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CHARTBOOK
Market Comment

Prepared by OceanFront Investment Counsel Inc.

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TABLE OF CONTENTS

Chartbook Market Comment: August 2023

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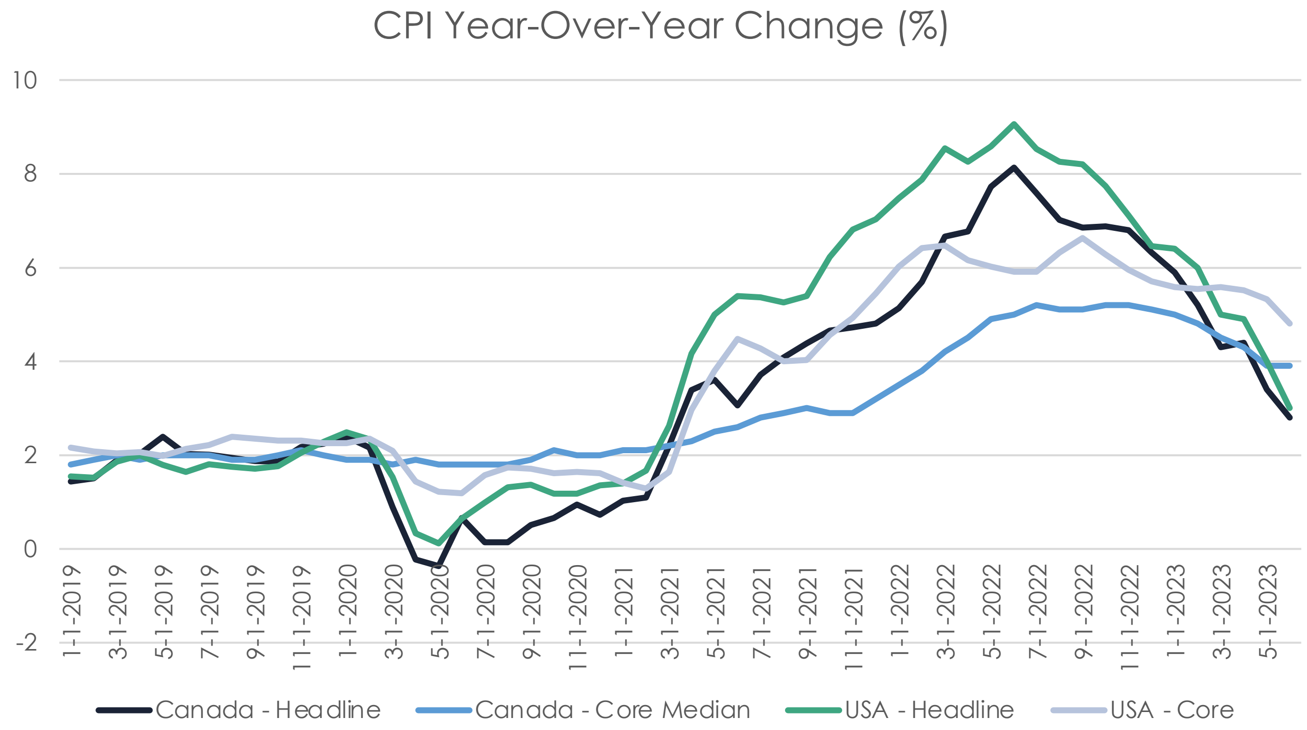
Market Comment

Last week the Federal Reserve (the "Fed") announced it would raise its policy interest rate by 25 basis points to a range of 5.25-5.5%. The Fed noted that it would look to adjust its policy as appropriate depending on the nature of future data releases and risks that may emerge. Essentially, the Fed is focused on its goal of returning inflation to its 2% objective and is prepared to raise rates even higher if that goal seems at risk.

This followed the Bank of Canada's announcement earlier in July that it would raise its policy interest rate by 25 basis points as well. In its press release, the Bank noted that "global inflation is easing, with lower energy prices and a decline in goods price inflation. However, robust demand and tight labour markets are causing persistent inflationary pressures in services". There are some areas of the economy where inflation has been more resilient than others, and large declines in energy prices, including the price of oil, have led the decline in inflation. Volatile energy prices now pose a significant risk to the upside for inflation, as they are now relatively low compared to the sky-high prices we saw in the first half of 2022.

