RJL PCS: INSIGHTS & STRATEGIES

DECEMBER 5, 2024

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December 2024 Insights & Strategies: Markets Closing Out a Good Year Despite Uncertainties

Macro Highlights for November

- November started with Trump's election victory and ended with his threats of a 25% tariff on all Canadian goods. Ultimate impacts on Canada are not yet known, although we expect some tariffs to impact trade, and for pressure on the CAD. In the U.S., we could see slower economic growth, more inflation pressures, slower rate cuts, lower taxes and strength in equities.
- Canadian October inflation numbers were announced showing that the Consumer Price Index (CPI) headline rebounded slightly more than expected, back up to 2.0%, from 1.6% in September. The BoC's preferred measures of CPI-Trim and CPI-Median were 2.6% and 2.5%, respectively, up from 2.4% and 2.3%. Along with possibly stronger GDP growth in 4Q24, BoC rate cutting could slow.
- A new Canadian two-month (GST/HST) tax holiday on certain items and proposed $250 rebate could temporarily boost GDP with some upward inflation pressures, although tariff clouds could more than trump any benefits.

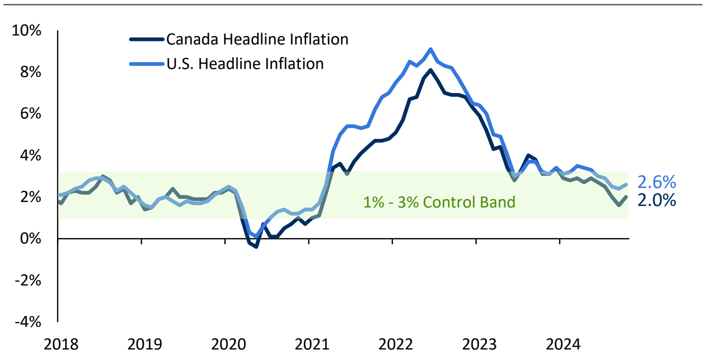
Financial Market Highlights

- The Canadian benchmark TSX Composite index was up 6.4% in November after increasing 10.5% in 3Q24, and is up 25.8% YTD, versus the U.S. benchmark S&P 500, which was up 5.9% in November after increasing 5.9% in 3Q24, and is up 28.1% YTD. All figures represent total returns in local currency.
- Market breadth has been an important topic in 2H24 as small and mid-cap stocks gained strength on a better economic backdrop in the U.S. markets, with the start of the interest rate easing cycle.
- Canadian sectors that did the best in November were Info Tech (+28.3%), Financials (+7.5%) and Energy (+5.4%), while Communication Services (-7.0%), Materials (-2.9%) and Real Estate (+1.0%) were the weakest.

Upcoming

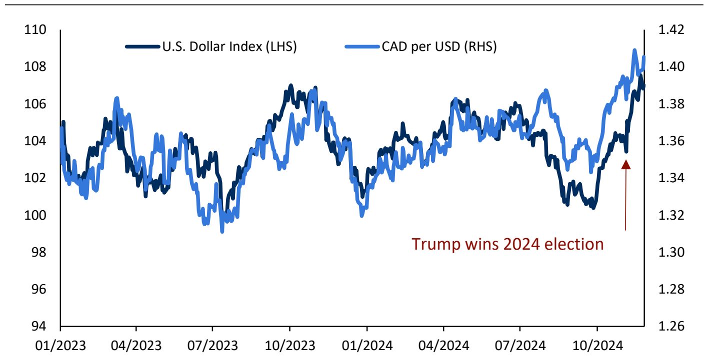
- We expect rate easing to continue in Canada through the end of the year, with another 25 bp cut on December 11, although any weakening in the labour data (due Dec 6) could increase the likelihood of a 50 bp cut. We expect continuing 25 bp reductions into 2025 until the policy rate hits 2.75% at the April 16 meeting.
- We see further downward pressure on inflation with the Canadian economy operating below potential.
- Trump's social media blasts, tariff threats, and bi-laterial negotiations are likely to cause more volatility and (Canadian) investor anxiety over the next couple of months until we gauge how seriously to take recent posts after the January 20th inauguration.

Chart 1 - Canada and U.S. Headline Inflation



Source: FactSet; Raymond James Ltd.; Data as of October 31, 2024.

Chart 2 - Trump's Victory Fueled USD Rally



Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024.

Executive Summary

One quote has been rattling around my brain recently. It's from famed economist John Maynard Keynes; "The market can stay irrational longer than you can stay solvent." My first takeaway is the most obvious, in that despite many people postulating about U.S. equity market valuations being stretched, and citing Warren Buffet's exceptional cash position, the economic backdrop and corporate earnings outlook could support the continuation of this state for some time. The second reason that the quote seems to resonate right now is if we consider the spirit of the quote as it might reflect on the current political environment. Specifically, I'm thinking about how it would relate to president-elect Trump's recent social media post threatening a 25% tariff on all goods entering the U.S. from Canada. That threat might sound irrational given its obvious negative impact on the U.S. economy and consumers. Although we don't anticipate it being ultimately executed as advertised, we cannot simply dismiss the potential damage that such a policy, even if watered down, could inflict on the Canadian economy. Investors should take this warning shot as a reminder to stay properly diversified and within their risk tolerance.

Looking back, as we finish off 2024, we can summarize it as both gut-wrenching and better than expected. In the U.S., we lived through one of the most contentious elections in recent memory, but exited with strong messages from U.S. voters about their concerns, mostly about the economy and their standard of living. Despite those concerns, the U.S. economy has actually been surprisingly resilient, with relatively high GDP growth, still low unemployment rate, and inflation that is heading back to trend. The price level reset from that period of high inflation has obviously had a major impact on many, but the rate of growth going forward is almost back to target. The Federal Reserve (Fed) now has a balancing act in managing its policy interest rate as it tries to bring it back to a neutral level to keep growth from slowing too much, while still working on getting inflation back to target without letting it push back up. The Fed's job may get more difficult if Trump follows through on massive tariff programs, as they would likely push inflation back up, but we'll have to wait to gauge the severity and extent of those impacts. With the favourable economic backdrop, and still strong corporate sales and earnings growth, the U.S. stock market has continued to push higher, helped in November with the 'Trump Trade' and expectations of lower taxes and deregulation. While growth may be more muted over the next 12 months, and valuations in certain sectors look strained, the overall backdrop remains favourable for a positive 2025.

The Canadian outlook is not as positive as the American one. Economic growth has been weaker north of the border, and although we're not seeing signs of contraction that would lead us into a recession scenario, we are still looking at meagre growth below the potential of the country. This has been partnered with a higher unemployment rate. Population growth has played an important part in both of these metrics, as more consumers have pushed up GDP, while adjusted for population, GDP per capita has shown declines in this proxy of standard of living. Having more people in the labour force, but unable to find jobs, has pushed up the unemployment rate. Recent announcements of significant immigration restrictions on both permanent and temporary residents, are expected to bring population growth down from over 3% in the last couple years to just below 0% over the next two years. These curbs seemed designed to allow housing and other services to catch up somewhat to the population growth. The reduction in the labour force will likely also alleviate some upward pressure on the unemployment rate, although this might also increase labour costs and therefore inflation pressure, which should be more that offset by lower shelter cost inflation. The end result will likely be the continuation of disinflation, and slower economic growth, which will further induce the BoC to continue lowering interest rates.

Before getting into more detailed discussions on economics and the financial markets, we should probably clarify our opinion on the recent tariff threats. As we opened our commentary above, we would be surprised to see such a broad and significant tariff implemented so quickly when the source of U.S. frustration seemingly lies more with Mexico and China, than with Canada. That being said, it would also be foolhardy to brush off such threats as a bluff. It is somewhat reassuring to see that Canada quickly pledged to pump more money into the Canada Border Services Agency and the RCMP. Canada needs to ensure that the rationale for this, and potentially other threats leading up to January 20, are addressed as quickly as possible. The Canadian Chamber of Commerce already published an analysis[1] that the previously threatened 10% universal tariff would reduce real income by 0.9% and labour productivity by nearly 1%. Retaliatory tariffs would further worsen Canadian income declines to 1.5% and productivity by 1.6%. A full 25% would be much more significant and likely drive Canada into a recession. Now, there's a multitude of reasons for the tariffs to not be implemented, especially anywhere close to the level indicated, including U.S. reliance on Canadian oil, but the federal government cannot take the risk of not being attentive to U.S. concerns, mostly about border security, that prompted this opening salvo. For now, promises and threats are not policy, but the discussion needs to start before more damage is done. The threats alone, even if not implemented, could cause many businesses to pause purchases or business investment decisions over the next couple of months, until clarity is provided, maybe in January or even later. Again, investors should take this opportunity, with their financial advisors, to confirm that they are properly diversified and positioned within their risk tolerance, especially given the potential for volatility ahead.

[1]Stephen Tapp, Partners in Prosperity: How the Canada-U.S. Trade Relationship Goes Beyond Buying and Selling, Canadian Chamber of Commerce https://businessdatalab.ca/publications/partners-in-prosperity/

Canadian Macro Discussion

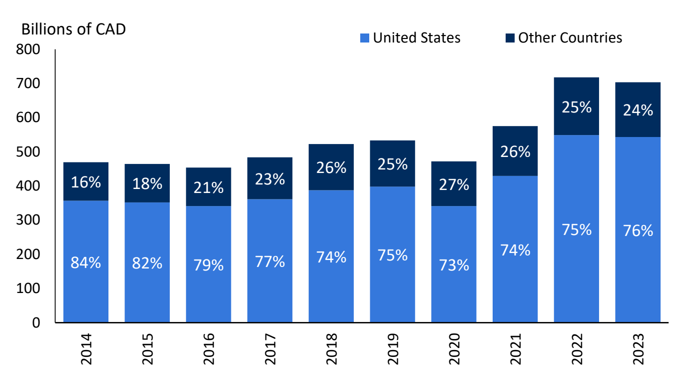
Trade & Tariffs

With the U.S. election decided and the pro-tariff president set to take office in just over two months, tariffs have usurped inflation and interest rates as the topic of the day. The importance of this topic cannot be overstated in Canada, but we have to be mindful of the transactional nature of President-elect Trump, using threats and rhetoric to achieve direct and indirect outcomes. As far as broad-ranging threats to implement tariffs on all countries, which may or may not include Canada due to the U.S.-Mexico-Canada Agreement (USMCA) on trade, and may or may not include exemptions on certain industries on which the U.S. relies, we will have to be prepared but still wait and see where promises intersect with policy. There is also the potential for tariffs to be used as punishment or enticement around Canada's failing to meet defense spending obligations under NATO agreements. The permutations are truly dizzying. There seems to be a growing belief in the U.S. that globalization and free-trade has not benefitted America (at least as much as it should have) as it doesn't bring jobs to Americans. and that U.S. protectionism will be a theme for at least the next four years. Economic damage and inflationary pressure are both possible results on both sides of the border.

