Equity Income Guided Portfolio

Quarterly report

Wealth Management
Dominion Securities

March 1, 2024 | Portfolio Advisory Group – Equities

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All values in Canadian dollars and priced as of Feb. 29, 2024, market close, unless otherwise noted.

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Canadian households are clamping down on spending

Inflation is slowing, but we don't expect central banks to cut rates until H2 2024

RBC Economics believes the ongoing slowdown in Canadian consumer discretionary spending continues to slow mainly due to higher debt payment obligations. Canadians continued to buy fewer discretionary goods and pared back spending on discretionary services. Discretionary services spending has softened each month since September 2023, other than in November prior to the holidays. Inflation-adjusted spending on hotels has been trending lower ever since the summer travel boom ended. Restaurant spending has also cooled off following the lead-up to the holiday season. The Canadian economy continues to be propped up by population growth. According to RBC Economics, real per capita retail sales (excluding autos) have declined for six consecutive quarters as of Q4.

RBC Economics expects Canadian Q4 GDP growth to remain in positive territory with a small, annualized increase of 0.5%. That outcome would prevent the economy from seeing two consecutive quarters of contraction, which is often used as the definition of a "technical" recession. But when measured against the country's rapid population growth, it's the sixth straight quarterly decline on a per-capita basis, alongside a rising unemployment rate.

Persistent upside surprises on the U.S. economy, including an extremely strong reading for Q3 GDP growth and strong job numbers in January, reinforced RBC Economics' view that it might take a longer period of restrictive monetary policy to get inflation in the U.S. sustainably back under control, delaying but not preventing an economic slowdown, in our opinion.

Canadian households are also feeling the impact of higher mortgages due to shorter fixed-rate mortgages, usually five years, compared with 30-year fixed-rate mortgages in the U.S. The weaker labour market in Canada resulted in a consumer spending slowdown relative to the U.S.; therefore, we want to maintain exposure to companies that have operations in the U.S.

The Canadian inflation outlook is still murky, according to RBC Economics, but inflation in January slowed to 3.2% from 3.4% in December on a year-over-year basis. The first Consumer Price Index report in 2024 came in softer than RBC Economics expected; while the breadth of inflation is still showing signs of a gradual easing, it is still wider than what would be consistent with the Bank of Canada's (BoC) 2% target. Shelter inflation will remain sticky, in our view, as higher interest rates feed through to mortgage interest costs with a lag and an undersupply of housing continues to boost rent prices. We think the most likely path for inflation going forward is still lower, with per-capita GDP and consumer spending continuing to decline. But we believe a strong start to 2024 for labour markets gives the BoC more leeway to wait for firmer signs that inflation is getting back under control before pivoting to interest rate cuts.

While inflation pressures have eased substantially and, in some cases, more than RBC Economics expected, they've not receded completely. Mindful of those risks and the potentially large negative impact from a policy error, central banks will be wary about cutting rates prematurely. In our view, a moderately weaker economic backdrop is more likely to be viewed by central banks as necessary to bring inflation fully back to target than something that would prompt immediate rate cuts.

According to RBC Economics, central banks kicked off the first round of policy meetings in 2024 by reinforcing that additional interest rate hikes won't likely be necessary, while at the same time stressing that it's too early to pivot to outright rate cuts. While inflation readings have been broadly moving lower, RBC Economics continues to expect patience from policymakers, and anticipates the BoC and U.S. Federal Reserve to make their first cuts in Q2 (June), with the Bank of England to follow in Q3 (August). RBC Economics anticipates the BoC to lower the overnight rate to 3%, and for the U.S. fed funds range to be at 3.25%–3.5% sometime in 2025.

RBC Economics' expectation that the BoC and the Fed will start cutting rates around the same time this year stems from two factors. First, the two countries have seen very similar progress with inflation over the past year. And secondly, the Fed has historically been more reactive at the turns of rate cycles, and we think it would have likely already acted if the U.S. economic backdrop looked like Canada's soft conditions. A similar flight path to rate cuts, on both sides of the border, should not result in material movement in the foreign exchange rate of the Canadian dollar vis-à-vis the U.S. dollar.

We are cognizant that the economy is in the early stages of what we continue to expect to be a shallow recession over the next 12 months, and we believe the Canadian equity market is partially reflecting this risk. We have noted a slowdown in dividend growth expectations from management teams in all sectors, with perhaps the exception in the oil patch, and have strived to balance the Portfolio between higher-dividend-yielding stocks and those that we think have the potential to increase their dividends over the near term.

Total return for the winter quarter (12/1/23–2/29/24)

	Total return
Equity Income Guided Portfolio	6.64%
S&P/TSX Composite Index	6.39%
S&P/TSX High Dividend Index	4.66%

Note: Past performance is no guarantee of future results and should not be viewed as an indicator of future results.

Source - FactSet

A falling interest rate environment should be beneficial for dividend portfolios, in our opinion. However, stronger-than-expected GDP and job growth in the U.S. has resulted in a rise in the U.S. 10-year Treasury bond yield, but the highs recorded in October 2023 have not yet been tested. However, we have noticed the pullback in the Canadian 10-year government bond yield due to weaker economic data. As interest rates fall, we expect the traditional defensive sectors (Consumer Staples, Utilities, Communication Services, and REITs) should outperform the broader S&P/TSX Composite Index.

We maintained our exposure to interest-rate-sensitive sectors to take advantage of falling interest rates and to reduce our exposure to slowing consumer spending. However, we continue to balance the Portfolio so it can benefit from an eventual recovery in the economy while not being overly exposed to high-growth stocks that are usually accompanied with higher valuations. In general, stock markets tend to start heading higher approximately five months before the end of a recession.

Performance

The Equity Income Guided Portfolio generated a total return of 6.64% for the quarter, outperforming the S&P/TSX High Dividend Index and the S&P/TSX Composite Index by 198 and 25 basis points, respectively.

From an attribution point of view, Utilities, Industrials, and Financials were the best-performing sectors during the quarter. On the flip side, the Consumer Discretionary, Energy, and Real Estate sectors were relative laggards.

