TD Wealth Private Investment Counsel

# June 2023 Market Newsletter

June 1, 2023

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## Opening Comments

- May was a month with continued returns to the headlines in the financial world. Front and center was the US Debt Ceiling situation which we summarized in our recent special update on May 26th.
- As we have already addressed this , we will focus our newsletter this month on Alternative Investments and our outlook, as well as implementation into client portfolios.

## Noteworthy News

- The Bank of Canada has not met since our last update, they are scheduled to announce any potential changes or lack thereof on June 7th. They continue to maintain a policy rate of 4.50%. However, the labour market is showing no signs of a slowdown, with April employment numbers coming in higher than expected which could force the central bank to start to reconsider holding rates steady.
- The US Federal Reserve has so far continued to raise rates and their next meeting on June 13th may also be affected by persistently strong inflation and employment data south of the border.

## Alternative Investments / Real Assets

- The real estate market has been hit by rate hikes. Global transaction volume for this sector tumbled 63% y/y in Q4/22. We believe that tighter lending conditions and disagreements over property valuations are responsible for this decline. Real estate valuations have also decreased by about 3.5% since their peak in June 2022 and this trend is expected to continue as the market adjusts to higher interest rates.
- High inflation, interest-rate volatility, and mounting recessionary fears have dampened transaction activity, prompting a flight to quality within the market. Our current positioning reflects an underweight position in both Canadian and Global Real Estate.
- However, for other alternative assets, such as infrastructure, we maintain a modest overweight view. Increases in cash flow from higher than expected inflation is buffering rising interest rates. Investor appetite remains strong, particularly for energy transition investments and critical infrastructure sectors that generate stable, growing cash flows.
- We maintain a modest overweight to private debt. High credit quality and global diversification provides safety in a potentially recessionary environment. Incremental income and potential capital appreciation from interest rate moderation provide upside.
- Alternative assets can potentially provide inflation protection and attractive absolute returns, while acting as long-term portfolio stabilizers via their diversification and less correlated income streams. They are not a fit for all investors and some may have lower liquidity than standard public market investments, so we continue to implement these in investor portfolios on a case by case basis, keeping in mind unique investor goals and restrictions.

Commercial Mortgage Backed Securities Delinquencies
Expected to Rise

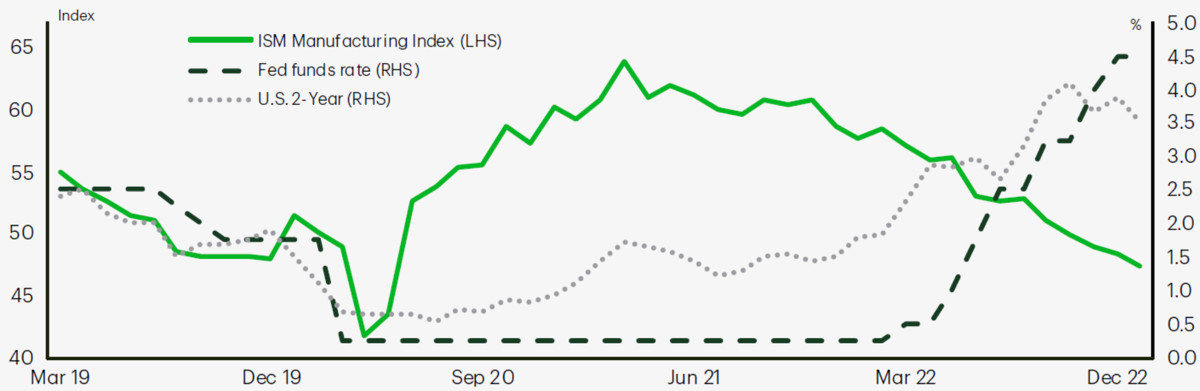
| Property Type | Current Delinquency Rate (Oct 2022) | Projected Delinquency Range by YE 2023 | Pre-Pandemic Delinquency Rate (Mar 2020) | Pandemic Peak | Historical Peak |
|---|---|---|---|---|---|
| Retail | 5.70% | 10.8% - 11.3% | 3.50% | 11.60% | 11.60% |
| Hotel | 4.90% | 8.3% - 8.8% | 1.40% | 18.40% | 21.30% |
| Office | 1.20% | 3.5% - 4.0% | 1.30% | 1.90% | 8.80% |
| Multifamily | 0.30% | 1.6% - 2.1% | 0.40% | 0.70% | 17.60% |
| Industrial | 0.40% | 0.8% - 1.3% | 0.30% | 0.70% | 10.90% |

Source: Fitch Ratings, Oct 2022

## Looking Forward

- Leading economic indicators are signaling that the U.S. economy may be approaching its limits. The ISM manufacturing index has been a reliable historical indicator in predicting economic slowdowns, or outright recessions.
- Business sentiment has steadily declined since interest rates began rising more than a year ago. Initially, it was coming off lofty levels, but it moved into contractionary territory five months ago and hasn't yet found a bottom. Because of this we continue to remain in defensive positioning within our portfolios.

Business Sentiment Dropping As Rates Rise




Source: FRB, ISM, TD Economics.

## Closing Thoughts

- Incorporating Alternative Investments your portfolios can potentially offer attractive diversification. If you have any questions about how or if we factor them into your personal portfolio, please do not hesitate to reach out to us. We wish everyone a great month of June! - Andrew & Nathan

| Market Performance (Source: Bloomberg) | | | |
|---|---|---|---|
| | May 31 2023 | Dec. 31, 2022 | YTD Change |
| **Equity Index Update** | | | |
| S&P 500 | 4181 | 3840 | +8.9% |
| S&P/TSX Comp. | 19575 | 19385 | +1.0% |
| MSCI EAFE | 2042 | 1944 | +5.0% |
| **Government Bond Yields** | | | |
| U.S. 10-yr Treasury | 3.64 | 3.88 | -0.24 |
| Canada 10-yr Bond | 3.19 | 3.30 | -0.11 |
| **Foreign Exchange Cross Rates** | | | |
| C$ (USD per CAD) | 0.74 | 0.74 | +0.0% |
| Euro (USD per EUR) | 1.07 | 1.06 | +0.9% |

| Official Policy Rate Targets<br>Central Banks | Current Target |
|---|---|
| Federal Reserve (Fed Funds Rate) | 5.00% - 5.25% |
| Bank of Canada (Overnight Rate) | 4.50% |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