QUARTERLY COMMENTARY

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Spring Showers

According to Wikipedia, “May you live in interesting times" is an English expression that is claimed to be a translation of a traditional Chinese curse. While seemingly a blessing, the expression is normally used ironically; life is better in "uninteresting times" of peace and tranquility than in "interesting" ones, which are usually times of trouble.

Well whether we like it or not these times certainly are interesting. In March, the markets saw Silvergate Bank, Silicon Valley Bank and Signature Bank wind down operations in the U.S. due to asset to liability mismatches and a bank run from depositors. The crisis in confidence quickly spread to Europe and saw UBS Group AG takeover rival Credit Suisse in a rushed sale.

There was an understandable kneejerk reaction by many depositors in the U.S. to seek a perceived safer haven for their personal savings before the federal government stepped in and essentially guaranteed bank deposits. Although it is possible we’ll see some other banks run into trouble in the near future, the markets have settled down and nothing disastrous like the great financial crisis of 2008 ever took hold.

Indeed, the stock markets in the first quarter of the year was robust – the TSX was up around 3.5%, the NASDAQ was up 9.5%, and the S&P 7.5%. That’s not enough to nullify all of the losses of last year, but put together with the positive returns at the end of 2022 it is a

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significant bounce. Last month the Bank of Canada became the world's first major central bank to pause its tightening campaign, leaving its benchmark rate at 4.50%. Governor Tiff Macklem said he wanted to let the eight previous rate hikes sink in and would hold off on further increases as long as inflation came down as forecast.

The Bank of Canada wrote in its latest release that global economic growth has been stronger than anticipated and has surprised on the upside, but it is expected to weaken as tighter monetary policy continues to feed through those economies. Inflation has been edging down, reaching 5.2% in February after peaking at 8.1%, but growth at the start of the year has vastly outpaced the bank's expectations. Despite this the bank expects CPI inflation to fall to around 3% in the middle of this year and recent data is reinforcing their confidence that inflation will continue to decline in the next few months. In the U.S. the Federal Reserve in its March 22 policy announcement, endorsed the health of the U.S. banking system but cautioned that recent developments were likely to result in tighter credit conditions and to weigh on economic activity. If a slowdown becomes evident then you'll see the Fed go to pause mode as well.

Where we go from here will depend on corporate earnings over the next few quarters and as earnings season has just begun we should get a good sense of what the short term direction of the markets will be. For calendar-year 2023, the consensus earnings estimate is for a 2% contraction. But that estimate is still coming down, and based on historical patterns, could continue to do so. I could easily imagine that corporate earnings contract 10% this year. If earnings fall only as much as the consensus estimates suggest, and the Fed is either done tightening or close to it, then perhaps spring really has sprung, and we can see the light at the end of the tunnel.

Last week saw a lower-than-expected core inflation figure in U.S. (core inflation removes the impact of food and energy prices, which tend to be more volatile than prices of other goods). The core PCE rate of change peaked at 5.42% last June, and as of