Portfolio positions

						EPS/AFFO/CFPS			Price to earnings/ AFFO/CFPS				Payout ratio			Forecast growth in EPS/ AFFO or CFPS	Forecast dividend growth rate to 2025
Symbol	Company name	Weight	Market cap (M)	Price 2/26/24	52-wk range	2023A/E	2024E	2025E	2023A/E	2024E	2025E	Div. yield	2023A/E	2024E	2025E		
Interest sensitive																	
CM	Can. Imp. Bank of Commerce	2.5%	$58,488	$62.81	64 - 47	$6.72	$7.03	$7.54	9.3x	8.9x	8.3x	5.56%	51%	51%	49%	5%	5%
BMO	Bank of Montreal	5.0%	$91,442	$126.83	132 - 103	$11.81	$12.54	$13.22	10.7x	10.1x	9.6x	4.76%	49%	49%	48%	6%	5%
BNS	Bank of Nova Scotia	2.5%	$77,541	$63.87	72 - 55	$6.54	$6.70	$7.51	9.8x	9.5x	8.5x	6.64%	64%	64%	60%	2%	7%
RY	Royal Bank of Canada	5.0%	$185,562	$132.32	139 - 108	NA	NA	NA	NA	NA	NA	4.17%	NA	NA	NA	NA	NA
TD	Toronto-Dominion Bank	2.5%	$144,622	$80.73	91 - 76	$7.91	$8.44	$9.13	10.2x	9.6x	8.8x	4.83%	49%	48%	48%	7%	12%
NA	National Bank of Canada	2.5%	$35,364	$104.54	105 - 84	$9.46	$9.70	$10.42	11.1x	10.8x	10.0x	4.06%	42%	45%	44%	3%	8%
MFC	Manulife Financial	5.0%	$58,410	$32.74	34 - 24	$3.47	$3.68	$3.95	9.4x	8.9x	8.3x	4.95%	42%	43%	44%	6%	9%
SLF	Sun Life Financial	2.5%	$42,806	$74.00	75 - 60	$6.36	$6.90	$7.71	11.6x	10.7x	9.6x	4.26%	47%	47%	45%	8%	12%
BAM	Brookfield Asset Mgmt.^	5.0%	$16,099	$41.06	42 - 28	$1.37	$1.61	$1.91	30.0x	25.5x	21.5x	3.26%	93%	94%	92%	18%	31%
IFC	Intact Financial	5.0%	$41,354	$235.96	237 - 182	$11.70	$14.86	$15.92	20.2x	15.9x	14.8x	2.05%	38%	33%	33%	27%	10%
AP.UN	Allied Properties REIT*	2.5%	$2,442	$17.47	29 - 15	$2.18	$2.04	$2.09	8.0x	8.6x	8.4x	10.30%	83%	88%	86%	-6%	0%
FCR.UN	First Capital REIT*	2.5%	$3,363	$15.85	18 - 12	$0.95	$1.03	$1.06	16.7x	15.4x	15.0x	5.45%	91%	83%	82%	8%	0%
T	TELUS	5.0%	$34,992	$23.84	29 - 21	$0.95	$1.08	$1.29	25.1x	22.1x	18.5x	6.31%	153%	144%	129%	14%	11%
BIP.UN	Brookfield Infr. Partners^	5.0%	$19,025	$29.16	37 - 21	$2.96	$3.26	$3.56	9.9x	8.9x	8.2x	5.56%	52%	50%	48%	10%	6%
FTS	Fortis	5.0%	$25,575	$52.13	62 - 50	$3.09	$3.25	$3.41	16.9x	16.0x	15.3x	4.53%	73%	73%	72%	5%	5%
ALA	AltaGas	2.5%	$8,049	$28.56	29 - 21	$2.86	$3.12	$3.20	10.0x	9.2x	8.9x	4.17%	39%	38%	39%	9%	6%
Consumer																	
QSR	Restaurant Brands Intl.^	2.5%	$34,720	$76.38	80 - 60	$3.24	$3.36	$3.82	23.6x	22.7x	20.0x	3.04%	68%	68%	62%	4%	3%
CTC.A	Canadian Tire**	2.5%	$8,158	$139.38	190 - 129	$10.42	$10.86	$13.53	13.4x	12.8x	10.3x	5.02%	67%	65%	53%	4%	2%
Industrial																	
CNR	Canadian National Railway**	2.5%	$113,910	$177.79	178 - 143	$7.28	$8.10	$9.12	24.4x	21.9x	19.5x	1.90%	43%	43%	41%	11%	10%
TIH	Toromont Industries**	2.5%	$10,469	$127.19	128 - 101	$6.38	$6.30	$6.50	19.9x	20.2x	19.6x	1.51%	27%	30%	30%	-1%	0%
TRI	Thomson Reuters^**	2.5%	$72,026	$159.09	162 - 117	$3.47	$3.58	$4.05	45.8x	44.4x	39.3x	1.36%	56%	60%	56%	3%	5%
Resources																	
CNQ	Canadian Nat. Resources#	5.0%	$96,313	$88.98	93 - 67	$13.54	$14.01	$14.36	6.6x	6.4x	6.2x	4.50%	27%	29%	31%	3%	10%
SU	Suncor Energy#	5.0%	$59,156	$45.68	48 - 37	$10.17	$10.67	$9.99	4.5x	4.3x	4.6x	4.77%	21%	20%	22%	5%	0%
ENB	Enbridge^^	5.0%	$98,755	$46.46	54 - 43	$5.48	$5.29	$5.55	8.5x	8.8x	8.4x	7.88%	65%	69%	68%	-3%	3%
TRP	TC Energy	5.0%	$55,080	$53.09	57 - 44	$4.30	$4.28	$4.36	12.3x	12.4x	12.2x	7.23%	87%	90%	91%	0%	3%
PPL	Pembina Pipeline*	5.0%	$25,710	$46.80	47 - 39	$4.82	$5.12	$5.41	9.7x	9.1x	8.7x	5.71%	55%	54%	53%	6%	8%
NTR	Nutrien^**	2.5%	$26,517	$53.57	83 - 48	$4.70	$5.00	$4.81	11.4x	10.7x	11.1x	4.03%	44%	41%	43%	6%	-3%

^ In U.S. dollars
^^ Distributable cash flow (DCF) instead of earnings per share (EPS)
* Adjusted funds from operations (AFFO) instead of earnings per share (EPS)
\# Cash flow per share (CFPS)
** FactSet estimates

Payout ratios based on earnings per share, except as noted above. Dividend growth rate is based on RBC Capital Markets' or FactSet's 2025 forecast dividend compared to the current annualized dividend. Growth in EPS/AFFO/CFPS are based on the RBC Capital Markets' 2024 forecast compared to 2023.

