April 2023 market update

Canadians are feeling the squeeze of higher rates

May 4, 2023

Introduction

Global equity markets were relatively volatile over April but finished the month higher. Sentiment swung as investors speculated about the size of the next interest rate hikes by the U.S. Federal Reserve Board ("Fed") and other central banks based on incoming economic data. Toward the end of the month, confidence in the U.S. banking system was frayed after First Republic Bank announced deposits dropped by 42% in the first quarter. Regulators stepped in and JPMorgan Chase & Co. agreed to acquire the troubled bank at the end of the month.

There were no Fed, Bank of England and European Central Bank meetings in April. The Bank of Canada ("BoC"), Bank of Japan and People's Bank of China held their key interest rates steady during the month. Inflation subsided again in March but remained relatively elevated. Global labour markets were strong, continuing to prop up consumer strength. Global manufacturing and service sector activity provided mixed results over April.

The S&P/TSX Composite Index posted a gain, with all 11 sectors delivering a positive return. In the U.S., the S&P 500 Index advanced, benefiting from the strong performance of the Communication Services sector. The price of oil and gold ticked higher over the month. Yields on 10-year government bonds in Canada and the U.S. finished largely unchanged.

Global economic activity solid, but not particularly great

The world's largest economies announced their first quarter gross domestic product growth rates in April, with data suggesting the global economy is expanding but at a slower pace. A preliminary estimate showed the U.S. economy expanded at an annualized pace of 1.1% over the first quarter of 2023, moderating from the 2.6% expansion in the final quarter of 2022. The U.S. consumer drove most of the growth, pushing household consumption higher over the quarter despite tight financial conditions. This was partially offset by a drop in real estate investment. China posted annual growth of 4.5% in the first quarter, with economic activity boosted by easing lockdown restrictions. Meanwhile, Europe's economy expanded by 0.1% over the first quarter of 2022, an increase from the revised 0.1% decline in the fourth quarter of 2022.

The data suggests the global economy could avoid a recession. However, a deterioration in economic conditions might persist. In its World Economic Outlook, the International Monetary Fund ("IMF") expects the global economy to grow slower this year than last. The IMF believes geopolitical tensions, particularly growing tensions between the U.S. and China, could hinder growth. Furthermore, ongoing geopolitical tensions could harm emerging markets economies, causing a slowdown in foreign investment amid global tensions and sluggish growth.

North American inflationary pressures easing

Inflation data from March showed pressures in Canada and the U.S. moderated but remaining at levels well above BoC and Fed targets. In Canada, the inflation rate slowed to 4.3% in March, its slowest pace since August 2021. Declining gasoline prices were the main driver behind the decline. While the drop in gasoline prices was welcome news, it could be short-lived. The Organization of the Petroleum Exporting Countries announced it will reduce oil production, which could put upward pressure on oil prices. In the U.S., the story was much the same with a decline in gasoline prices pushing the inflation rate lower to 5.0%. This marked its lowest level in almost two years. Falling inflation figures suggest the monetary tightening program by both central banks have helped. But inflation remains too high and broad-based. The BoC has paused its interest rate increases as it monitors the slowdown in inflation and the Canadian economy. Meanwhile, the Fed appears poised to keep attacking inflation with more rate hikes on the way.

Canadians feeling the squeeze

Recent data suggests Canadian households are beginning to feel the pinch from ultra-high inflation and rising interest rates. Retail sales in Canada dropped 0.2% in February, the third month in the past four without any sales growth. Lower sales at gasoline stations and general merchandise retailers drove the decline. Excluding automotive sales, retail sales fell by 0.7%. And the outlook for March is not promising. Statistics Canada estimates a 1.4% decline in March. Canadian households appear to be cutting back on spending amid tight financial conditions. Despite pulling back on discretionary spending, Canadians are having difficulty paying for the necessities. A survey by the Angus Reid Institute found two-fifths of Canadians are turning to their savings accounts to help keep up with inflation. They are also holding back on contributions to their TFSA and RRSPs, which could have long-term implications for their overall financial plan. A strong labour market is supporting Canadians, but a pullback in spending could weigh on Canada's economic health.

U.S. credit conditions expected to tighten

The collapse of Silicon Valley Bank and subsequent deterioration of several U.S. regional banks sent ripples among investors, concerned about significant trouble in the global banking system. Regulators and lawmakers stepped in to do what they could to restore confidence in the banking system. But the effects of this episode might not be over. The Fed stated that the U.S. banking system remains strong, but warned that credit conditions could tighten. A recent Federal Reserve Bank of New York survey shows that may be happening. The survey found 58.2% of Americans are having difficulties getting credit this year compared to the same time last year. This will add to the financial struggles many U.S. households are facing. The same survey showed more Americans believe they may miss a minimum debt repayment over the next year. Further rate hikes and ongoing U.S. banking system struggles could exasperate the problem. Tighter credit conditions in the U.S. could have an impact on households and businesses, which may negatively affect economic growth.

Market performance - as at April 30, 2023

Equity Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
S&P/TSX Composite Index C$	20,636.54	2.67%	**2.67%**	6.46%	**6.46%**	-2.29%	**-2.29%**
MSCI USA Index US$	3,950.69	1.18%	**1.39%**	8.53%	**8.71%**	-3.46%	**2.18%**
MSCI EAFE Index US$	2,143.85	2.45%	**2.67%**	10.28%	**10.46%**	6.52%	**12.74%**
MSCI Emerging Markets Index US$	977.05	-1.34%	**-1.13%**	2.16%	**2.33%**	-7.28%	**-1.87%**
MSCI Europe Index US$	1,971.69	3.62%	**3.84%**	13.87%	**14.05%**	10.22%	**16.66%**
MSCI AC Asia Pacific Index US$	160.32	-1.10%	**-0.89%**	2.94%	**3.11%**	-3.21%	**2.45%**

Fixed Income Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
FTSE Canada Universe Bond Index C$	1,095.61	0.98%	**0.98%**	4.23%	**4.23%**	1.83%	**1.83%**

FTSE World Investment Grade Bond Index US$	210.42	0.71%	**0.92%**	4.06%	**4.23%**	-2.25%	**3.46%**

Currencies	**Level**	**Month to date**	**Month to date (C$)**	**Year to date**	**Year to date (C$)**	**1 year**	**1 year (C$)**
CAD/USD	0.7379	-0.55%	-	-0.29%	-	-5.76%	-

Commodities	**Level**	**Month to date**	**Month to date (C$)**	**Year to date**	**Year to date (C$)**	**1 year**	**1 year (C$)**
West Texas Intermediate (US$/bbl)	76.78	1.47%	-	-4.34%	-	-27.13%	-
Gold (US$/oz)	1,990.00	1.05%	-	9.10%	-	5.04%	-