Also of note, the Fed is no longer forecasting a recession but does expect a slowdown in growth. This would be the so-called "soft-landing" scenario where inflation cools without a recession or significant increase in unemployment. The data backs up this sentiment, as the economy has remained resilient despite the much higher interest rates while inflation has fallen dramatically. With US CPI inflation at 3.0%, there is some work to do to return inflation to the Fed's target of 2%, but the soft-landing scenario is looking likelier than ever at the moment.

Inflation



Inflation continues to decline in Canada and the USA. In Canada, year-over-year headline inflation is now below 3%. Core inflation, which strips out the volatile food and energy prices, remains more resilient.

 Source: Bloomberg, OceanFront Investment Counsel Inc.

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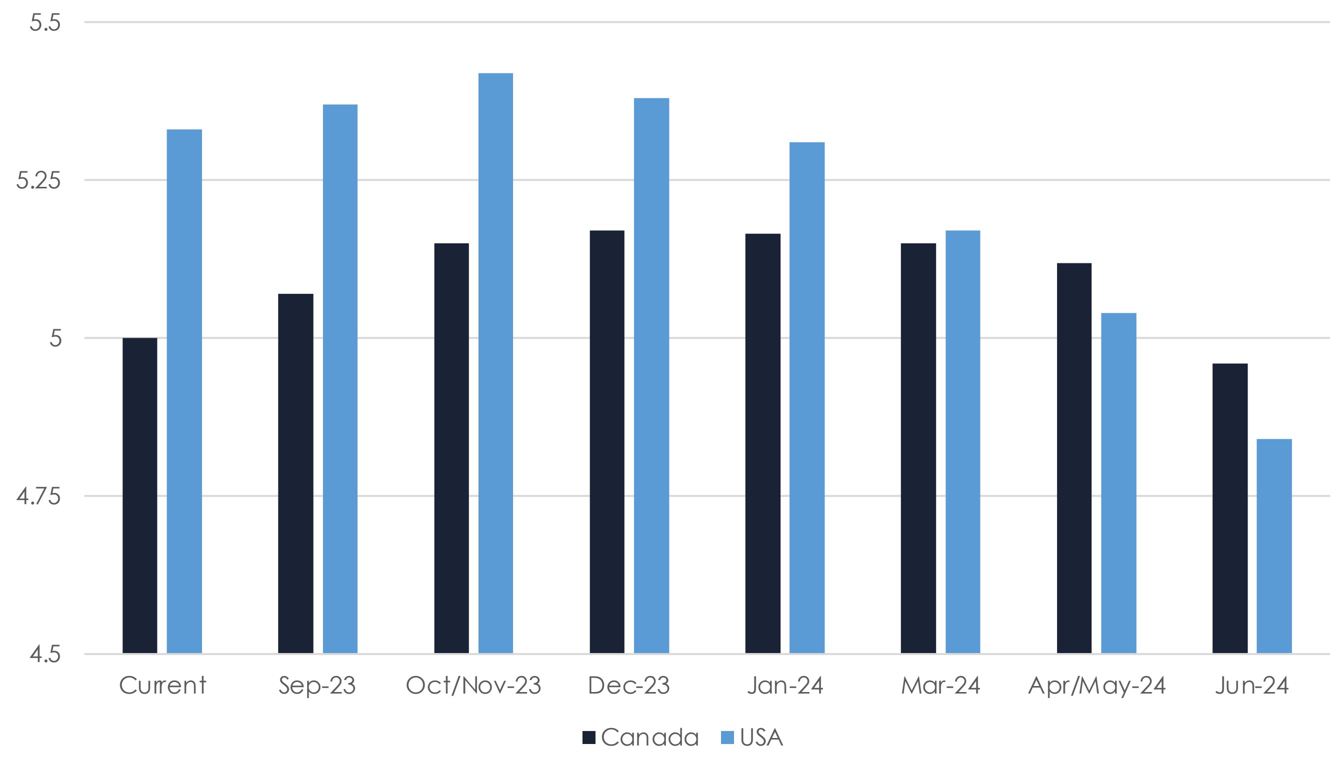
Interest Rate Expectations