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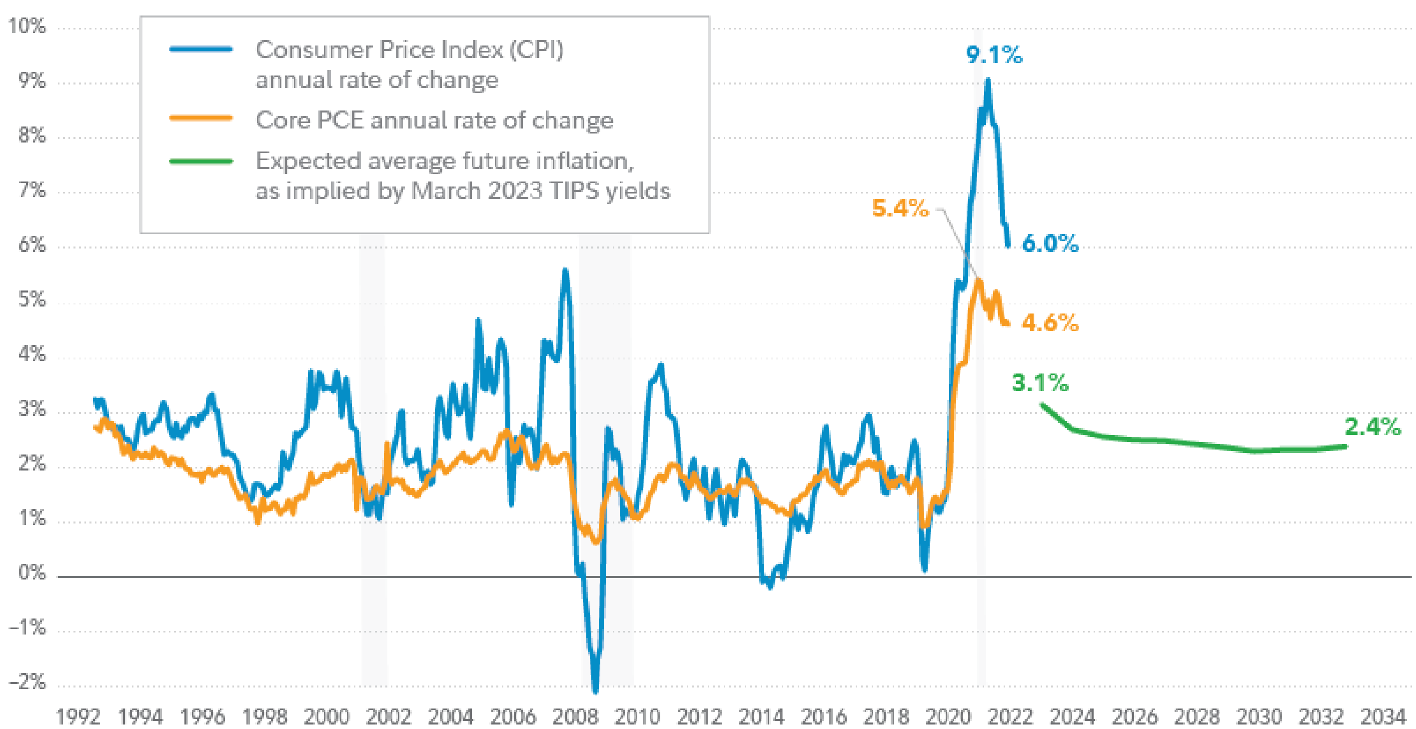
last week's report was down to 4.60% (compared with the Fed's 2% target). As for the future trajectory of inflation, markets seem to be showing an expectation for a fairly quick reversion to lower inflation. Expectations implied by yields for Treasury Inflation-Protected Securities (TIPS) show an expectation for a rapid return to a lower, more normal rate of inflation.

Reported inflation vs. inflation expectations



Will this indicator's expectation be as accurate this time as it has been in past? Or is the market thinking wishfully in assuming we'll revert to a 2% level of inflation again so quickly? The next 6 months to a year will provide a much better picture of whether inflation will be truly tamed.

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Whether we're headed for a recession is a topic of great debate. We don't know when a recession might begin, how long it will last, or precisely when equity markets will recover from one but equity prices frequently begin to fall prior to the start of a recession, hit their low point during the recession, and typically start to recover before the end of it. An analysis of 11 cycles since 1950 shows that recessions have persisted between two and 18 months, with the average spanning about 10 months. Since it's impossible to time these things the best thing to do during uncertain times is to have some funds available in case a really good buying opportunity presents itself. That doesn't mean you sell in anticipation of an event that might not even happen though. When you are invested in great companies paying good dividends, that's always enough to get you through the any rough period.

Thank you for your continued trust and confidence. Should you have any questions or concerns at any time or if you would like to have a detailed discussion of your personal portfolio, please do not hesitate to let me know.

Sincerely,

Richard