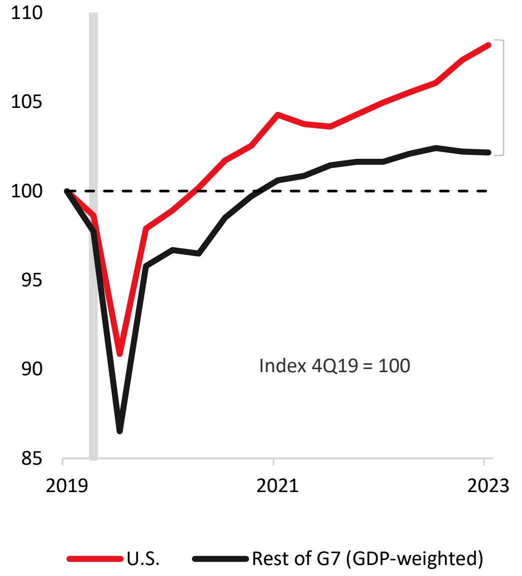
MARKET OUTLOOK | APRIL 2024

Outlook highlights

- Economic data has been uniformly better-than-expected in major developed economies, though performance divergences have continued to widen
- Better-than-expected economic data has come at an inflationary cost, which could push out the timing of future policy rate cuts
- Soft landing odds are likely to deteriorate the longer that policy rates remain elevated, due to high levels of global indebtedness
- Household spending is likely to slow under the weight of high interest rates, elevated debt loads, and impending mortgage maturities
- Fiscal health is key to promoting economic growth and tackling key challenges affecting households and businesses
- 2024 budget aims to address issues related to housing, affordability, and healthcare, but are forecasted to increase the deficit

Key developments

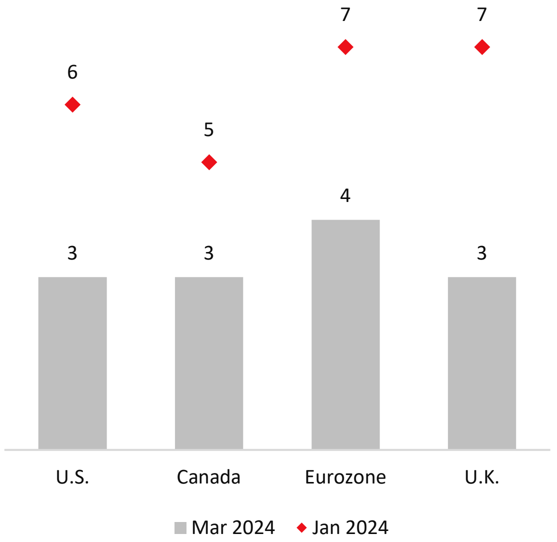
Growth profiles are diverging



Other G7 countries lag the U.S., weighed down by high interest rates and weak demand.

Investors have pared their monetary policy easing expectations

Economic data have been uniformly better than expected across major economies, leading to sticky inflation

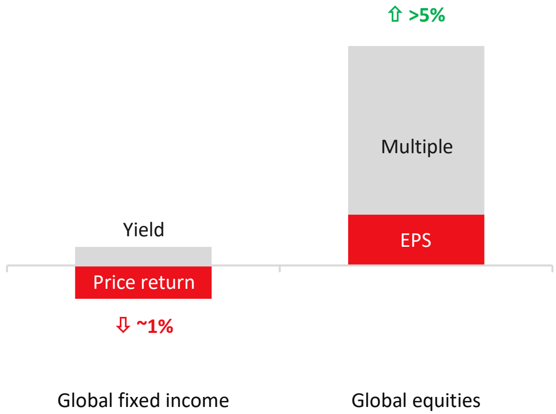


# of year-end policy rate cuts priced in[1]

Performance of the two major asset classes has been lopsided

The prospect of fewer policy rate cuts has kept bond yields elevated…

…but equities have continued to trend higher amid healthy earnings growth.



YTD total return[2]

Sources: Bloomberg, Scotia Wealth Management | 1 – As at March 27, 2024 | 2 - MSCI World Index used to measure global equity returns. ICE BofA Global Broad Market Index used for global fixed income returns.