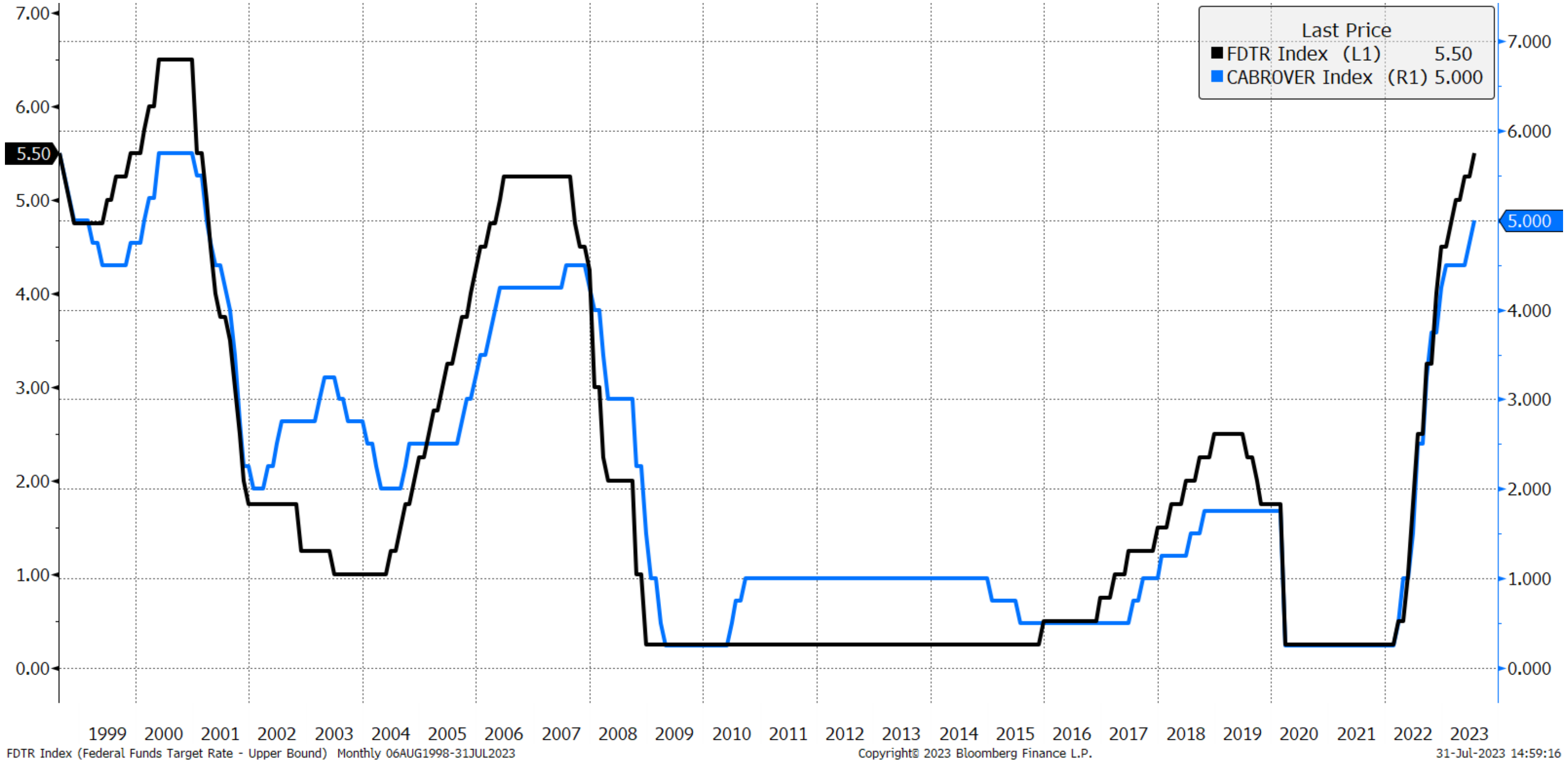
Markets are expecting that we are within 25 basis points of the peak in interest rates, with perhaps one small cut but no major changes expected over the next year or so. Any flare ups in inflation could dramatically change this outlook.



