raises the potential of creating a self-fulfilling prophecy, as fears that things will take a turn for the worse in the months ahead impact current spending and investment decisions and start a downward spiral.

Measures of consumer and business confidence across the 38 member countries of the Organisation for Economic Co-operation and Development (OECD) have fallen notably this year, with the former hitting its all-time low in June.

CHART 19: HURT FEELINGS

Consumer & business confidence, OECD
(index; long-term average = 100)



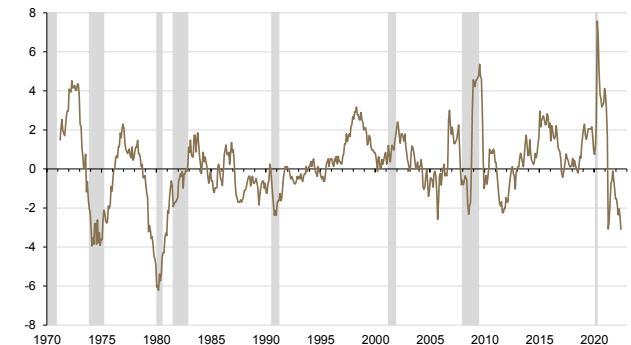
Source: Guardian Capital based on data from the OECD to June 2022; shaded regions represent periods of US recession

Further, while consumers' savings cache can blunt the impact of higher costs of living and bridge the gap between prices and wages, it cannot do so forever.

The longer the elevated inflation persists, and the more the pressures broaden and intensify, the more it will erode the purchasing power of income and savings — and real wages are already deteriorating materially — ultimately weighing on real spending.

CHART 20: LIKE A PAY CUT

Real* wage rate production & nonsupervisory workers, US
(year-over-year per cent change)



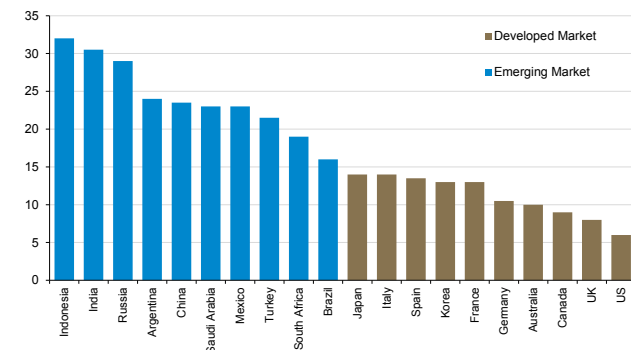
*The consumer price index for urban wage earners and clerical workers is used by the BLS to deflate the earnings series for production and nonsupervisory employees
Source: Guardian Capital based on data from the BLS to June 2022; shaded regions represent periods of US recession

The risk here is particularly acute among those economies that are most sensitive to higher costs of necessities such as food and energy, both of which have been greatly impacted by the war in Ukraine as supplies of cereal grains and energy products have been curtailed due to the conflict (and sanctions).

With respect to food, the impact is most evident in emerging markets (EM), where grocery bills account for a relatively larger share of budgets — and rising costs of food have served as a catalyst for civil unrest and political turnover in the past.

CHART 21: A BIGGER PIECE OF THE PIE

Share of consumer expenditure on food, G20
(percent)



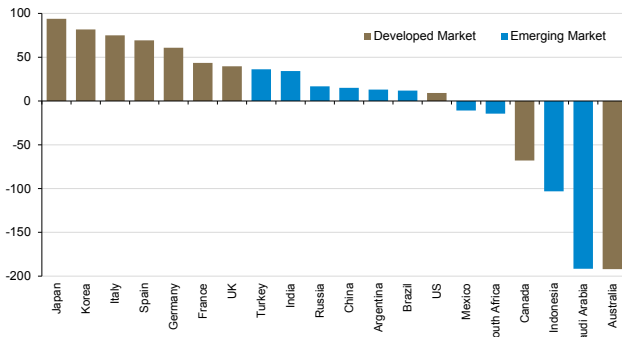
Source: Guardian Capital based on data from the US Department of Agriculture & Our World In Data for the years 2015 to 2016

In terms of energy, those regions that rely most heavily on imports to meet domestic needs typically face the greatest cost pressures — and the fact that Europe, in particular, is so dependent on Russia for oil and gas makes the situation there even more

difficult, as the potential for supply shortages looms.

CHART 22: ENERGY DEPENDENCE

Net energy imports as a share of domestic energy use, G20 (per cent; <0 denotes more energy exported than used)



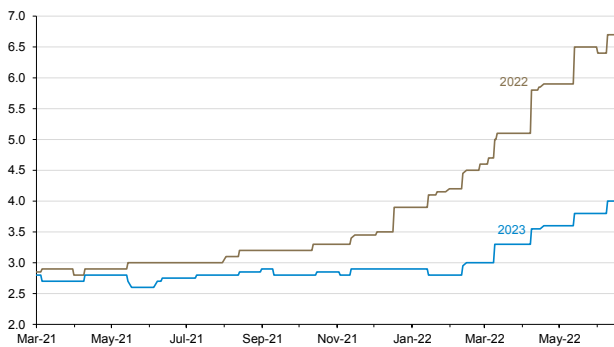
Source: Guardian Capital based on data from the World Bank as at 2014

More broadly, there is also the potential that the underlying strength of households and businesses could prove to be too much of a good thing in the near term, as it may well be the case that demand continues its surprising resiliency and sees a wage-price spiral that leads inflation expectations to become untethered.