The odds of a soft landing have increased…

Soft landing odds supported by several factors…

Low unemployment and strong wage growth…

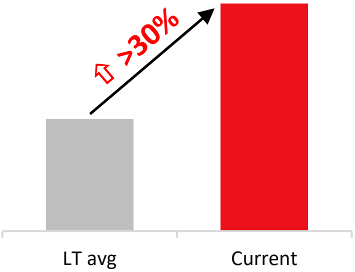
…may continue to support consumer spending.

While still elevated, inflation is down from multi-decade highs…

…and sentiment indicators are showing signs of having bottomed.

…but the major risks have yet to fully abate.

Uncertainty on timing/extent of future easing may unearth vulnerabilities related to excess indebtedness



U.S. monetary policy uncertainty index

>330%
Global debt-to-GDP

Widening of geopolitical conflicts could increase uncertainty

U.S. election: transformative fiscal policy or higher tariffs could disrupt global trade and increase inflation

Recent market calm may be short-lived[1]…

~30% lower
Equities

~10% lower
Fixed income

Change in volatility measures (YTD vs 2022/2023 avg)

…but volatility can be mitigated and capitalized on.

Diversification and a high-quality bias can help insulate portfolios

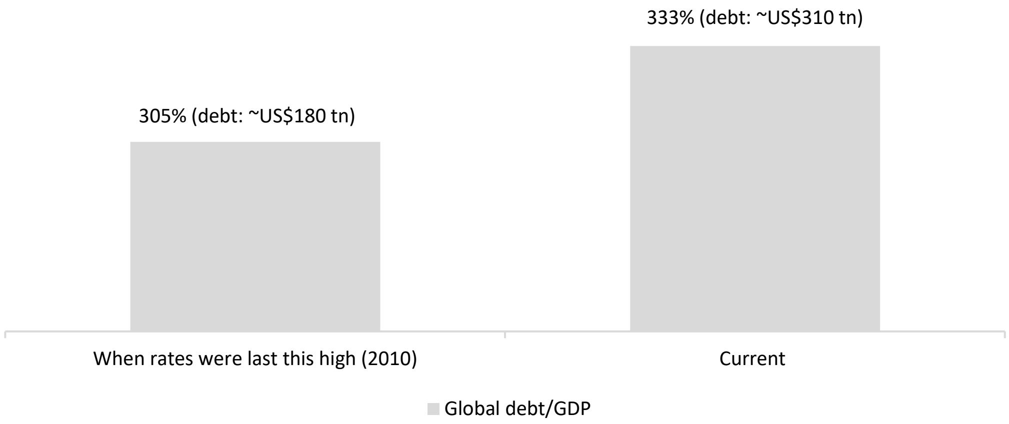
A selloff may provide opportunity to increase risk asset exposure

Sources: Bloomberg, Institute of International Finance, Scotia Wealth Management, Baker-Bloom-Davis | 1 – Equity and fixed income market volatility represented by the VIX and MOVE indices, respectively.

…but are predicated on lower interest rates.

Current long-term rates are inconsistent with global debt levels…

The G7 GDP-weighted 10-year yield is hovering near its highest level in over a decade. Since then, the global economy has become far more indebted.



⇧ ~30 ppt

⇧ >US$130 tn

The ultra-low rate environment of the last 15 years saw a massive increase in debt issuance. Long-term rates remain anchored by excess global debt.

…and cannot persist for long, in our view.

Added debt-servicing costs would take a significant slice out of economic output if all outstanding debt were refinanced at current rates.

G7 countries (ex. Japan) would see a significant rise in interest outlays if all federal debt were refinanced at current rates.[1]

~ 1.5% of GDP

Canada, with its excessively indebted households, would feel an added pinch from high rates.[2]