Data as of July 31, 2023

Historical Interest Rates

Overnight interest rates in Canada and the USA, the rates which are set by the central banks in each country, recently reached 20+ year highs.



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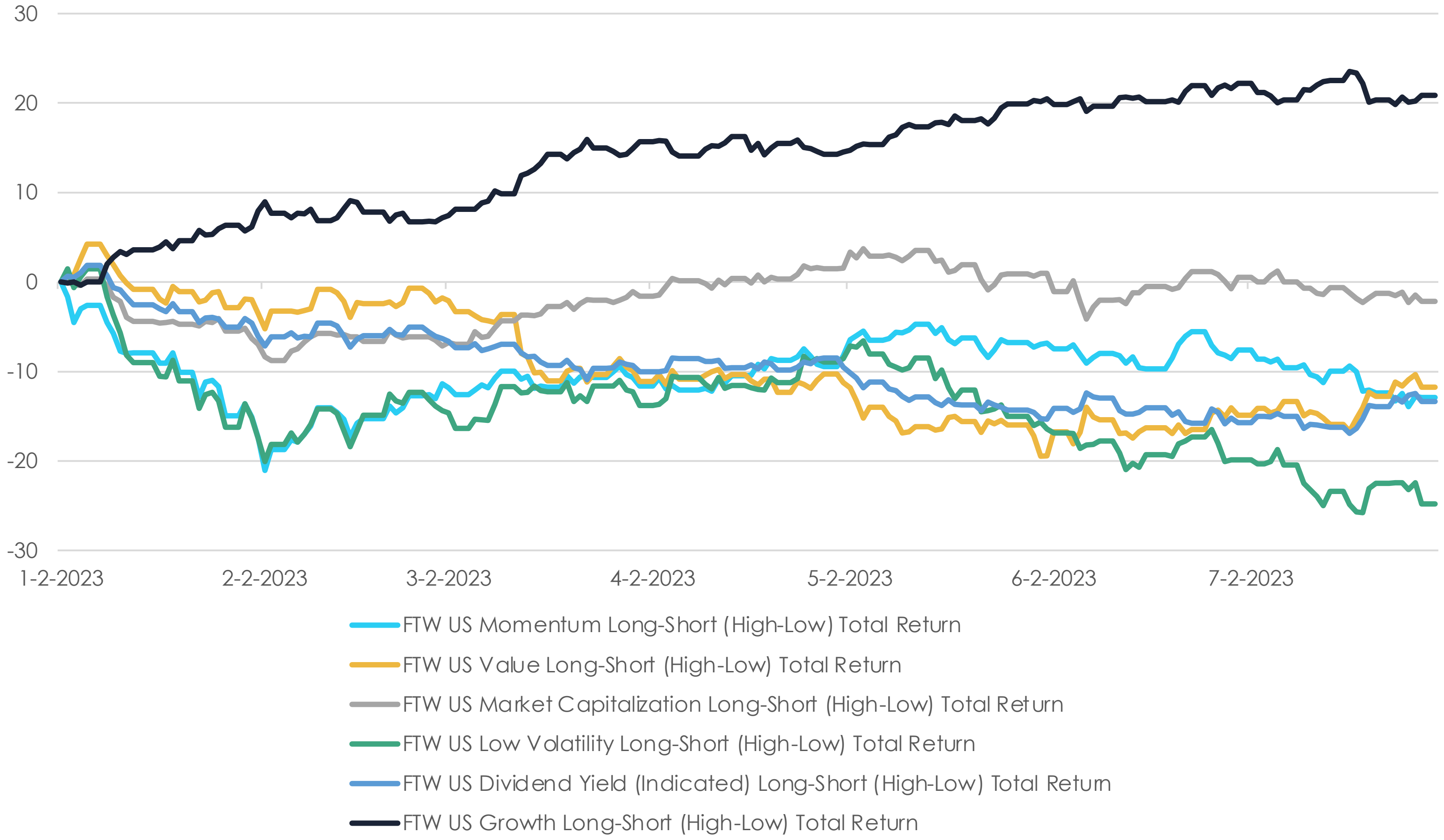
Factor Returns



This chart shows the year-to-date performance of certain factors like growth, value, size (aka "market capitalization"), and others. You can see that only the growth factor has been positive this year, far ahead of all the others. Stocks classified as growth companies typically exhibit strong earnings growth and make up much of the Nasdaq index, which has been a top performer this year after a very poor return in 2022.

