Economic Commentary

Second Quarter 2024

Inflation Levels Decline On Uneven Path

Progress continues to be made on the inflation front, however, declines have not occurred on a path that central bankers would like to see. Although current inflation levels are much lower than the peak levels reached in 2022, monthly improvements have not exhibited a consistent downward trend. Canadian inflation started the year at 3.4%, fell during the first two months of the year, and then moved higher in March to 2.9%. Further progress was made in April, with inflation declining to 2.7%, however, there was a surprise uptick to 2.9% again in May. U.S. inflation, which also started the year at 3.4%, has not had a consistent trend either and was 2.9% in May. Inflation in Europe, which peaked at much higher levels than in North America, has shown more dramatic improvement. May inflation in the Eurozone was 2.6% and in the U.K it was 2.0%. Inflation still remains higher than the central bank target of 2% and continues to be the major factor that will impact monetary policy going forward.

Bank of Canada Cuts, But FED Remains On Hold

The Bank of Canada was the first major central bank to cut interest rates, with a 25 bp drop at its June meeting. A decline in April inflation to 2.7% was a key factor contributing to the rate cut. Markets were expecting a further 25 bp cut at the July meeting, however, the surprise uptick in May inflation to 2.9% diminished hopes that a subsequent rate cut would occur. The European Central Bank had its June meeting the day after the Bank of Canada and lowered interest rates by 25 bp as well. Although the U.S. Federal Reserve has pivoted from an environment of interest rate hikes to potential rate cuts, they have not changed their overnight rate so far this year. The Fed was calling for 75 bp in rate cuts in 2024, however, at their most recent meeting they have scaled that back to only one. Persistent inflationary pressure has kept the Fed on the sidelines longer than expected this year. Financial markets are anticipating two interest rate cuts by the Fed this year, with the first cut expected in September.

Economic Growth Showing Signs Of Slowdown

Economic conditions in North America remain fairly strong considering the magnitude of interest rate hikes that has occurred over the past few years. The potential for a recession has diminished dramatically, however, signs are beginning to reflect a moderating trend in the economy. In the U.S., higher mortgage rates have had a negative impact on the housing market while the consumer sector, which had been the driving force behind the economy, has slowed recently. Softness is also evident in both the manufacturing and service sectors, with recent economic data indicating a contracting economy. After outpacing Canadian growth for sometime, U.S. economic growth lagged Canadian growth during the first quarter. First quarter U.S. GDP came in at 1.4%, slightly less than the 1.7% growth rate in Canada.

North American labour markets continue to add jobs at a healthy pace, both in Canada and the U.S. This resiliency in the labour markets has contributed to both the Fed and the Bank of Canada being less aggressive with their interest rate cuts. Although unemployment rates have inched higher, most of the increase has been the

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Key Metrics

Indicator	Value	Chg Q2	Chg 1Y
S&P/TSX Composite	21,875.79	-0.5%	12.1%
S&P 500 (USD)	5,460.48	4.3%	24.5%
iShares MSCI EAFE ETF (USD)	78.33	-0.2%	11.3%
USD/CAD	$ 0.73	-1.0%	-3.2%
WTI Crude ($/bl))	$ 81.54	-2.0%	15.4%
GoC 10Y Bond	3.50%	3 bps	23 bps
GoC Deposit Rate	4.75%	-25 bps	0 bps
Cdn CPI YoY	2.9%	0.0%	0.1%
US 10Y Treasury	4.40%	20 bps	56 bps
Fed Funds Rate	5.50%	0 bps	25 bps
USD CPI YoY	3.3%	-0.2%	0.3%

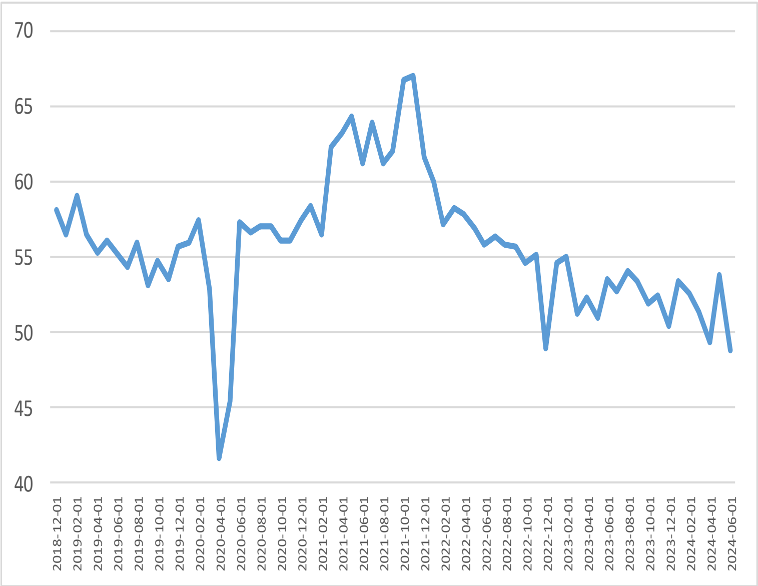
Top Themes

Declines in inflation continue, but path remains uneven

Global central banks begin cutting rates, U.S. FED holding steady for now

Data beginning to reflect moderating trend in the economy

Top Chart: ISM Services PMI Index



Source: Bloomberg, Lincluden

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result of an expanding labour force. Wage gains continue to be a concern, which has helped contribute to on-going inflationary pressures. Recent job openings data in the U.S., however, indicate that there are now fewer jobs available than there were previously. The ratio of job openings to unemployed people in the U.S. continues to decline, with the most recent data showing a ratio of 1.2:1.

Equity Markets Mixed While Bond Yields Creep 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%.