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CHARTBOOK
Market Comment

Prepared by OceanFront Investment Counsel Inc.

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OCEANFRONT INVESTMENT COUNSEL INC.

CONTRIBUTORS

OCEANFRONT
INVESTMENT COUNSEL INC.

PORTFOLIO MANAGERS

Scott Keast, CIM, CFP®
Shane McMahon, CIM, CFP®
Matthew Cameron, CFA®, CIM®
Adam Carris, CFA®, CIM®, CFP®

ASSOCIATE ADVISING REPRESENTATIVE

Kim Reynolds, CIM®, CFP®

OCEANFRONT
WEALTH INC.

SENIOR WEALTH PARTNER

Bruce Lindsay, CFP®, CH.F.C.®, CLU®

Market Comment

The US regional banking crisis rattled markets in March, as a number of small and mid-size banks in the US faced liquidity issues. Some banks, like Silicon Valley Bank ('SVB"), were caught offside holding their reserves in high quality US Treasury Bonds that had declined in value due to rising interest rates. When interest rates were near zero, SVB had made the decision to hold their reserves in safe, long-term Treasury Bonds without hedging the interest rate risk. This turned out to be a very unfortunate decision when the Federal Reserve began quickly raising rates, contrary to their previous guidance on interest rate expectations. There were many factors that contributed to the collapse of SVB, but the increase in rates was probably the most important.

The good news is that authorities around the world have moved to shore up liquidity in the banking system through various means and the problems seem to be contained, at least for now. Throughout this period, volatility in the stock market has been fairly calm while bonds have experienced substantial swings up and down as interest rate expectations get re-priced.

The regional bank crisis has changed the outlook for interest rates, as this event in itself tightens financial conditions by way of contracting credit. This may allow the Fed to pause their cycle of rate hikes and markets are now pricing in a lower Fed Funds interest rate by the end of the year, a dramatic shift from just a few weeks ago.

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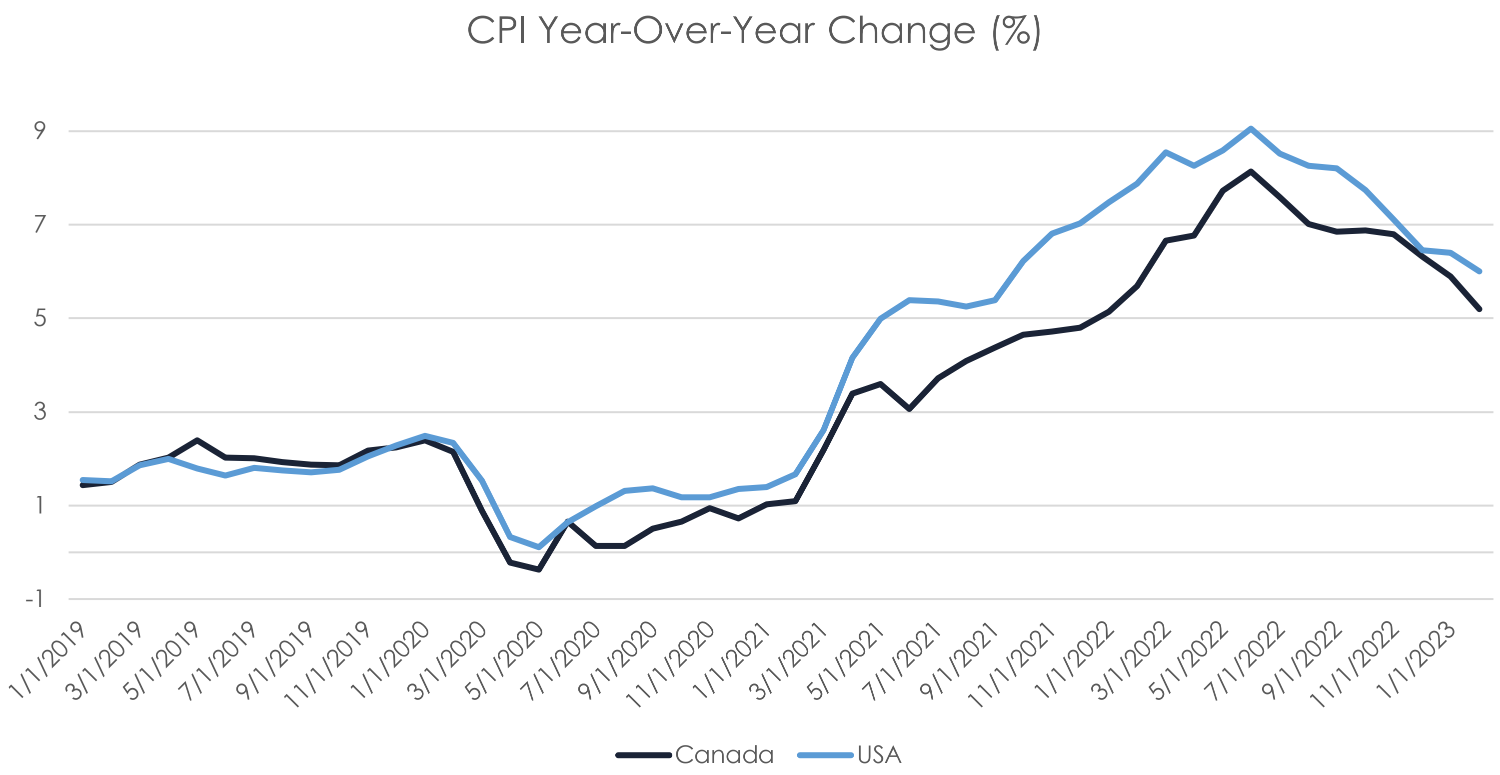
Inflation

