Accilent Quarterly Commentary

Q3 2021.

QUARTERLY BY ACM INVESTMENT COMMITTEE

THE TREND IS YOUR FRIEND….UNTIL IT'S NOT.

The title of our commentary this quarter is "The Trend is your Friend…until it's not". It's an old saying by Proprietary Traders borrowing from the adage to "swim against the current". Admittedly though, I added the, "…until it's not", which I think is quite apropos when it concerns our current circumstances. Sometimes the inertia of the markets can have a life of its own and can propel the market to new highs, beyond the expectations of rationale expectations. Resulting in distortions until there's a breaking point.

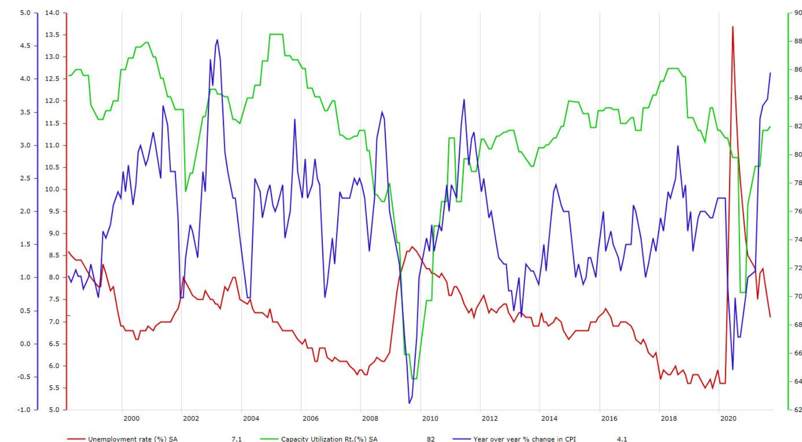
1987 had a similar feel to it, right before what's known by many as the Flash Crash. The mechanisms of sell-off can tend to take on different forms each time but the bubble prior to the pop always exhibits some kind of excess. In 1987s pull-back a strategy called "portfolio insurance" and automated "stop loss" orders were the main culprit of the severe one-day correction. As stocks fell, they triggered automated selling, pre-set at lower levels, culminating in a snowball effect.

Leading up to that point, however, global growth was slowing, inflation was climbing higher, a few bellwether companies hadn't produced the expected earnings, many portfolios were well above water and real estate was witnessing a boom like no other – there was excess, much like today.

ECONOMY

Canada:

Despite facing the uncertainty that always comes with an election and news of two of the largest developers in China being on the verge of collapse, the Canadian economy added to strong numbers coming out of Q2. COVID infections continued drop and more of the economy returned to something that resembled an old normal. Although, a good chunk of the service sector is still hindered by social distancing regulations at the local level. New headwinds are arising, as we always suspected they would in the guise of higher prices - inflation. Investors and corporate boards have had to rethink the sustainability and stability of hard-won gains in bottom line earnings and economic growth.

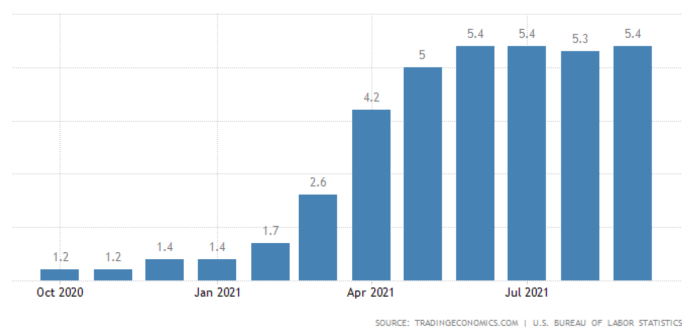


For the most part, many took solace in seeing further reductions in the unemployment rate in Canada – falling to 7.1% down from 8.2% almost 3 months ago. Troubling though, is year-over-year inflation has now increased to 4.1%. We see no sign yet of it slowing down, despite central bankers telling us these increased pricing levels are "transitory" and that lower inflation is coming. More Canadians are

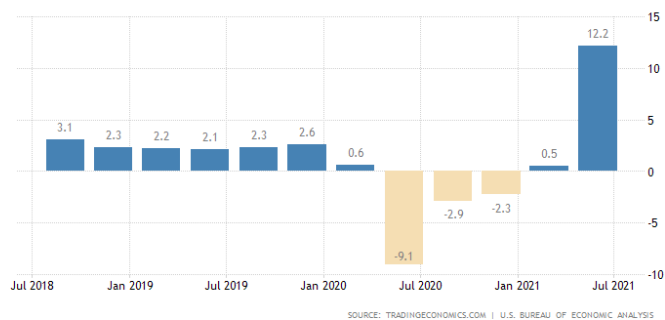
indeed back to work but they are facing a new economic landscape where their earnings are amounting to less real buying power and the spectre of higher interest rates will also way heavily on the real estate market. The Central Bank of Canada has made clear that Quantitative Easing will be withdrawn in 2022 and interest rates will begin to rise. This does not bode well for those holding bond portfolios with maturities more than a few years.