Canada is in a unique position to be both harmed and benefitted by Trump's tariff push. In Canadian dollar terms, Canada directs approximately 77% of its goods exports to the U.S., representing $544 billion in 2023 (Chart 3), while $439 billion flowed from the U.S. as imports into Canada. The U.S. is therefore Canada's largest trading partner, by far. Energy is the largest component of those Canadian goods exports, at 22% or $158 billion in 2023 (Chart 4), including $151 billion of oil and gas, followed by autos & parts at $128 billion. Canada's status within the USMCA could position it to benefit if the U.S. plays hardball with the rest of the world, as long as we can work closely with our neighbour to retain or regain preferential access as these tariff walls are erected. Trump's most recent 25% tariff threat, applicable to all goods from Mexico and Canada is very likely a shot across the bow in order to accelerate discussions and force Canada into quick concessions and action on border security, and likely defence spending as a whole. Unfortunately, due to asymmetry of the potential and immediate economic damage, Canada must take the initiative in addressing Washington's concerns. Canada quickly responded with a commitment to increase funding for the CBSA and RCMP, but we expect that this will be a long-term ongoing process and that it is likely that many additional and different issues will surface as we progress.

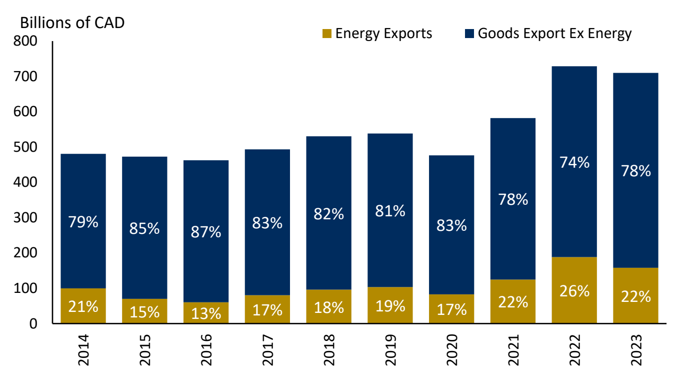
Energy will be a very important and interesting sector to watch here. Promising a new golden age of growth and low inflation, we doubt that President Trump will want Americans to be grumbling about higher prices at the pump. With pressure on oil prices in the near term from lower demand, specifically out of China, and excess supply while the U.S. could be poised to increase production even further, threats of rising gas prices might not seem like an immediate concern, but a lot can happen in four years, and we could imagine that the administration might be more open to excluding oil and gas from Canada from tariffs, more than any other product. At last measure, Canada was delivering 4.3 million barrels per day (in July) to the U.S., representing 97% of Canada's oil exports and 54% of American oil imports. This reliance on the U.S. should be diluted a little with the Trans Mountain pipeline expansion, but there's no doubt that there's heavy client concentration here that can quickly be addressed. That's an important tap to keep open when you consider Canada's oil production of approximately 4.9 million barrels per day, and that Canada supplies almost a quarter of the 20+ million barrel per day of oil that Americans consume.

Chart 3 - Around 76% of Canada's Goods Export Are to the U.S.



Source: Statistics Canada, Raymond James Ltd.; Data as of December 31, 2023.

Chart 4 - Around 20% of Canada's Goods Export Are Energy Products



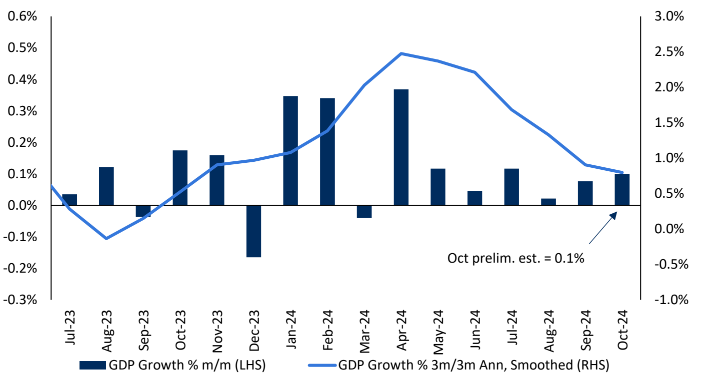
Source: Statistics Canada, Raymond James Ltd.; Data as of December 31, 2023. Energy exports include products under oil and gas extraction and utilities industry.

Economic Growth Still Below Potential in Canada

In contrast to the strong economic growth of the U.S., Canada is lagging behind. September's monthly GDP edged up by only 0.1%, which was below Statistics Canada's preliminary estimate of 0.3% (Chart 5). This put annualized 3Q24 GDP growth at 1.0%, with weakness in goods more than offsetting slight improvements in retail trade, finance and insurance. The work stoppages at CN and CP Rail helped drag on growth in 3Q24 and port and postal strikes in 4Q24 might have a more modest effect. Given the soft momentum heading into Q4, the BoC's latest Monetary Policy Report's estimates of 1.5% growth for Q3 2024 and a modest pick-up to 2.0% in Q4 2024 now seem overly optimistic. The economy continues to operate below its potential, with an 'excess supply' situation where demand is not keeping pace with supply. Indicators from the BoC and the Canadian Federation of Independent Businesses (CFIB) (Chart 6), both show slack in the Canadian economy, suggesting downward pressure on both GDP and inflation.

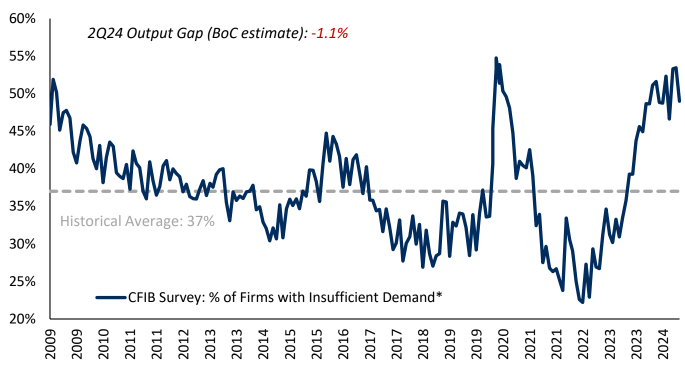
The government's recent u-turn on immigration policy likely means that the potential growth of the Canadian economy will fall. The potential growth rate is generally the increase in the labour force (which will now likely shrink modestly in 2025 and 2026), plus productivity growth (which Canada has long been lagging in, suffering declines in productivity for several years, and which the BoC categorized as an emergency situation). In its October Economic Report, which assumed population growth of 1.7% in 2025 and 2026, the BoC forecasted potential output growth of 2.4% in 2024 followed by 1.9% in 2025 and 2026. These forecasts will likely be reduced in the next revision. The BoC was expecting lower interest rates to help stimulate that growth, bringing it up by 2.25% in 2025 and 2026, but this would still be below the anticipated global growth rate of 3.2% through 2024 and 2025, according to the International Monetary Fund (IMF) in its recent October 2024 *World Economic Outlook Update*. The bottom line, is that the slightly declining population with reduce both potential and actual GDP growth.

Chart 5 - GDP Weakened in 3Q24



Source: Statistics Canada; Raymond James Ltd.; Data as of September 30, 2024.

Chart 6 - Growing Excess Supply in the Canadian Economy

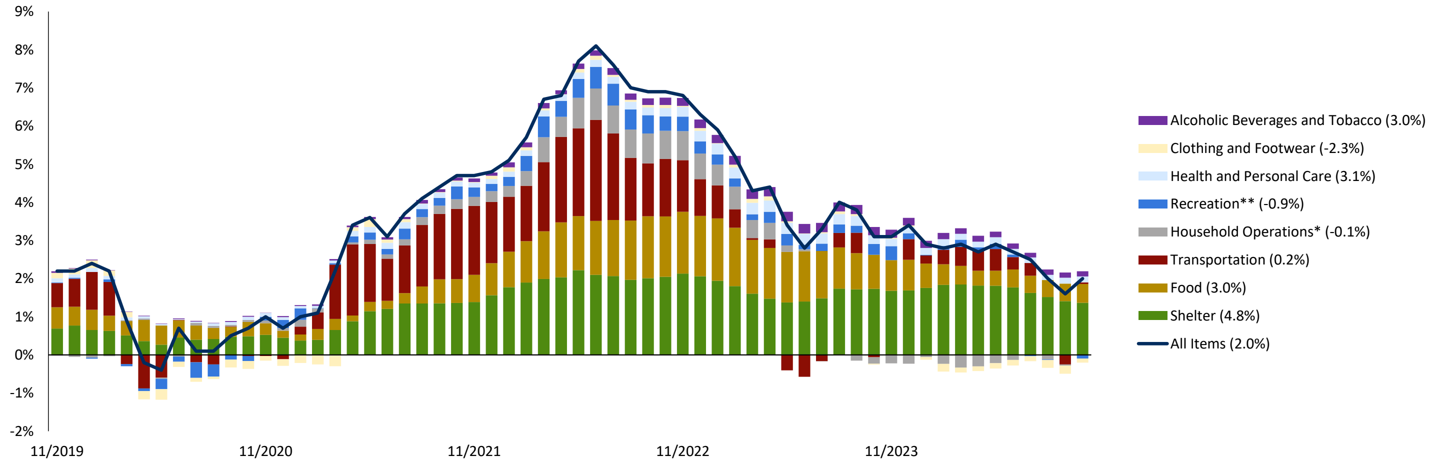


Source: CFIB, Raymond James Ltd.; CFIB survey as of November 30, 2024. *Domestic demand prior to 2024, domestic and foreign demand from January 2024 onward. Output gap estimates as of Q2 2024.

Inflation in Canada

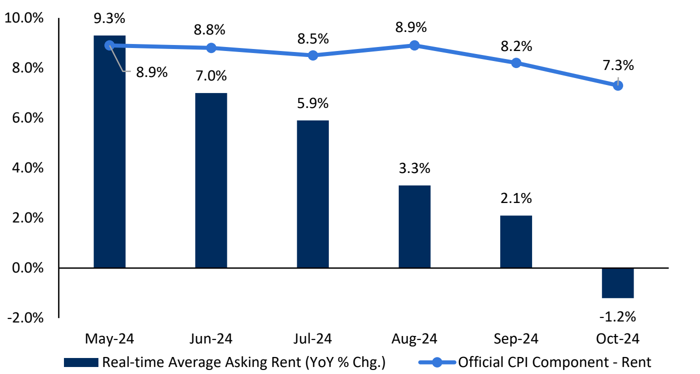
Inflation, measured by the CPI, picked up a little in October, to 2.0%, from the 1.6% recorded in September. This was generally anticipated, with consensus expecting 1.9%, but with slightly higher increases in items like clothing & footwear, rents, and airfares (Chart 7). Each October there is an adjustment for property tax inflation, which ran at a 32-year high this year at 6.0% versus 4.7%. Excluding the property tax adjustment and outliers and more volatile components, the CPI-trim and CPI-median measures that the BoC pays more attention to were 2.6% and 2.5%, respectively (versus 2.4% and 2.3% in September). The good news is that one of the still elevated and key components of the CPI, home rent prices, has seen a significant slowdown in year-over-year change in real-time data, even hitting -1.2% in October, indicating that asking rents are now lower compared to last October (Chart 8). However, the official inflation measure of rent has only slightly decreased from May to October, standing at 7.3%, which lags behind the real-time data significantly. Therefore, we remain confident that inflation will continue to ease, though the process may be a bit bumpy, especially when considering potential tax breaks and the "Working Canadians Rebate" (Chart 9). Overall, a rate close to the 2% level is the most comfortable position, and therefore allows the BoC to continuing easing its policy rate towards a more neutral level.

