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MARKET REVIEW

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WATCH EPISODE

MARKET COMMENTARY

Inflation, a lagging indicator, is moving in the right direction but remains too hot and well above the Federal Reserve's target range. Employment, a coincident indicator, is healthy and provides ammunition for the Federal Reserve to rapidly raise interest rates to achieve price stability. High inflation does not appear to be embedded in future expectations, with the 5-year and 10-year breakeven inflation rate at 2.49% and 2.38%, respectively.

Restrictive monetary policy combined with an accelerated pace of quantitative tightening elevates the risk of a hard landing. Leading indicators of a pending recession are providing a mixed view. The U.S. treasury yield curve has been inverted since June, suggesting a recession is (potentially) on the horizon. On the flip side, the high yield debt spread remains below the long-term historical average and does not reflect growing concern of default risk. As well, the ISM Manufacturing and Services Indices continue to report expansionary economic activity.

The cushion provided by excess savings accumulated during the pandemic and a strong labour market has allowed most households to maintain their consumption despite their eroding purchasing power. The pace inflation subsides is critical as savings will eventually be depleted. A more cautious outlook by consumers and corporations means softer demand and weaker job growth. The latter is already showing up in Canada while the unemployment rate is still holding steady in the United States.

Volatility will remain elevated until there are more visible signs that inflation is declining. Investors are encouraged to be patient and use pullbacks to invest in quality income and growth stocks.

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