As it stands, broad gauges of consumer, business and market inflation expectations have increased notably, while consensus forecasts for inflation for this year and next have been revised up sharply.

CHART 23: INFLATED EXPECTATIONS

Consensus real GDP growth forecasts, World (percent)



Source: Guardian Capital based on data from Bloomberg to July 22, 2022

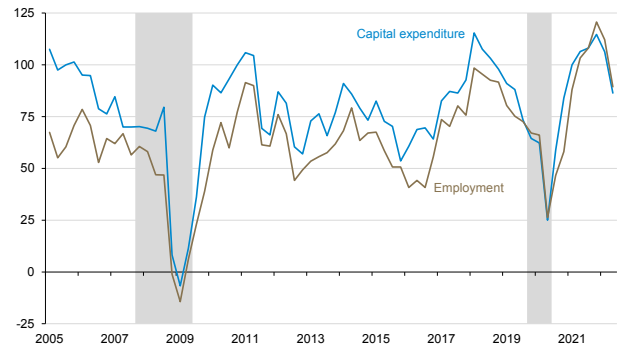
Such an environment would put added pressure on central banks to move policy further into contractionary territory to get a handle on inflation.

The higher costs of capital would deter business investment and hiring decisions — and there are already signs of this happening, with recent surveys

of business leaders indicating reduced expectations for capital spending and employment, though gauges for both still remain elevated.

CHART 24: RETHINKING BUSINESS PLANS

CEO Economic Outlook⁹ capital spending & employment plans (index)



Source: Guardian Capital based on data from Business Roundtable and Bloomberg to Q2 2022; shaded regions represent periods of US recession

Additionally, higher rates constrain profitability, place pressure on market valuations and weigh further on residential real estate markets, which have already seen a sizable decline in activity in response to increased rates — the adverse impact on asset prices would have a negative wealth effect that would create further repercussions for spending.

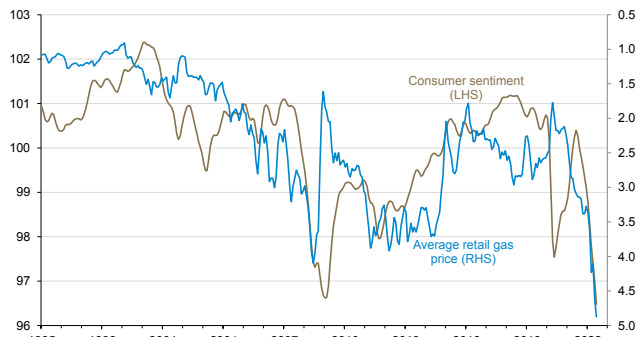
Weighing the odds

The general optimism at the year's outset has now been largely replaced with growing pessimism, as increased cost pressures more than offset the quality of life benefits associated with record low unemployment and easing public health restrictions.

It is not a coincidence that historically low consumer sentiment comes as gas prices, perhaps the most visible variable cost to most households, touched their own highs in June — though the fact that pump prices have retreated since suggests some sentiment improvement may be in the offing.

CHART 25: GAS PAINS

OECD consumer confidence & retail gas prices
(index; long-term average = 100) (US dollars; inverted scale)



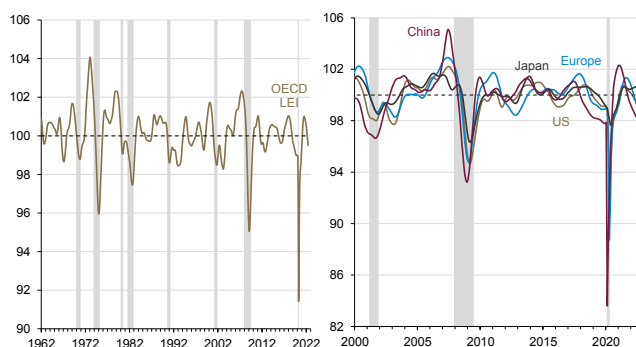
Source: Guardian Capital based on data from the OECD and Bloomberg to June 2022; shaded regions represent periods of US recession

This creates a challenging environment for policymakers. The rapid stimulus-supported recovery has resulted in economies that are operating with excess demand that needs to be tempered in order to rein in price pressures and limit the longer-term demand destruction of high inflation. Yet there is reason to believe that households and businesses have the capacity to absorb this impact.

That said, global growth momentum is slowing and there is still an abundance of headwinds that combine with the pervasive negativity to create a fragile backdrop and raise the risks of a downturn materializing sooner rather than later — and aggressively tightening policy would only serve to exacerbate the slowdown.

CHART 26: FOLLOW THE LEADER?