Chart 7 - Major Components' Contributions to Canada CPI (Stacked Bars) and Latest Monthly CPI (Bracket Beside the Legend)



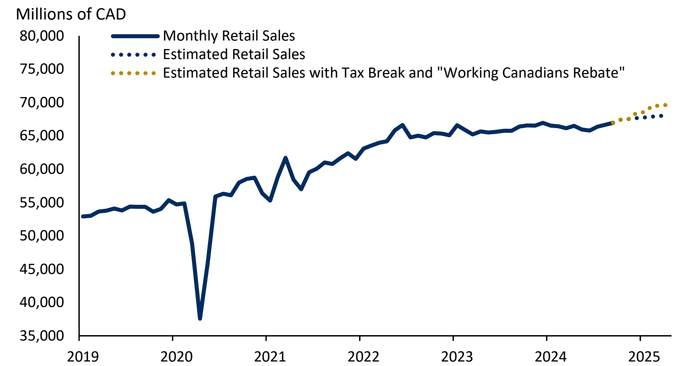
Source: Statistics Canada; Raymond James Ltd.; Data as of October 31, 2024. *Household operations, furnishing and equipment; **Recreation, education and reading.

Chart 8 - Official Rent CPI Tends to Lag Behind Real-Time Data, Quite Significantly This Time



Source: Statistics Canada, Urbanation Inc, Rentals.ca Network; Data as of October 31, 2024.

Chart 9 - Estimated Impact from Tax Break and "Working Canadians Rebate" on Retail Sales (For Illustrative Purpose Only)



Source: Statistics Canada, Raymond James Ltd.; Flash estimate is used for October retail sales, future monthly values are assumed to grow at the same pace as inflation. Assumes the ~6 billion of stimulus is fully spent.

Canadian Interest Rates - More Cuts Expected

On October 23, the BoC reduced its policy rate by 50 bps, the largest cut since starting the rate easing cycle on June 5, bringing the rate down from 5.00% to now 3.75%. With inflation essentially back to the 2% target (1.6% in September), and signs that the economy remains weak, but could still improve slightly in 4Q24, we see a 25 bp cut at the December 11 meeting. We would prefer to see a 50 bp cut, and think that the economy would benefit from it, but that being data dependent, the BoC will be slightly more cautious with the 25 bp move. Into 2025 we expect 25 bp cuts at each meeting until we reach the 2.75% level after the April 16, 2025, announcement (Chart 10).

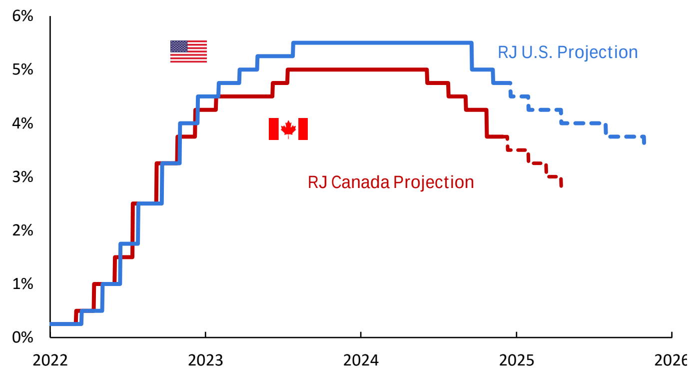
It's worth pointing out that as inflation has been declining, the "real" interest rate, which is the policy rate minus the inflation rate, has remained elevated, which means monetary policy is acting to slow down the economy (Chart 11). This is obviously the opposite of what Canada needs right now, which reinforces the strategy of cutting the policy rate, perhaps even more quickly than we are modelling. If we see economic deterioration and/or unemployment rate increases over the next few months, we could envision the BoC dropping the policy rate to as low as 2.25%, which is the lower end of the estimated 'neutral rate' range[2].

The recent announcement from the federal government to cut immigration targets (both permanent and temporary) for 2025 and 2026, could also slow or reduce consumer spending and economic growth. With the pace of population growth slowing or even contracting, we see risks in residential investment and possibly corporate profits, given the potential upward pressure on wage growth. Therefore, the BoC's policy rate may need to be more accommodating, to offset some of these factors.

Another important reason to cut interest rates is the still pending wave of mortgage renewals that will hit the Canadian economy through 2025 and into 2026. Despite rates being on the decline, many mortgage holders will be facing higher rates on their renewals, which will mean higher monthly payments and/or extended amortizations, driving up long-term borrowing costs. This is not the environment in which the BoC wants consumers reducing their spending because of higher mortgage payment burden. We touch on this topic more in the Housing Section.

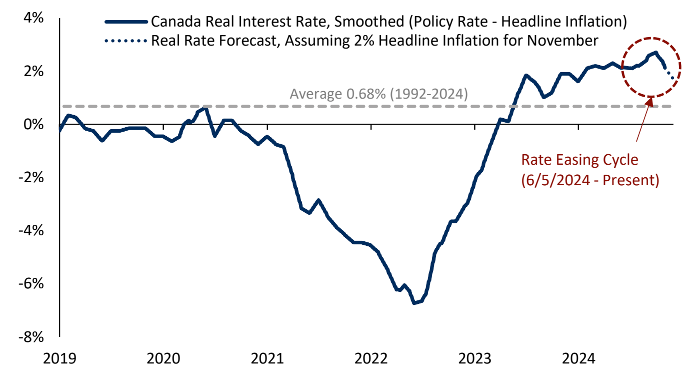
[2]The BoC estimates a range for the neutral rate, or R-star, which is the rate that is expected to allow the Canadian economy to grow in a balanced environment, without overheating and causing inflation. The BoC is currently estimating that level to be in the 2.25-3.25% range, and reexamines this target every April.

Chart 10 - BoC and Fed Easing Rates at Different Paces



Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024.

Chart 11 - Rate Cuts Are Not Keeping Pace With Disinflation



Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024.

Foreign Exchange

The stark contrast in economic growth rates between the U.S. and Canada, relative productivity, and GDP per capita, combined with the expectation of faster and deeper policy rate cuts in Canada than in the U.S. all lead to pressure on the Canadian dollar, against the U.S. dollar. With anticipated immigration curbs in Canada further pressuring GDP growth, we see the BoC continuing on its rate reduction path to help support the economy, while the Fed potentially slows down its rate cutting, leading to a wider divergence in short-term yields and hence further pressure on the Loonie. One key thing that could offset that pressure would be increasing commodity prices - notably in energy and mining sectors where Canada has an abundance of resources.

Canadian Population Growth

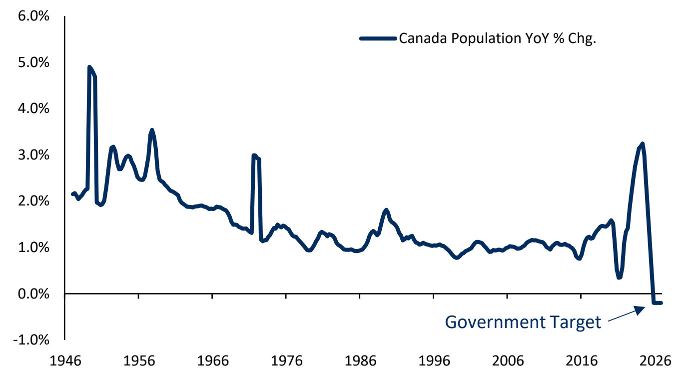
We have discussed the dramatic population growth in Canada multiple times over the past year. In addition to increased targets for permanent residents (500k per year), the government also lost control of temporary residents coming into the country, mostly through a student visa program. Combined, this resulted in the Canadian population growing by an estimated 3.3% in 2024, up from 3.1% growth in 2023. This worked out to approximately 1.2 million extra people being added to the country each year. Unfortunately, without corresponding increases in job creation, housing availability, or other infrastructure and services like health care, we saw significant strains. While more consumers and labour resources help to ease some staffing shortages, and ended up keeping GDP growth mostly positive, adjusting for the population growth, GDP per capita, a proxy for standard of living, has been on the decline.

Most recently, facing a lot of scrutiny, the federal government has dramatically shifted gears, announcing that the target for new permanent residents in 2025 will be 395k, and then fall to 380k in 2026 and 365k in 2027. Many (40%) of those new permanent resident spots are expected to be filled by temporary residents already in the country - just switching their status. On the temporary resident side, the goal is to reduce that group to 5% of the population by the end of 2026, from 7.3% (~3 millon) currently. That means reducing the non-resident population by approximately 445k in each of 2025 and 2026. The math works out as, in 2025, the government is expecting 1.27 million temporary residents to leave the country, while welcoming 380k new temporary workers, 310k new students, and 140k other/asylum claimants. Note however that some of those 1.27 million departing temporary residents are expected to convert their status and become part of the 390k incoming permanent residents. The net effect would be a population decline of 50k, not adjusting for natural births and deaths.

These measures would essentially bring overall population growth from over 3% per year to slight declines over the next two years (Chart 12). While Canadian GDP has been bolstered by the population growth over the last couple of years, the GDP per capita has been essentially flat from 10 years ago, except for significant volatility surrounding the pandemic. Facing a further flattening to slightly declining population through 2025 and 2026, Canada will see downward pressure on GDP growth, a potentially shrinking labour force (Chart 13), bringing the unemployment rate lower, but also increased wage growth that could push up inflation, more than offset by some relief on the housing strain (lower rents) that could alleviate some inflation pressures.

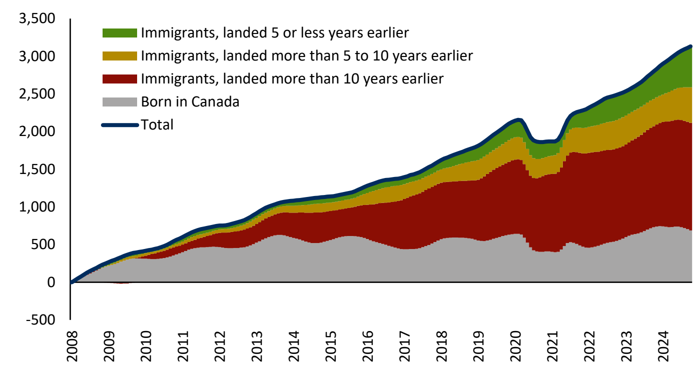
The BoC, in its October Monetary Policy Report that was published just before the new immigration guidelines assumed population growth of 1.7% in 2025 and 2026. Now with population growth estimated at -0.2% in both years, the BoC will need to reduce some of its key assumptions, reducing GDP forecasts and potential growth, which could potentially increase the justification of rate cuts to stimulate growth.

Chart 12 - Government Targets Unprecedentedly Low Population Growth in 2025 and 2026



Source: Statistics Canada; Population estimates as of 3Q24.