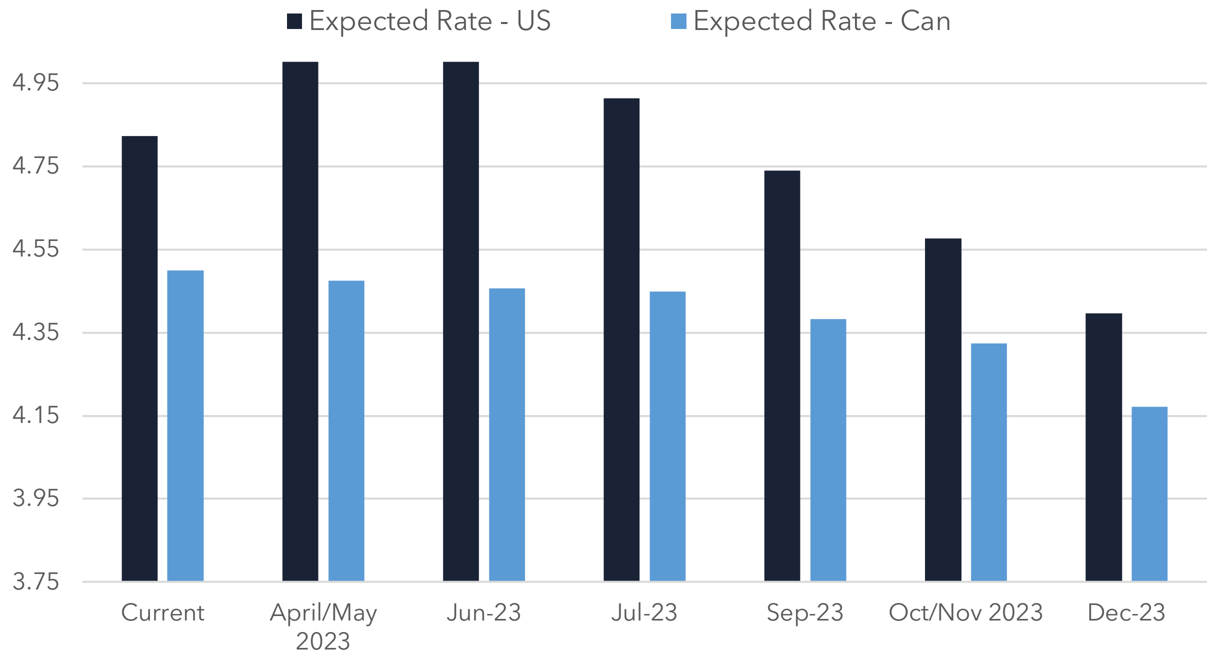


The most recent data showed inflation at 5.2% YoY in Canada and 6.0% YoY in the USA. The rate of inflation remains in steady decline in both economies.

