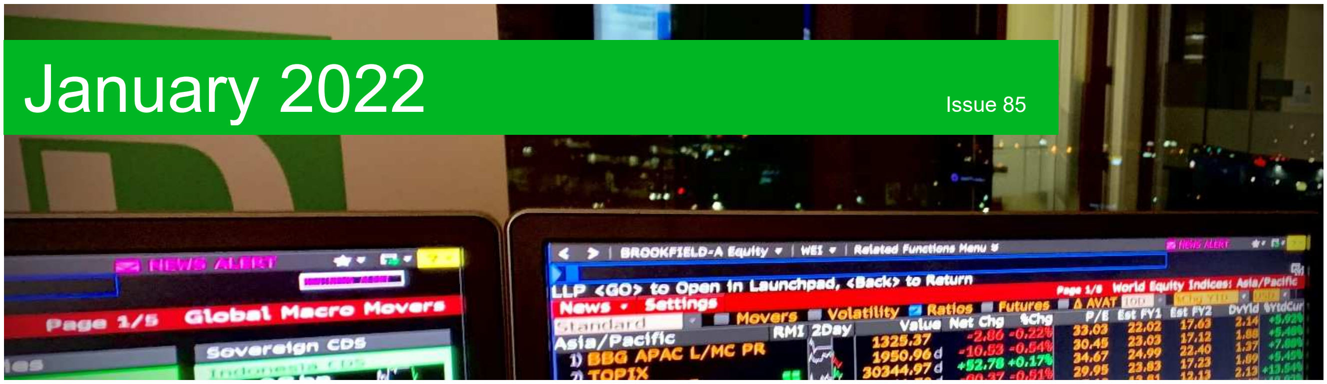
The Charter Group Monthly Letter

January 2022

Issue 85



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Economic & Market Update

Food Fight

Without trying to give too much away about my eating habits, I have spotted higher prices over the last year at both Starbucks and McDonald's.

Price sticker shock is becoming a more common occurrence at grocery stores and restaurants.

Too be honest, in the past I have not paid enough attention to food prices, but when the price of a venti-sized True North Blend coffee ticked over $3 last year, I started to notice.

In the case of Starbucks, the costs contained in a cup of coffee include labour, operations, the store building, packaging, and ingredients, among others. Of these, we know by watching the news that there are labour pressures in Canada. People are worried about working during the pandemic, some received government assistance, some looked at the pandemic as a chance to review life priorities that involved quitting previous employment, and some embraced the notion of early retirement.

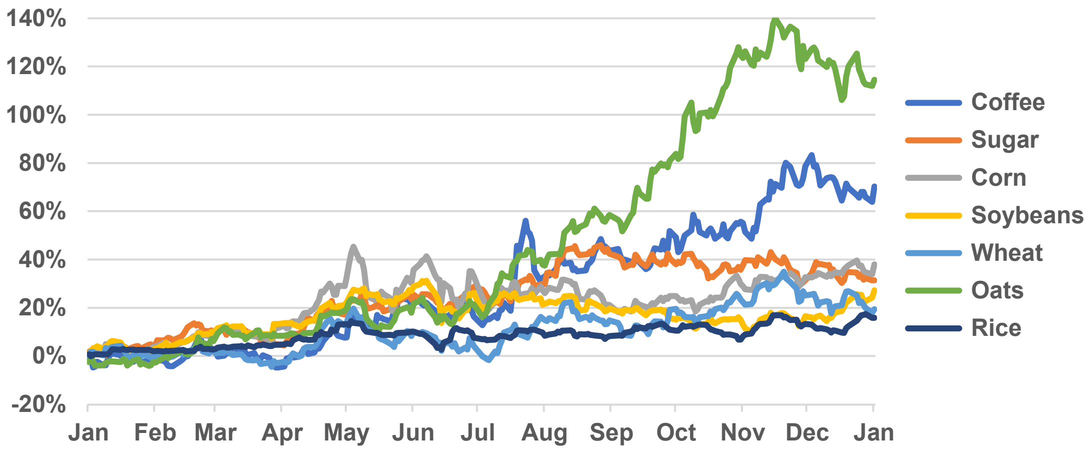
There has been a focus on rising labour costs causing this, but what about the costs of the ingredients that go into the food we eat?