>$15 bn

extra annual mortgage interest payments

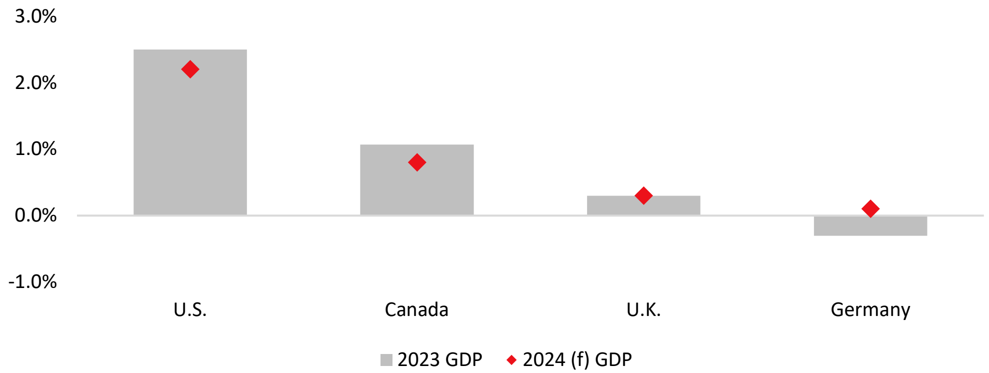
>0.5% of GDP

Sources: Bloomberg, Institute of International Finance, Statistics Canada. Table 10-10-0006-01 Funds advanced, outstanding balances, and interest rates for new and existing lending, Bank of Canada, Scotia Wealth Management | 1 – For added federal outlays, the current weighted average coupon was compared to the current yield of the matching tenor. The final number is GDP-weighted. | 2 - Based on all outstanding fixed rate mortgages, the current weighted-average interest rate, and the average 5-year fixed rate being offered by Canada's Big 5 Banks as of March 28, 2024.

Productivity may affect monetary policy synchronicity

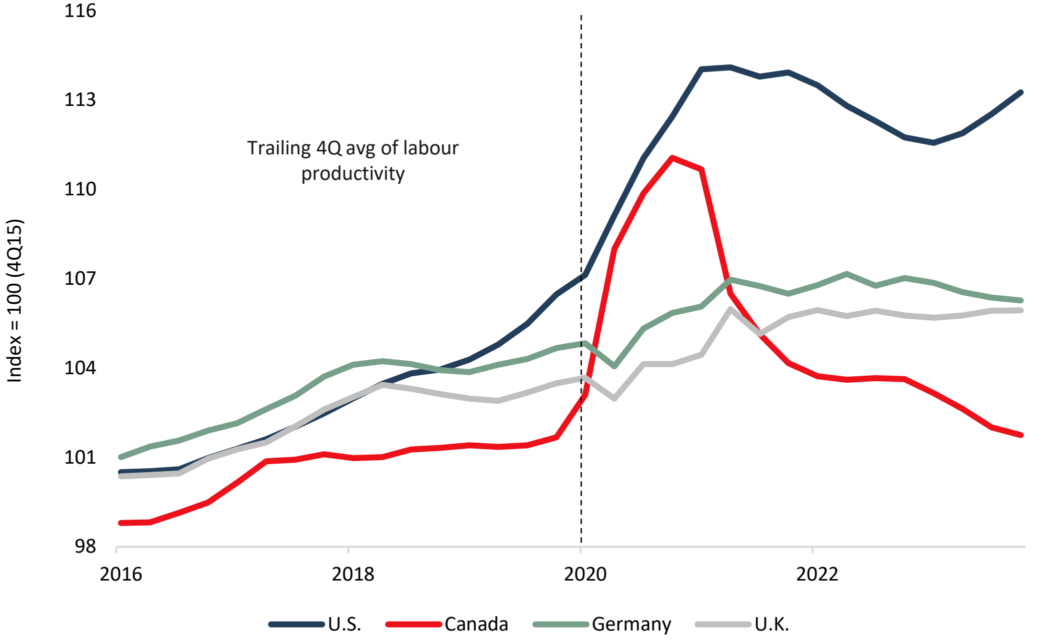
Stronger U.S. GDP growth may lead the Fed to ease more gradually, resulting in less synchronous monetary policy[1]

Current policy rate	5.00%	5.50%	4.00%	5.25%
# of 25 bps rate cuts priced 1-year ahead	5	3	6	5



However, widening labour productivity differentials may keep the Fed from falling too far behind

The U.S's robust post-pandemic labour productivity could keep unit labour costs in check relative to aggregate output.