RBC Capital Markets is acting as financial advisor to Royal Bank of Canada in respect of an agreement to acquire HSBC Bank Canada, as announced on November 29, 2022.

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Source - RBC Capital Markets, FactSet

Sector commentary

Banks and Insurance

Falling interest rates and prospects of a soft landing should support Financials

We believe the Canadian banks are well positioned for the year ahead, driven in part by the buildout of reserves in 2023 and an improvement in underlying fundamentals. On the former, we think the banks are in a strong position to handle a potential uptick in loan losses due to the group proactively strengthening capital ratios. On the latter, we believe operating leverage will revert to positive territory (i.e., revenues are expected to grow faster than expenses) following the current period of strong emphasis on expense control. However, we are keeping our exposure to Canadian banks unchanged until we see evidence of provisions for credit losses reaching peak levels. We believe fundamentals for the insurance companies are healthy, supported by an increase in premiums and the potential for an improvement in assets under management.

We are maintaining **Royal Bank of Canada (RY)** at a 5% weight.

We are maintaining our 2.5% position in **The Bank of Nova Scotia (BNS)**. We believe BNS will be a "show me" story in 2024 as the company executes on its strategic proposal to enhance efficiency while growing profits. Management had noted this may include the exiting of several businesses in Latin America and reinvesting back into core segments. However, BNS generates an above-average dividend yield and trades at a valuation discount relative to peers. Therefore, we believe a half-weight position remains appropriate for an income-oriented portfolio. RBC Capital Markets is forecasting a 7% dividend increase through 2025.

We are maintaining our 5% position in **Bank of Montreal (BMO)**. RBC Capital Markets thinks the Bank of the West acquisition will be approximately 7% accretive to 2024 earnings and to result in over US$800 million in expense synergies. BMO shares trade in line with the peer group average on a price-to-book (P/B) basis, and RBC Capital Markets is forecasting 5% dividend growth through 2025.

We are reducing our position in **Toronto-Dominion Bank (TD)** to 2.5%. TD has the highest capital ratio relative to peers and provides the bank with greater optionality to navigate credit risks and/or return capital to shareholders, in our view. However, TD's challenges with anti-money laundering procedures will likely weigh on the stock over the near term, in our opinion. RBC Capital Markets is forecasting a 12% dividend growth rate through 2025.

We are maintaining the 2.5% position in **Canadian Imperial Bank of Commerce (CM)**. The slowdown in the Canadian housing market and softer consumer loan growth are likely to weigh disproportionately on CM, in our view. However, Canadian Imperial is amongst the cheaper banks within the peer group and generates an above-average dividend. We believe shares could outperform if a soft-landing scenario were to materialize. RBC Capital Markets is forecasting a 5% dividend growth rate through 2025.

We are introducing a 2.5% position in **National Bank (NA)**. We view NA as a high-quality bank with strong credit quality, capital, and cost control. RBC Capital Markets believes the bank will repurchase approximately two million shares over the next three quarters and projects the dividend to grow by roughly 8% through 2025. All in, we believe these characteristics are supportive of NA's premium valuation relative to peers.

We are increasing our position in **Manulife Financial (MFC)** to 5.0%. We believe the reduction in MFC's long-term care exposure is a step in the right direction and effectively decreases the company's underlying risk profile. RBC Capital Markets believes further reductions could lead to higher returns and valuation expansion. We also believe a reacceleration in the Asian regional economy could act as a catalyst. MFC is trading at a discount to peers on a price-to-book (P/B) basis and provides an attractive dividend yield. RBC Capital Markets is projecting a dividend growth rate of 9% through 2025.

We are reducing our position in **Sun Life Financial (SLF)** to 2.5% as we believe there are more attractive opportunities elsewhere in the sector. The shares trade at a premium to peers on a P/B basis, which we believe is warranted given Sun Life's ability to generate an above-average return on equity. Improving financial market conditions should also benefit the company, given that asset and wealth management accounts for roughly half of its overall business. RBC Capital Markets is forecasting the dividend to grow by 12% through 2025.

We are maintaining the 5% position in **Intact Financial Corporation (IFC)**. Shares have performed well on the back of solid underwriting income and investment income. The combined ratio is strong, in our view, standing at approximately 90% as of Q4 2023 results. We believe IFC will continue to hold up well in a risk-off environment. RBC Capital Markets projects the dividend to grow by approximately 10% through 2025. Shares are trading on a P/B ratio of around 2.7x, a slight premium to the five-year historical average.

We are increasing the position in **Brookfield Asset Management (BAM)** to 5%. BAM management believes it will be able to reach around US$90 billion to US$100 billion in fundraising in 2024, in line with 2023 levels. The company also plans to grow its fee-bearing capital to approximately US$1 trillion by 2027 from US$457 billion at the end of 2023. As a result, RBC Capital Markets believes BAM can grow its dividend by approximately 31% through 2025. BAM shares trade at a premium relative to peers, but we believe this is warranted given management's track record of strong execution and its clean balance sheet.

Real Estate

Improving fundamentals; discounted valuations

While not all real estate is created equal, we are seeing evidence that underlying property fundamentals are slowly recovering across most subsectors. For context, RBC Capital Markets estimates the sector will grow earnings by approximately 3% in 2024. We are also cognizant that most real estate investment trusts (REITs) are trading at significant discounts to net asset values (NAV) mostly because of the weakness in the commercial real estate subsector (retail and office properties). Furthermore, we believe lower interest rates and improved credit availability could help to narrow the discounted valuations.

We are maintaining the 2.5% position in **First Capital Real Estate Investment Trust (FCR.UN)**. Management provided an update to its strategic plan, and, in our opinion, balance sheet improvement and stronger earnings will be driven by the company's ability to execute on its $1 billion asset disposition program. The key, in our view, is that management expects these sales to be primarily low-yielding assets and non-grocery-anchored in nature. The company intends to use the proceeds to pay down debt and reinvest in higher-growth properties. Overall, we believe there is a credible plan to drive a re-rating in the units. In the meantime, we're comfortable with the approximate 5.5% yield.