All of this has reduced the labour supply. One very effective way of raising the cost of something is to reduce the supply of it. However, apart from rising labour costs, it is probably the increased costs of the ingredients that finally forced food retailers to begin passing on costs to you and me.

Many of those ingredients start off as basic commodities which have mostly seen significant price hikes over the previous 12 months (**Charts 1,2,&3**).

Chart 1:

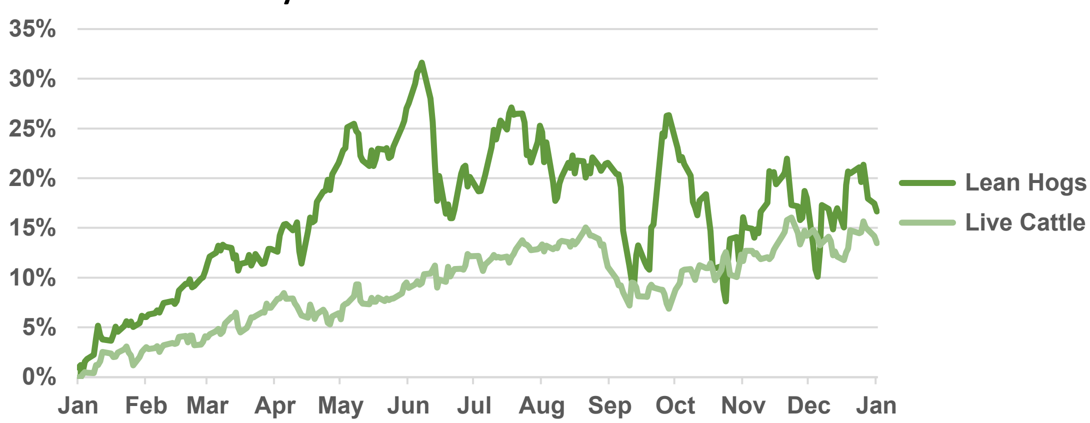
Food & Grains Commodity Futures Prices: One-Year Chart



Source: Bloomberg Finance L.P. as of 1/7/2022. The price on a particular date is the price of the nearest maturing futures contract on the following exchanges, Coffee: Intercontinental Exchange (ICE), Sugar: ICE, Corn: Chicago Board Options Exchange (CBOE), Soybeans: CBOE, Wheat: CBOE, Oats: CBOE, Rough Rice: CBOE.

Chart 2:

Livestock Commodity Futures Prices: One-Year Chart



Source: Bloomberg Finance L.P. as of 1/7/2022. The price on a particular date is the price of the nearest maturing futures contract on the Chicago Mercantile Exchange (CME).

A big story of 2021 was the rising prices of food commodities compared to previous years when they didn't move much, including during the Commodity Super-cycle of 1998-2012.

Before jumping further into this subject, I just want to be clear that I am not talking about *all* commodities. What we have seen over the last year differs significantly from the "Commodity Super-cycle" that we saw from 1998-2012. That was driven by the explosive economic growth in People's Republic of China (PRC) added to the overall global demand for raw materials and energy. Except for a few instances overseas, we didn't see much general inflation from this. The increasing efficiencies from technology, further offshoring to lower-cost labour jurisdictions, and a comparatively peaceful global geopolitical environment ameliorated things, keeping the prices for goods, services, and food relatively stable over those years.

Chart 3:

CRB Foodstuff Spot Price Index: One-Year Chart

Source: Bloomberg Finance L.P. as of 1/7/2022. Also, Commodity Research Bureau and Barchart.com.

Also, this time around, not all energy and raw material commodities are rising like they did during the Super-cycle. A few have been lambasted by supply-chain disruptions globally or by demand fluctuations in the PRC. Last year saw peak-to-trough declines in natural gas futures of -44%, iron ore futures of -48%, in lumber futures of -73%.[1]

So, what drives the prices of food commodities and where might prices go in the future?

Was it because of the weather?

Weather is a huge factor and there was no shortage of weather-related stories in the news during 2021. However, the weather across the continental U.S. (including the "seasonal" crop-growing regions) was not much different than the previous five-year average over which crop prices were lower (**Charts 4&5**). There was drought in the U.S. southwest, but that region has predominantly "permanent" crops (no need for replanting every year) for which there are few futures contracts available to gauge current and historical pricing.