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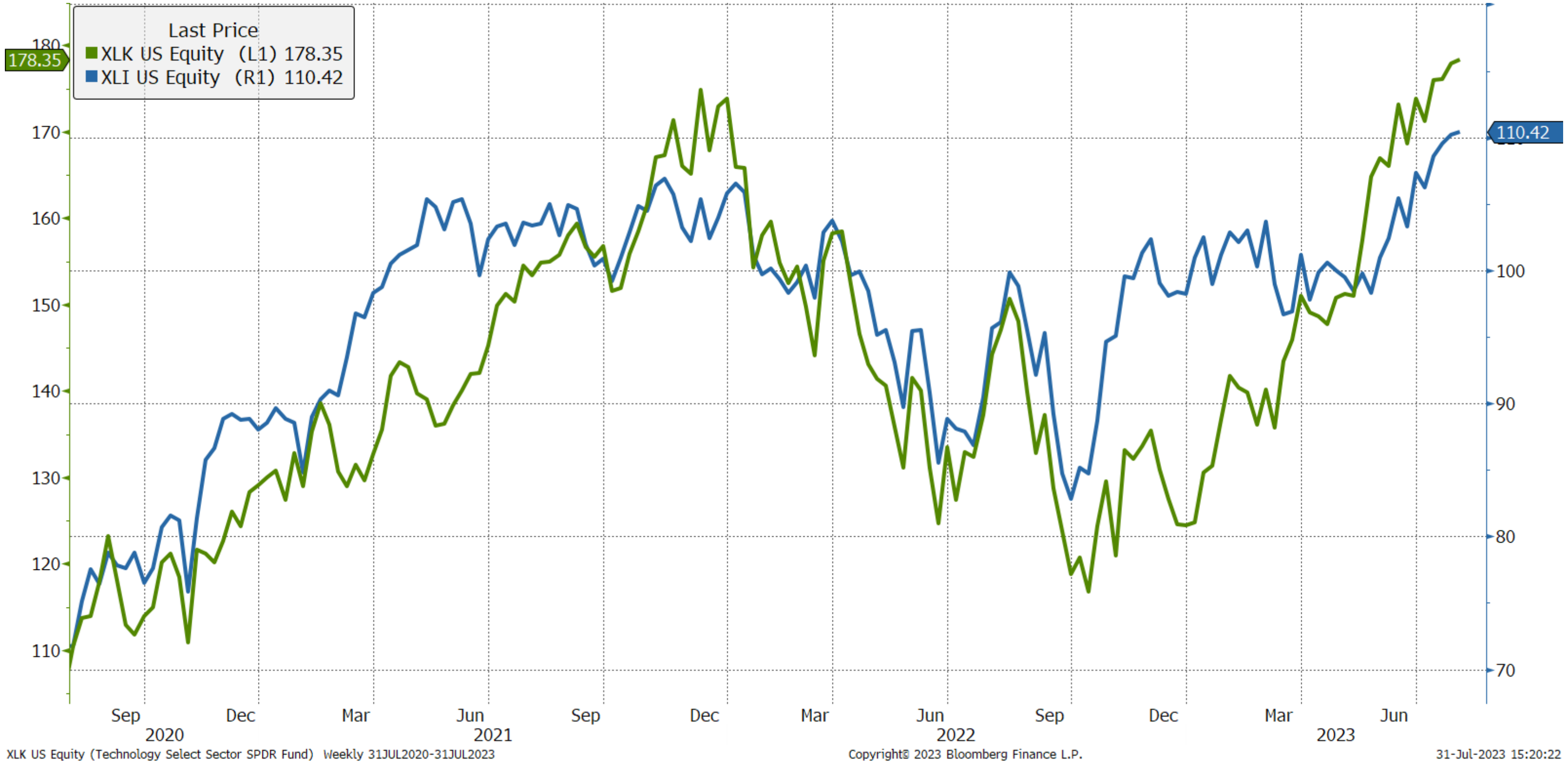
Industrials versus Technology