We are maintaining the 2.5% position in **Allied Properties (AP.UN)**. Management decided not to increase the distribution, which we believe is the right decision. Instead, the company's priority is to direct excess cash flows towards strengthening the balance sheet. All in, we believe the distribution can be supported if occupancy stays above 80%. Overall, we believe an upward re-rating will take time, but also have a positive view on the above-average yield and the discounted valuation. The units currently trade 29% below RBC Capital Markets' 2024 NAV estimate.

Energy and Materials

Shareholder returns remain a key focus

We saw relatively stable oil prices last quarter as there have been no major moves in the geopolitical headwinds that have driven oil price movements over the past couple of quarters. Oil prices remain well above breakeven levels, giving us confidence that the constituent names will be able to continue with their shareholder return programs. This is reinforced by strong balance sheets in the oil patch, with debt levels at roughly half of what they were in 2020. Furthermore, the decarbonization efforts through the Pathways initiative is helping Canadian oil & gas companies be recognized by investors beyond Canada. Moreover, the Trans Mountain Pipeline Expansion should aid in narrowing the price spread between West Texas Intermediate crude oil and Western Canadian Select crude, helping to prop up free cash flow for the Canadian oil producers. The fertilizer market is also looking stronger through 2024, in our view, with RBC Capital Markets projecting stabilization in fertilizer prices, tightness within nitrogen supply, and higher prices for phosphate that should remain supportive for the year ahead.

We are maintaining our 5% weight in **Canadian Natural Resources (CNQ)**. Production and adjusted funds from operations continue to come in strong, while net debt is improving as CNQ inches closer to its net debt target of $10 billion. Once this is achieved, the company plans to increase its return of capital to 100% of excess free cash flow, all the while management continues to raise the dividend and buy back shares. We are keeping an eye on the underlying commodity given potential supply/demand imbalances, but we are comfortable with our position in CNQ as investors are being paid an attractive and growing dividend, while the valuation for what we believe is a high-quality company is in line with the peer group.

We are maintaining our 5% weight in **Suncor (SU)**. The company is performing well with strong production and adjusted funds from operations, as well as capital expenditures that have recently come in below RBC Capital Markets' expectations. Suncor has focused on its corporate-level speedbumps and has addressed initiatives that are aimed at revamping employee impact as well as safety procedures across all its assets. The company remains committed to achieving its net debt target of $12 billion, Once achieved, it intends to increase the allocation of excess funds to buybacks from 50% currently to 75%, with the rest used for ongoing debt reduction. Valuation remains below the peer group average, and we are comfortable with our position given the improving internal controls, growth from recent M&A, and an attractive shareholder return program.

We are maintaining our 2.5% position in **Nutrien (NTR)**. Looking out through 2024, RBC Capital Markets' expectations call for the ag/fertilizer markets to stabilize. Potash demand has started the year mixed, but RBC Capital Markets believes the longer-term potash market will be balanced, with new supply supported by steady demand growth. The nitrogen market remains constructive, as North American producers benefit from low-cost U.S. natural gas. Furthermore, RBC Capital Markets expects NTR's retail segment to normalize margins after the company works off high-cost inventories. With a continued focus on cash generation and capital return, we are comfortable with the dividend yield and believe RBC Capital Markets' forecast for free cash flow will be supportive of moderate share buybacks and dividend increases.

Utilities, Pipelines, and Midstreams

Attractive dividend yields amongst energy infrastructure and utilities companies; debt reduction remains in focus

Pipelines and midstreams continue to be an important component for dividend portfolios, in our view, given their above-average dividend yields and some catalysts that are emerging on the horizon. Midstream and pipeline valuations continue to trade at a discount to regulated utility stocks. We believe this is a function of investors having lower dividend growth expectations and higher leverage profiles for midstreams and pipelines and the perceived cushion that Utilities stocks can provide during periods of economic uncertainty.

We think the regulated utility sector remains attractive due to stable cash flows and attractive dividend growth. The previously elevated valuations have eased, presenting attractive opportunities, in our view.

We are maintaining our 5% position in **TC Energy (TRP)**. The company boasts predictable cash flows, with approximately 95% of its EBITDA stemming from regulated and long-term contracted assets. The mechanical completion of the Coastal GasLink project removes an overhang on the stock, and our focus turns towards asset sales and debt repayment. Overall, we believe the risks and rewards are compelling for income-oriented investors due to the company's 7%+ dividend yield and a valuation that is below its five-year average on forward earnings.

We are maintaining our 5% position in **Enbridge (ENB)** given management's projected capital allocation framework that aims to right-size the balance sheet, alongside capital deployment that supports both growth initiatives and shareholder returns. The company also addressed the funding gap without the need to issue additional equity, which we believe should be well received by the investment community. In the near term, we believe the stock may be range-bound until we see improved integration of the Dominion utilities assets. RBC Capital Markets estimates the dividend will grow by approximately 3% through 2025.

We are maintaining our 5.0% position in **Pembina Pipeline (PPL)**. We believe the company is well positioned to benefit from growing natural gas and natural gas liquids volumes in the Western Canadian Sedimentary Basin, alongside further infrastructure opportunities. The company's EBITDA is supported by 85% fee-based revenues, primarily take-or-pay or cost-of-service contracts, which underpin the steady dividend. RBC Capital Markets forecasts the dividend will be increased by about 8% through 2025. Finally, PPL noted that neither it nor its joint venture will be eligible to participate in the first phase of the Canadian government's Trans Mountain divestiture process.

In the Utilities sector, we are maintaining the 5% position in **Brookfield Infrastructure Partners L.P. (BIP.UN)** given its resilience to an uncertain economic environment and a healthy, growing dividend yield. We believe BIP has multiple avenues of growth for funds from operations, largely through its inflation-indexed contracts and capital recycling program, which management thinks has been successful so far. We continue to favor BIP amongst other Canadian Utilities companies as we believe it has more global assets with revenues tied to economic activity. Additionally, more than 90% of BIP.UN's debt is fixed with an average maturity of seven years. The company targets distributions to increase by 6%–9% per annum over the long term.

We are maintaining our 5% weight in **Fortis (FTS)**. The company has reiterated its capital plan for 2024–2028, which supports rate base growth of roughly 5% per annum, further underpinning the 4%–6% annual dividend growth guidance through 2028. We continue to view Fortis as a steady dividend payer with attractive dividend growth and a supportive balance sheet.