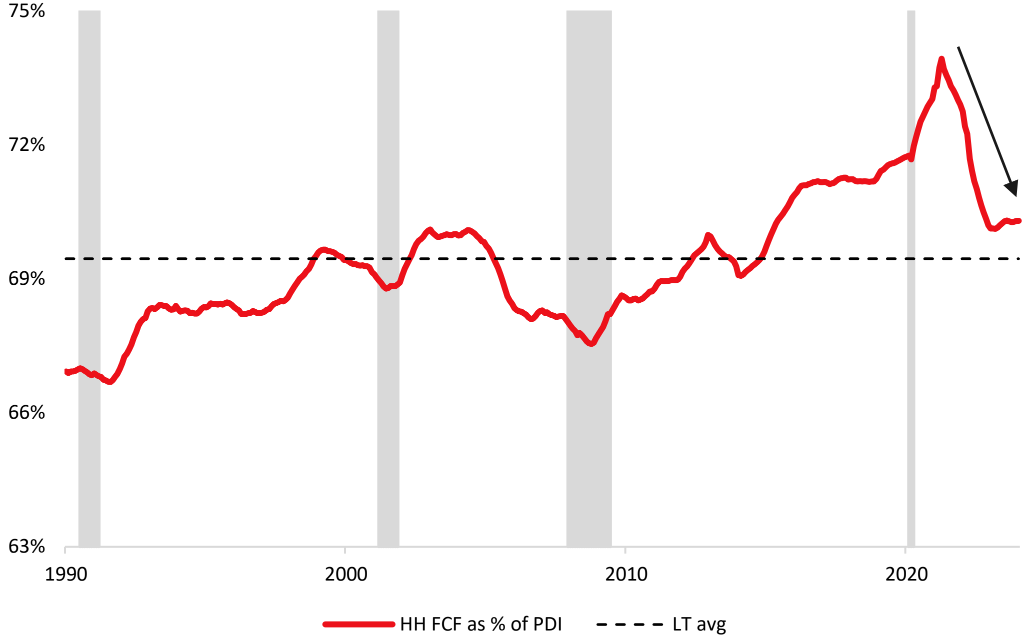


Sources: Bloomberg, Scotia Wealth Management | 1 – Based on 3M1Y forward rates as of March 27, 2024. GDP growth rate is based on Bloomberg consensus.

Household budgets are tightening…

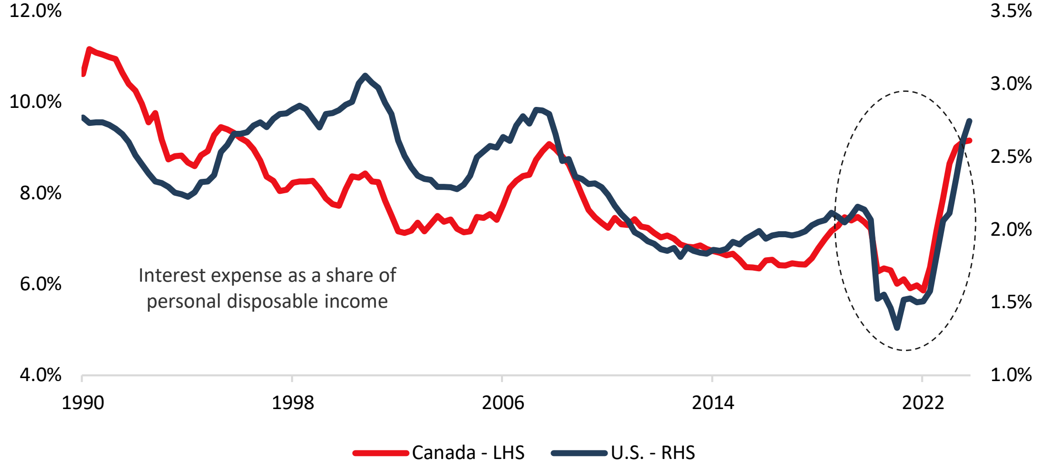
Households may pare discretionary spending as high inflation has led to tighter budgets

Spending on necessities has increased as a share of personal disposable income, leaving less room for discretionary spending[1]



Rising debt, and the higher cost to service it, is a headwind for consumption

Interest expense as a share of personal disposable income has increased sharply since central banks began raising policy rates