Chart 13 - Cumulated Contribution to Labour Force by Immigrant Status Since 2008 (In Thousands)



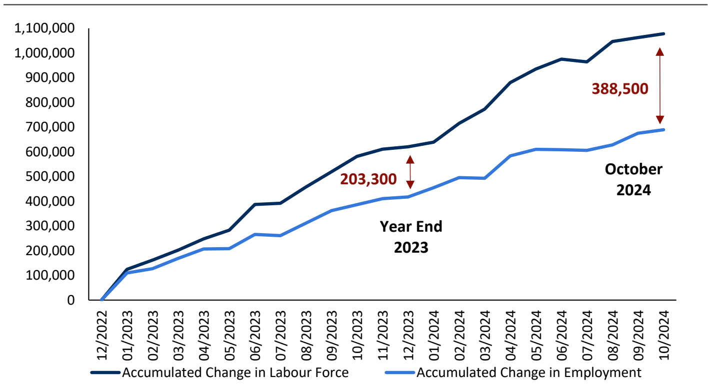
Source: Statistics Canada, Raymond James Ltd.; Data as of October 2024.

Canadian Labour Markets

October's employment numbers showed only 14.5k increase in the number of jobs in Canada, down from 46.7k in September. While youth employment improved (+33.0k) there was a concerning 11.1k decline for 25-54 year olds, raising our concerns about layoff activity in this core age group. This is also with the backdrop of the population growing 85.2k in October, although the labour force (the number of people that are employed or actively looking for work) only grew by 15.4k, which helped the unemployment rate stay flat at 6.5%. Still, over the past year, the labour force has increased by 2.3%, significantly outpacing the creation of new jobs at 1.5% (Chart 14). Consequently, we have observed higher unemployment rates among newcomers across all age groups (Chart 15). However, government intentions to reduce the number of new permanent and temporary residents in Canada should also put downward pressure on the unemployment rate later in 2025.

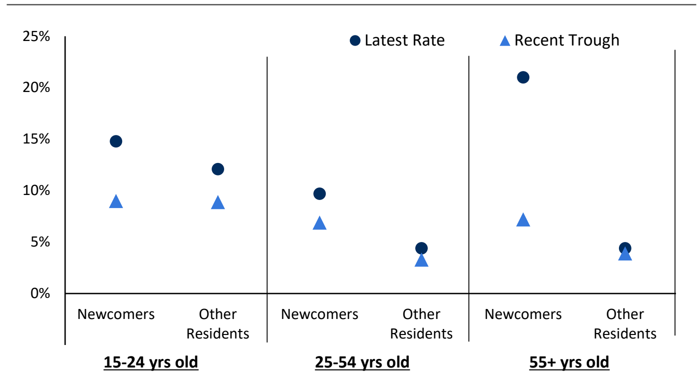
Annual average hourly earnings grew 4.9%, from 4.5%, suggesting wage inflation could continue to be a problem, especially within the public sector. Overall, wage growth is currently around 4% although expectations have been coming down since the spike in mid-2022 and are now forecasted at 2.9-3.5% over the next 12 months, depending on the business survey. Again, with immigration changes, and potentially tighter labour market, we could see higher wage demands towards the end of 2025 and into 2026.

Chart 14 - Growth of the Labour Force Outpaces Job Additions



Source: Statistics Canada; Raymond James Ltd.; Data as of October 31, 2024.

Chart 15 - Unemployment Rates, 3-Month Moving Average, NSA



Source: Statistics Canada and Bank of Canada calculations; Newcomers are who have arrived within the last five years. Recent trough is the lowest recorded rate between 01/2022 to 10/2024.

Canadian Housing

The big news affecting housing this month was the federal government's u-turn on immigration, which will reverse unprecedented growth into a slightly contracting population over the next couple of years. This affects the supply/demand dynamics of various segments of the Canadian housing market.

Canada has been facing a growing housing affordability and availability crisis for years, with weak supply growth but massive demand growth. Developers have been getting on board with the need and government incentives to increase the availability of purpose-built rental properties, and recently declining interest rates have provided the promise of growing interest in residential investment. Buildings that had already begun construction will most likely continue and help to alleviate the availability deficiency, although new starts may face headwinds as developers reevaluate demand given the changing immigration environment, offset by declining interest rates and therefore more favourable financing terms. The declining rate environment is also likely to still allow for house prices to edge higher, while rents on new leases are already falling in Toronto, Vancouver, and Calgary, and rent growth has quickly slowed in Montreal and Ottawa.

With the rate cutting cycle that started in June, we expect that home buyers started to come back to the market, preparing for subsequent declines in mortgage rates. As that browsing turned into offers, and sellers likely reasoned that they needed to balance further rate cuts against the likelihood of prices moving up, in October, the number of homes sold in Canada increased 30% from a year earlier, and were up 7.7% from September. By the end of October, the number of newly listed properties was down 3.5% from the previous month, with 174,458 listed properties across Canada, up 11.4% versus last year. The price of a "typical" home, as measured by the MLS House Price Index, remains muted (Chart 16). However, we expect it to gradually turn the corner in early 2025 as we enter the middle and move towards the end of the rate easing cycle. As rates approach buyers' expected lows, more buyers tend to enter the market, which then drives up valuations (Chart 18).

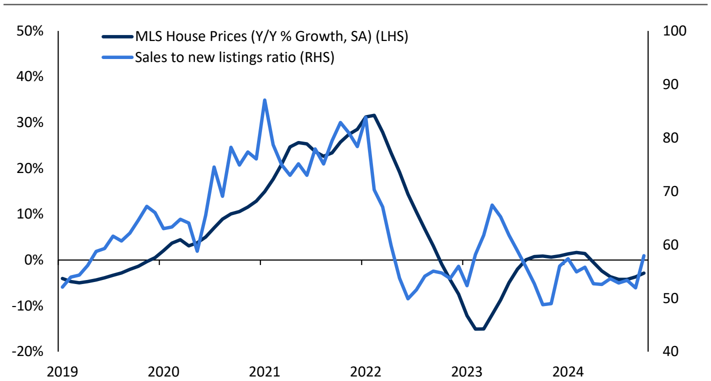
Mortgage renewals in Canada remain a concern. In 2025, 1.2 million mortgages will come up for renewal, followed by another 980k in 2026. Most of them will be renewed at rates that are significantly higher than the terms that are expiring. At least 1.05 million, or 85%, of the mortgages being renewed in 2025 were last set when the BoC rate was at or below 1%.

As interest rates have been dropping, mortgage rates have also come down. However, both fixed and variable mortgage rates are still much higher than pre-pandemic levels (Chart 17). We expect homeowners with three- to five-year fixed-rate mortgages to face a disposable income shock when they renew, with average rate increases between 170 and 240 bps. This increased financial burden might push financially stretched homeowners to sell their properties to downsize, contributing to a rise in new listings.

In July, mortgage debt totalled $2.2 trillion and was growing at approximately 3.5% per year. The delinquency rate has also been rising, to reach 0.192% in 2Q24, but remains below the pre-pandemic rate of 0.28%. This will likely rise however through 2025 as more strain and higher rates and payments are imposed on homeowners. To cope, many mortgage holders are reducing the term lengths on renewals with the expectation that as rates continue to fall, there will be more opportunities to lock in for a longer period at a later date.

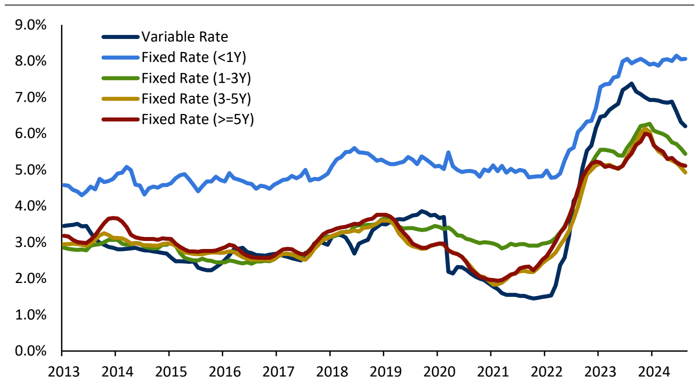
The BoC had been expecting residential investment to grow by 6% in both 2025 and 2026. With the recent u-turn on immigration policy, and therefore population growth over the next two years, we see more downward pressure on rents, housing prices, and new home construction.

Chart 16 - Increase in Home Sales, But Prices Remain Muted



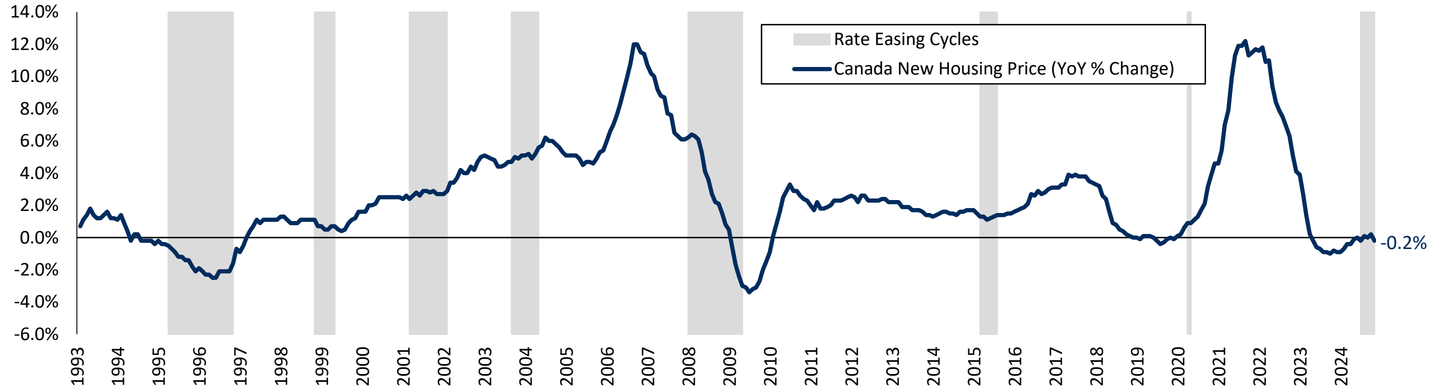
Source: CREA; Raymond James Ltd.; Data as of October 31, 2024.

Chart 17 - Households Likely to Face Higher Mortgage Rates Upon Renewal



Source: Statistics Canada; Data as of August 31, 2024.

Chart 18 - Canada New Housing Price (YoY % Change)



Source: Statistics Canada; Raymond James Ltd.; Data as of October 31, 2024.

U.S. Macro Discussion

In the U.S., we continue to track towards a soft landing scenario. The last time the U.S. achieved this type of slowdown was in 1994-95 and it's the ideal scenario to reset the economy and phase into a new growth cycle. A soft landing is where the economy goes through a cyclical slowdown, but without going through a couple of quarters of negative GDP growth, which is generally referred to as a technical recession. Of course a true recession is usually only labled so after the fact and is gauged on the length and depth of the slowdown and typically includes a significant number of layoffs and marked increase in the unemployment rate. The U.S. economy is nowhere near this situation currently, with still solid GDP growth, good corporate earnings, and still low unemployment rate. There are signs of a slowing growth rate, but nothing drastic.

U.S. Continues Towards a Soft Landing

U.S. real (meaning growth above the impact of inflation) GDP growth was 2.5% in 2023, and seems on track for 2.7% in 2024 after 3Q24 growth came in at 2.8% (annualized over 2Q24, or 2.7% over 3Q23). We are expecting moderating job growth and the cumulative effect of interest rates hitting U.S. consumers to dampen spending, leading to a forecast of 2.1% GDP growth in 2025 (vs. 2024).