We are maintaining the 2.5% position in **AltaGas (ALA)** to provide more defensive characteristics. AltaGas has a dividend yield of approximately 4%, which we view as attractive, supported by a 2025 AFFO payout ratio of roughly 39%, per RBC Capital Markets' estimate. Furthermore, RBC Capital Markets believes the strength and stability of the utility business will allow AltaGas to grow its dividend by 5%–7% per annum through 2028 and is forecasting dividend growth of 6% for 2025.

Consumer

Balanced exposure given an uncertain consumer outlook

The health of the consumer continues to be closely watched, as both the Bank of Canada (BoC) and investors are keeping a keen eye on inflation measures and whether softer monetary policy can be enacted. January's inflation data came in lower across the board, with headline inflation slipping into the BoC's 1%–3% y/y target range. We believe that the sector positions held in this Portfolio provide diversification through consumer types and geographies, while providing sustainable yields across the economic cycle.

We are maintaining our 2.5% weight in **Canadian Tire (CTC.A)**. While quarterly results did not overly impress, the unusually warm winter season has in part driven this lack of demand with margins compressing in the quarter. Much of these results were understood by the market with valuation already well below retail peers. While we continue to watch for a shift in interest rate policy and, in turn, a strengthening consumer, we are comfortable with our position in CTC.A. We believe the company should provide some economic sensitivity for the Portfolio while delivering an attractive and sustainable dividend yield, along with a payout ratio of approximately 50% based on RBC Capital Markets' 2025 estimate.

We are maintaining our 2.5% weight in **Restaurant Brands International (QSR)**. Same store sales at Tim Hortons continues to impress, while growth in system-wide sales climbs higher on the back of consolidated same store sales and net restaurant growth. We believe the Burger King "Reclaim the Flame" initiative will likely accelerate in the quarters ahead following QSR's decision to acquire approximately 1,000 units from Carrols Restaurant Group. We believe this is not a change in strategy, supported by management's intention to sell most locations over the next five to seven years. Management has introduced multi-year operation and financial targets, and will be focusing on initiatives to drive sales, including further globalization of the brands, and continued dividend growth while maintaining a 50%–60% payout ratio. Valuation appears fair and, in our opinion, QSR should be able to continue to grow this dividend alongside its earnings in the near-to-medium term.

Industrials

Paying up for quality and growth

The Canadian Industrials sector is not amongst the higher-yielding sectors in the S&P/TSX Composite Index, but it encompasses high-quality businesses with proven histories of consistent shareholder returns. The Industrials companies within the Portfolio have strong track records of strategic execution, healthy balance sheets, and quality management teams.

We are maintaining our 2.5% position in **Thomson Reuters (TRI)**. The emergence of generative artificial intelligence is renewing TRI's growth prospects and management expects the business to generate organic growth greater than 6%. This, in conjunction with margin expansion, should generate higher free cash flow and allow TRI to return more capital to shareholders. RBC Capital Markets believes TRI can grow its dividend by 8%–12% per annum over the next few years with a targeted FCF payout ratio of approximately 50%–60%. TRI is trading at a premium to its historical average, but we believe this is warranted due to its stronger growth profile.

We are maintaining a 2.5% position in **Toromont (TIH)**. The company has a long history of dividend increases, and we expect more increases and share buybacks in the future as the company is in a net cash position (cash holdings exceeding debt). We still expect the company will use its strong balance sheet to complete an acquisition over the medium term. Significant infrastructure investments from the provincial (namely Ontario and Quebec) and federal governments should continue to support construction demand in Toromont's regions (i.e., Eastern Canada). The consolidated backlog exiting Q4 was $1.2 billion (flat y/y), of which approximately 90% of the Equipment Group's backlog ($957 million) is expected by management to be delivered in the next 12 months. TIH shares trade at a premium valuation relative to peers, but we believe this is warranted given the company's consistent history of strong execution and no financial leverage.

We are keeping the 2.5% position in **Canadian National Railway (CNR)**. The company believes it will be able to grow earnings by 10% through 2024, supported by its expectation for pricing growth at a rate of 3%–4% above inflation and mid-single-digit volume growth. RBC Capital Markets believes executing on the latter will be key to achieving the company's earnings target. As a result, we believe investors may take a wait-and-see approach over the near term. Overall, we view the high barriers to entry in the railroad industry as a positive for the company and continue to favor the stock for long-term growth. Canadian National Railway has a long history of returning capital to investors, and RBC Capital Markets is forecasting the dividend to grow by 10% through 2025.

Communication Services

Industry growth is expected to moderate due to intensified competition

Following a year of increased wireless competition and elevated interest rates, RBC Capital Markets sees a better set-up in 2024. First and foremost, intensified competition will likely moderate industry growth. However, RBC Capital Markets believes the market can expand and should act as an offset. Additionally, 2024 looks to be a relatively light year from a regulatory agenda perspective, and thus should be favourable to the telecommunications companies, according to RBC Capital Markets. Overall, we believe the focus has shifted towards improving leverage and payout ratios in the year ahead.

We are maintaining the 5% position in **TELUS (T)**. We believe TELUS will benefit from declining capital intensity, and thus, free cash flow generation should improve in 2024. All in, we believe this provides the company with additional financial flexibility to strengthen the balance sheet and to support its 7%–10% annual dividend growth target.

BCE Inc.

(TSX: BCE; $50.32)

We are removing the 2.5% position in BCE from the Portfolio

- **Deteriorating business fundamentals:** Management is guiding towards flat-to-low single-digit revenue growth in 2024. The company expects this, in turn, to allow earnings before interest, depreciation, and amortization (EBITDA) to grow modestly on a year-over-year basis. However, we think BCE's decision to lay off approximately 9% of its workforce later this year will ultimately weigh on earnings and free cash flow generation. Overall, we believe BCE will have a lower margin of error when it comes to financial flexibility.
- **Reduction in leverage is likely a multi-year story:** RBC Capital Markets estimates BCE's leverage to remain around 3.5x through 2025 and does not expect leverage to dip below 3.0x until 2029. As a result, we believe the upside optionality may be limited until we see a meaningful improvement in the balance sheet.
- **Elevated payout:** While we do not believe the dividend is at risk in the near term, we acknowledge that risks have increased due to the slowing fundamentals and the longer lead time that we think it will take to strengthen the balance sheet. RBC Capital Markets estimates the free cash flow payout will be approximately 114% by the end of 2024 and will improve to about 100% by the end of 2025.