Increase in credit card debt in the U.S. and Canada since start of 2022 >30%

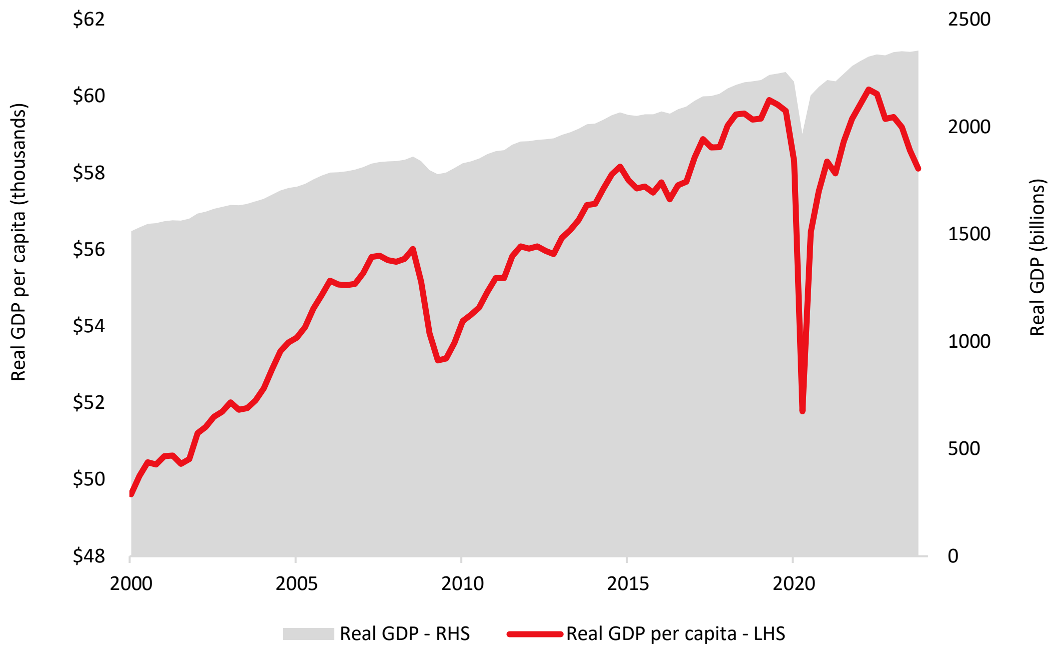
Sources: Bloomberg, Scotia Wealth Management | 1 - Household free cash flow % = (Personal disposable income – food & energy spending – interest payments – housing and utilities spending)/personal disposable income. Based on U.S. data.

Scotia Wealth Management.

High rates to weigh on indebted households

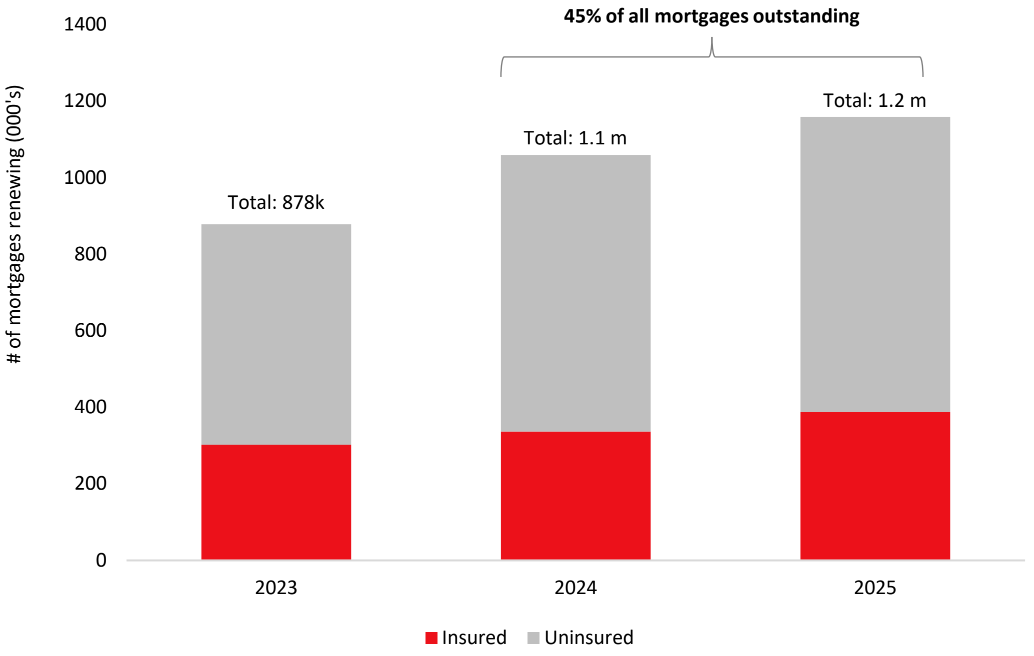
Population growth and strong U.S. demand have helped support the Canadian economy in recent quarters...