 Source: Bloomberg, OceanFront Investment Counsel Inc.

Interest Rate Expectations

The regional bank issues in the US have changed the interest rate outlook in the US, where there are now expectations for a lower Fed Funds rate by the end of the year, similar to the outlook for the Bank of Canada's overnight rate.



Data as of April 10, 2023

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Interest Rate Expectations (cont.)

This chart shows how quickly interest rate expectations changed during the failure of Silicon Valley Bank. Just days before the failure, markets were pricing in 3-4 further interest rate hikes from the Federal Reserve. The day the bank failed, markets began pricing in 3-4 cuts by the end of 2023!

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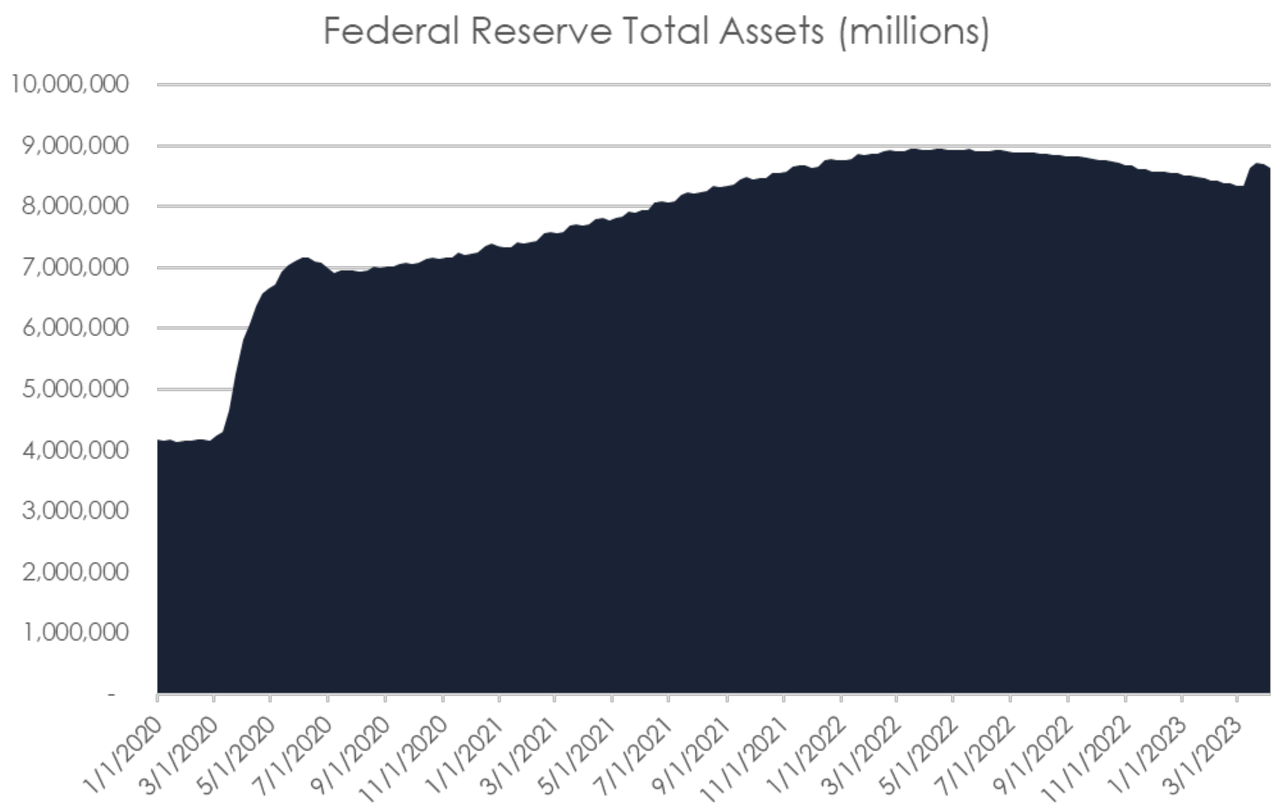
Quantitative Easing?

