MONTHLY COMMENTARY

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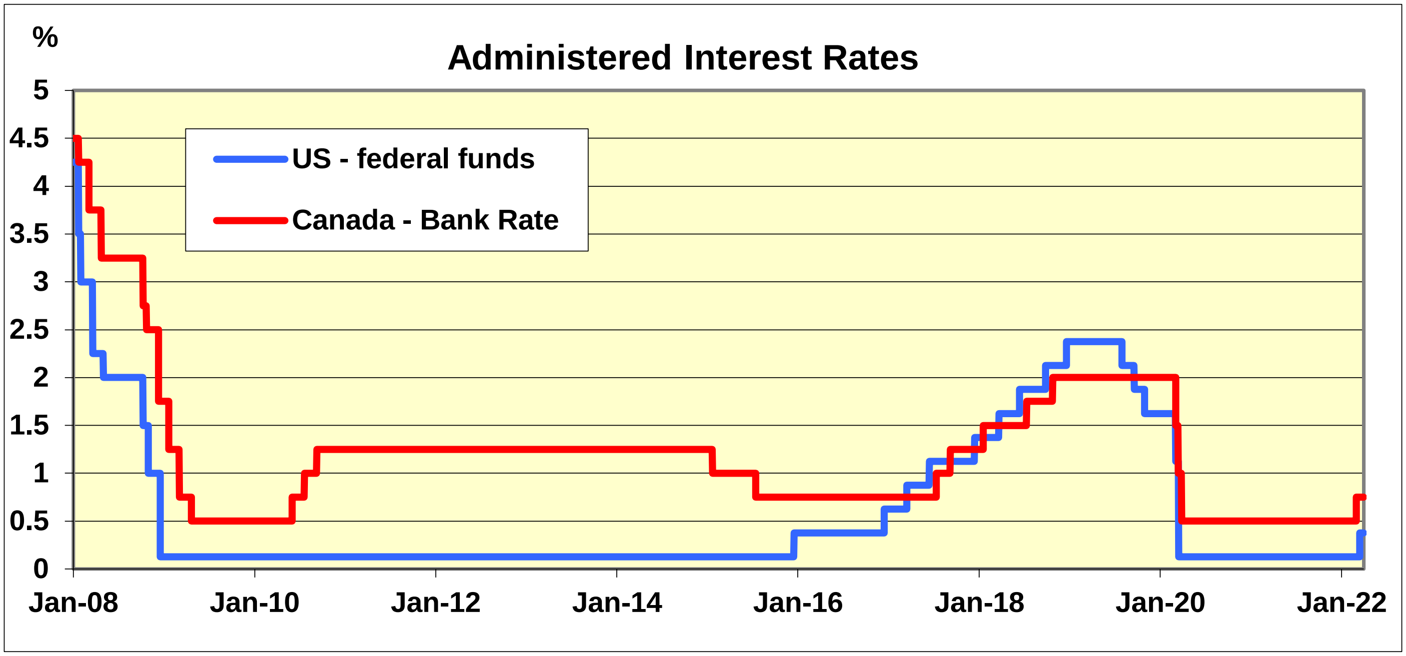
North American rates head higher



Source: U.S. Federal Reserve Board; Bank of Canada

MARKET FOCUS

Fed turns decidedly "hawkish"

Following its two-day monetary policy meeting in March, the U.S. Federal Reserve (the "Fed") raised administered interest rates by 25 basis points (a basis point is 1/100th of one per cent). This moved the federal funds rate target to a range of 0.25% to 0.50% (from 0.00% to 0.25%). As outlined in the accompanying graph, this is the first interest rate hike since December 19, 2018. In the press release that accompanied the announcement, the Fed specifically stated that "inflation remains elevated" and continues to be a key concern. In the update to its December 2021 projections, personal consumption expenditure (PCE) inflation is now expected to be 4.3% for 2022, well above the prior forecast of 2.6%. According to the statement, "the Committee expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities at a coming meeting," thus initiating "quantitative tightening." A further 25-basis point rate hike at each of the Fed's remaining six policy meetings of 2022 would take

the federal funds Target to a range of 1.75% to 2.00%. This is in line with the current “projected appropriate policy path” (median 1.90%). Another 90 basis points of tightening is anticipated for 2023 with the median forecast set at 2.80%. The next Fed policy meeting is scheduled for May 3, 2022, and May 4, 2022.

Bank of Canada

The Bank of Canada also announced that it was raising administered interest rates at the conclusion of its March policy meeting, with its target also moving up 25 basis points. The new range for overnight borrowing was set at 0.25% to 0.75% (previously 0.25% to 0.50%). The change also reinstates the 50-basis point range between the deposit rate and the Bank Rate (the lower and upper limits of the target range). The last time Canadian administered interest rates were increased was on October 24, 2018, when the range was set at 1.50% to 2.00%. The move came as no surprise to the market, as a 25-basis point rate hike was anticipated at the January policy announcement window. At that time, analysts suggested that the delay in raising rates was due to a desire to prevent a move up in the Canadian dollar ahead of any rate action in the United States. Given that the pace of inflation in both Canada and the U.S. stands at multi-decade highs, market watchers will continue to debate how far the two central banks are “behind the curve.”

LONGER VIEW

Interest rates were at their bottom since the start of the pandemic. The U.S. Federal Reserve and the Bank of Canada both began to hike rates in March by 25 basis points. It is widely expected rates to rise to 2% within a year. Compared to running inflation at 5.7% in Canada and 7.9% in U.S., real interest rates are negative. There are multiple factors both domestic and external that drive inflation higher. Tight labour markets have also caused wages to rise. Supply-chain disruptions were supposed to ease but got complicated with the Russia-Ukraine conflict. Even with rate hikes, inflation is unlikely to fall meaningfully in the near term.

Investors need growth to preserve purchasing power. Corporate earnings generally grow with inflation and companies that have pricing power will likely outperform.

For more information, we encourage you to speak to your advisor or visit us at assante.com