Leading economic indicator, OECD
(index; 100 = long-term trend growth rate)



Source: Guardian Capital based on data from the OECD and Bloomberg to June 2022; shaded regions represent periods of US recession

The bottom line is that the outlook remains highly uncertain and the months ahead will see

policymakers weigh each datapoint carefully to determine whether the odds favour the upside risks to inflation, the downside risks to growth or the baseline scenario of a soft landing — which is seeing its potential runway narrow.

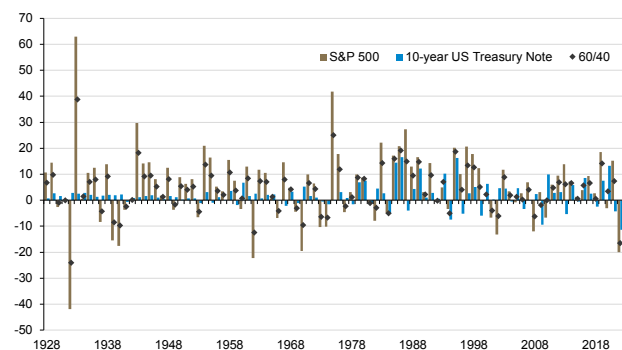
Making markets

The economic backdrop has proven to be particularly difficult for investors, as there has been nowhere to hide, with all asset classes turning in historically poor performance over the first six months of the year.

The surge in interest rates has resulted in bonds, traditionally viewed as the “risk-free” asset, recording their worst performance over the last century, while risk assets have faced tremendous selling pressure (worst first six months since 1970), as markets adapt to the new interest rate and growth regime.

CHART 27: A HISTORIC HALF

First half of calendar year total return
(percent)



*60/40=60% S&P 500, 40% 10-year US Treasury Note

Source: Guardian Capital based on data from Bloomberg to June 2022

While this has undeniably proven painful for investors, a broad-based reset of valuations does greatly improve the return outlook for the future.

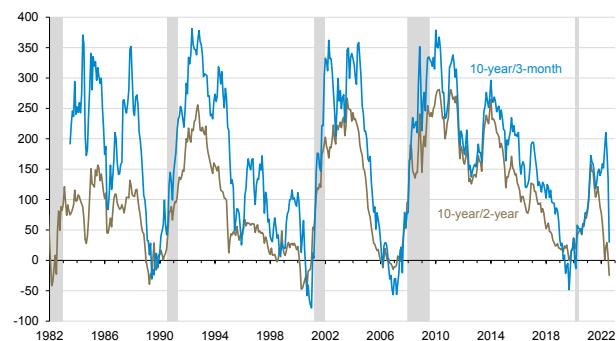
To borrow a phrase from ecology in this economics-centric missive, sometimes a burn-off is necessary to clear out the underbrush and unviable plant life that is threatening the longer-term health of an ecosystem — the process ultimately helps revitalize the area and supports new growth for years to come.

For the near term, however, the market is still smoldering, and green shoots may seem few and far between, with volatility likely to persist — and as discussed, there are real risks that the fire could well flare up and spread further, with efforts to control the blaze potentially just helping to ignite the embers.

Typically, a more uncertain outlook for growth is constructive for bonds, as potential economic weakness raises the odds that policymakers will have to backtrack — and the fact that yield curves have inverted at most points (an ominous signpost that points to rising recession risks in the year ahead), suggests that markets are actively pricing in this prospect.

CHART 28: HEAD OVER FEET

US Treasury yield curves
(basis points)

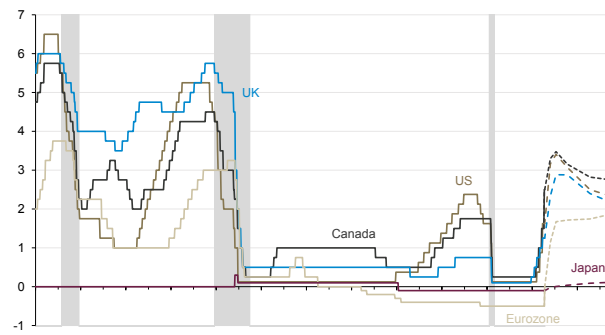


Source: Guardian Capital based on data from Bloomberg to July 22, 2022; shaded regions represent periods of US recession

The anticipation that central banks will, however, continue to tighten financial conditions (and perhaps in a more aggressive fashion than currently priced) to rein in price pressures, along with the apparent willingness to sacrifice growth to get ahead of the inflation curve, is likely to mean continued (albeit more moderate than seen so far this year), headwinds for bond performance in the coming months.