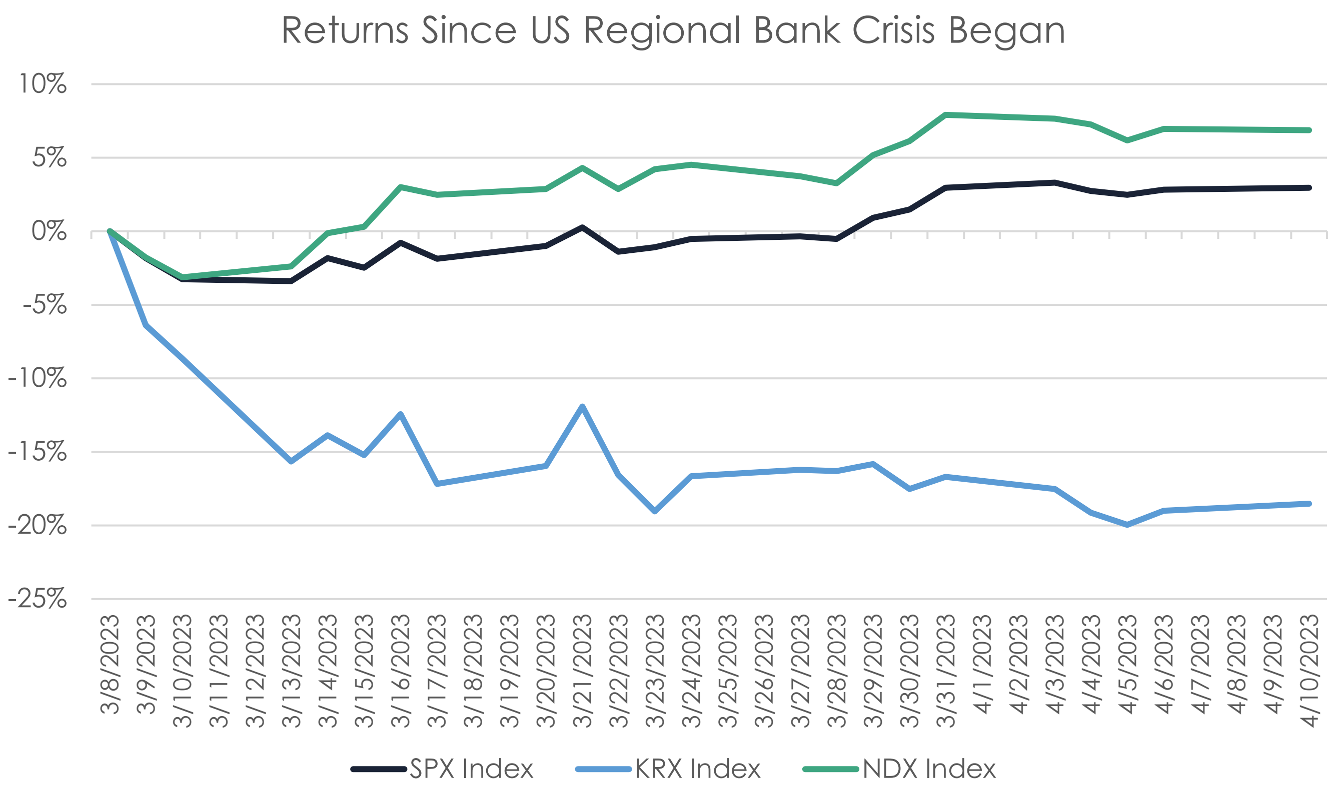


In the wake of the problems at Silicon Valley Bank and other banks, the Federal Reserve made a liquidity facility available to backstop the banking system. This has resulted in a quantitative easing-like effect of injecting new money into the financial system, which is inflationary, just as the Fed is fighting to bring inflation down. The Fed had begun reducing its assets in 2022, removing liquidity from the financial system to fight inflation. With the recent liquidity provided to banks, they have already re-accumulated roughly half that amount of assets (although this is supposed to be a temporary measure).

