

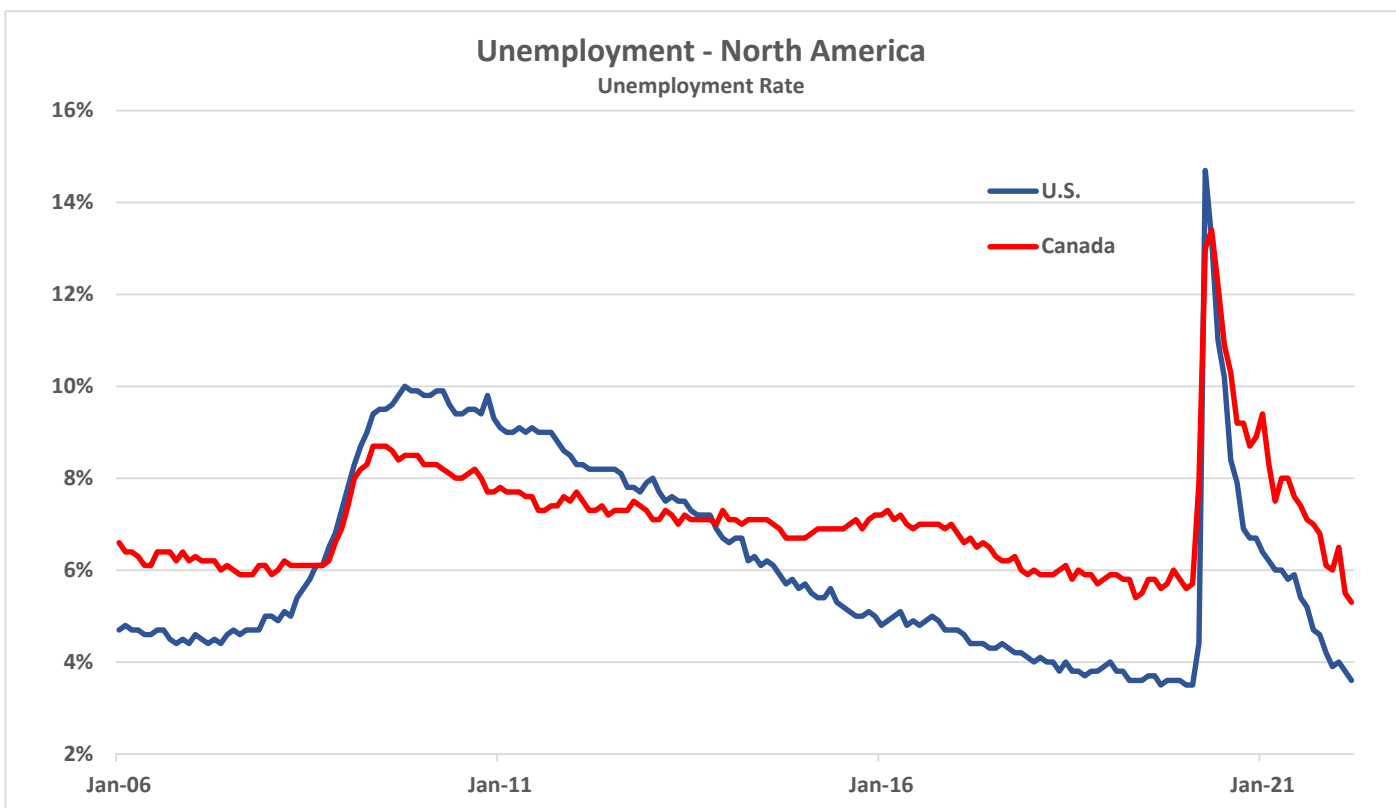
## MONTHLY COMMENTARY

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### North American labour markets tighten



Source: U.S. Bureau of Labor Statistics; Statistics Canada

### MARKET FOCUS

#### Canada sees new low unemployment rate

The pandemic's impact on the Canadian job market in early 2020 was dramatic. A total of three million jobs were lost in March and April of that year. The participation rate (the percentage of the working age population that is either working or looking for work) fell to a record low of 59.9% in April 2020. The unemployment rate subsequently hit a record high of 13.4% in May 2020. Since then,



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the recovery of the jobs lost has been anything but smooth, but total employment eventually reached a new high in November 2021. Statistics Canada further announced that 287,600 (1.5%) more jobs were added between December 2021 and March 2022. At the same time, the participation rate recovered to 65.4%. And, as can be seen in the accompanying graph, the unemployment rate declined to 5.3%, the lowest level on records dating back to 1976. It remains to be seen if the tightening job market will entice more workers to leave the sidelines. Despite the improvement, participation remains below its record high of 67.7% (December 2003). The improvement in the labour market has produced some wage gains. However, average hourly earnings stood with an annual gain of 3.4% in March, approximately half of the 6.7% advance in the Consumer Price Index.

## U.S. wages climb but lag inflation

Like Canada, the U.S. saw a record 22 million job losses during the first wave of COVID-19 restrictions. By April 2020, the U.S. unemployment rate had jumped to 14.7% and the participation rate had fallen to 60.2%. As can be seen in the graph above, the March 2022 report from the U.S. Bureau of Labour Statistics revealed that the unemployment rate had fallen back to 3.6%, only marginally higher than the pre-pandemic low of 3.5% recorded in February 2020. Similarly, non-farm payrolls stood with a 5.0% annual gain and the participation rate recovered to 62.4% in the March data. Average hourly earnings were also up 5.6% on a year-over-year basis, a new post-pandemic high. Still, like Canadian workers, their U.S. counterparts now see a vast rift between that wage growth and the March 8.5% inflation rate. The gap between earnings growth and inflation will continue to raise questions about the potential for a wage-price spiral and the scope of near-term central bank rate hikes.

## LONGER VIEW

Interest rates are at their bottom with the next move likely to be higher, and some investors are hung up on when this will take place. Judging by economic growth, unemployment rates and inflation, we believe the economies are ready for higher rates. So, anytime is fine as long as it is gradual and does not present a shock. We are confident central banks will be managing the hike cycle carefully. How much higher? We suspect the terminal rate is around 2%. A terminal rate is the maximum lending rate of a central bank at the end of a hike cycle. Two percent is substantially lower than normal; but it is important to recognize that we are in a “new normal” where the debt outstanding is significantly bigger, and lower is actually reasonable.

Economies typically start to slow as interest rates peak. We expect central banks to take their time to hike rates to 2%, in possibly two if not three years. Given that 2% is a low hurdle compared to corporate earnings growth, equity should continue to perform as it is obvious that certain sectors will fare better. Long-dated bonds, both 10-year Canada government bonds and U.S. Treasury bonds, are currently yielding below the terminal rate and unlikely to improve anytime soon.

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