Fed Rate Cuts Still Expected

Fed Chairman Jerome Powell has reminded us that decisions on rate cuts are based on data and their models, and their models do not incorporate what might or might not come about once the new administration takes over in January. His most recent comments were that "the economy is not sending signals that we need to be in a hurry to lower rates", reinforcing the idea that the Fed may still be more cautious about easing up. Before the next rate announcement however, the Fed will have additional data points on CPI (Dec 11) and payroll data (Dec 6) from which to better gauge the need for rate cuts following the next FOMC meeting (Dec 17-18). While continuing strong economic signals are reducing the odds of another rate cut before the end of the year, we continue to expect a 25 bp cut on December 18.

U.S. Debt Continues to Grow

One aspect that we want to monitor is the U.S. debt. With expectations of the new government accelerating the growth of the debt, which is now ~US$36 trillion, up from ~US$30 trillion at the start of 2024, the national debt is on track to rise by another US$20 trillion over the next 10 years. Interest payments alone are now US$900 billion per year. Now you would expect debt to rise if the U.S. had to step in to support a weak economy, but this is happening while the U.S. economy is growing at a relatively high pace. The U.S. Treasury has not had any difficulty finding buyers for this increasing debt, and with the U.S. having the benefit of reserve currency, this could potentially continue for a long period still.

U.S. 10-Year Rates Settling Back Down

With growing concerns about inflationary fiscal policies, and the growing U.S. debt and interest payments, the 10-year Treasury yield rose through the first half of November, to hit 4.44%, but has since settled back to around 4.25% as investors ended the month as (PCE) inflation data met expectations and Fed meetings soothed reinflation concerns and providing confidence of a rate cut on December 18. Trump's Treasury Secretary pick of Scott Bessent also calmed markets, given his reputation as a fiscal conservative expected to prioritize market stability and economic growth.

The early spike may have seemed surprising given that the Fed was lowering its policy rate, but the 10-year rate is determined by bond investors, and is more of an expression of the outlook on economic growth, inflation risk, and conviction that the U.S. will be able to continue making interest payments and ultimately repay its debt. The 10-year rate is influenced by the Fed's policy rate, and is normally higher, which gives us our normally sloped yield curve, but the premium that investors demand for holding that debt over 10 years is influenced by multiple factors. At the current time, it is likely the threat of inflation and that cash entrusted to these bonds will need to be worth that much more 10 years from now to compensate for that risk, which is driving the yields higher, despite being lower than a year ago.

Rising 10-year rates have implications for the economy, bond market, and equity market. For the economy, we need to consider longer-term lending that is not tied to the Fed's short-term policy rate. When consumers take longer-term loans for vehicles or houses, that have terms that are locked in for five to 30 years, those rates are determined by similar longer-term rates that their financial institution uses to source those funds. Investors holding fixed income investments usually expect their investments to increase in value during easing cycles, but if the longer-end of the yield curve rises, those bonds lose value. In the equity markets, stock valuations are often determined by discounting future cash flows to determine their current value. The discount rate is often tied to the 10-year Treasury rate, and therefore higher yields reduce the current value of those future cash flows and are seen in lower P/E ratios. Yields can also make fixed income more attractive and draw some investors to reallocate stock market weightings into the safer return of the bond market.

Trump 2.0

Many market commentators have been looking to Trump's first term as president for insights into what to expect during his second term. In this section we take a look at how the economic environment this time around is different than eight years ago, to judge if those comparisons are applicable.

In the table below, we compare the current U.S. economic landscape that Trump will inherit in his second term with the conditions during his first presidency. Overall, the current U.S. economy appears healthy, although lingering effects from COVID-19 remain, such as inflation above 2%, an inverted yield curve, and the national debt issue previously discussed. On the bright side, we also see increases in household net worth and productivity. However, this aggregate data doesn't capture the fact that U.S. households may be experiencing more financial difficulties in 2023 compared to 2016, leading to a greater divide in financial well-being amid high interest rates, according to the Economic Well-Being of U.S. Households in 2023 report from the Federal Reserve. This trend is worth monitoring consistently. Nonetheless, we believe the overall current U.S. economy is comparable to the pre-COVID economy (Table 1).

Table 1 - How does the current U.S. economic landscape compare to the period during Trump's first presidency?

Better	Worse	Neutral
Household Net Worth	**Inflation**	**Real GDP Growth**
Stimulus during the pandemic, rising home prices, and a stock market surge collectively drove U.S. household wealth to record levels.	While food, energy, and goods inflation have returned to pre-COVID levels, services inflation remains high, making the path to the 2% target a bumpy one.	Despite initial concerns about a potential recession, growth continued to outperform the long-term historical average of 2%. Nevertheless, we anticipate a slowdown in Q4 2024 before a rebound in 2025.
Labour Productivity	**Yield Curve**	**Fixed Investment (Equipment)**
After decades of sluggish productivity growth, we are witnessing an initial uptick in labour productivity in 2024, likely due to A.I. advancements, though the trend's sustainability is uncertain.	Inflationary pressures have not been fully eliminated, keeping the front end of the yield curve elevated. The yield curve remains partially inverted.	Despite the high interest rate environment, the growth rate of fixed investment in equipment for 2024 remains consistent with the average pace observed from 2017 to 2019.
Ouput Gap*	**Leading Economic Indicator**	**Labour Market**
Technological advancements enable the economy to operate above its estimated full capacity. A positive output gap indicates that demand is higher than normal.	The LEI has experienced some recovery since its mid-2023 low. While the YoY change is still negative, we anticipate further improvement, as we expect consumer sentiment to strengthen and new orders in the services and manufacturing sectors to pick up in 2025.	While unemployment is currently on the rise, it's still considered low by historical standards, and we don't expect a significant jump. The stronger wage growth compared to pre-COVID levels also suggests that there isn't much slack in the labour market. The participation rate is just slightly below what it was before the pandemic.
	National Debt	**Household Leverage**
	National debt has surged during and after the pandemic due to fiscal stimulus and "big ticket" government funding programs like the CHIPS Act. Additionally, elevated policy rates have increased the financial burden of interest costs.	While household debt has reached a new high and is putting disproportionate pressure on low-income families due to rising living costs and interest rates, the increase in disposable income has helped maintain a relatively stable leverage ratio at the aggregate level.

Source: Raymond James Ltd., as of November 2024.

*Output gap: the difference between what an economy actually produces and what it would produce in an ideal world.

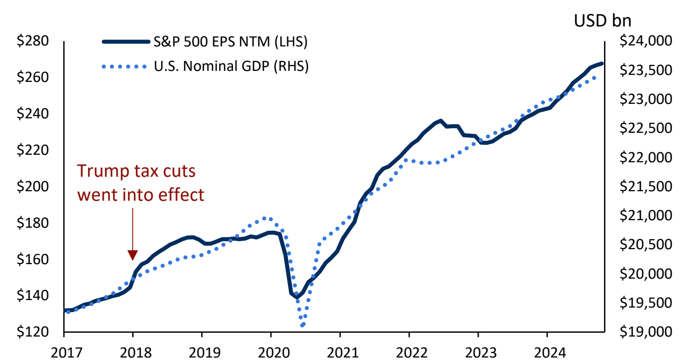
With about 50 days until Trump's inauguration, we would like to provide a high-level overview of the potential impacts of his key policies, along with observations from his first presidential term. Again, keep in mind that key policies take time to develop, and many initial proposals are often watered down. Therefore, as we continue to monitor the situation, investors should stick to well-established investment plans and avoid making decisions based solely on short-term fluctuations.

Corporate Tax Cut

The corporate tax cut is one of the key items Trump is proposing. Corporate tax cuts could lead to an immediate boost in corporate earnings and encourage businesses to invest for the long term. When the Tax Cuts and Jobs Act (TCJA) took effect at the beginning of 2018, the market quickly incorporated the tax cut into the projected earnings per share (EPS NTM) for the next 12 months (Chart 19). However, the effect of the tax cut on nominal GDP did not match the EPS NTM increase, likely because GDP reflects changes later in the process, and some benefits of the tax cut may have been lost along the way.

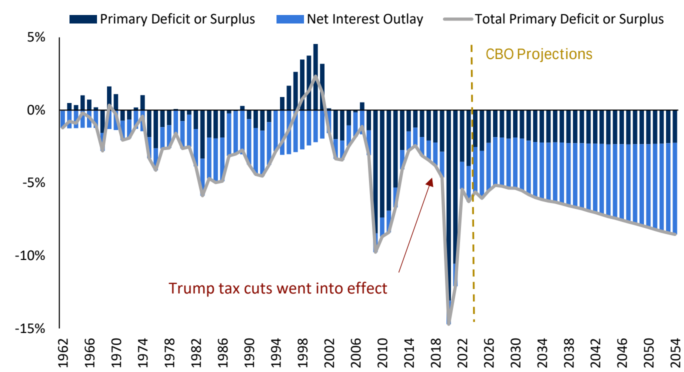
We are skeptical about Trump's ability to pass another round of significant tax cuts, as the budget deficit has risen from about 3% of GDP in 2016 to around 6% in 2023, according to the Congressional Budget Office (CBO) (Chart 20). Additionally, the slim majority in the House could also complicate this process. More importantly, as noted in Table 1, the U.S. economy is currently operating above its estimated full capacity, meaning that any new tax cuts might do more to increase inflation than to boost aggregate demand.

Chart 19 - Corporate Tax Cuts Likely to Boost Forward EPS



Source: FactSet; Raymond James Ltd.; Data as October 31, 2024.

Chart 20 - Widening Budget Deficit May Hinder Trump's New Tax Cuts



Source: CBO; Raymond James Ltd.

Deregulation

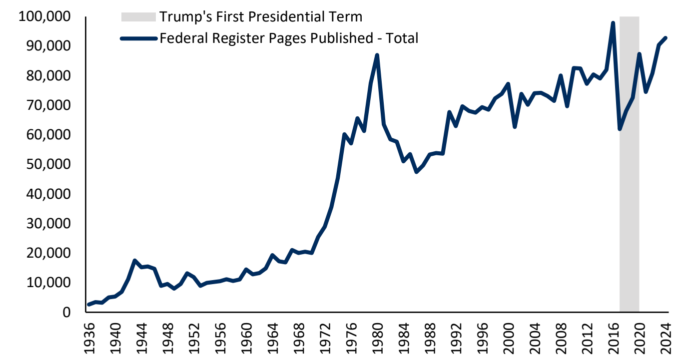
Trump's potential deregulation could further enhance productivity and GDP in the short term. He has highlighted three key areas:

- Financial Sector: Easing regulations may help businesses secure loans more easily, boosting investment.
- Technology Sector: Loosening restrictions on A.I. could strengthen U.S. leadership in this field.
- Energy Sector: Expanding all forms of energy production to boost energy products export.

However, this deregulation also carries risks, including increased financial instability, unethical AI practices, and environmental concerns over a long term. Interestingly, despite Trump making similar claims about deregulation during his first term, the total page count of the Federal Register eventually returned to similar levels after some early successes in 2017 (Chart 21).