These banking issues have thus far resulted in a contraction in credit as banks have become more reluctant to extend loans, which is deflationary. At this time it's unclear what the net effect of these actions will be on inflation.

Resilient Index Returns

Since the days leading up to the failure of Silicon Valley Bank, both the S&P500 Index and Nasdaq 100 Index show positive returns, while the KBW Regional Bank Index is down nearly 20%. This appears to be a good sign that the bank issues are contained.



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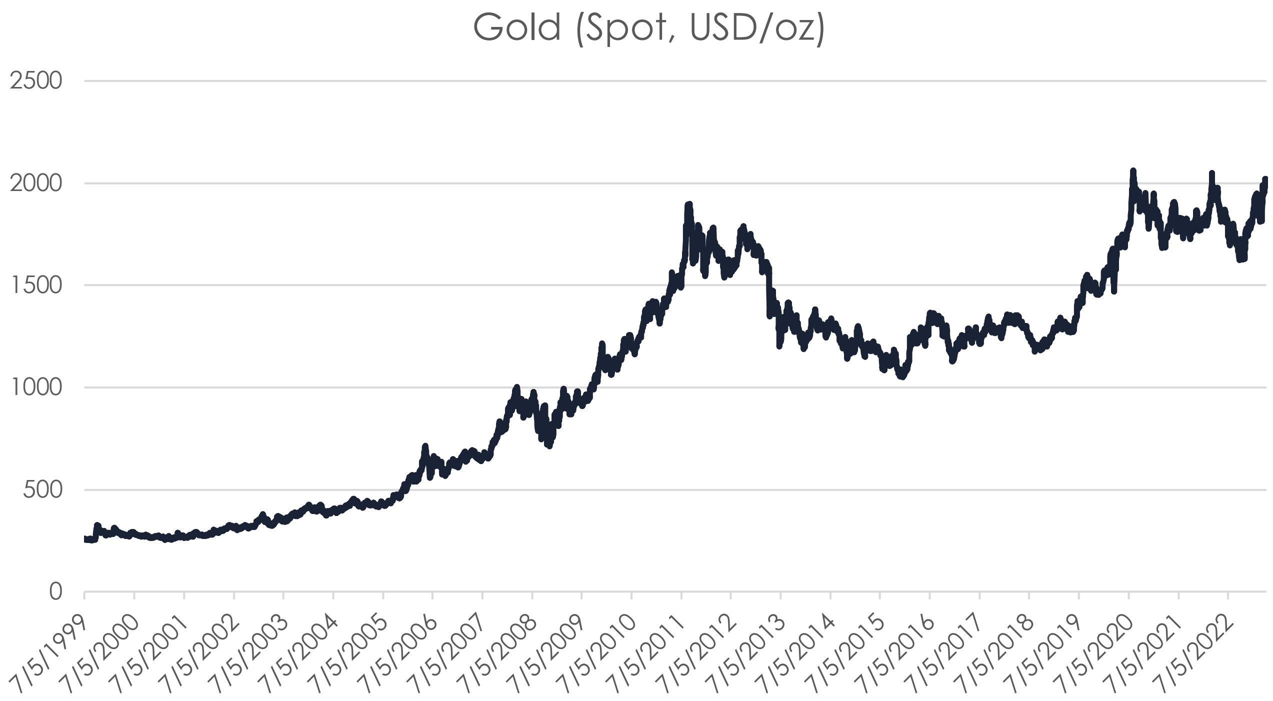
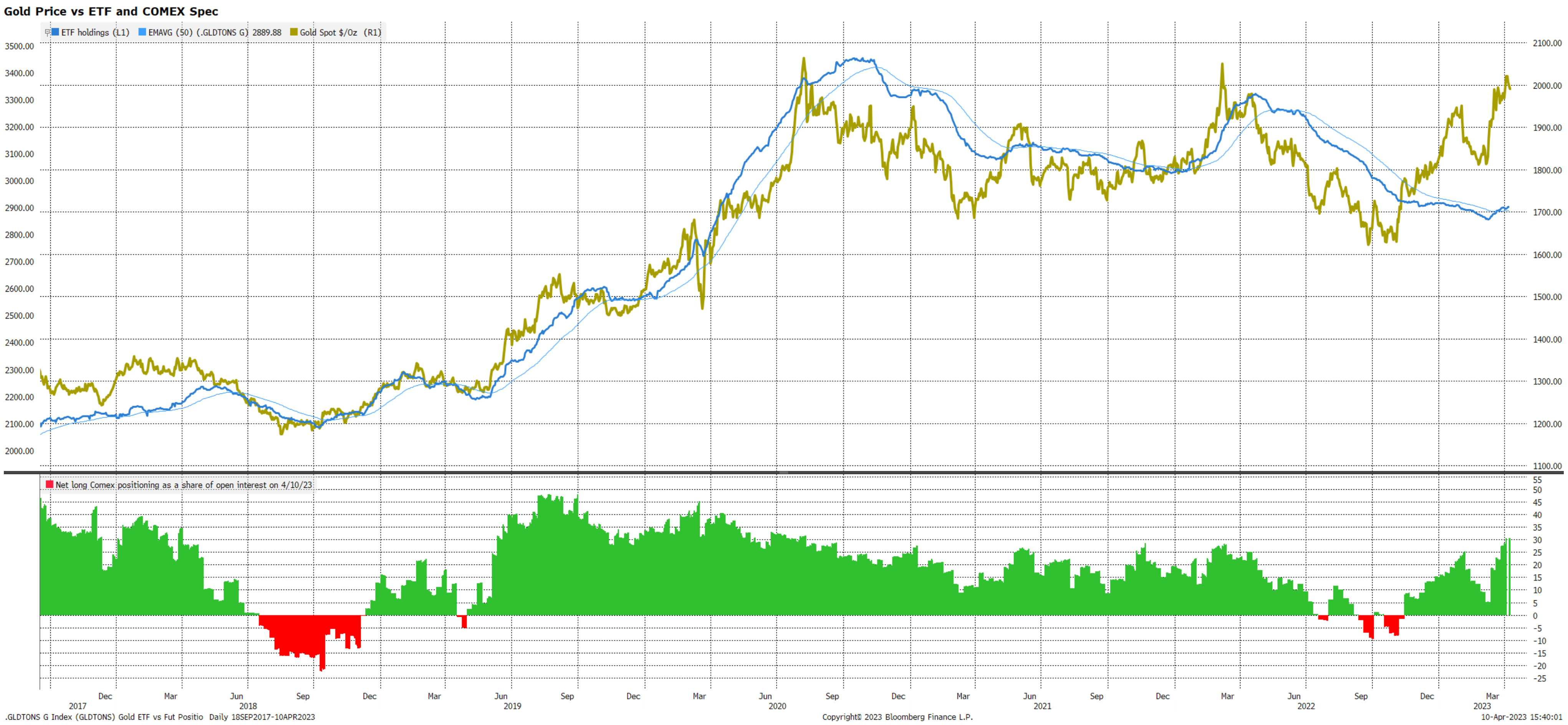
Gold

Gold has quietly been among the very best performing assets since the beginning of 2022. After an epic bull market run in the early 2000's, investments in gold have been essentially dead money since that bull market ended in 2011/2012.

With gold showing strength and knocking on the door of new all-time highs in price, perhaps a new bull market is coming.



Gold Positioning & Demand



Gold speculative positioning from COMEX trading flipped from net short to net long in late 2022, but holdings in ETFs have just recently begun to increase. If ETF holdings catch up to COMEX positioning, it would be a big tailwind for gold demand in a market where new supply is slow to respond.

Gold Versus Real Interest Rates

Gold tends to have a strong negative correlation to real (inflation adjusted) interest rates, the theory being that gold competes with bonds as a store of value and is more attractive than bonds when real rates are low or negative. Interestingly, there is currently a large disconnect in this relationship, which suggests that either gold is too highly priced or inflation expectations are too low.

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