CHART 29: NOT DONE YET

Overnight index swap-implied forward policy rates
(percent)

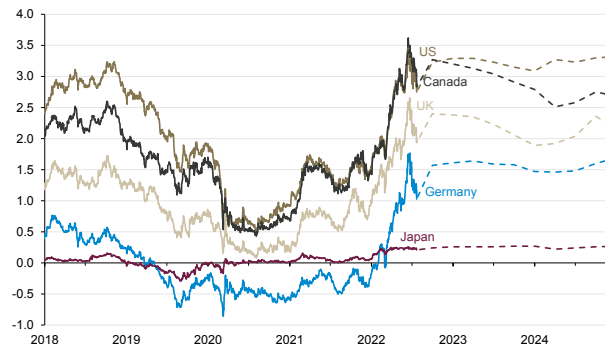


Source: Guardian Capital based on data from Bloomberg to July 22, 2022 (dashed lines represent OIS data as at July 22); shaded regions represent periods of US recession

That said, expectations are for government bond yields to largely remain range-bound around current levels — higher levels that offer some compensation for the volatility and provide some cushion against further rate increases that did not exist earlier.

CHART 30: TREADING WATER

10-year sovereign bond yields
(percent)



Source: Guardian Capital based on data from Bloomberg to July 22, 2022 (dashed lines represent consensus forecasts as at July 22)

For riskier assets, the significant correction in valuations against seemingly indiscriminate selling has, undoubtedly, created opportunities for selective investors, but the risks to the outlook speak in favour of maintaining a focus on quality of return over potential quantity at the moment.

CHART 31: VALUATION VOLATILITY

Forward price-to-earnings ratio, MSCI ACWI* (ratio)



*MSCI ACWI = MSCI All-World Country Index[®]. Source: Guardian Capital based on data from Bloomberg to July 22, 2022; shaded regions represent periods of US recession

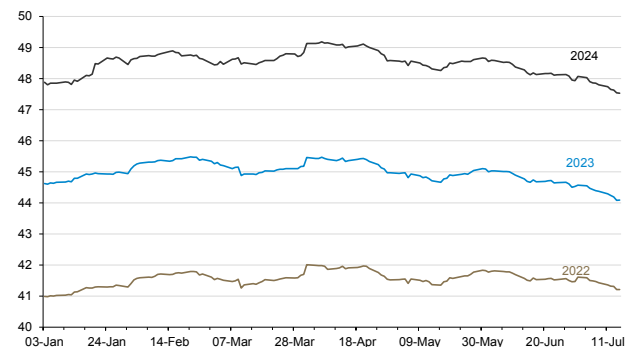
In particular, the potential for earnings expectations to see a significant shift lower represents the main potential downside for equities.

To this point, despite the growing list of headwinds that are weighing on the macro outlook, earnings have come in better than anticipated (especially for the “value” strategies and their relatively heavy exposure to commodity markets).

It has actually been the case that consensus earnings forecasts for the broad global equity market have not just held in, but have been edging higher for the current year — and while earnings forecasts for the next two years have seen their levels drift marginally lower, they are still expected to record gains.

CHART 32: EARNING THEIR KEEP

Consensus calendar year earnings per share, MSCI ACWI* (US dollars)



*MSCI ACWI=MSCI All Country World Index; source: Guardian Capital based on data from Bloomberg to July 22, 2022

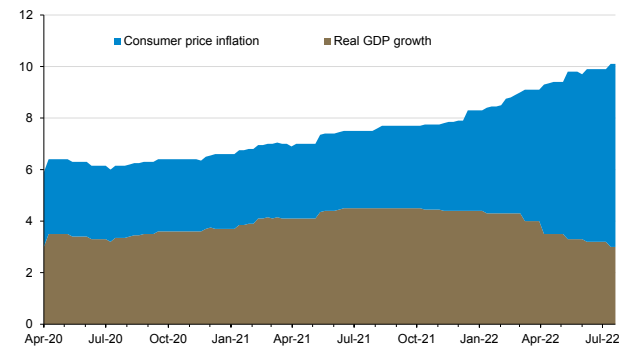
While this may seem counterintuitive given the more dour economic outlook, and add fodder for expectations of a downward adjustment, there is good reason for this seeming resiliency.

First of all, earnings are “nominal” figures, meaning that they incorporate not just the volume of goods and services that are sold by companies, but prices too.

So, while it may be the case that expectations are being revised lower for the growth in volumes (that is, “real” gross domestic product), the rising inflation expectations (the growth in prices) mean that forecasts for “nominal” output have been rising.

CHART 33: OF NOMINAL IMPORTANCE

Consensus 2022 real GDP growth & inflation forecasts, world (percent)



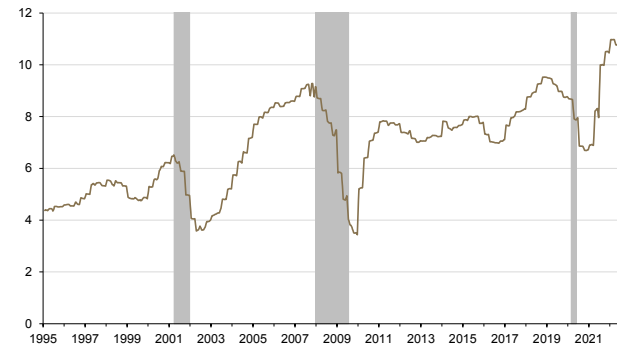
Source: Guardian Capital based on data from Bloomberg to July 22, 2022

Secondly, while rising inflation clearly impacts businesses via higher costs of production (labour, capital, raw materials and shipping prices have all increased sharply this year), the fact that the underlying demand has remained strong means that companies have been able to pass these costs through to customers.

