Autumn 2024
Building your financial future

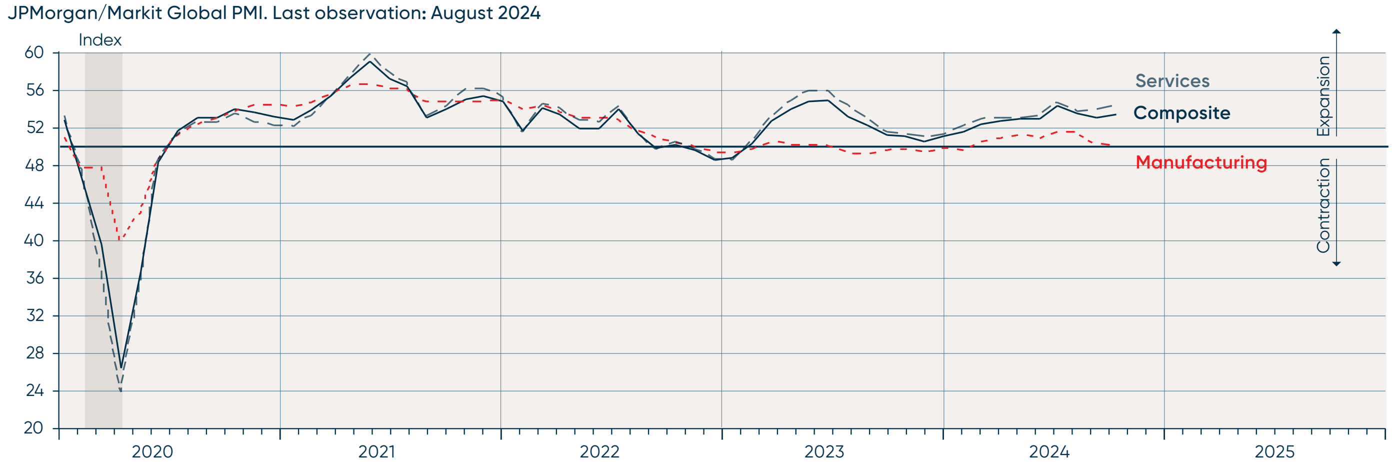
Investment Strategy

World

Without collapsing, global economic growth has certainly slowed recently. The manufacturing sector, in particular, has contributed to this trend, contracting in August after a brief recovery at the start of the year. Geographically, the eurozone and China are the main drivers of this global economic underperformance. In the single currency zone, although growth remained positive in the second quarter, it fell below potential, mainly due to difficulties in Germany. In China, the persistent fall in house prices is eroding the confidence of consumers, for which housing represents around three quarters of total wealth. And unfortunately, the authorities' stimulus efforts seem to have had very limited impact, judging by the small increase in the money supply. Weak demand is allowing deflation to take hold; the GDP deflator fell for a fifth consecutive quarter in Q2, something not seen since the late 1990s. Unless the authorities take more vigorous measures, domestic demand in China could remain weak. Similarly, external demand could be affected by a slowdown in the advanced economies. And given the size and integration of the Chinese economy, this weakness is bound to have repercussions on a global scale, particularly through the fall in commodity prices. China remains the main source of demand for many of these products, particularly oil. Headwinds from the eurozone and China could continue to keep global growth below potential in 2024, and a significant slowdown in the U.S. is unlikely to offset this momentum. We forecast growth of 3.1% in 2024 and 2.8% in 2025. A coordinated easing of monetary policy, which seems likely in the months ahead, could help to mitigate the slowdown, but these rate cuts could come too late to prevent the processes already underway from weighing on growth.