Despite the wild weather stories in the news, overall last year looked much like the previous five years, and food commodity prices didn't rise then.

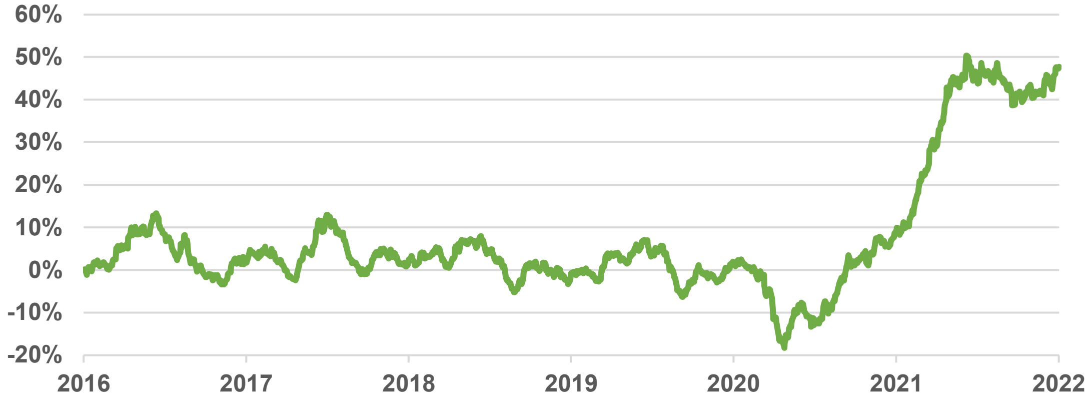
Coffee and orange juice are exceptions that are "permanent" crops with futures contracts. There was both a drought *and* frost damage in Brazil which crimped global coffee supply, added to price pressures. So, there was probably a "weather factor" involved in making my venti True North Blend more expensive in addition to Starbucks' other increased costs. However, despite the Brazilian weather, and despite the extreme weather events on the news, in the U.S. overall (**Chart 5**) and across the world, it was basically an average

[1] Source: Bloomberg Finance L.P. as of 1/7/2022. In U.S. dollar terms.

weather year for agriculture. If climate change does impact food going forward, that would likely be *on top* of the current pricing and exasperate the food inflation problem further!

Chart 4:

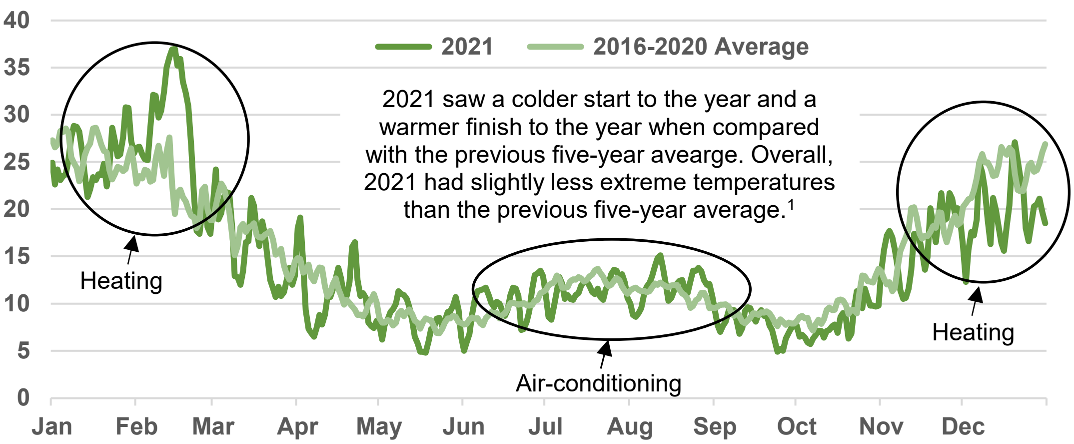
CRB Foodstuff Spot Price Index: Five-Year Chart



Source: Bloomberg Finance L.P. as of 1/7/2022, Also, Commodity Research Bureau and Barchart.com.