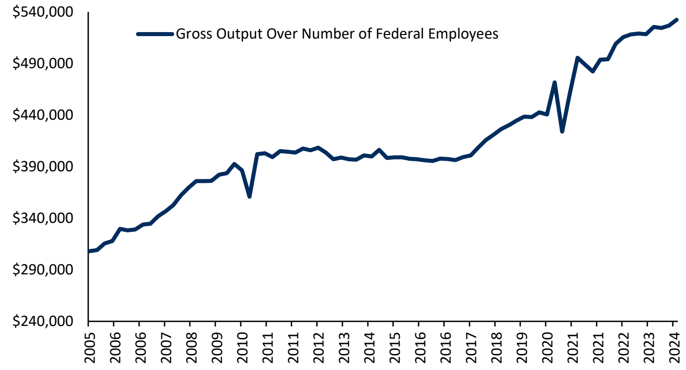
Another notable headline is that Trump has appointed Elon Musk and Vivek Ramaswamy to new cost-cutting roles aimed at improving efficiency in government spending. However, as highlighted by Eugenio Alemán, our Chief Economist at Raymond James Financial, in a recent weekly report, federal government employees make up only 1.9% of total nonfarm employment. When we evaluate the efficiency of federal employees by comparing gross output to their numbers, it becomes clear that they are actually more productive (Chart 22). Therefore cost-cutting will likely need to come from government programs. The largest line items in the U.S. federal budget include Social Security, Medicare, Defense, and Education, plus the massive interest payments on public debt that seem destined to increase. Significant cutting to any of these programs could result in massive backlash or disruptions, and therefore will likely require years of planning and negotiations.

Chart 21 - Number of Federal Register Pages Largely Unchanged At Trump's First Term End



Source: Federal Register; Data as November 2024.

Chart 22 - Federal Employees Are Arguably Becoming More Efficient Over Time



Source: BEA, FRED, Raymond James Ltd.; Data as of June 30, 2024.

Tariffs

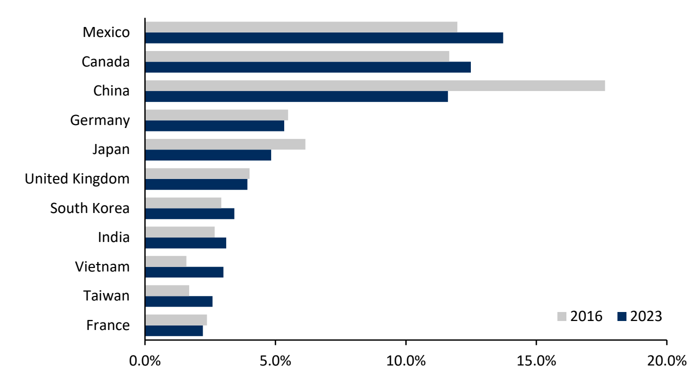
Tariffs have always been a hot topic on Trump's agenda. During the first Trump administration, countries generally responded to new U.S. tariffs carefully to avoid escalating tensions. Although counter-tariffs did not force the U.S. to make concessions, some nations successfully lifted tariffs by negotiating broader trade deals or increasing their purchases of U.S. goods.

For the second Trump term, it may be harder for governments to strike deals to avoid higher tariffs. This could lead to a stronger U.S. dollar, similar to what we saw in 2018 (Chart 23), and could also increase inflationary pressures. However, the exact impact is still uncertain due to various factors, like how tariff revenues are used, demand elasticity, domestic employment levels, and retaliation by trading partners. Additionally, many imports from China have shifted to Mexico in recent years, making Mexico a likely high-priority target for Trump this time around (Chart 24).

Chart 23 - Elevated Fed Policy Rate and Tariffs May Add Upward Pressure on the USD

Source: Bloomberg, Raymond James Ltd.; Data as of November 30, 2024.

Chart 24 - Shares of U.S. Import (Dollar Value) 2016 vs. 2023, Big Decline in China



Source: BEA, Raymond James Ltd.; Data as of December 31, 2023.

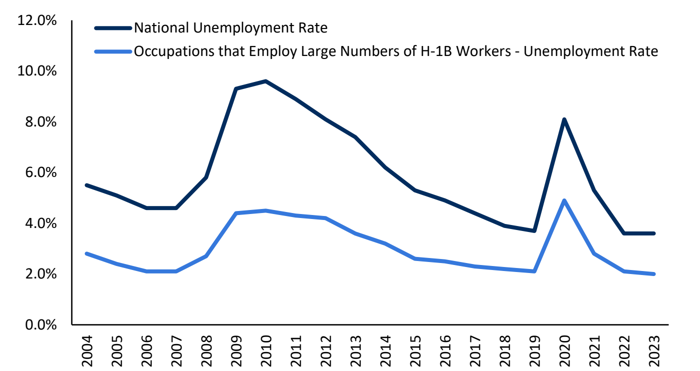
Immigration

Trump's immigration policies might be one of the most overlooked topics when it comes to their potential impact. Recently, he appointed Stephen Miller as Deputy Chief of Staff, who is known for his tough stance on both legal and illegal immigration. The denial rate for new H-1B[3] petitions rose from 6% in 2015 to 24% during the second half of Trump's first term. However, immigrant and native-born workers often have different skill sets, which makes them complementary in the labour market rather than direct competitors. As a result, unemployment rates have stayed relatively low in occupations with many H-1B workers from 2004 to 2023, even during COVID-19 (Chart 25). This trend suggests a high demand for these workers, so cutting H-1B visas could lead to wage growth and inflationary pressures. Plus, immigrants also drive consumption, so tightening immigration could hurt both supply and demand, ultimately affecting GDP.

In addition, if Trump were to deport up to a million unauthorized immigrants each year, sectors like construction, agriculture, and hospitality, where many unauthorized workers are employed, would likely feel the biggest impact, potentially leading to higher prices again. However, looking at historical trends, the unauthorized immigrant population in the U.S. has remained fairly stable, and the decline during Trump's first term wasn't significant (Chart 26). In the end, deporting unauthorized immigrants can be quite expensive.

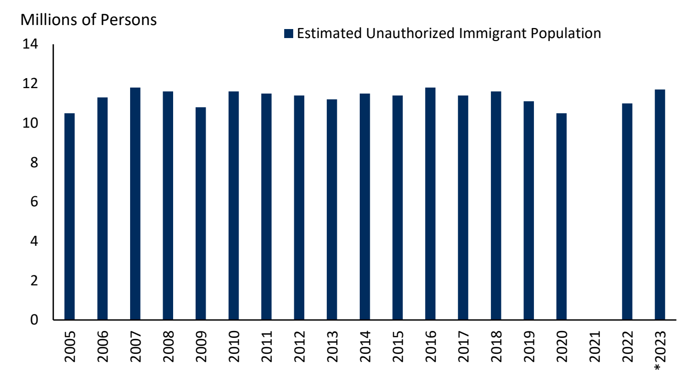
[3]The H-1B program allows employers to hire skilled foreign workers in specialty occupations and authorizes the temporary employment of qualified individuals.

Chart 25 - Relatively Low Unemployment in H-1B Intensive Occupations



Source: American Immigration Council; Data as of December 31, 2023.

Chart 26 - Historical Estimated Unauthorized Immigrant Population



Source: Office of Homeland Security Statistics; *estimate as of July 2023 by Center for Migration Studies; 2005-2009, based on 2000 Census; 2010-2014, based on 2010 Census; 2015-2017, method update; 2018-2020, method update; 2022, based on 2020 census.

In summary, while Trump will start his second term with a fairly healthy U.S. economy, there are several concerns to consider. Internally, issues like the national debt and inflation, along with external factors such as how trade partners react and exchange rates, could limit the scale of many of his key policy proposals. Based on what we saw during his first term, some of these policies might be softened. That said, it's still a bit early to fully assess the impact of his policies this time around.

The effects of these policies on the markets are discussed in the Financial Markets Discussion.

Financial Markets Discussion

Stock Indices Rally as Election Results Settle

In November, the TSX Composite, Canada's main stock market index, saw a 6.2% price return and a 6.4% total return. This performance was in line with the U.S. large-cap benchmark, the S&P 500, which posted a 5.7% price return and a 5.9% total return in local currency. The TSX Composite's gains were primarily driven by the Info Tech sector, while the S&P 500's growth was more broad-based, supported by strong performances in consumer discretionary, financials, industrials, and energy sectors. Among major equity indices, U.S. small caps, represented by the Russell 2000, experienced the largest jump following Trump's election win, generating a total return of 10.8% (Chart 27).

So far this quarter, the top-performing sectors of the S&P/TSX Composite have been Info Tech, up 27.6%, Energy, up 10.5%, and Financials, up 8.4%. Conversely, the noticeable laggards have been Communication Services, down 11.1%, Real Estate, down 4.7%, and Materials, only up by 0.6%.

Top 3 Sectors (November):

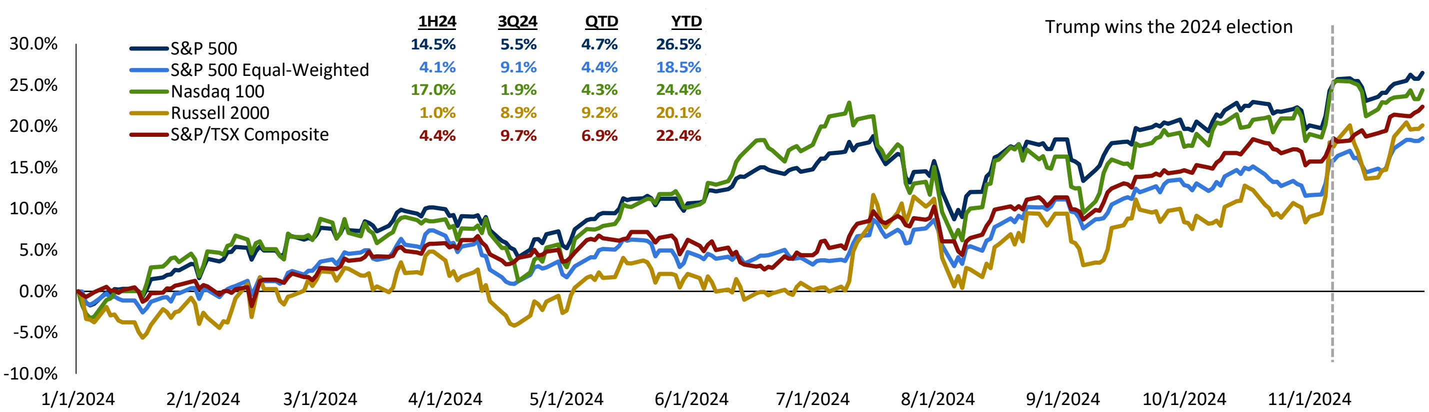
- **Info Tech**: The information technology sector experienced a broad-based gain in November, following ten months of underperformance compared to the TSX Composite. This significant rally was further boosted by Shopify, which alone constitutes more than half of the sector and achieved a total return of 48.6% due to its strong 3Q24 earnings.
- **Financials**: This sector has continued to react favourably to the BoC's ongoing easing. We continue to watch how lower provisions for credit losses can offset the downward pressure on net interest income as the rate easing cycle progresses for the banks. Companies in the capital markets industry are outperforming due to strong year-to-date market performance. Insurance stocks are benefiting from forward earnings momentum, which supports their solid returns.

