

Morningstar Managed Investments Program

Reallocation Memo – December 2020

Affected Portfolios:

- Conservative
- Moderate
- Balanced
- Growth
- Aggressive

Updates:

We are trimming our exposure to high yield bonds in several portfolios in favour of local currency emerging markets debt. Riskier fixed-income markets have rallied significantly since the height of the crisis in March. Credit spreads have tightened across the credit spectrum, and proportionately more so in high yield. Both segments maintain positive valuation implied returns, and we are taking the opportunity to rotate further into local currency emerging markets debt, where the recovery has lagged on a relative basis. Several emerging markets central banks have enacted new asset purchasing programs in response to the crisis, like the quantitative easing programs running in developed markets. While these have been more constrained than the developed markets programs, they should still provide some defense for taking on interest risk in these markets. Many emerging markets central banks cut rates aggressively going into the crisis, bringing overall policy rates to historic lows. This cycle has slowed down dramatically in recent months. Still, policy rates in the emerging markets complex remain meaningfully higher than their developed markets peers. From a real yield perspective, there continues to be dispersion across the complex. Select constituents are running negative real yields while several others offer quite attractive valuations, despite rate cuts, given how inflation has fallen. On average, emerging markets countries are clearly offering an attractive real yield pickup over developed markets.

We are introducing a new mandate in the portfolios, the Schwab Fundamental Emerging Markets Large Company ETF. The ETF focuses on large-cap stocks from emerging markets and weights them based on a combination of fundamental metrics such as leverage adjusted sales, retained operating cash flow and dividends plus buybacks giving it a pronounced value tilt. The construction methodology is a full replication of the underlying index, and it currently holds approximately 320 stocks, with the top 10 accounting for close to one quarter of the weight. The fund reconstitutes its holdings annually but rebalances a different fourth of its assets each quarter. We are sourcing this new position by trimming exposure to the Invesco Select Emerging Markets Equity Fund and reducing or eliminating exposure to the iShares MSCI South Korea Capped ETF. Both mandates have performed well this year, and we are taking the opportunity to reduce portions of the markets which have outperformed to move towards the more value-oriented sectors in this space, particularly energy and financial services.

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Mandate	Conservative			Moderate			Balanced			Growth			Aggressive		
	New Target	Prior Target	Change	New Target	Prior Target	Change	New Target	Prior Target	Change	New Target	Prior Target	Change	New Target	Prior Target	Change
Leith Wheeler High Yield Bond Fund (CAD Hedged)	2.00%	3.00%	-1.00%	1.50%	2.00%	-0.50%	1.50%	2.00%	-0.50%	0.75%	1.00%	-0.25%	0.00%	0.00%	0.00%
iShares JP Morgan EM Local Currency Bond	2.00%	1.00%	1.00%	1.25%	0.75%	0.50%	1.25%	0.75%	0.50%	1.00%	0.75%	0.25%	0.00%	0.00%	0.00%
Schwab Fundamental Emerging Markets Large Company ETF	0.50%	0.00%	0.50%	0.75%	0.00%	0.75%	2.00%	0.00%	2.00%	2.25%	0.00%	2.25%	2.00%	0.00%	2.00%
iShares MSCI South Korea Capped ETF	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	1.00%	-1.00%	0.50%	1.25%	-0.75%	1.00%	1.75%	-0.75%
Invesco Select Emerging Markets Equity	0.75%	1.25%	-0.50%	0.75%	1.50%	-0.75%	2.25%	3.25%	-1.00%	2.50%	4.00%	-1.50%	2.50%	3.75%	-1.25%

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Published December 18, 2020

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