Chart 5:

Heating & Cooling Energy Usage - Continental U.S.



Source: Bloomberg Finance L.P. as of 1/7/2022. The chart represents the sum of Heating & Cooling "Degree Days" for 74 U.S. cities. The "Degree Days" are averaged over the 74 cities and is unadjusted for population so that the more densely populated Northeast doesn't overwhelm the statistics. As a result, it is more of an indication of the general weather for the U.S. as opposed to an indication of total absolute heating and cooling energy usage.

1 The averaged sum daily total of Heating & Cooling Degree Days for 2021 was 14.41 versus 14.71 for the 2016-2020 period average. The reason why the chart line for 2021 is more choppy than the chart line for 2016-2020 is because the latter is an average for each particular date over the last five years. The averaging itself creates a smoothing effect.

More than weather events during 2021, the pandemic was likely the main culprit behind rising food commodity prices. Transportation labour shortages, container shortages, rising shipping fuel costs were issues that we saw in 2021 that we didn't see in the previous five years and impacted the prices for goods that we buy. They also impacted the price of the food that we buy. Unfortunately, those imbalances may not dissipate soon.

More than the weather, it was likely the supply-chain disruptions impacting the prices of the other goods we buy that were also contributing to the increase in food commodity prices.

Model Portfolio Update[2]

The Charter Group Balanced Portfolio
(A Pension-Style Portfolio)

	Target Allocation %	Change
Equities:		
Canadian Equities	12.0	None
U.S. Equities	38.0	None
International Equities	8.0	None
Fixed Income:		
Canadian Bonds	22.0	None
U.S. Bonds	6.0	None
Alternative Investments:		
Gold	8.0	None
Silver	1.0	None
Commodities & Agriculture	3.0	None
Cash	2.0	None

There were no changes to the asset allocations or the investment holdings in our model portfolios during December.

Despite the lagging performance in precious metals and bonds, the model portfolios saw their best results annual results in almost a decade. Stocks continued to benefit from government financial assistance plus the liquidity provided by central banks in most of the developed countries around the world.

Beginning in the autumn of 2020 and continuing through most of the year in 2021, it felt as though investors were migrating to the positions and themes contained in our model portfolios. Much of this was likely driven by the realization that the next decade won't resemble the previous decade when it comes to economics and geopolitics, and how those factors might impact the investments markets going forward.

No changes in the model portfolios during December.

A very positive year despite lagging performance from precious metals and bonds.

The model portfolios seemed to capture a slow transition from the winning stocks of the last decade to those that might be the stars of the next decade.

[2] The asset allocation represents the current *target* asset allocation of the Balanced Model Portfolio as of 1/7/2022. The asset allocations of individual clients invested in this Portfolio may differ because of the relative performance of the asset classes since the last rebalancing and because of differences in the timing of deposits and withdrawals. The Balanced Model Portfolio is part of a sequence of five portfolios ranging from conservative to aggressive: Conservative, Balanced Income, Balanced, Balanced Growth, and Growth.

Two of the themes that weren't being sufficiently addressed, in my view, were the on-going significance of the Baby-Boom generation (the need for increased healthcare delivery) and the dilemma of powering the expected tsunami of electric vehicles hitting the roads over the next decade (the need for nuclear energy to supplement alternative energy production). Hopefully the stocks we have in the model portfolios will be able to capture continued upside as these themes are embraced by more investors.

The themes of the Baby-boom demographic as well as reliable power have note received much attention, but that may be changing.

Separately, and from a general perspective, many investors don't seem ready to accept that we may not be going back to the interest rate landscape that we saw over the last dozen years. That landscape was crucial to driving the success of many businesses that have become household names. Lower cost for credit enabled these companies to expand, and enabled consumers to buy more of the resulting goods and services. Many of those household names are still attracting capital, but things might be in the late innings. What happens if higher sustained interest rates drive investors instead towards companies that are less dependent on credit *and* which sell goods that are less dependent on consumers being able to get credit? Could that be the investment story of 2022?