- **Consumer Staples**: This sector has been struggling since August but managed to regain some lost ground in November, primarily due to a rebound in Alimentation Couche-Tard, which accounts for nearly half of the sector. The earnings outlook for this sector remains somewhat pressured. With inflation stabilizing, it's becoming harder for companies to justify price hikes for everyday goods. Consumer spending is now driven more by discounts and promotions, which could hurt companies' pricing power and profits.

Bottom 3 Sectors (November):

- **Communication Services:** 2024 has been a tough year for this sector, with intensified competition and regulatory issues remaining significant concerns.
- **Materials:** In Canada, this sector is heavily weighted towards gold. Its underperformance in November was largely due to a roughly 3.0% decline in gold prices. The gold price has been under pressure since Trump's victory in the 2024 presidential election, as uncertainty has decreased and market expectations of a high-rate environment have increased.
- **Real Estate:** This sector experienced a strong rally when the rate easing cycle began in June, but it lost a few percentage points in October and the first half of November. There are early signs of upward momentum building again, but macroeconomic headwinds, namely reduced immigration targets potentially leading to two consecutive years of negative population growth, may weigh on its future performance.

Chart 27 - Selected Indices Price Returns



Source: FactSet, Raymond James Ltd; Data as of November 30, 2024. Price return in local currency.

Table 2 - S&P/TSX Composite Sector Performance and Valuations (Ranked by Quarter-to-Date Total Return)

Sector Name	Sector Weight	2024 YTD Total Return	QTD Total Return	1M Total Return	Current P/E NTM	Historical P/E NTM
Information Technology	10.2%	44.0%	27.6%	28.3%	39.0	22.8
Energy	17.3%	28.6%	10.5%	5.4%	15.1	14.6
Financials	32.5%	32.3%	8.4%	7.5%	12.3	11.4
S&P/TSX Composite	--	25.8%	7.3%	6.4%	15.8	14.5
Consumer Staples	3.9%	19.6%	4.2%	7.2%	17.8	15.9
Consumer Discretionary	3.3%	15.3%	3.8%	3.6%	15.9	14.4
Industrials	12.6%	14.0%	3.4%	5.0%	22.2	15.9
Utilities	3.8%	17.5%	1.7%	3.5%	22.1	18.0
Health Care	0.3%	13.0%	0.6%	-3.9%	5.7	16.0
Materials	11.6%	28.3%	0.6%	-2.9%	15.4	17.0
Real Estate	2.0%	12.3%	-4.7%	1.0%	15.4	14.7
Communication Services	2.6%	-13.2%	-11.1%	-7.0%	13.4	15.7

Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024. The S&P/TSX Healthcare sector has been excluded from the performance commentary due to its minimal representation in the S&P/TSX Composite Index.

Canadian Outlook by Sector

Heading into 2025, we provide our general views on certain key TSX sectors:

Financials

The financials sector is the most influential on the TSX Composite, representing approximately one-third of its weight. Within this sector, banks have the most influence, making up ~60%, with insurance companies at ~20%, followed by diversified financials, including asset managers, at ~15%, and companies that have significant real estate investments, in contrast to the TSX real estate sector, at ~5%. This sector is therefore most influenced by the outlook of the Canadian economy, which is weak but showing modest signs of improving, and an interest rate environment high enough to generate a good yield on the difference between lending and borrowing rates, while reducing concerns of non-performing loans and defaults. A lot may depend on the federal goverment's ability to deal with Trump's tariff threats, enabling ongoing GDP growth and reassuring business owners that it is safe to invest in production improvements, despite the potentially volatile trade environment.

Energy

Energy is the second most influential sector of the TSX Composite, at ~17% weighting. The overarching factor in the energy market currently is the unfavourable supply/demand outlook. On the supply side, we expect a Trump administration to ease the way for more production from the U.S., while OPEC+ looks to be ending voluntary supply cuts. Saudi Arabia has already reduced its output to ~9 million barrels per day (mln bpd); well below its 12.5 mln bpd potential. Saudi Arabia's breakeven on such a move is estimated at US$50/barrel, meaning that even if the price per barrel fell from the ~US$69 price currently, the Kingdom would still end up in a better revenue position as long as the price held in above US$50. That's a bet that Saudi Arabia might be willing to take at some point in the next couple of years. This makes the commodity price downside risk a possibility. The upside risk obviously comes from conflicts in the Middle East, although so far it seems that players have managed to keep oil supply disruption, including restrictions in the Strait of Hormuz, off the table.

On the demand side, we see only modest demand increases in 2025 - perhaps just enough to keep prices stable, depending on the supply picture. We are focused mostly on China, which is in the midst of a stimulus program that is falling somewhat flat so far. The chances of China's 7% demand growth seen in 2023 coming back any time soon seems unlikely. Beyond crude, on the natural gas side, we see growing demand for liquified natural gas (LNG) around the world, and the start-up of LNG Canada's facility in Kitimat, B.C. in mid-2025 as a positive for the Canadian producers, although there would seem to be plenty of spare capacity available to take advantage of any increase in price.

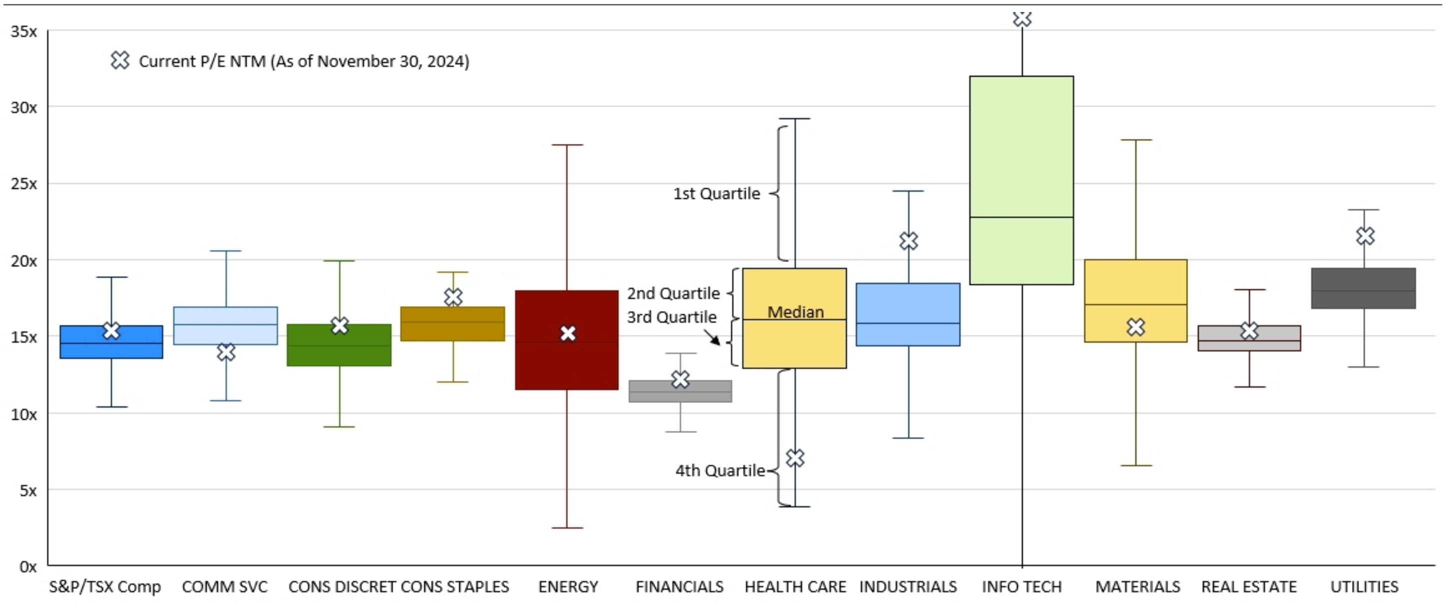
Offsetting the weak commodity dynamics in the energy sector, we also have Canadian energy companies that are flush with cashflow and trading at relatively good valuations. Despite discussions of electrification and peak oil demand, we see lots of long-term potential for the Canadian energy sector despite short-term pressures. In the short term, with a generally weak commodity pricing cloud, we see investors favouring larger cap names, and by sub-sector we see more interest on the natural gas side and its use in supporting the buildout of baseline electricity capacity than in crude oil-focused names.

Materials

Materials carries roughly 14% weighting in the TSX Composite, and is dominated by gold, with ~50% weighting in the sector. While gold had a strong run through much of 2024, with USD strength and a shift of sentiment to risk assets following the U.S. election, we have seen a bit of a pullback in the commodity price.

Industrial metals such as copper, aluminum, and iron picked up as excitement of China stimulus came out, although enthusiasm has waned slightly since then. We continue to like materials such as copper and uranium that we believe will play a major role in global electrification efforts, and even with the growing computing buildout for A.I., including its massive power requirements. The prospects for copper are of great interest in Canada as it makes up ~7% of the materials sector, with all base metals representing ~13%. It's near-term prospects seem balanced between the declining prospects of China's old economic growth model and the growth opportunities developing from the green transition, including in China, which now represents approximately two-thirds of copper demand across that country. This green, or clean, technology push is primarily driven by electric vehicles, renewable energy generation, and power infrastructure.

Chart 28 - S&P/TSX Composite Sector Current vs. Historical P/E NTM



Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024. Historical P/E: 1/1/2000 – 11/30/2024. Excluding outliners.

U.S Equities

The U.S. markets have wrapped up another earnings season, with still solid earnings gains, although earnings beats were a little lighter than in previous quarters. The economic backdrop remains favourable for continuing the current bull market as overall earnings for the S&P 500 are expected to be US$243 for 2024, up 9% from US$223 in 2023, and optimistically expected to be up another 12% to US$273 in 2025. That being said, there is no denying that the S&P 500 seems somewhat expensive at over 22x P/E (2024), although that can currently be rationalized given the growth expectations. For context, the very long-term average P/E is approximately 16x, although over the last 20 years, the average has been closer to 20x, and ranged from 17x to 24x, excluding outliers from the GFC and COVID periods.

There also seems to be optimism around expected Trump policies, specifically around deregulation and lower taxes that are expected to sustain tailwinds for some financials, industrials, and energy, although cabinet picks (RFK Jr) and tariffs, and the potential for trade wars in general, creating some uncertainty in pharma/health care and global equities broadly. There is much debate on how aggressive a Trump administration will be on implementing tariffs, or if they will remain as more of a threat and negotiation tactic. There remains much uncertainty about how all these aspects will impact economic growth, inflation, the deficit, and interest rates, and that will in turn end up influencing equity prices. We know better than to claim we know what Trump will indeed do, versus promise or threaten, such that it will likely be a good idea to remain well diversified and as protected as possible against extreme outcomes.