US:

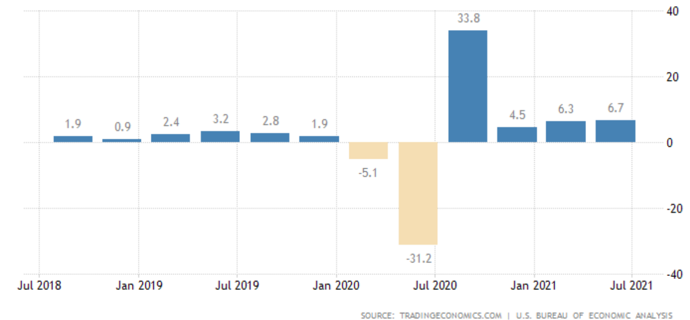
The story on investors' minds as we head into the ending months of 2021 is inflation. The annual inflation rate in the US edged up to a 13-year high of 5.4% in September. As the following chart shows, the rise in inflation in 2021 has been dramatic, almost quadrupling from the annualized rate of 1.4% in January.



To note, GDP growth has held strong as well, at 12.2% annualized as of the end of June.



Thus far then, real GDP is holding up in the 6.7% range based on best estimates for Q2.



Interestingly, consensus forecasts for Q3 Real GDP have declined sharply, from 6.7% previously to 3.2%. This suggests the consensus view may be that inflation will persist while nominal growth begins to return to more normal levels.

Calendar		Actual	Previous	Consensus
2021-06-24	Q1	6.4%	4.3%	6.4%
2021-07-29	Q2	6.5%	6.3%	8.5%
2021-08-26	Q2	6.6%	6.3%	6.7%
2021-09-30	Q2	6.7%	6.3%	6.6%
2021-10-28	Q3		6.7%	3.2%

SOURCE: TRADING ECONOMICS; U.S. BUREAU OF ECONOMIC ANALYSIS

If the current consensus for Q3 turns out to be accurate, investors will likely be disappointed, and look to the Fed to make things better. But the Fed will face an interesting dilemma if higher inflation numbers persist while at the same time the economy shows signs of slowing.

PORTFOLIOS AND THE MARKETS

Inflation worries and debt repayments…

The U.S. stock market as measured by the S&P 500 Index returned 2.79% for the 3 months ending September 30th and is up 14.90% for

the year. Returns have held up despite a rocky September, which saw a decline of 4.44% for the index. It was a month with talk of higher inflation and hints of an admission by the Fed that it may not be as transitory as initially thought, along with forecasts of slower growth and a rising 10-year Treasury yield, these items did not sit well with investors. Since October however, many companies are reporting earnings above expectations, and markets have recovered and seem poised to eclipse previous high marks.

Unprecedented amounts of money printing by the Fed and direct payments by the government are undoubtedly helping to sustain this market. Ultra-low interest rates continue to feed a T.I.N.A. (there is no alternative) mentality, and it seems that less and less thought is going into valuation. Hedge fund legend David Einhorn recently warned that he believes investors aren't doing their homework. He is predicting stubborn inflation, in part to blame on the private sector allocating too much capital to fast-growing technology companies, and not enough to companies that manufacture goods and supply more traditional services. Should this continue, supply shortages may become long-lived.

Sticking with a fundamental and quantitative approach that puts a reasonable valuation on the future cash-flows of a company that are likely to occur, and able to flow to shareholders and reinvestment, is as important as it has ever been. Referencing the large amounts of capital being allocated to fast-growing technology companies, the question becomes, "How likely is it that the fast growth will come to fruition?" And if it does not, where will the cash flows come from that will justify today's stock prices? As an example, a newer electric car manufacturer's stock is selling for 127 times the consensus earnings estimates, while the stock of one of the worlds' premier car manufacturers of all time (which will, by the way, sell lots and lots of electric cars), is selling for 7 times the consensus earnings estimates. The tide is in and high at the moment when it comes to the up-and-comers. Someday the tide will recede, and as Warren Buffett famously mentioned, that's when "you discover who's been swimming naked."

Evergrande and Fantasia, amongst some of the largest real estate promoters in the world, are facing insolvency. The elevated risk of default was embodied in volatile trading, resulting in lower markets. Should both fail, the impact would be felt globally as, 40% of all Chinese household's assets are real estate, banking exposure may precipitate another credit crisis and construction is almost 25% of China's GDP.