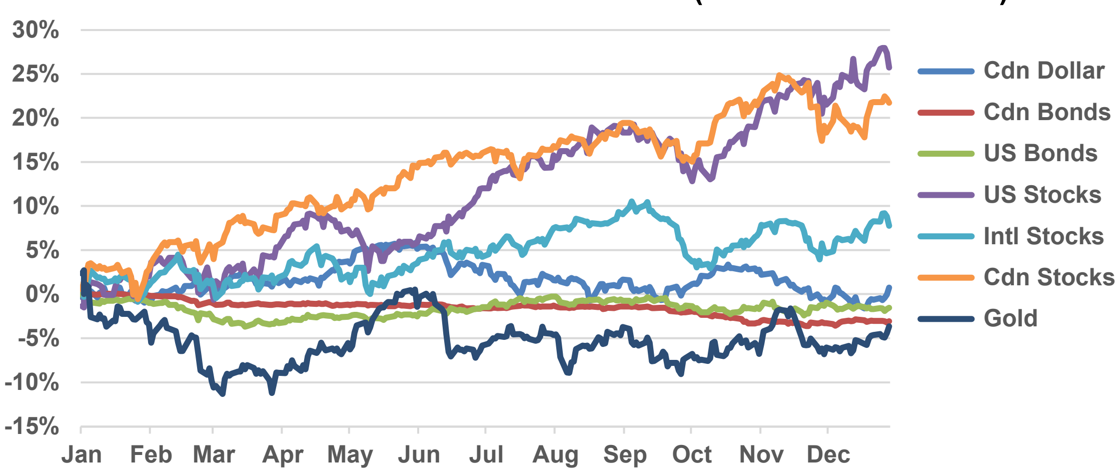
Investors are still grappling with the possibility that the cost of credit may be higher going forward.

This will impact both companies and consumers, and present new investment risks and opportunities.

Below is the 12-month performance of the asset classes that we have used in the construction of The Charter Group's model portfolios. (**Chart 6**).[3]

Chart 6:

12-Month Performance of the Asset Classes (in Canadian dollars)



Source: Bloomberg Finance L.P. for the interval from 1/1/2021 to 12/31/2021

[3] Source: Bloomberg Finance L.P. – The Canadian dollar rate is the CAD/USD cross rate which is the amount of Canadian dollars per one U.S. dollar; Canadian bonds are represented by the current 3-year Government of Canada Bond; US bonds are represented by Barclays US Aggregate Bond Index; U.S. stocks are represented by the S&P 500 Index; International stocks are represented by the MSCI EAFE Index; Canadian stocks are represented by the S&P/TSX 60 Composite Index; Gold is represented by the Gold to US Dollar spot price.

Top Investment Issues[4]

Issue	Importance	Potential Impact
1. U.S. Fiscal Spending Stimulus	Significant	Positive
2. Coronavirus Geopolitics	Moderate	Negative
3. Canadian Dollar Decline	Moderate	Positive
4. Short-term U.S. Interest Rates	Moderate	Positive
5. Canadian Federal Economic Policy	Moderate	Negative
6. China's Economic Growth	Moderate	Negative
7. Deglobalization	Medium	Negative
8. Global Trade Wars	Medium	Negative
9. Canada's Economic Growth (Oil)	Light	Positive
10. Long-term U.S. Interest Rates	Light	Negative

[4] This is a list of the issues that we currently deem to be the ten most important with respect to the potential impact on our model portfolios over the next 12 months. This is only a ranking of importance and potential impact and *not* an explicit forecast. The list is to illustrate where our attention is focused at the present time. If you would like an in-depth discussion as to the potential magnitude and direction of the issues potentially affecting the model portfolios, I encourage you to email me at mark.jasayko@td.com or call me directly on my mobile at 778-995-8872.

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The Charter Group is a wealth management team that specializes in discretionary investment management. For an annual fee, we manage model portfolios for private clients and institutions. All investment and asset allocation decisions for our model portfolios are made in our Langley, B.C. office. We do not outsource any of the decision-making for our model portfolios – there are no outside actively-managed products or funds. We strive to bring the best practices and the calibre of investment management normally seen in global financial centres directly to the Fraser Valley and are accountable for the results.

Accountability is further enhanced by the fact that we commit our own investable wealth to the same model portfolios in which our clients are invested.

The information contained herein is current as of January 7, 2022.

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