THE PLAYBOOK

MONTHLY COMMENTARY

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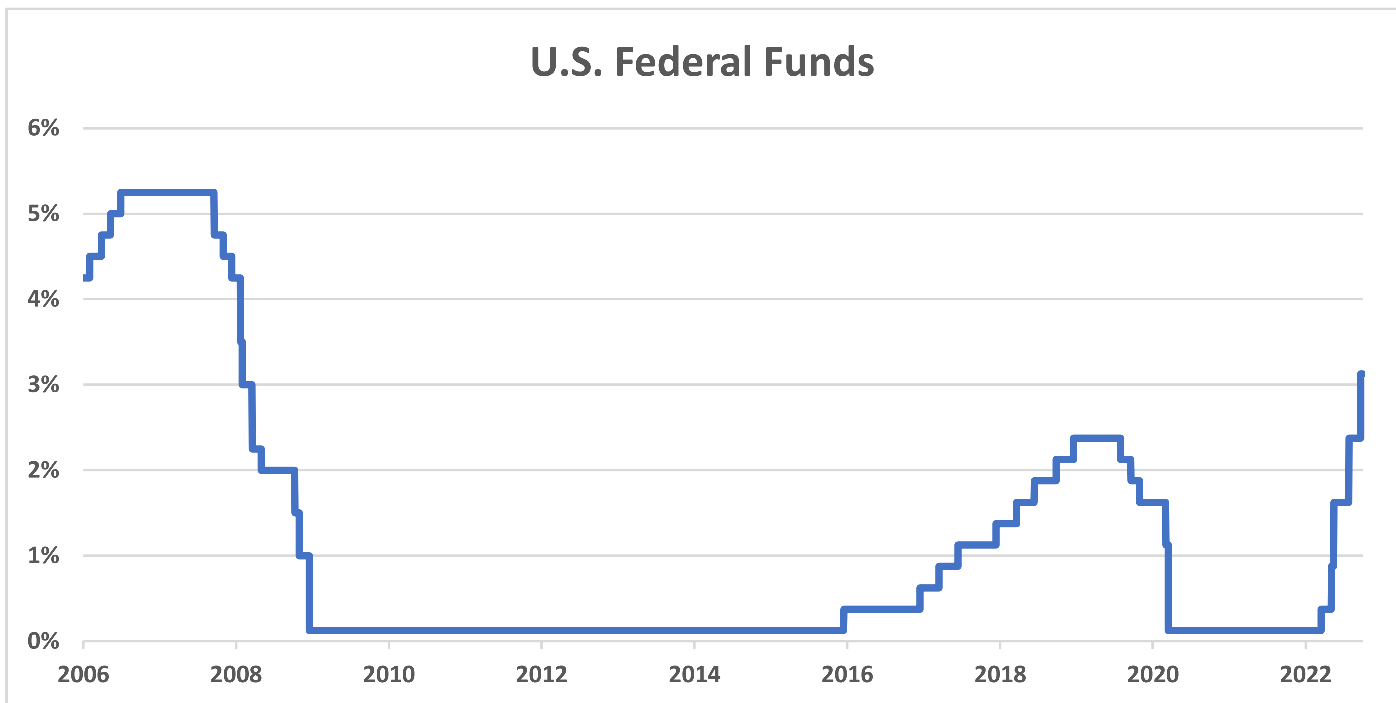
Alfred Lam, MBA, CFA
Senior Vice-President & Chief Investment Officer
CI GAM | Multi-Asset Management

Richard J. Wylie, MA, CFA
Vice-President, Investment Strategy
CI Assante Wealth Management

Rate hikes continue



Source: U.S. Federal Reserve Board.

MARKET FOCUS

U.S. Fed continues to focus on inflation

Following its latest two-day monetary policy meeting, the U.S. Federal Reserve (the "Fed") raised administered interest rates by 75 basis points (a basis point is 1/100th of one per cent), moving the federal funds rate target to a range of 3.00% to 3.25% (from 2.25% to 2.50%). This follows an identical 0.75% increase at the previous policy window and brings the cumulative tightening to 3.00%. As can be seen in the accompanying graph, this is now the highest level for administrated interest rates since January 2008. In the press release that accompanied the announcement, the Fed specifically stated once again that "inflation remains elevated". Projection materials were also provided and show that personal consumption expenditure inflation is now expected to average 5.4%

over 2022 compared to the 5.2% forecast provided in June. This price gauge is now expected to fall back to 2.0% by 2025. GDP growth for 2022, which was anticipated to be 1.7% in June is now forecast at only 0.2%. The dot plot chart – the projection of short-term interest rates – points to further tightening of monetary policy over the balance of 2022 and into early 2023. It now appears that federal funds will likely reach a peak of 4.625% – as the center point of the range – some time in 2023. Scattered, modest rate cuts are now part of the forecast for 2024 and 2025. The next Fed policy meeting is scheduled for November 1 and 2, 2022.

Canadian job market weakens further

Statistics Canada announced that another 39,700 jobs were lost in August 2022. This was the third consecutive monthly decline and the first time it had occurred since November 2015 to January 2016. The cumulative loss of 113,500 was sufficient to take overall employment back to the level last seen in February 2022. At the same time, the unemployment rate jumped from 4.9% in July to 5.4% in the August report. This is also the highest level seen since February of this year. Running counter to these weaker trends, average hourly earnings rose 0.6% in August to stand with a 5.4% advance on a year-over-year basis. This is now the fastest growth pace seen since January 2021 but remains well behind the growth in the consumer price index (7.0% in August). With both North American central banks significantly raising interest rates and the U.S. posting two consecutive quarterly declines in economic output, worries over a potential Canadian recession have emerged. If these fears are realized, the recent softening of the domestic job market may persist for some time to come.

LONGER VIEW

The Federal Reserve has raised rates aggressively this year and that is expected to cool inflation. The side effect of this strategy is a slowing economy and rising unemployment. Until we know how bad these side effects will be, the markets will remain a "guessing game". Over the long term, we expect rates to average 2.25-2.5%; this means the 10-year bond at 3.7% yield today is oversold. Stocks will likely continue to benefit from low long-term interest rates and technology advancement. Economic cycles have been short and volatile as they are heavily influenced by dramatic policies. Therefore, investors should not be overly excited or concerned about what they see in the immediate term.

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

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