

# Wickham Investment Counsel Inc.

Quarterly Review

Mar 2023

## The Pause That Refreshes

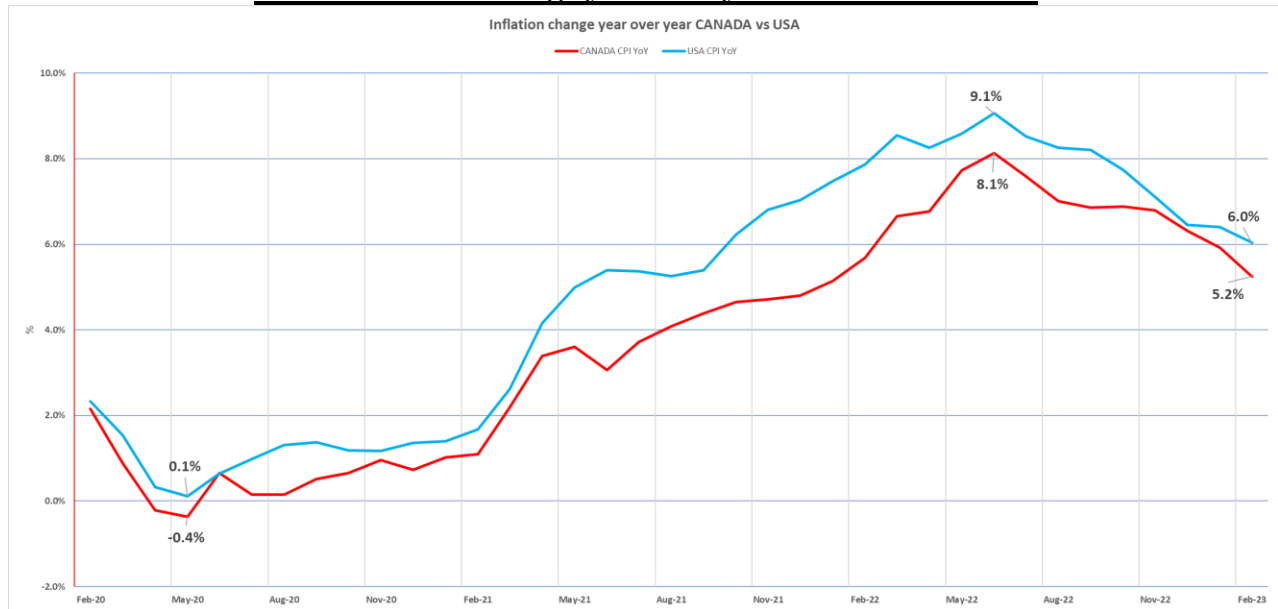
Last year Central Banks changed course to dramatically tighten monetary conditions to fight inflation, and this resulted in one of the worst years for a traditional balanced portfolio. Both bonds and stocks suffered, causing a -16.9% decline overall. Now things are changing as we enter the second quarter of 2023. The Bank of Canada increased its overnight rate by 25 basis points to 4.50% in January marking the Banks' eight consecutive increase and brings cumulative tightening since March 2022 to 4.25%. The Bank also said it would continue its Quantitative Tightening (QT) program, passively running off its government of Canada bond holdings. But by March 2023 the Bank decided to put its rake hikes on pause and reassess the situation over time. Most economists now expect rates to be steady in 2023 and some think a cut is possible.

At 5.2%, inflation is gradually easing but is still running well above the 2% target and may not reach it until 2025. The Canadian economy is expected to grow by 0.7% this year and 1.4% in 2024. Indeed, the economy was still growing in Q1, and employment was surprisingly strong, holding the unemployment rate at a healthy 5.0%. The US Federal Reserve has been more aggressive however and pressed ahead with its ninth consecutive rate hike to 4.75 – 5.00% but signaled that it may be near the end of its monetary tightening campaign. The annual rate of inflation was 6% in February. Money supply and credit are now declining. No rate cuts are expected until 2024.

Financial markets are forward-looking and do not agree with this assessment. The bond and stock markets rallied in the first quarter. Interest rate futures suggest that the US hiking cycle is over, and the Fed will cut rates by .75–1.00% by year end. This *opposing view* would see near term recessionary conditions bring down inflation and shift the monetary needle towards growth. This opposing view was reinforced by the prominent regional banking failures in the US and Europe, and concerns about commercial real estate. The US regional banking crisis is not over, and it is thought that another major European bank will fall (after Credit Suisse). We begin to see significantly and fundamentally strong growth stocks like technology and health care participate in the market rally. Even some of the weakest companies bounced off their lows.