World: The global manufacturing sector is losing steam

JPMorgan/Markit Global PMI. Last observation: August 2024



NBC Economics and Strategy (data via Refinitiv)

NATIONAL BANK FINANCIAL
WEALTH MANAGEMENT

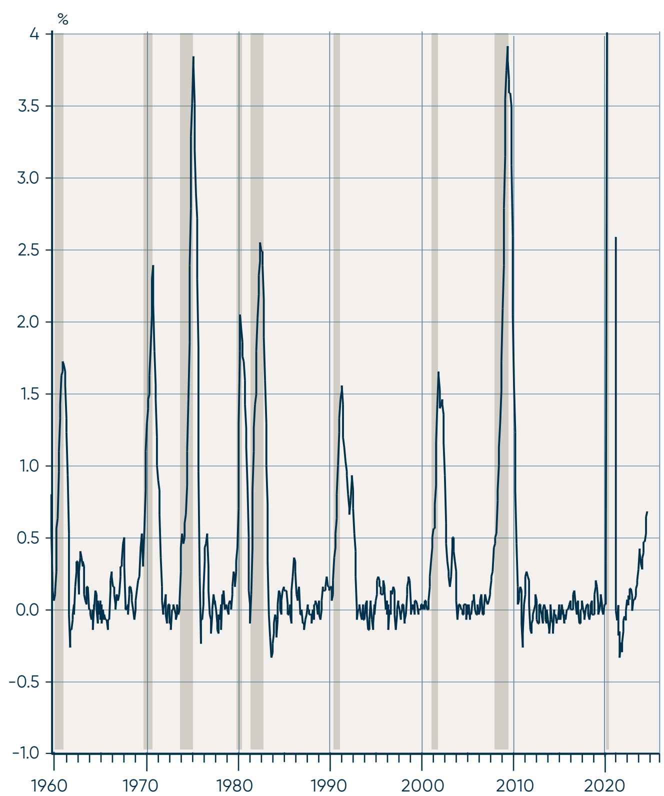
In this issue

United States

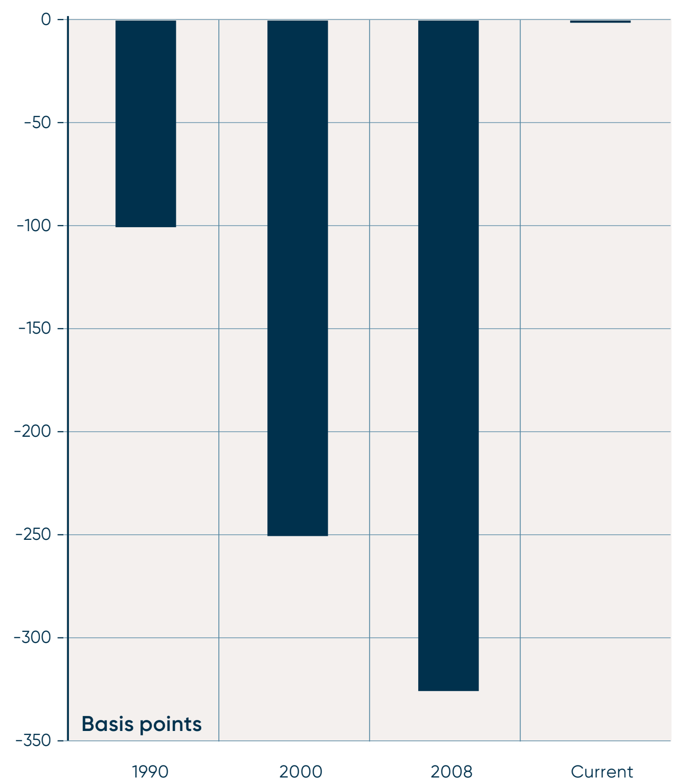
At the Jackson Hole symposium in August, Federal Reserve Chairman Jerome Powell highlighted the progress made in bringing inflation back to the central bank's target, returning the second part of its mandate—full employment—to the fore. On this front, Powell showed himself to be a little more worried, saying that the Fed "would not look favourably on any further deterioration in the labour market", which led the markets to anticipate a more pronounced interest rate cut. Despite this shift in focus, it remains that the Fed could be underestimating the risks to the labour market, and above all, that it has not acted in a sufficiently pre-emptive manner. Initial estimates of revisions to the non-farm payroll survey indicate that employment was not as robust as previously thought between Q2 2023 and Q1 2024. Recent data are also likely to be revised downwards due, among other things, to the increase in bankruptcies not fully captured in real time by the survey. Over and above this methodological flaw, a number of indicators point to a deterioration in the labour market, such as a weak diffusion of hiring at the sectoral level, a fall in the use of temporary employment agencies, and a rise in the number of workers forced to work part-time. Although the unemployment rate remains relatively low, trend reversals have historically been a harbinger of economic difficulties. In this respect, the Sahm rule, which stipulates that an increase of 0.5 percentage points in the three-month moving average of the unemployment rate over the previous twelve-month trough generally results in a recession, was triggered in July. Historically, the Fed has tended to start its monetary easing cycle before this rule is triggered, but this has not been the case in the current cycle. As a result, monetary policy remains very restrictive relative to the economic cycle, which should lead to a marked slowdown in growth by the middle of next year. According to this scenario, the US economy should grow by 2.5% this year and 0.9% next year.