To this point, profit margins have held in well at historically elevated levels, meaning that inflation-boosted top-line growth is flowing through to the bottom lines as well.

CHART 34: A MARGIN FOR ERROR

Profit margins, MSCI ACWI*
(percent)



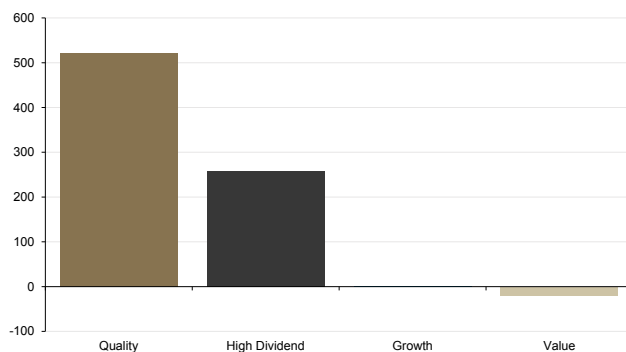
*MSCI ACWI=MSCI All Country World Index; source: Guardian Capital based on data from Bloomberg to July 22, 2022

Going forward, the ability to continue to exert pricing power will likely become of increasing importance to sustaining earnings — and supporting asset performance in the absence of a mark-up in valuations.

On that score, there would be support for exposure to the securities of high-quality companies that offer a layer of defense against a more adverse shift in economic conditions — their more dominant position within markets and industries provides pricing power that stands to protect margins and profitability, while low leverage provides insulation to higher interest rates. These traditionally perform well amid more uncertain and volatile environments.

CHART 35: QUALITY AMID VOLATILITY

MSCI World Style Index¹¹ return amid high volatility*
(basis point difference in annualized return versus MSCI World)

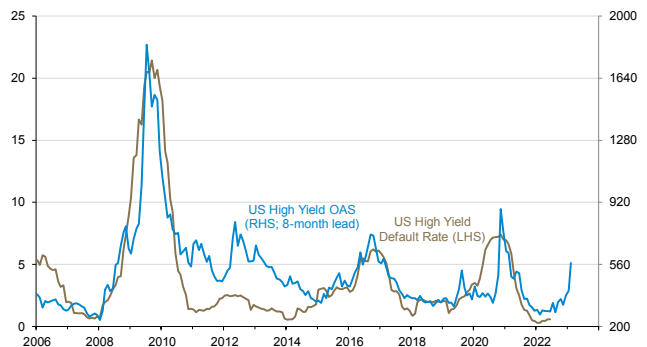


*based on monthly data since 1990 when equity volatility (CBOE equity volatility index or VIX) is above average; source: Guardian Capital based on data from Bloomberg to June 2022

In terms of credit, while it is the case that defaults currently remain historically muted and there is scope for the credit cycle to not become particularly harsh, rising rates and a downgraded economic outlook still suggest that lower-quality issuers will face rising pressures in the months ahead.

CHART 36: THE TREND IS NOT YOUR FRIEND

High Yield bond par-weighted default rate & OAS*, US
(basis point difference in annualized return versus MSCI World)

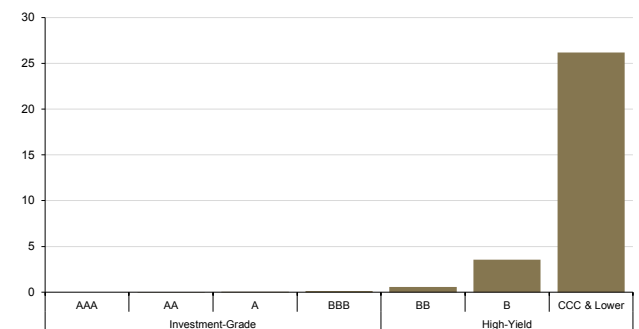


*OAS=option-adjusted spread; Source: Guardian Capital based on data from Bloomberg & Bank of America to June 2022

Investment grade corporate bond issuers, however, have historically offered negligible default risk while also showing less sensitivity to interest rates than government debt — the rise in yields and widening in credit spreads also point to increasingly compelling risk/reward trade-offs for the asset class.

CHART 37: DEFAULT SETTINGS

Average global default rate by credit rating, last 30 years
(percent)

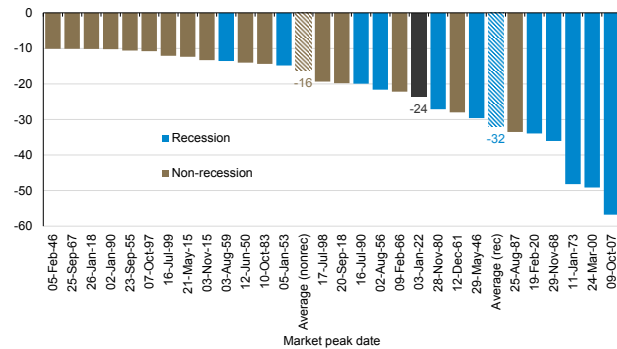


Source: Guardian Capital based on data from S&P Global Ratings¹² for the period ended December 2021

More generally, while there are clear and present downside risks, the magnitude of the damage done to this point would suggest that, barring an exogenous shock that further erodes the outlook, the bulk of the price adjustment may be done.