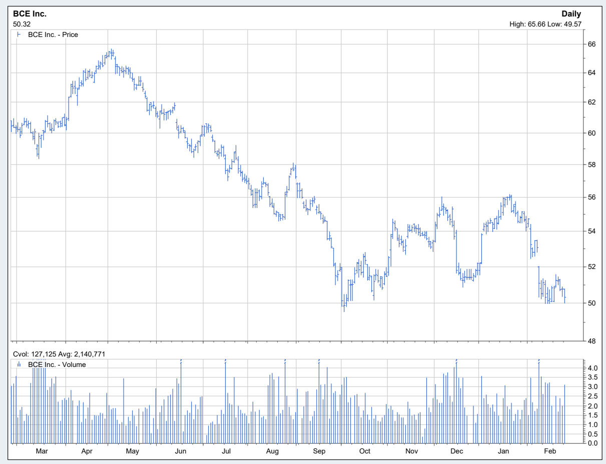
Risks

Risks include, but are not limited to, a prolonged economic downturn, increased wireless competition, inability to gain market share in Fibe television and internet, and a substitution away from telephony and television that exceeds RBC Capital Markets' expectations.

Company description

BCE is Canada's largest telecom services company and one of the country's largest corporations. BCE provides local, long distance, wireless, satellite, television, and internet services across Canada. BCE has a 100% stake in Bell Media, Canada's largest integrated media company.

1-year pricing chart



Source - FactSet; data through 2/26/24

Brookfield Asset Management Ltd.

(NYSE: BAM; US$41.06)

We are increasing the position in Brookfield Asset Management to 5.0% (from 2.5%)

- **Benefitting from strong fundraising:** Despite a slowing economic outlook, we are comforted by BAM's fundraising ability. In the year ahead, BAM believes it will be able to raise approximately US$90 billion to US$100 billion in new capital, similar to levels reached in 2023. As a result, we believe this will be supportive of growth in fee-related earnings (FRE). From 2014 through 2023, FRE has compounded at a rate of roughly 23% per annum. RBC Capital Markets believes FRE will grow by approximately 18% in 2025 compared to 2024 levels.
- **Strong balance sheet and solid dividend growth:** In our view, BAM has a strong balance sheet and is supported by its net cash position. For context, its closest peers are sitting in a net debt position. Alongside a recovery in the financial markets and BAM's financial strength, we believe BAM will be able to deliver an above-average dividend growth rate for years to come. The company's dividend policy is based on a fixed quarterly dividend, revised annually, and its growth appears to be based on its guidance for next-twelve-months-FRE. RBC Capital Markets projects the dividend to grow by 31% through 2025.
- **Valuation:** Shares are trading at approximately 21.5x FRE on RBC Capital Markets' 2025 estimate, which is a discount to its closest peer and allows for a higher multiple if it can execute on its growth plans.

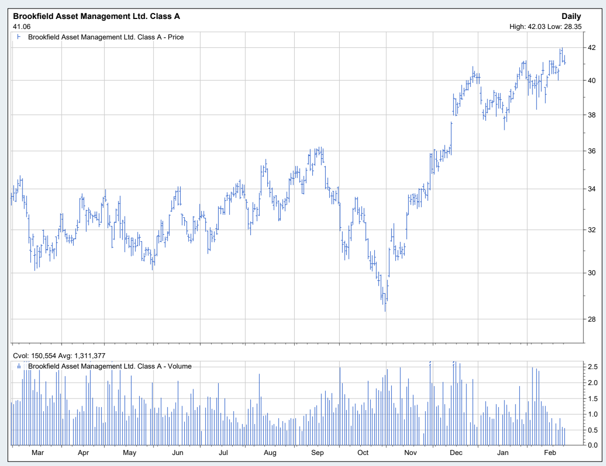
Risks

Risks include, but are not limited to, an economic downturn, a softer environment for capital markets, deteriorating fund performance, and rising/elevated interest rates.

Company description

Brookfield Asset Management has US$440 billion in fee-bearing capital (US$850 billion in assets under management) in five asset classes (real estate, renewable energy, infrastructure, private equity, and credit), and recently expanded into three new strategies (transition funds, impact funds, and secondary funds). BAM also owns a 68% interest in Oaktree Capital Management, but it does not invest its proprietary capital. Brookfield Corp. remains BAM's largest shareholder with a 75% ownership stake.

1-year pricing chart



Source - FactSet; data through 2/26/24

Manulife Financial Corporation

(TSX: MFC; $32.74)

We are increasing our position in Manulife Financial to 5.0% (from 2.5%)

- **Experiencing a favourable rate of change:** MFC's exposure to long-term care (LTC) has often been perceived by RBC Capital Markets as one of the company's highest risks. The recent LTC transaction may mark the start of more deals from MFC to reduce its LTC exposure, and further validate that MFC's LTC exposure is less troubling than believed by investors. This could lead to improved valuation over time, in our view. As a result, we are taking a favourable stance following MFC's decision to reduce approximately 14% of its LTC exposure. More importantly, the transaction was conducted close to book value, which we view as an attractive price for a higher-risk asset. All else equal, we believe the business is experiencing a favourable rate of change which, in turn, could prompt an upward re-rating in the stock assuming more of these transactions can take place. In addition, RBC Capital Markets expects double-digit growth from the company's Asian operations for 2024, which should also help the stock re-rate higher, in our view.
- **Solid yield and dividend growth:** MFC is generating an attractive yield of approximately 5%, supported by a solid payout ratio in the low-to-mid-40% range, according to RBC Capital Markets. Looking through 2025, RBC Capital Markets projects the company can grow its dividend by approximately 9%.
- **Inexpensive valuation:** MFC trades at approximately 1.5x price-to-book, a discount to the peer group average of roughly 1.6x. We believe additional reductions in the LTC business could allow for an expansion in return on equity. If achieved, we believe MFC's valuation should improve relative to peers.