U.S.: Shouldn't the Fed have acted sooner?

Three-month moving average of the unemployment rate relative to the minimum of the three-month averages from the previous 12 months.



Rate cuts already delivered by the Fed at the time the Sahm rule was triggered.



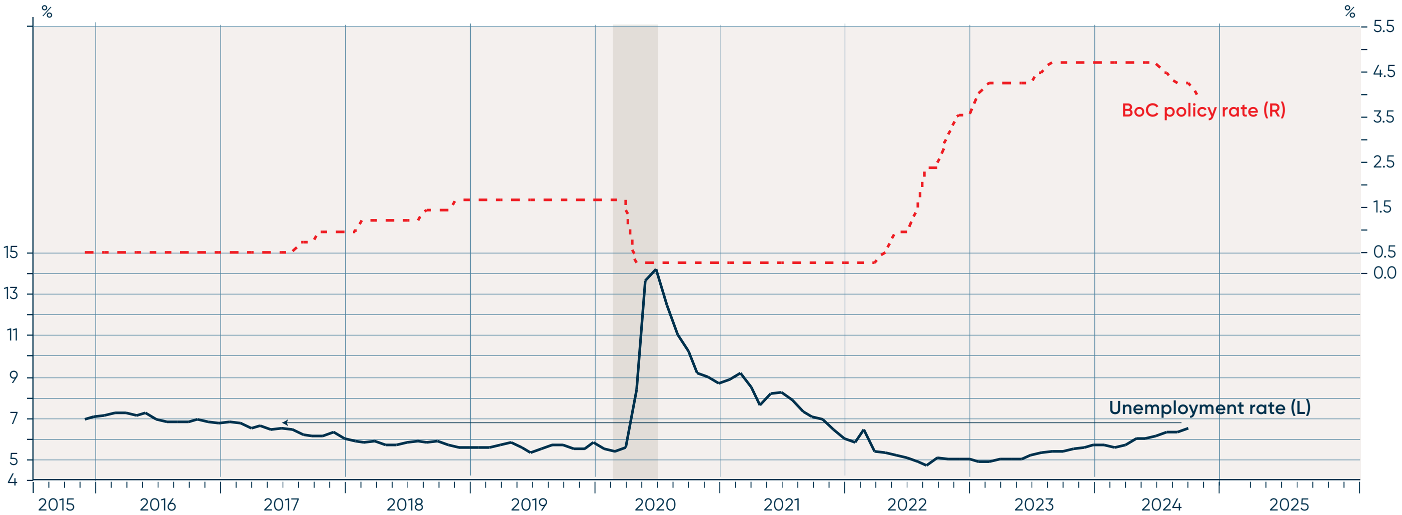
NBC Economics and Strategy (data via Bloomberg and Refinitiv)