CHART 38: NEEDLE AND THE DAMAGE DONE

S&P 500 declines of 10% or more since World War II
(percent)

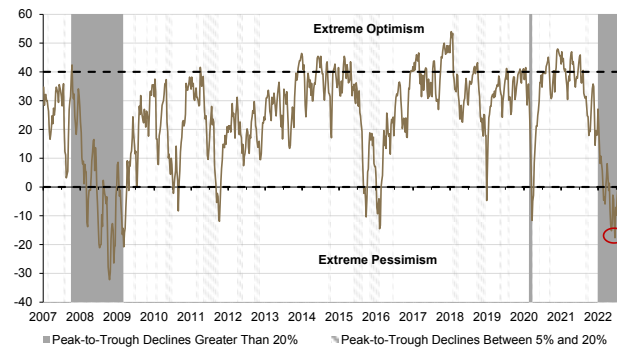


Source: Guardian Capital based on data from Bloomberg to July 22, 2022

Moreover, the abundant pessimism that is putting undue weight on a worst-case scenario materializing, arguably shifts the balance of risk in favour of potential upsides — “bad” outcomes may not end up being “as bad as feared” as the backstop provided by underlying strength of consumer and business finances and a general lack of material imbalances could limit the overall economic fallout.

CHART 39: DOWN IN THE DUMPS

Investors Intelligence bull-bear differential
(percentage points)



Source: Guardian Capital based on data from Investors Intelligence, Ned Davis Research, Wall Street Journal & Bloomberg to July 19, 2022

As such, despite the deterioration in the outlook in recent months, there is arguably scope for markets to see some gains in the months ahead in the absence of additional headwinds — however, the persistence of risks suggests that maintaining exposure to higher-quality assets and those with less dependence on the economic cycle could be prudent.

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- ¹ The Global Economic Policy Uncertainty Index is designed to measure policy-related economic uncertainty based on research from Baker, Bloom and Davis (2016), *Global Economic Policy Uncertainty Index*, https://www.policyuncertainty.com/global_monthly.html.
- ² The Citi Economic Surprise Index measures the pace at which economic indicators are coming in ahead of or below consensus forecasts. When the index is negative, it means that the majority of reports are coming in below expectations, while a positive reading indicates that most data is coming in ahead of expectations.
- ³ OECD+ is an aggregate including the 36 OECD economies and six major non-member economies (Brazil, China, India, Indonesia, Russia and South Africa).
- ⁴ The Purchasing Managers Index (PMI) is a measure of the prevailing direction of economic trends in manufacturing; a monthly survey of purchasing managers to determine whether business conditions are improving, unchanged, or deteriorating compared to the previous survey. A level above 50 represents improving conditions, while a level below 50 represents deteriorating conditions, and a level of 50 represents no change from the previous survey period.
- ⁵ The Global Supply Chain Pressure Index is composite of 27 variables designed to provide a more comprehensive summary of potential disruptions affecting global supply chains. The index is normalized such that a zero indicates that the index is at its average value with positive values representing how many standard deviations the index is above this average value (and negative values representing the opposite). Federal Reserve Bank of New York, *Global Supply Chain Pressure Index*, <https://www.newyorkfed.org/research/gscpi.html>.
- ⁶ The Drewry World Container Index consists of eight route-specific indices representing individual shipping routes and a composite index. All indices are reported in USD per 40ft Container.
- ⁷ The S&P Goldman Sachs Commodity Price Index serves as a benchmark for investment in the commodity markets and as a measure of commodity performance over time.
- ⁸ Statistics Canada, *Reconciling Canadian-U.S. measures of household disposable income and household debt*, November 27, 2015, <https://www150.statcan.gc.ca/n1/pub/13-605-x/2012005/article/11748-eng.htm>.
- ⁹ CEO Economic Outlook Index, a composite index of CEO plans for capital spending and employment, and expectations for sales over the next six months.
- ¹⁰ The MSCI ACWI is a market capitalization weighted index of equities in both Developed and Emerging Markets.
- ¹¹ The MSCI factor/style indexes are rules-based indexes that capture the returns of systematic factors that have historically earned a persistent premium over long periods of time – such as Value, Low Size, Low Volatility, High Yield, Quality and Momentum and Growth.
- ¹² S&P Global Ratings, Default, Transition, and Recovery: 2021 Annual Global Corporate Default And Rating Transition Study, <https://www.spglobal.com/ratings/en/research/articles/220413-default-transition-and-recovery-2021-annual-global-corporate-default-and-rating-transition-study-12336975>.

Market Returns at June 30, 2022 All returns in CAD.

