MONTHLY COMMENTARY

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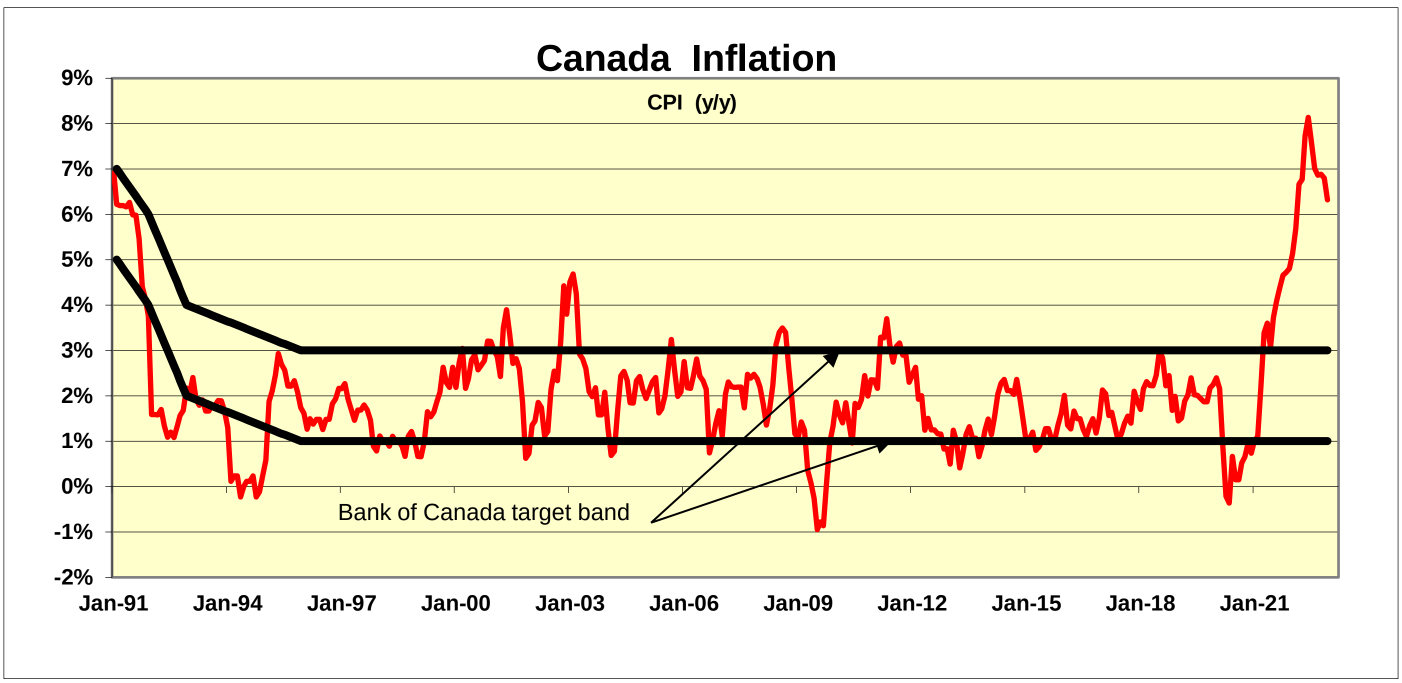
Inflation remains above target



Source: Bank of Canada; Statistics Canada

MARKET FOCUS

Inflation vs. Bank of Canada

The latest figures from Statistics Canada revealed that its Consumer Price Index (CPI) edged 0.1% lower (seasonally adjusted) in December. However, price pressures continue to be elevated. Food prices were up 10.1% compared to a year ago, and that advance came on the back of a 5.2% increase during the prior year. Gasoline prices were up a comparatively modest 3.0% (year-over-year) in this report, but that annual gain followed a 33.3% advance in the previous 12 months. Overall, the CPI was up 6.3% on a year-over-year basis. This is the smallest annual gain since February 2022 as the pace of inflation continues to slowly ease from the 8.1% peak recorded in June 2022 – the fastest pace since January 1983 (8.2%). Even with the apparent moderation, inflation remains well-above the Bank of Canada's (BOC) target band. The BoC initiated its inflation target in February 1991. The relatively new GST. As can be seen by the accompanying graph, it was hoped that inflation could be coaxed down from the

prevailing 6.9%. The process was successful and it critically aided in lowering inflation expectations, which is a key driver of price pressures. It was renewed, with the 1% to 3% target band established in mid-1994. While a number of break-out periods have taken place, the current run-up is the largest deviation by a significant margin. The 25-basis point interest rate hike by the BoC on January 25, 2023, brings the cumulative increase to 4.25%. It remains to be seen if another move is in store at the next policy announcement window, scheduled for March 8, 2023.

U.S. output contracts

Updated data from the U.S. Federal Reserve Board (the "Fed") revealed a 0.7% decline in industrial production in December 2022. In addition, revised figures now show a similar 0.6% drop in November. For the fourth quarter of 2022, as a whole, industrial output contracted at an annualized 1.7% rate. This is the first production decline since the dramatic, pandemic-induced 41.6% annualized rate in the second quarter of 2020. In line with the slippage in output, capacity utilization fell to 78.6%, the lowest since October 2021 and a sharp drop from the 80.2% seen as recently as April 2022. The decline in U.S. industrial activity comes as the demand for goods weakens amid faltering economic growth and higher interest rates in the U.S. and globally. While this shift will raise concerns over a potential near-term recession, the majority of market participants continue to anticipate another interest rate increase from the Fed at their next two-day policy meeting, scheduled to begin on January 31, 2023

LONGER VIEW

The U.S. Federal Reserve has raised rates aggressively in 2022 and this has already had an impact on cooling 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% to 2.5%. This means the 10-year bond at 3.5% yield today (1/26/2023) 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