INDEX VALUES, AS AT; Sep 30 2021			**RETURNS**		
Market	**MTH-END**	**QTR-END**	**MTH-END**	**% QTR**	**YTD %**
S&P 500	4298	3973	4298	8.18%	14.40%
JAPAN - NIKKEI 225	28792	29179	28792	-1.33%	4.90%
UNITED KINGDOM - FTSE 100	7037	6714	7037	4.81%	8.90%
MSCI EAFE (LOCAL CURRENCY)	1305	1255	1305	3.98%	11.20%
MSCI WORLD (LOCAL CURRENCY)	2598	2245	2598	15.72%	31.40%
MSCI EMERGING (LOCAL CURRENCY)	3017	2812	3017	7.29%	12.20%
S&P/TSX COMPOSITE INDEX	20166	18701	20166	7.83%	15.70%
S&P/TSX COMPOSITE INDEX (Total Return)	74882	68987	74882	8.55%	17.30%
CDN UNIVERSE REFINITIV BONDS				1.90%	-3.80%
GOLD (COMEX)	1765	1705	1765	3.56%	-7.00%

Despite the volatile September, most markets posted positive returns for the quarter, with the only exception being Japan's which finished the quarter in negative territory. Both Gold and Bonds advanced to post positive gains, however, they are both still negative for the year. It's our view that bonds have an inordinate amount of risk given we are headed for higher interest rates, and certainly higher inflation.

The three sectors with the largest gains in Canada were Energy, Technology and Financials. The greening of the global economy is in some way responsible for the spike in traditional energy resource

prices. Europe's green initiatives have resulted in a shortage of power being created and a heavier reliance on natural gas and oil.

Market	Sep-21	Jun-21	YR-END	% QTR	%MTH
S&P / TSX Composite	***20166***	***18701***	***17433***	7.83%	2.20%
Energy	***1989***	***1767***	***1488***	12.56%	5.80%
Materials	***2908***	***2731***	***2944***	6.48%	-6.40%
Industrials	***4364***	***4370***	***4112***	-0.14%	0.00%
Consumer Discretionary	***2935***	***2819***	***2517***	4.11%	0.00%
Consumer Staples	***5937***	***5627***	***5507***	5.51%	1.20%
Health Care	***332***	***376***	***273***	-11.70%	0.80%
Financials	***3399***	***3165***	***2808***	7.39%	0.50%
Information Technology	***1085***	***882***	***892***	23.02%	18.20%

With the general decline in production of these two commodities, related to COVID, ion conjunction with, government imposed green regulations, supply fell short which propelled these commodities to multi year highs.

MANDATE RETURNS (Before Fees*)						
	3mos	6mos	1yr	3yr		Vol
INCOME	0.83%	5.82%	12.56%			4.66%
CONSERVATIVE	0.50%	4.66%	10.78%	7.28%		5.70%
BALANCED	0.34%	4.88%	11.46%	7.19%		6.37%
GROWTH	0.12%	4.79%	12.94%	7.51%	6.74%	7.41%

*before fees

Our mandates responded well this quarter despite the sharp downturn in September. Chief among them is the Income Mandate, with a greater focus on dividend producing securities, it weathered the volatility in September best. This focus on cash-flow in portfolios will be for us a major component of every portfolio at least for the foreseeable future.

ASSET CLASS BENCHMARKS						
XSB	-0.90%	-1.40%	-1.49%	2.49%	1.45%	1.57%
Equity-TSX	0.10%	8.76%	28.26%	11.19%	9.65%	14.21%
ALT - PSP	4.01%	7.76%	36.26%	15.90%	13.38%	19.17%
BENCHMARKS MIXES						
INCOME	-0.90%	-1.40%	-1.49%	2.49%		1.65%
CONSERVATIVE	-0.59%	1.59%	6.82%	5.39%		4.75%
BALANCED	-0.38%	3.61%	12.65%	7.19%		7.71%
GROWTH	-0.23%	5.14%	17.18%	8.47%	6.78%	9.37%

Relative to our benchmarks, we're confident our risk measures will protect against an inevitable downturn in the coming quarters. Part of that view manifested itself in September when we decided to rebalance portfolios to raise cash – on average to 10% in portfolios. We viewed the volatitlity as an opportunity to crystalize gains in APO (APOLLO GLOBAL MGMT), CNQ (CANADIAN NATURAL RESOURCES) and SU (SUNCOR). We remain vigilant in deploying those funds in positions which will soften any downswing in the coming months.

Should you have any questions related to our services, your account, or this commentary, please do not hesitate to contact your Portfolio Managers Mark Taucar (905)-715-2260 or John Lombard (905)-484-3482.

This communication is intended for information purposes only and does not constitute an offer to sell or a solicitation to buy securities. No securities regulatory authority or regulator has reviewed or assessed the merits of the information provided. This communication is not intended to assist you in making any investment decision regarding the purchase of securities. Rather, Accilent Capital has prepared relevant documents for delivery to prospective investors that describe certain terms, conditions and risks of investment and certain rights that you may have. You should review all relevant documents with your professional adviser(s) before making any investment decision.

This report may have forward looking statements. Forward looking statements are not guarantees of future performance as actual events.

While every effort has been made to ensure the correctness of the tables, graphs – all data. Accilent Capital does not warrant the correctness, completeness or accuracy of financial data in this publication.