CANADIAN EQUITIES

INDEX RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
S&P/TSX Composite	-8.7	-13.2	-9.9	-3.9	7.6	8.2
S&P/TSX 60	-8.3	-12.6	-9.6	-2.4	8.5	8.9
S&P/TSX Completion	-10.2	-15.3	-10.9	-9.1	4.7	5.9
S&P/TSX SmallCap	-13.4	-20.8	-14.2	-13.8	3.4	4.3
S&P/TSX Composite High Dividend	-9.1	-9.2	1.3	9.8	8.8	8.4
S&P/TSX Composite Dividend	-8.3	-11.1	-3.9	4.8	8.4	9.0

S&P/TSX SECTOR RETURNS (%)

Communication Services	-5.7	-8.8	-0.7	4.8	7.3	10.0
Consumer Discretionary	-6.1	-10.2	-17.1	-16.5	4.0	11.5
Consumer Staples	-5.7	-6.2	-1.1	11.5	8.7	14.8
Energy	-11.9	-1.9	26.2	37.1	8.0	4.5
Financials	-8.8	-13.1	-11.2	-1.8	8.4	11.4
Health Care	-18.0	-49.6	-53.9	-69.6	-22.4	-18.4
Industrials	-1.1	-12.7	-9.3	-1.1	10.2	13.8
Information Technology	-9.1	-30.7	-55.3	-56.5	13.7	17.8
Materials	-14.8	-23.6	-8.3	-4.2	7.1	1.3
Real Estate	-9.9	-17.8	-21.7	-11.6	5.2	8.1
Utilities	-2.9	-3.5	1.3	7.8	10.4	9.0

U.S. EQUITIES

INDEX RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
S&P 500	-6.4	-13.4	-18.3	-6.9	11.2	15.7
Dow Jones Industrial Average	-4.7	-7.9	-12.6	-5.3	9.8	14.4
NASDAQ	-6.9	-19.9	-28.0	-20.8	12.3	16.9
Russell 1000	-6.6	-13.9	-19.3	-9.4	10.9	15.5
Russell 2000	-6.4	-14.5	-21.8	-22.1	5.0	12.0
Russell 3000	-6.5	-14.0	-19.4	-10.3	10.5	15.3
Russell 1000 Growth	-6.1	-18.3	-26.5	-15.4	14.1	17.5
Russell 1000 Value	-6.9	-9.3	-11.0	-2.9	7.0	13.1

S&P 500 SECTOR RETURNS (%)

Communication Services	-5.9	-18.1	-28.7	-26.1	6.0	8.5
Consumer Discretionary	-9.0	-23.7	-31.4	-21.0	9.6	16.2
Consumer Staples	-0.6	-1.5	-3.6	11.1	8.6	13.3
Energy	-15.2	-2.1	34.6	45.8	6.9	6.8
Financials	-9.1	-14.8	-17.0	-9.0	7.1	15.2
Health Care	-0.7	-2.8	-6.4	7.7	12.0	17.7
Industrials	-5.6	-12.0	-15.0	-9.8	6.6	14.0
Information Technology	-7.5	-17.6	-25.4	-10.0	20.1	21.5
Materials	-12.1	-13.1	-16.1	-4.9	8.6	12.5
Real Estate	-5.1	-11.9	-18.3	-1.2	8.4	N/A
Utilities	-3.1	-2.0	1.6	19.1	9.6	13.1

INTERNATIONAL EQUITIES

INDEX RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
MSCI World Index (Net, C\$)	-6.8	-13.4	-18.8	-10.8	7.5	12.1
MSCI EAFE Index (Net, C\$)	-7.5	-11.7	-17.9	-14.3	2.1	7.9
MSCI ACWI (C\$)	-6.6	-12.9	-18.5	-12.2	6.9	11.4
MSCI France (C\$)	-8.6	-12.0	-20.5	-14.9	3.0	9.4
MSCI Germany (C\$)	-11.8	-15.5	-27.2	-28.3	-2.8	6.5
MSCI Japan (C\$)	-6.1	-11.8	-18.6	-16.6	1.6	8.1
MSCI UK (C\$)	-6.8	-7.5	-6.9	0.0	2.1	6.2
S&P/IFC Investable (Emerging Markets)	-4.9	-8.8	-16.0	-21.1	2.6	6.4
MSCI EAFE Growth (Gross, C\$)	-6.8	-14.0	-25.1	-20.3	3.7	9.2
MSCI EAFE Value (Gross, C\$)	-8.1	-9.2	-9.8	-7.6	1.0	7.3

INTERNATIONAL EQUITIES

MSCI EAFE SECTOR RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
Communication Services	-5.7	-8.0	-10.6	-17.4	-1.3	5.9
Consumer Discretionary	-5.9	-12.8	-25.4	-24.5	2.0	8.7
Consumer Staples	-2.4	-5.4	-13.6	-10.5	1.3	7.8
Energy	-10.4	-0.9	14.6	26.4	4.3	4.3
Financials	-7.2	-11.1	-13.0	-8.6	-0.7	7.3
Health Care	-3.1	-6.5	-11.0	-6.1	5.7	10.8
Industrials	-9.3	-15.8	-25.7	-21.2	1.5	8.5
Information Technology	-12.0	-21.0	-34.5	-27.1	5.5	12.0
Materials	-14.7	-18.5	-16.7	-15.2	5.7	7.6
Real Estate	-7.5	-13.0	-16.3	-17.6	-2.2	N/A
Utilities	-8.6	-8.9	-13.6	-8.5	3.6	6.8

Sources: Bloomberg Finance L.P., FTSE Bond Analytics, TD Securities, Thomson Financial

Market Returns at June 30, 2022 All returns in CAD.