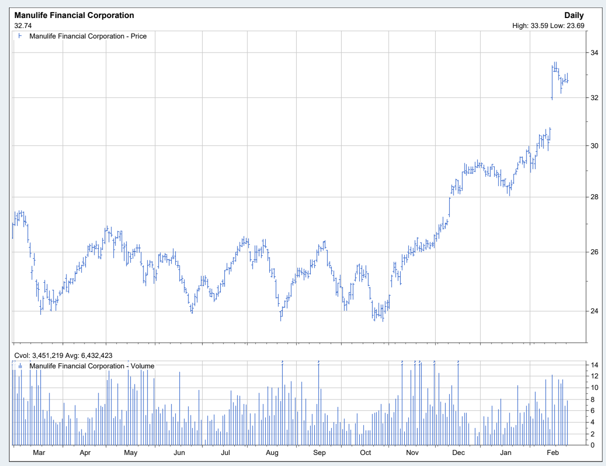
Risks

Risks include, but are not limited to, a prolonged economic downturn, larger-than-assumed credit losses, changes in actuarial assumptions, appreciation in the Canadian dollar, and/or unfavourable economic developments in Asia.

Company description

Manulife is Canada's largest insurer and a leading global provider of financial protection and wealth management products and services. Manulife is among the largest life insurers globally as measured by market capitalization.

1-year pricing chart



Source - FactSet; data through 2/26/24

National Bank of Canada

(TSX: NA; $104.54)

We are adding a 2.5% position in National Bank of Canada to the Portfolio

- **Continued growth:** In our view, we believe several headwinds that currently weigh on the group could potentially inflect favourably later this year. In our view, NA continues to prove itself as a well-run, high-quality bank, as RBC Capital Markets points to strong credit quality, reserves, and cost controls, with revenue growth likely to continue in the year ahead.
- **Dividend growth:** NA's healthy capital position provides flexibility for attractive shareholder returns, in our opinion. RBC Capital Markets believes NA will repurchase around two million shares over the next three quarters and projects dividend growth to be strong at approximately 8% through 2025 supported by a 44% payout ratio.

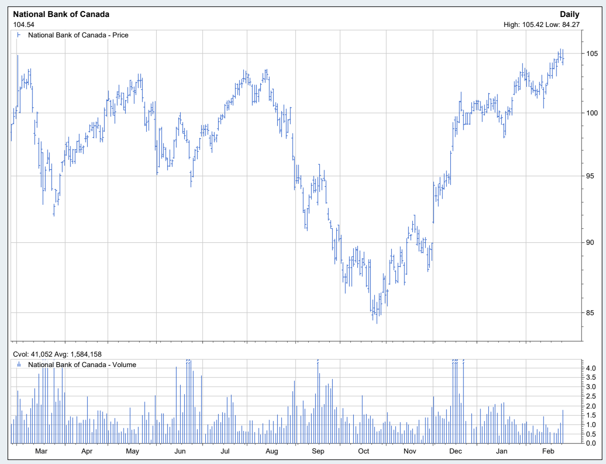
Risks

Risks include, but are not limited to, deterioration of the overall economy, the Canadian housing market, regulatory and political risk, weakening retail credit quality, and loss of market share.

Company description

National Bank is a Montreal-based, fully integrated financial services company that is the smallest of the Big Six Canadian banks.

1-year pricing chart



Source - FactSet; data through 2/26/24

Sun Life Financial Inc.

(TSX: SLF; $74.00)

We are reducing our position in Sun Life Financial to 2.5% (from 5.0%)

- **Maintaining our lifeco exposure:** We are comfortable maintaining the Portfolio's exposure to life insurance companies at 7.5%. However, we believe MFC is experiencing a favourable rate of change, and thus, the risks and rewards have improved relative to SLF, in our opinion.
- **Underlying business fundamentals still healthy:** SLF remains a high-quality business, in our view, supported by its industry-leading return on equity. The company is also well capitalized and should benefit from improving financial market conditions. As a result, we believe SLF will be in a good position to continue growing its dividend. RBC Capital Markets estimates SLF will be able to grow its dividend by approximately 12% through 2025.
- **Trading at a premium valuation:** SLF trades at a premium relative to peers on a price-to-book basis. We believe this is warranted due to the company's historical track record in delivering on its objectives and its above-average return on equity profile. Therefore, we believe a 2.5% weight is prudent and reallocating the proceeds into MFC presents a more attractive opportunity, in our view.

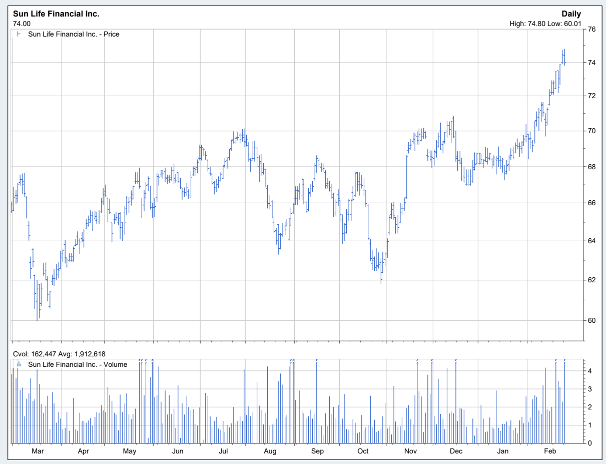
Risks

Risks include, but are not limited to, a prolonged economic downturn, larger-than-assumed credit losses, changes in actuarial assumptions, appreciation in the Canadian dollar, and/or unfavourable economic developments in Asia.

Company description

Sun Life is one of Canada's Big 3 lifecos and has operations in Canada, the U.S., Asia, and the UK. The company has a substantial wealth management presence through majority-owned MFS, a large U.S. asset management company.

1-year pricing chart



Source - FactSet; data through 2/26/24

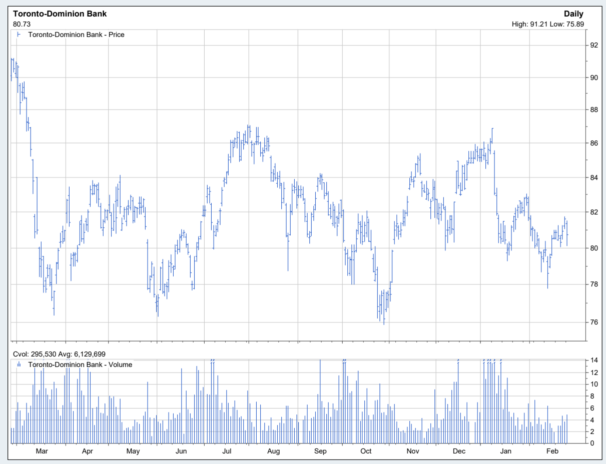
Toronto-Dominion Bank

(TSX: TD; $80.73)

Company description

Toronto-Dominion Bank is Canada's second-largest bank by market capitalization. The bank has a large footprint in both Canada and the United States. Canadian Personal and Commercial Banking serves approximately 15 million customers, while the U.S. Retail Bank serves 10 million customers.