With rising equity valuation multiples and somewhat increased 10-year Treasury yield, the S&P 500 equity risk premium is down to a 22-year low and teetering on becoming negative. Calculated as the S&P 500 earnings yield minus the risk-free rate, typically dictated by the 10-year Treasury yield, the equity risk premium represents the reward that investors are getting for taking the added risk of equity investing versus what they could get risk-free. A negative measure can reduce the attractiveness of equities and result in investors shifting to favour lower-risk assets until the earnings yield rises or Treasury yields decline.

Despite some near-term weakness or pressure given the extended valuations, we still see more tailwinds for the U.S. equity market given the economic outlook and profit outlook. As far as some themes to consider:

- Cyclicals (ex-technology) have outperformed defensive stocks, but have not kept pace with the broader market and therefore could benefit from some ‘catch up’ trades.
- Small cap equities have shown some improvements but still lag larger caps as far as valuations go given some positive earnings and guidance.
- Global bank earnings have held up well, and with an improving economic picture and the prospective of deregulation that could prompt more M&A activity, fees could be looking up.

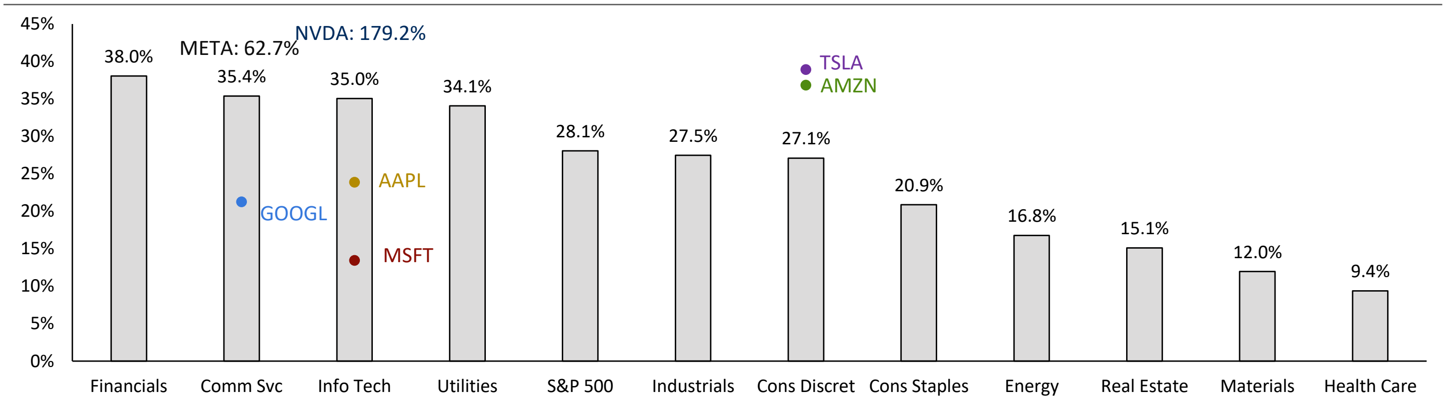
The main U.S. index that we follow, the S&P 500, is on track to post a second consecutive year of 20%+ gains. This milestone was last attained in 1998, during a soft landing and a technology revolution - sound familiar? While the U.S. economy remains strong, despite showing some signs of growth slowing, the stock market has remained enthusiastic. Investor sentiment (The Conference Board Consumer Confidence) remains bullish, with over 56% of investors expecting stock prices to go up over the next 12 months, up from 39% at the start of the year and 51% last month. This is the highest optimism level since this tracking started in 1987. Investors' allocations to equities is also approximately 70%, near the highest level in 20 years. This is reason to be cautious in the near-term, yet a solid economic backdrop likely supports continuing (if more modest) gains in the next 12 months. With the uncertainty of the election now behind us, we expect that the market will at least be more prepared for potential tariffs, tax cuts, and increasing national debt. Having a better idea of what to expect typically helps the market, versus uncertain paths before an election.

Rotation and Market Breadth

Much has been discussed about the Magnificent Seven (M7) stocks in the U.S., and their outsized impact on the main S&P 500 index, and the technology-driven Nasdaq 100, over the last couple of years. Over the last few months, we have started to see more breadth come into markets, as a broader selection of companies have posted better earnings and subsequently received better investor recognition, as evidenced by growing price-to-earnings (P/E) multiples. Over the past year, M7 as a group has maintained a forward P/E multiple in the 30-35x range, while the other 493 companies in the index have collectively moved up from a 17x P/E to roughly 21x. This is also due to greater confidence in broad strength in the U.S. economy, with now declining interest rates, which help small and mid-sized companies more than the mega-cap companies that are generally flush with cash. Approaching the end of the year, we saw investors move back into the mega-caps once again, likely after the solid 3Q24 results and positive guidance into 4Q24 and 2025, specifically with continuing enthusiasm about A.I.

In Chart 29 we show the breadth of YTD returns across the sectors of the S&P 500, while also highlighting the individual YTD return from each of the M7 members.

Chart 29 - S&P 500 Sector and "Magnificant Seven" Year-to-Date Total Returns



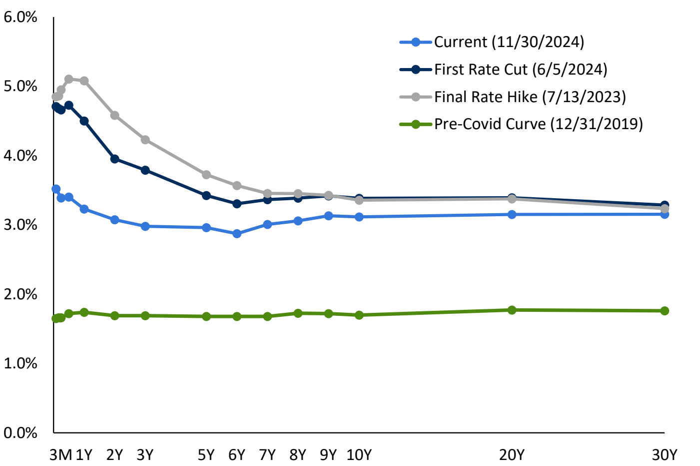
Source: FactSet; Raymond James Ltd.; Data as of November 30, 2024.

Fixed Income & Treasury Yields

When comparing the end of November to the previous month, both the Canadian and U.S. treasury yield curves seem to have barely moved. However, during the month, both curves initially rose after Trump won the 2024 presidential election but then declined towards the end of the month. In Canada, we expect the yield curve to continue to uninvert as the rate-cutting cycle progresses into 2025, given the overall weakening economy.

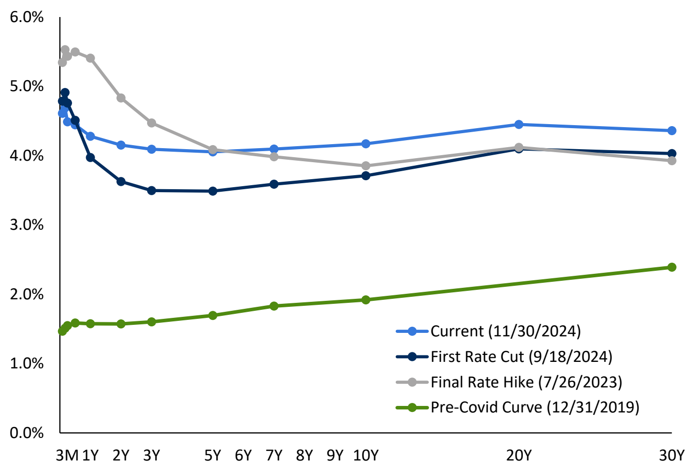
In contrast, the U.S. faces more uncertainty. Fed Chair Powell has stated that the Fed won't speculate about Trump's impact on the economy, meaning the front end of the yield curve still largely depends on inflation and labour force conditions. However, the mid and long ends of the curve, determined by bond investors, reflect expectations for economic growth, inflation risk, and the national debt and deficit, may experience more fluctuations as Trump steps into the White House again. Trump's key policies on tariffs and immigration could fuel future inflationary pressure, while deregulation and corporate tax cuts may boost company profitability and increase long-term return expectations. Overall, his policies may keep the yield curve higher than what we would otherwise expect.

Chart 30 - Canada Government Yield Curves



Source: Factset, Raymond James Ltd.; Data as of November 30, 2024.

Chart 31 - U.S. Treasury Yield Curves



Source: Factset, Raymond James Ltd.; Data as of November 30, 2024.

International Equities

The North American stock market outperformed other developed and emerging markets last month. Germany and the U.K. led among developed markets outside of North America. However, Trump's election victory caused the U.S. dollar to surge, making returns in other developed markets look poor in USD terms. Additionally, the threat of tariffs from Trump added extra downward pressure on these markets.

China's equity market remained quite volatile throughout the month. With the boost from the largely insufficient fiscal support fading and the recent Trump victory, we expect its performance to be under pressure for a while. Meanwhile, India's equity market is facing growing concerns about its high valuation, which has also dampened its recent performance.

Table 3 - Global Equities Performance

Select Global Equity Indices	1Mo (in LCL)	1Mo (in USD)	1Mo (in CAD)	3Mo (in LCL)	3Mo (in USD)	3Mo (in CAD)	YTD (in LCL)	YTD (in USD)	YTD (in CAD)	Current PE NTM	Historical PE Median	Premium (RED) / Discount (GREEN)
Major Aggregates												
World (Global)*	4.7	4.7	5.1	4.4	4.4	8.5	22.1	22.1	29.6	19.3	15.9	3.4
EAFE (DM ex U.S. & Canada)*	-0.2	-0.2	0.2	-5.1	-5.1	-1.4	6.5	6.5	13.1	13.7	13.5	0.2
EM (Emerging Markets)*	-2.5	-2.5	-2.0	-0.6	-0.6	3.3	8.0	8.0	14.7	12.0	11.7	0.3
Selected Developed Markets												
Nikkei 225 (Japan)	-2.2	-0.8	-0.4	-0.5	-3.5	0.3	16.1	8.9	15.7	21.0	18.9	2.2
Euro STOXX 50 (Europe)	-0.3	-3.2	-2.8	-2.7	-7.5	-3.9	9.7	1.6	7.9	13.8	13.2	0.6
FTSE 100 (U.K.)	2.6	1.0	1.5	-0.4	-4.3	-0.6	11.1	6.8	13.5	11.6	12.4	-0.8
CAC 40 (France)	-1.5	-4.2	-3.8	-5.0	-9.4	-5.8	-1.2	-5.5	0.3	13.8	13.4	0.4
DAX (Germany)	2.9	0.1	0.5	3.8	-0.9	2.9	17.2	12.0	19.0	13.4	12.6	0.8
Hang Seng (Hong Kong)	-4.2	-4.3	-3.9	9.0	9.2	13.5	19.0	19.4	26.8	8.9	12.4	-3.5
Selected Emerging Markets												
CSI 300 (China)	0.7	-1.0	-0.5	18.3	15.8	20.1	17.5	15.2	22.1	14.5	13.7	0.9
Nifty 50 (India)	-0.2	-0.7	-0.2	-4.2	-4.9	-1.4	12.5	10.7	17.4	22.6	18.6	4.0

Source: FactSet; Raymond James Ltd; Total returns, data as of November 30, 2024. LCL: listed in local currency. Historical P/E Median: 1/1/2000 – 11/30/2024. *Indices are represented by their corresponding iShares ETFs, serving as proxies.

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