The reason that stock markets tend to perform well in the run-up to the Fed's rate cut is that investors hope for a soft landing but may, nevertheless, experience a recession. Consensus earnings estimates for the S&P 500 companies for 2023 are still close to the 220 level of last year and with a recovery to 248 in 2024. Indeed, corporate revenues seem to have held up in Q1, but rising costs are hurting margins. This has resulted in a modest lowering of Q1 profit expectations. Consequently, some companies are reducing employees/freezing hiring and others are reducing their sales outlook this year. And that is exactly what the Central Bankers are hoping for.

## Chart: Inflation change year over year CANADA vs USA



Source Canada CPI: [www.150.statcan.gc.ca](http://www.150.statcan.gc.ca) USA CPI: [www.bls.gov/cpi](http://www.bls.gov/cpi)

|                             | Dec 31,<br>2016 | Dec 31,<br>2017 | Dec 31,<br>2018 | Dec 31,<br>2019 | Dec 31,<br>2020 | Dec 31,<br>2021 | Dec 31,<br>2022 | Mar 31,<br>2023 | % Change<br>Dec-Mar |
|-----------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|---------------------|
| <b>Stock Market Indices</b> |                 |                 |                 |                 |                 |                 |                 |                 |                     |
| S&P/TSX Comp.               | 15,288          | 16,209          | 14,323          | 17,063          | 17,433          | 21,223          | 19,385          | 20,100          | 3.69%               |
| Dow Jones Ind.              | 19,763          | 24,719          | 23,328          | 28,538          | 30,607          | 36,338          | 33,147          | 33,274          | 0.38%               |
| S&P 500                     | 2,239           | 2,674           | 2,507           | 3,231           | 3,756           | 4,766           | 3,840           | 4,109           | 7.01%               |
| Nasdaq Comp.                | 5,383           | 6,903           | 6,635           | 8,973           | 12,888          | 15,645          | 10,466          | 12,222          | 16.78%              |
| <b>Commodities</b>          |                 |                 |                 |                 |                 |                 |                 |                 |                     |
| Gold - US\$                 | 1,252           | 1,309           | 1,281           | 1,523           | 1,895           | 1,829           | 1,826           | 1,986           | 8.76%               |
| Crude Oil WTI - US\$        | 53.72           | 60.42           | 45.41           | 61.06           | 48.52           | 75.21           | 80.26           | 75.67           | -5.72%              |
| Natural Gas - US\$          | 3.74            | 2.95            | 2.94            | 2.19            | 2.54            | 3.73            | 4.68            | 2.18            | -53.42%             |
| <b>Currencies</b>           |                 |                 |                 |                 |                 |                 |                 |                 |                     |
| € in Cdn \$                 | 1.42            | 1.50            | 1.56            | 1.46            | 1.56            | 1.44            | 1.45            | 1.47            | 1.38%               |
| £ in Cdn \$                 | 1.66            | 1.69            | 1.74            | 1.72            | 1.74            | 1.71            | 1.63            | 1.68            | 3.07%               |
| US\$ in Cdn \$              | 1.34            | 1.26            | 1.37            | 1.30            | 1.27            | 1.26            | 1.36            | 1.35            | -0.74%              |
| <b>Interest Rates</b>       |                 |                 |                 |                 |                 |                 |                 |                 |                     |
| Cdn Prime rate              | 2.70            | 3.20            | 3.95            | 3.95            | 2.45            | 2.45            | 6.45            | 6.70            | 3.88%               |
| US Prime rate               | 3.50            | 4.50            | 5.50            | 4.75            | 3.25            | 3.25            | 7.50            | 8.00            | 6.67%               |
| Cdn 10 Yr bond              | 1.72            | 2.04            | 1.95            | 1.64            | 0.70            | 1.45            | 3.30            | 2.89            | -12.42%             |
| US 10 Yr bond               | 2.44            | 2.40            | 2.69            | 1.92            | 0.93            | 1.52            | 3.88            | 3.57            | -7.99%              |

Source: The Globe & Mail