1-year pricing chart



Source - FactSet; data through 2/26/24

We are decreasing the position in Toronto-Dominion Bank to 2.5% (from 5.0%)

- **AML investigation and associated regulatory risk:** TD is currently subject to an anti-money laundering (AML) investigation that involves the U.S. Department of Justice. While the potential monetary penalty could be significant (potentially greater than US$1 billion), it is not our primary concern given TD's strong capital position. Rather, the investigation could result in other limitations that could constrain growth in the U.S. for years to come, as well as increase compliance-related expenses. Although we view such a materially negative outcome as a low probability risk, it is a risk nonetheless that we think warrants lower exposure to the bank at this time.
- **Strong capital position:** TD has a group-leading capital position. In the event that growth by acquisition is restrained in the U.S., we believe TD's excess capital can be deployed towards share repurchases and greater organic growth opportunities across North America.
- **Sustainable dividend and attractively valued:** Given TD's strong capital position, we believe dividend growth can continue in the year ahead, which RBC Capital Markets projects at 12% through 2025 supported by a 48% payout ratio. TD currently trades below its long-term average price-to-book ratio, but off its previous lows seen in 2023.

Risks

Risks include, but are not limited to, deterioration of the overall economy, the Canadian and U.S. housing markets, regulatory and political risk, weakening retail credit quality, and loss of market share.

Methodology

The objective of the Equity Income Guided Portfolio (EIGP) is to provide investors with an attractive rate of current income with the potential for growing cash flow plus long-term capital appreciation by investing in a diversified Portfolio of higher-yielding Canadian securities, such as common stocks, Real Estate Investment Trusts (REITs), and income trusts that trade on the S&P/ TSX Composite Index. This Portfolio consists of approximately 20–30 stocks and may be appropriate for investors who have a moderate risk tolerance in relation to an equity investment. Because of its focus on income and income growth, this Portfolio would ordinarily exhibit greater defensive characteristics relative to the broad equity market during bear markets and may underperform during bull markets.

The top-down strategy process employed by RBC Capital Markets plays a different role in the EIGP process than with our other Guided Portfolios. While the recommended sector “overweights” and “underweights” are taken into consideration, the Investment Committee aims to diversify the Portfolio adequately across the four broader economic sectors (interest sensitive, consumer, industrial, and resources), even though dividends may be modest. In this way, we address one of the most common pitfalls inherent in income investing: investors who focus too narrowly on the size of the dividend will more than likely find themselves heavily concentrated in the Financials and Utilities sectors, which tend to react negatively to rising interest rates.

Once the “sector weights” are established, an eligible universe of securities is determined. Careful consideration is given to identifying a pool of fundamentally preferred companies that have the potential to return, on a sustainable basis, a significant amount of cash flow to investors. The resulting universe will consist of securities with either an attractive dividend yield or a yield that may appear less attractive, but that we believe have strong potential for growth. In addition, companies that, in our view, pay out too high a percentage of their cash flows in dividends or distributions will be excluded.

Additional factors analyzed include a company’s financial strength and debt levels, the amount of cash generated by the business relative to capital expenditure requirements, its longer-term return on capital, the proportion of income paid out versus reinvested, historical and forecast dividend growth rates, and trading liquidity.

The current dividend yield for the S&P/TSX Composite Index is approximately 3.13%; the EIGP currently offers investors a yield of approximately 4.83% plus the potential for capital appreciation and an inflation hedge.

Disclosures and disclaimers

Equity Income Guided Portfolio Investment Committee

Kapil Bapat, CIM, Portfolio Advisor
kapil.bapat@rbc.com; RBC Dominion Securities Inc.

Dominick Hardy, CA, CFA, CPA, Portfolio Advisor
dominick.hardy@rbc.com; RBC Dominion Securities Inc.

Patrick McAllister, CFA, Manager, Equity Advisory & Portfolio Management
patrick.mcallister@rbc.com; RBC Dominion Securities Inc.

Sunny Singh, CFA, Portfolio Advisor
sunny.singh@rbc.com; RBC Dominion Securities Inc.

Richard Tan, CFA, Portfolio Advisor
richard.tan@rbc.com; RBC Dominion Securities Inc.

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Distribution of ratings – RBC Capital Markets Equity Research
As of December 31, 2023

			Investment Banking Services Provided During Past 12 Months	
Rating	Count	Percent	Count	Percent
Buy [Outperform]	829	57.17	253	30.52
Hold [Sector Perform]	575	39.66	154	26.78
Sell [Underperform]	46	3.17	6	13.04

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Allied Properties REIT (AP.UN; Outperform; $17.47)
AltaGas (ALA; Outperform; $28.56)
Bank of Montreal (BMO; Outperform; $126.83)
Bank of Nova Scotia (BNS; Sector Perform; $63.87)
BCE (BCE; Sector Perform; $50.32)
Brookfield Asset Management (BAM; Outperform; US$41.06)
Brookfield Infrastructure Partners L.P. (BIP.U; Outperform; US$29.16)

Canadian Imperial Bank of Commerce (CM; Sector Perform; $62.81)

Canadian National Railway Company (CNR; Sector Perform; $177.79)

Canadian Natural Resources (CNQ; Outperform; $88.98)

Canadian Tire (CTC.A; Outperform; $139.38)

Enbridge (ENB; Outperform; $46.46)

First Capital REIT (FCR.UN; Outperform; $15.85)

Fortis (FTS; Sector Perform; $52.13)

Intact Financial (IFC; Sector Perform; $235.96)

Manulife Financial (MFC; Outperform; $32.74)

National Bank of Canada (NA; Sector Perform; $104.54)

Nutrien (NTR; Outperform; US$53.57)

Pembina Pipeline (PPL; Outperform; $46.80)

Restaurant Brands International (QSR; Outperform; US$76.38)

Sun Life Financial (SLF; Outperform; $74.00)

Suncor Energy (SU; Outperform; $45.68)

TC Energy (TRP; Outperform; $53.09)

TELUS (T; Outperform; $23.84)

Thomson Reuters (TRI; Sector Perform; US$159.09)

Toromont Industries (TIH; Outperform; $127.19)

Toronto-Dominion Bank (TD; Outperform; $80.73)

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