Economic Commentary

First Quarter 2024

Inflation Levels Improve But Remain Elevated

North American inflation has improved significantly from the peak levels reached in 2022, however, levels remain higher than central banks would like to see at this point in the economic cycle. After increasing to 3.4% to end the year in both Canada and the U.S., annual inflation rates for January declined to 2.9% and 3.1%, respectively. U.S. inflation surprised on the upside again in February, with the annual rate moving up to 3.2%. Better progress has been made in Canada, with the annual inflation rate coming in at a better-than-expected 2.8%. Despite the improvements made over the past two years, inflation remains higher than the central bank target of 2%. In addition, the core rate of inflation remains higher than the headline rate, with Canadian core at 3.1% and the U.S. at 3.8%. Further improvements in core readings are required before central banks are confident that inflationary pressures have been contained. Inflation declines in Europe continue to outpace the progress made in North America as Eurozone inflation now stands at 2.6%, after peaking at 10.6%. Inflation in the U.K. is now at 3.4%. Inflation will continue to be the driving force impacting global financial markets and central bank monetary policy throughout the balance of the year.

Central Banks Maintain Interest Rates

Despite pivoting from an environment of consistent interest rate increases to one where they are contemplating the prospect of lowering rates, the Bank of Canada and the U.S. Federal Reserve kept interest rates unchanged during the first quarter. Going into the year, the U.S. Federal Reserve indicated that they could lower rates by 75 bp during 2024. Market expectations were more aggressive, calling for potentially seven interest rate cuts this year in the U.S. Given the sticky inflation that has existed so far this year, market expectations have back-tracked and are now in line with those implied by the Fed. The Fed did confirm at their most recent meeting that they were still looking to lower rates by 75 bp this year, surprising some given that persistent inflationary pressures still exist. The Fed did, however, indicate that interest rates could remain higher for longer as they scaled back the interest rate cuts expected next year. Both the European Central Bank and the Bank of England kept rates unchanged during the quarter.

Economic Growth Remains Resilient

Economic growth remains resilient, particularly in the U.S., which continues to be driven by the consumer sector. In addition, the manufacturing sector is now growing at an expansionary pace. Fourth quarter GDP came in at an annual rate of 3.4%, a drop from the 4.9% rate for the third quarter, but still higher than expectations. Canadian GDP has started the year off on a strong note, with January GDP up 0.6%, with indications for February solid as well, with monthly growth of 0.4%. These stronger-than-expected growth figures have increased the likelihood that there will be a soft landing, if not, a no landing scenario. Prospects for recessionary conditions have diminished, however, there could still be a lagged impact on the economy from the significant rate hikes that have occurred over the past two years.

North American labour markets continue to exceed expectations, both in Canada and the U.S.

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Key Metrics

Indicator	Value	Chg Q1	Chg 1Y
S&P/TSX Composite	22,167.03	6.6%	14.0%
S&P 500 (USD)	5,254.35	10.6%	29.9%
iShares MSCI EAFE ETF (USD)	79.86	6.0%	15.2%
USD/CAD	$ 0.74	-2.2%	-0.2%
WTI Crude ($/bl))	$ 83.17	16.1%	9.9%
GoC 10Y Bond	3.47%	36 bps	57 bps
GoC Deposit Rate	5.00%	0 bps	50 bps
Cdn CPI YoY	2.8%	-0.6%	-1.5%
US 10Y Treasury	4.20%	32 bps	73 bp
Fed Funds Rate	5.50%	0 bps	50 bps
USD CPI YoY	3.2%	-0.2%	-1.8%

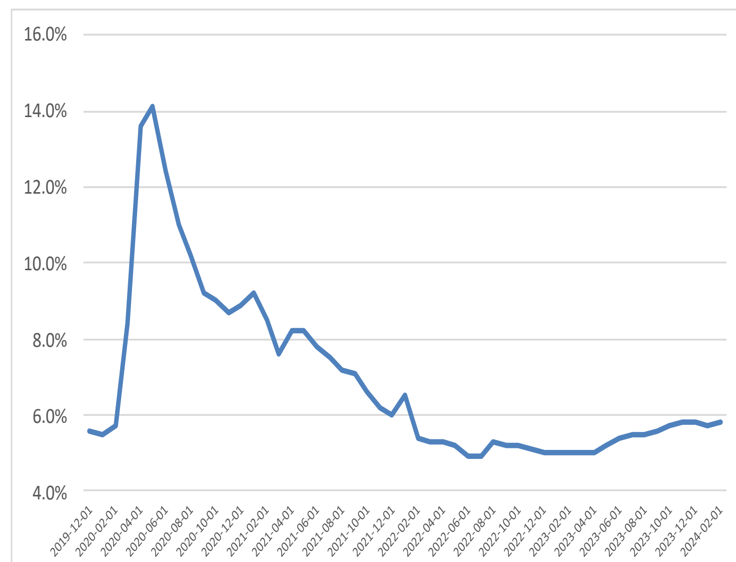
Top Themes

Inflation remains persistent, above desired targets

Market expecting Central Bank rate cuts in 2024

U.S consumer continues to drive resilient economic growth

Top Chart: Canada Unemployment Rate



Source: Bloomberg, Lincluden

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Monthly job gains have been stronger than forecast, with unemployment rates remaining near pre-pandemic levels. There has been a significant increase in the size of the labour force which has put additional strain on the labour market. Wage gains have been a concern as well, which has helped contribute to the inflationary pressures. Recent job openings data in the U.S. indicate that there are fewer jobs available now than there were previously. The ratio of job openings to unemployed people in the U.S. is now 1.36:1, easing substantially from the peak level of 2:1 in 2022. Although this figure still indicates tightness in the labour market, the declining trend could indicate some potential weakness on the labour front.

Equity Markets Advance While Bond Yields March Higher

Equity markets moved higher during the first quarter as economic growth continues at a strong pace. Prospects for an economic recession have diminished, contributing to the strength in equity markets. Higher bond yields, along with a potential delay in the start date for central bank interest rate cuts, have not diminished the bullishness in equities. Bond yields moved higher during the quarter as central banks remained on hold with regard to monetary policy. Market expectations for the magnitude as well as timing of interest rate cuts have now moved back in line with what the Fed is projecting. This has contributed to the upward pressure on bond yields. The benchmark 10 year U.S. Treasury yield increased by 36 bp, finishing the quarter at 4.20%.