Much of the technology sector (green) is classified as "growth" and thus has been a top performer of late, recently hitting new all-time highs in price. Also hitting new all-time highs recently but getting less attention is the industrial sector. Major sectors like these climbing to new highs suggest a new bull market has begun.

 Source: Bloomberg, OceanFront Investment Counsel Inc.

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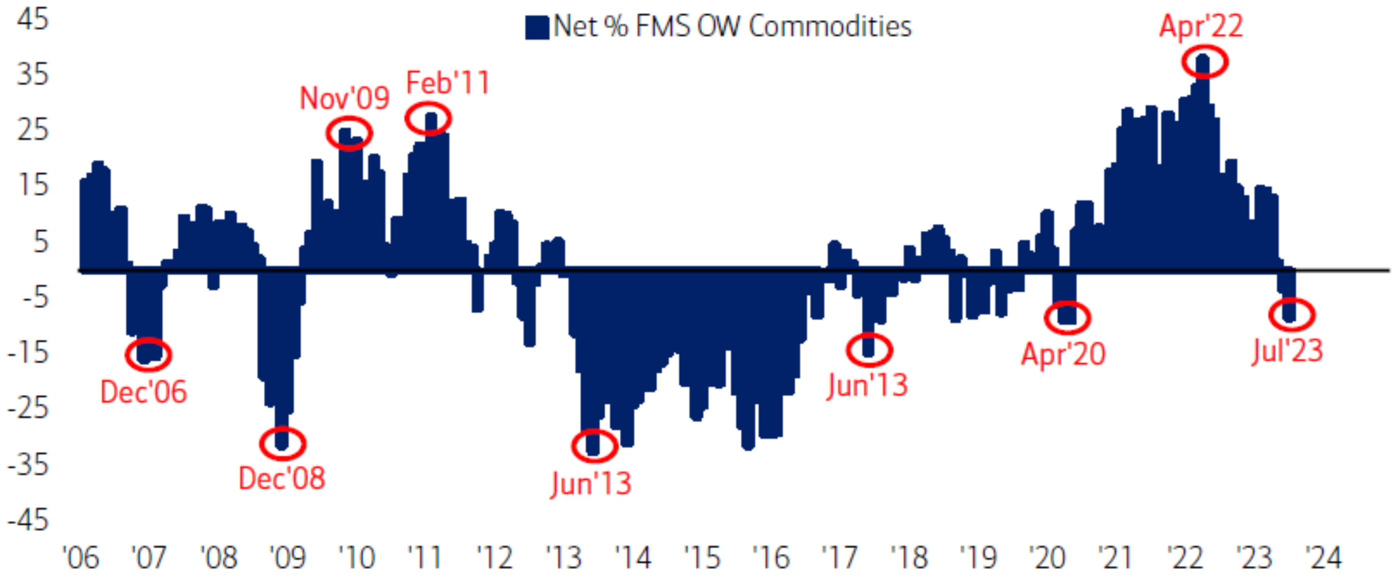
Volatility Index

The volatility index has settled at very low, calm levels, the lowest since 2019 just before the explosion in volatility in the first days of the COVID pandemic. Are we entering a new regime of sustained lower volatility, as typically occurs during bull markets, or is this a sign of complacency with higher volatility around the corner? Time will tell.

Fund Manager Survey

Chart 3: FMS investors most UW commodities since May'20
Net % FMS investors saying they are OW commodities



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

Commodities seem to have fallen out of favor with fund managers this year, as surveyed fund managers recently said they were mostly underweight commodities. The last time fund managers were this underweight the sector led to excellent returns in 2021/2022. These fund managers getting back on-board with commodities again would be a nice tailwind for the sector.

