

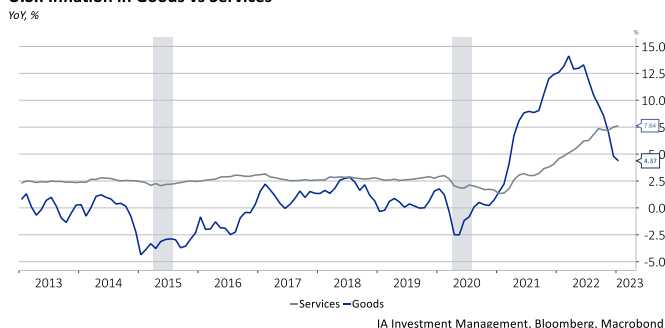
Keys to the market

What happened last week

February 17, 2023

The financial markets seem to be on the brink of giving in to monetary policies and terminal rates. Inflationary pressures are proving to be unexpectedly resilient in the United States, as shown last week by the January CPI and PPI indicators, which exhibited obvious strength. With unemployment at all-time lows and consumer spending maintaining its momentum, central bankers on both sides of the border have come out in support of further rate hikes, if necessary, and the markets have thus adjusted their expectations of higher terminal rates. The U.S. dollar has rallied and erased its losses so far in 2023. Stocks and bonds alike sold off, with generally negative sentiment taking hold of the markets ahead of a holiday weekend in the U.S. and Canada.

U.S.: Inflation in Goods vs Services



Bond market

The fixed income markets tended not to like the latest CPI print in the United States, exhibiting concerns that inflation may be too sticky and that as a result the US Fed may have to act more aggressively. Indeed, some Fed speakers suggested that a 50-basis-point hike may be more appropriate at its next meeting because inflation remains too high and employment numbers are persistently strong. Yields increased by 10+ basis points on the news and the curve steepened, as expectations of sticky inflation got priced in. The market also started pricing in a 5.25% terminal rate and only a modest cut by year-end, which is more consistent with our stance that Fed policy makers should be taken at face value. Meanwhile, spread product was little changed, as it continued to lose momentum after its hot start to the year.

Highlights

- Expectations of a Fed pause in interest rate hikes have faded as a result of strong inflation numbers and a historically low unemployment rate.
- The markets are now pricing in further rate hikes and a potentially higher terminal rate.

On our radar

- Canada: December retail sales and January CPI
- United States: January existing and new home sales, PCE, minutes of the latest FOMC meeting and University of Michigan sentiment indicators for February

Stock market

As the earnings season comes to an end in the United States, the focus turned to smaller-capitalization companies, which started to report this week. The key highlight was the market's strong reaction to tech companies' improved fundamentals. Their shift in priorities drove better results, as companies transitioned from being growth driven to being profit driven, as they embrace what we call the "Meta playbook." Such companies include Roblox, Twilio, The Trade Desk and Airbnb, to name only a few.

It's also important to stress that, throughout the earnings season, we've seen business owners demonstrate more optimism than they did last year. In fact, company optimism jumped to its highest level since the first quarter of 2021. We think this business confidence, coupled with better economic data, is driving the market rally that we've recently been witnessing.

Markets

(Total Return, in \$CAD)

As of February 16, 2023	WTD %	MTD%	YTD%	1Y%	3Y%	5Y%
Equities						
S&P 500	0.79	1.28	6.00	-1.51	8.84	11.89
S&P/TSX	0.04	-0.70	6.66	-0.57	8.12	9.21
NASDAQ	1.86	3.65	12.92	-9.73	9.47	14.53
MSCI ACWI	1.02	1.09	6.60	-1.77	6.85	8.79
MSCI EAFE	1.29	0.66	7.16	0.77	4.08	4.28
MSCI EM	0.51	-1.13	5.06	-10.99	0.24	0.78
Commodities (USD)						
Gold	-1.57	-4.77	0.68	-1.79	5.05	6.39
CRB	-0.12	-0.71	-0.31	-7.62	11.30	4.59
WTI	-1.54	-0.48	-2.21	-16.20	14.67	4.94
Fixed Income						
FTSE TMX Canada Universe	-0.83	-2.26	0.76	-6.48	-2.80	0.70
FTSE TMX Canada Long	-1.78	-4.34	0.87	-12.74	-7.00	-0.34
FTSE TMX Canada Corporate Overall	-0.62	-1.53	1.40	-4.52	-1.42	1.54
Currencies						
DXY	0.22	1.72	0.32	8.52	1.57	3.11
USDCAD	0.85	1.14	-0.71	6.08	0.52	1.39
USDEUR	0.04	1.78	0.30	6.55	0.49	3.06
USDJPY	1.96	2.96	2.15	15.95	6.86	4.75
USDGBP	0.57	2.72	0.75	13.27	2.85	3.20

Source: iA Investment Management, Bloomberg

	CA	US
Bond yields		
2Y	4.14	4.64
5Y	3.45	4.07
10Y	3.29	3.86
30Y	3.28	3.91
Credit spreads		
IG corporate bonds	157	123
HY bonds	329	424

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ROOTED IN HISTORY, INNOVATING FOR THE FUTURE.

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