Canada

Some forecasters, including the central bank, were pinning far too many hopes on a recovery in the economy and a stabilization of the unemployment rate in the second half of the year, in the wake of the interest rate cuts; however, even though interest rates are starting to come down, monetary policy is far too restrictive for this recovery and stabilization to occur, and recent economic data confirms this. With the Canadian economy stagnating in June and July, the 2.8% growth expected in Q3 by the Bank of Canada is now virtually unattainable. As a result, GDP per capita is continuing the downward trend that began in 2022, illustrating the fact that the economy is still growing below potential and that excess supply continues to increase. Not only do companies seem to have excess inventories, they also seem to have too many workers. For now, this is limited to a hiring freeze at the macro level as evidenced by the average increase in jobs of just 6,000 per month from June to August. Those trying to enter the labour market—young people and newcomers—are the main victims of Canada's weak hiring climate. At the aggregate level, the unemployment rate rose by two tenths to 6.6% in August, its highest level since May 2017, outside of the pandemic. By way of comparison, the policy rate stood at just 0.5% at the time, in stark contrast to September's 4.25%. With widespread inflation a thing of the past in Canada, the door seems wide open for the Bank of Canada to return its policy rate to neutral (between 2.5% and 3.0%) in the near future. In the meantime, the damage to the labour market could be greater than necessary. We anticipate economic growth of just 0.9% in 2024 and 1.3% in 2025, which would translate into an unemployment rate of around 7.4% by mid-2025.

Canada: The policy rate should continue to weigh on the labour market

Unemployment rate and Bank of Canada policy rate



NBC Economics and Strategy (data via Statistics Canada)

Investment Strategy

The third quarter mostly brought good news for investors, with gains across most asset classes, though equities faced notably higher volatility compared to the first half of the year. In the midst of this turbulence, several lagging market segments managed to make up some ground, as was the case for defensive sectors and Canadian equities, but also bonds, which performed particularly well during the period.

A surprise rise in the unemployment rate fuelled much of the volatility during the summer months; however, with inflation now largely under control, the Federal Reserve responded to weakening labour market conditions by cutting its key rate for the first time since 2020, formally marking the beginning of a path towards a withdrawal of its restrictive monetary policy. This decision is in line with measures taken by other central banks, notably the Bank of Canada, which has already cut rates three times in response to a more pronounced weakening in the job market and inflationary pressures on our side of the border.

Looking ahead, while most investors and economists continue to expect a soft landing thanks in part to lower interest rates, the outlook remains fragile. Weakness in housing and manufacturing activity, combined with the potential for further increases in unemployment, could ultimately be followed by a slowdown in consumer spending, the backbone of economic growth. Given this uncertainty, investors should brace for sustained equity volatility through the rest of 2024 and into early 2025 as central banks aim to stabilize rates at neutral levels—or potentially lower if the economy falters. That said, we can count on bonds to play their diversification role should the situation indeed deteriorate, now that inflation is no longer the problem it used to be.

Against this backdrop, a balanced approach between stocks and bonds within tactical asset allocation is still warranted, though a shift towards a more defensive stance may be considered depending on how the economic backdrop develops over the coming months. Geographically, our overweight position in U.S. equities remains unchanged, reflecting confidence in the U.S. market's resilience and signals from our quantitative model.