...but falling GDP per capita suggests the average Canadian is not reaping the benefits.



A large number of mortgages are coming due for renewal and will likely face higher rates

Mortgage renewals this year and next are ~40% of GDP. Renewals at higher rates could weigh on household spending and economic growth.



Fiscal health hinges on budget & socioeconomic goals

Diverse revenue streams

Less reliance on a single source of revenue can help to mitigate the risk of economic downturns

- Property taxes
- Service fees
- Inv. income
- Gov't transfers

Debt sustainability

Excess indebtedness can raise debt-servicing costs and impair ability to finance future projects

Where does the current liability service ratio stand?

Liability servicing limit **25%**

Economic responsiveness

Policies, procedures and strategies to help manage shortfalls stemming from a potential economic downturn

Reserve fund utilization

Defer non-essential spending

Debt financing (i.e., municipal bonds)

Provincial/Federal assistance

Priorities and challenges

Short-term priorities: Infrastructure maintenance, community wellbeing

Long-term priorities: Infrastructure development, green energy

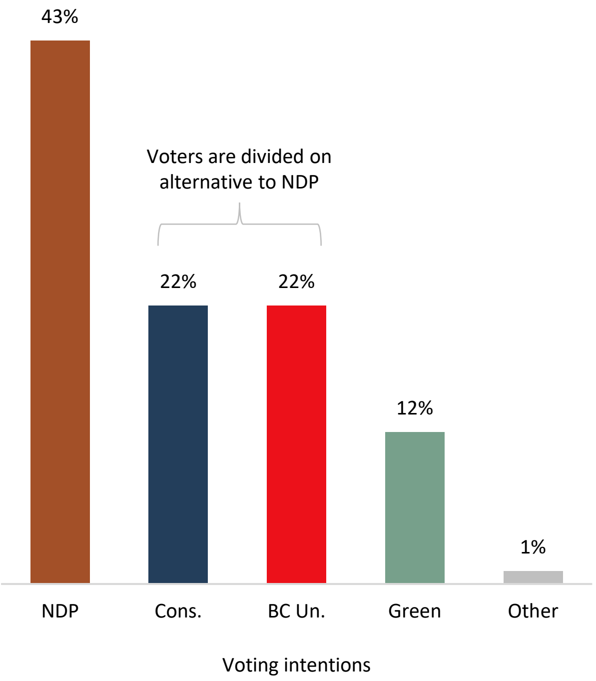
Potential challenges

- ✓ Housing
- ✓ Cost of living
- ✓ Healthcare

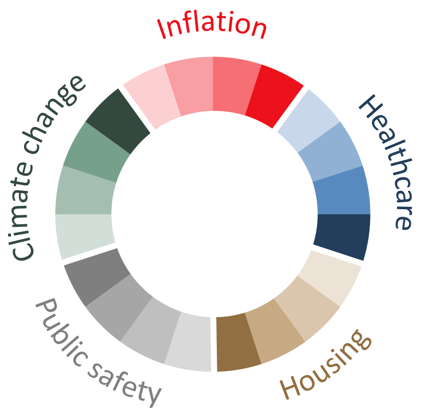
Sources: Scotia Wealth Management

NDP re-election points to rising deficits

Fractured opposition gives the incumbent party an edge



Budget 2024 aims to address top issues facing the province…



- ✓ 25% ⇧ In BC Family Benefit
- ✓ Building more LT care homes
- ✓ Rent increase cap, home flipping tax
- ✓ Expand access to legal aid services
- ✓ CleanBC Roadmap to 2030

…but these measures come at a significant cost.

Record high 2024/25 deficit is projected to decline in absolute terms…

$7.9 bn ⟩⟩⟩ **$6.3 bn**

2024/25 estimate — 2026/27 estimate

…and rise relative to GDP as the economy slows.

	2023	2024e	2025e	2026e
Real GDP	1.0%	0.8%	2.3%	2.4%
Debt/GDP	17.6%	21.0%	24.8%	27.5%

⇧ **1.8x**

From 2022/23

Sources: Scotia Wealth Management, Angus Reid Institute, British Columbia Budget and Fiscal Plan: 2024/25 – 2026/27

THANK YOU

Scotia Wealth Management.

Disclaimer