CANADIAN FIXED INCOME

INDEX RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
FTSE Canada 91 Day TBill	0.1	0.1	0.3	0.4	0.9	0.8
FTSE Canada Short Term Overall Bond	-0.8	-1.5	-4.4	-4.8	0.9	1.4
FTSE Canada Mid Term Overall Bond	-1.9	-4.8	-11.3	-11.1	0.4	2.0
FTSE Canada Long Term Overall Bond	-4.4	-11.8	-22.1	-19.7	-1.0	1.9
FTSE Canada Universe Bond	-2.2	-5.7	-12.2	-11.4	0.2	1.7
FTSE Canada High Yield Overall Bond	-1.9	-5.0	-8.0	-6.9	3.9	5.2
FTSE Canada Real Return Bond Overall	-3.6	-8.9	-17.4	-12.3	0.7	0.9

SECTOR RETURNS (%)

FTSE Canada Federal Bond	-1.8	-4.2	-9.5	-9.2	-0.1	1.0
FTSE Canada Provincial Bond	-3.1	-7.7	-15.6	-14.3	-0.2	1.9
FTSE Canada All Corporate Bond	-1.5	-4.8	-11.0	-10.1	1.0	2.5

GLOBAL FIXED INCOME

INDEX RETURNS (%)	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
FTSE World Government Bond	-1.2	-5.9	-13.0	-13.3	-1.3	1.7

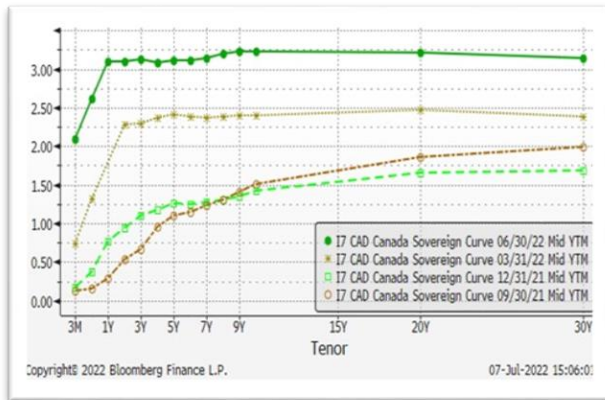
COMMODITY

	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
Bloomberg WTI Cushing Crude Oil Spot Price	-5.9	8.9	40.3	50.0	17.9	4.7
Bloomberg European Dated Brent BFOE Price	-2.1	11.5	51.7	59.5	18.8	4.1
Edmonton Crude Oil Syncrude Sweet Blend FOB Spot	-5.0	8.1	56.7	62.6	19.1	5.9
S&P GSCI Nat Gas Index Spot	-32.1	-0.7	48.5	54.8	12.2	9.3
S&P GSCI Copper Index Spot	-10.8	-17.7	-13.4	-8.2	6.7	3.1
S&P GSCI Gold Index Spot	-0.3	-4.5	0.9	6.3	7.6	3.6

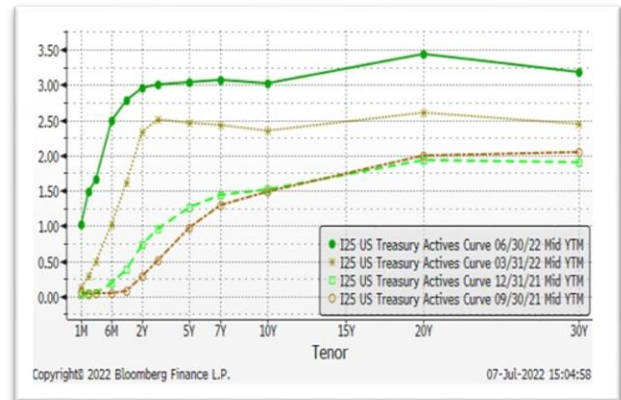
CURRENCY

	1 Mo	3 Mos	YTD	1 Yr	5 Yrs	10 Yrs
CAD/USD (% chg)	2.0	3.3	2.1	4.2	-0.1	2.4
CAD/Yen (% chg)	-3.4	-7.7	-13.4	-14.9	-3.9	-2.9
CAD/GBP (% chg)	-1.7	-4.7	-8.4	-8.4	-1.5	-0.2
CAD/Euro (% chg)	-0.5	-3.0	-6.1	-8.2	-1.9	0.4

GOVERNMENT OF CANADA YIELD CURVE



U.S. TREASURY YIELD CURVE



Sources: Bloomberg Finance L.P., FTSE Bond Analytics, TD Securities, Thomson

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