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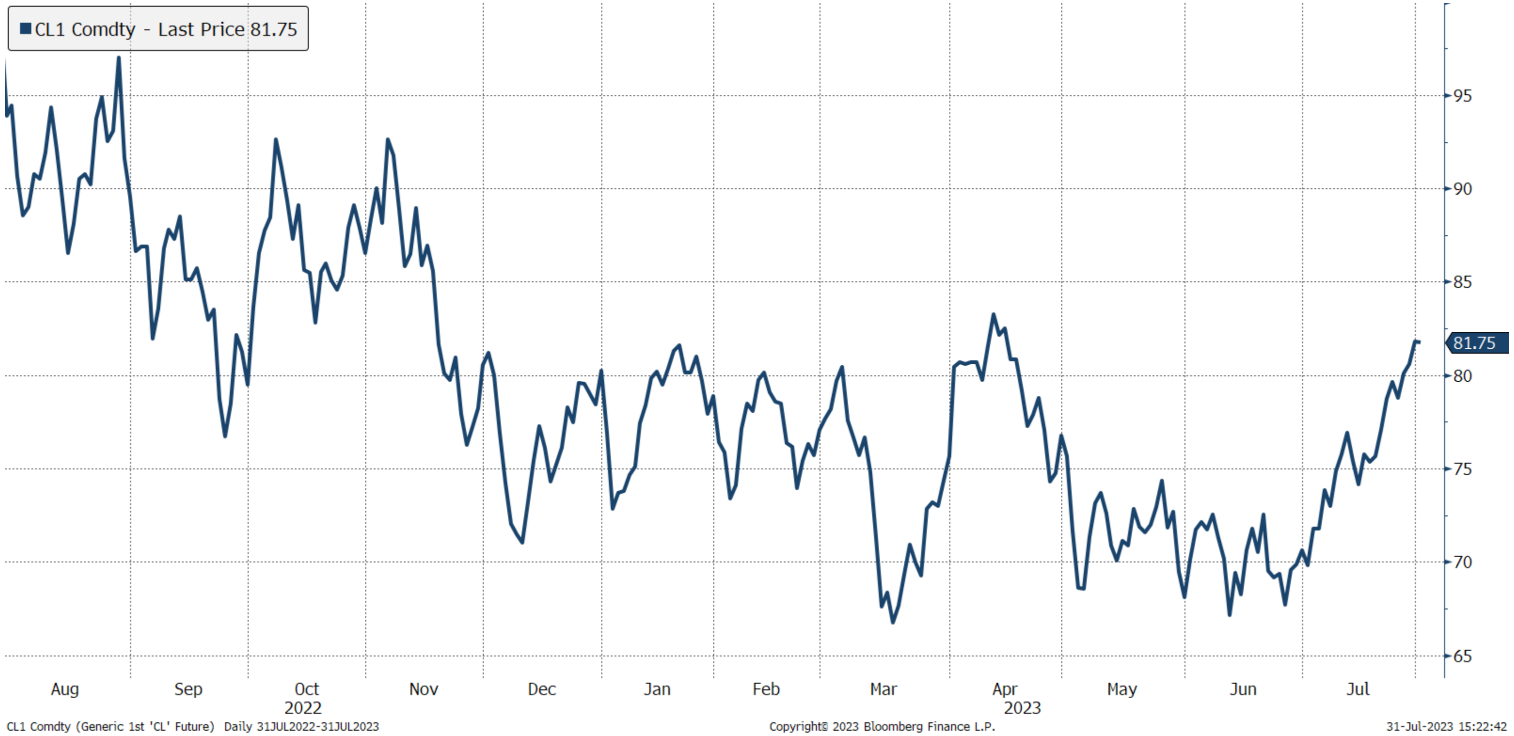
Oil



As seen in the last slide, commodities, including oil, have fallen out of favor with fund managers. This makes sense when looking at the price chart of the price of oil, which did nothing but zigzag for six months with no progress up or down until July.

Oil making continued progress higher would be a boon for the oil and gas sector but could be a significant setback in the fight against inflation.

 Source: Bloomberg, OceanFront Investment Counsel Inc.

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