MODEL PORTFOLIOS

Income Portfolio	Asset Class	Minimum/ Maximum	Benchmark	Recommended Weighting	Change from Previous Quarter
Investor profile: You want to preserve your capital or establish a source of periodic income to finance ongoing expenses. You do not find the stock market very attractive because of its volatility, but you are not against the idea of investing a small part of your portfolio in stocks, mainly to counteract the effects of inflation. Your tolerance for risk is low.	Cash equivalents	0% to 20%	5.0%	3.0%	-2.0%
	Fixed income (duration: 7.25 years)[1]	60% to 100%	70.0%	73.0%	0.0%
	Canadian equities		8.0%	7.0%	0.5%
	U.S. equities	0% to 30%	8.0%	8.5%	1.0%
	Foreign equities		4.0%	3.5%	0.5%
	Alternative investments[2]	0% to 20%	5.0%	5.0%	0.0%
Conservative Portfolio					
Investor profile: On the whole, you want your portfolio invested in fixed-income securities. Although you can tolerate limited volatility to ensure that your assets will grow, you prefer having a portfolio consisting mainly of fixed-income investments for reasons of stability. Your tolerance for risk is low.	Cash equivalents	0% to 20%	5.0%	3.0%	-2.0%
	Fixed income (duration: 7.25 years)[1]	45% to 80%	55.0%	58.5%	-2.0%
	Canadian equities		14.0%	13.0%	1.5%
	U.S. equities	20% to 45%	14.0%	14.5%	1.5%
	Foreign equities		7.0%	6.0%	1.0%
	Alternative investments[2]	0% to 20%	5.0%	5.0%	0.0%
Balanced Portfolio					
Investor profile: You give equal importance to achieving growth in your investments and receiving income. You can tolerate moderate changes in market value to ensure growth, but you prefer having a mix of fixed-income investments and equities for reasons of stability.	Cash equivalents	0% to 20%	5.0%	3.0%	-2.0%
	Fixed income (duration: 7.25 years)[1]	30% to 65%	40.0%	44.0%	-2.0%
	Canadian equities		18.0%	17.0%	1.5%
	U.S. equities	30% to 65%	18.0%	18.5%	1.5%
	Foreign equities		9.0%	7.5%	1.0%
	Alternative investments[2]	0% to 25%	10.0%	10.0%	0.0%
Growth Portfolio					
Investor profile: Your main goal is capital growth. Although you can tolerate greater volatility in order to increase the value of your assets, you are not prepared to invest your entire portfolio in stocks. Your tolerance for risk is high.	Cash equivalents	0% to 25%	5.0%	3.0%	-2.0%
	Fixed income (duration: 7.25 years)[1]	20% to 45%	30.0%	34.0%	-2.0%
	Canadian equities		22.0%	21.0%	1.5%
	U.S. equities	40% to 75%	22.0%	22.5%	1.5%
	Foreign equities		11.0%	9.5%	1.0%
	Alternative investments[2]	0% to 25%	10.0%	10.0%	0.0%
Maximum Growth Portfolio					
Investor profile: You want to maximize the eventual return on your capital by investing all or most of your portfolio in the stock market. In doing so, you accept higher volatility of your investment returns in the hope that these returns will ultimately be higher. Your tolerance for risk is high.	Cash equivalents	0% to 30%	5.0%	3.0%	-2.0%
	Fixed income (duration: 7.25 years)[1]	0% to 30%	15.0%	19.5%	-2.25%
	Canadian equities		26.0%	24.75%	1.75%
	U.S. equities	55% to 100%	26.0%	26.75%	1.5%
	Foreign equities		13.0%	11.0%	1.0%
	Alternative investments[2]	0% to 30%	15.0%	15.0%	0.0%

1 FTSE TMX Canada Universe Index
2 Includes 3-month T-bills, global infrastructure and gold.

FORECAST

	2022	2023	2024 (Forecast)	2025 (Forecast)
Gross Domestic Product %				
Canada	3.8	1.2	0.9	1.3
U.S.	1.9	2.5	2.5	0.9
Inflation %				
Canada	6.8	3.9	2.5	1.9
U.S.	8.0	4.2	2.8	1.9

	September 2024		December 2024		December 2025	
	Canada	U.S.	Canada	U.S.	Canada	U.S.
Rate %						
Short-term rates (T-bills, 91-day)	3.95	4.90	3.25	4.10	2.70	3.05
10-year bond yields	2.95	3.70	2.85	3.60	2.80	3.25
30-year bond yields	3.10	4.00	3.00	3.90	3.00	3.55
Canadian Dollar	US $0.73		US $0.71		US $0.74	