RAYMOND JAMES®

PRIVATE CLIENT SOLUTIONS

ASSET ALLOCATION QUARTERLY

- **Odds of a Global Recession Remain High for 2023**
- **Inflation to Fall from the Peaks**
- **Elevated Volatility and Uncertainty to Persist**
- **China Reopening and a Warmer Winter in Europe Are Positives**
- **Many Opportunities across Global Equities and Fixed Income**

The Seventh Inning Stretch

January 2023

Raymond James Ltd. 5300-40 King St W. | Toronto ON Canada M5H 3Y2. | 2200-925 West Georgia Street | Vancouver BC Canada V6C 3L2.

Quarterly Outlook: The Seventh Inning Stretch

Nadeem Kassam, MBA, CFA
Head of Investment Strategy

Tavis C. McCourt, CFA
Institutional Equity Strategist

Ellis Phifer, CFA, CMT
Institutional Fixed Income Strategist

Ed Mills
Washington Policy Analyst

Eugenio J. Alemán, Ph.D.
Chief Economist

Eve Zhou
Multi-Asset Analyst

It's usually during the seventh inning stretch when baseball fans rise and sing along to the unofficial anthem of North American baseball "Take Me Out to the Ball Game". It's also when fans take cheering for the home team to a whole new level. But the seventh inning is also an indication that the majority of the game has passed, and if the home team is down, it's time to cheer hard and pray for the win! Similar to the seventh inning stretch, which marks the 80 per cent point of the game, we believe several economic and market indicators suggest today that most of this economic cycle is behind us. This is perhaps why a majority of strategists and economists are suggesting a recession will begin at some point in 2023. While we are in agreement that a recession is likely ahead for several advanced economies including in Canada, the U.S. and the U.K. in 2023 or possibly in early 2024, we believe it will come down to the bottom of the ninth in terms of the black swan event that will eventually push the global economy into a slowdown – the length and severity of which will depend on several factors. Today, our base case assumption is for a mild recession to unfold in North America during 2023.

Key Takeaways:

- **In the Seventh Inning, but Feels like the Bottom of the Ninth!** All said, we expect global growth to be considerably weaker in 2023, with the risks of a recession over the next 12 months rising to ~65 per cent for both the U.S. and Canadian economies. While we are not there yet, North American economies are slowing quickly. Strong labour markets and cooling inflation remain the silver lining heading into 2023, which could prevent a more severe downside scenario.

- **Equity Positioning Stays at Neutral – Focus on Getting on Base Rather than Trying to Knock it Out of the Park!** We continue to suggest investors remain selective with a defensive posture, as the Fed-led rate hikes are likely to peak sometime in 2023. This, coupled with a softer outlook for the USD, should enable value stocks globally to outperform growth over the near-term, with developed markets (e.g., MSCI EAFE) and emerging markets (e.g., MSCI EM) likely putting up a good showing in 2023, especially as China abandons its zero-COVID-19 position. Attractive valuations and a low-bar for earnings across several markets globally make for a rather compelling case for equities outside of North America. In the U.S., we see lower risks and attractive upside for mid- and small-cap equities (e.g., S&P Mid-Cap 400 and S&P Small-Cap 600) versus large-cap equities (e.g., S&P 500), while we maintain a slight overweight to Canadian equities (e.g., S&P/TSX Composite and S&P/TSX 60). For our S&P 500 and S&P/TSX Composite sector recommendations, please click here.

- **Fixed Income Allocation Stays at Neutral, but Consider Adding to the Roster (i.e., Duration) in the Off-season**. We advise clients to consider adding duration (through longer maturities) to their portfolios to capture higher yields in the current environment. While we like shorter-maturity yield levels for short-term cash needs, we prefer longer-duration fixed income products for a higher total return. The growing risks of a recession provide less confidence regarding adding to credit, so we continue to suggest that corporate bond holdings be reduced to underweight in total alongside an increase in quality and defensive positions. In relative terms, U.S. yields are higher across the board than Canadian ones, so we prefer holding U.S. treasury over Canadian sovereign bonds.

Contents

Asset Allocation Recommendations

Tactical (9-12-Month) Asset Allocation Recommendations

	- Neutral +	Comments
Equity		We are maintaining a neutral allocation towards equities as the growing risks of a recession rises for 2023. However, despite this, we are seeing some good opportunities across markets globally, which have reflected these and other risks either in forward valuations, earnings or both for 2023. We suggest investors remain highly selective & well-diversified across global equities and focus on markets that offer compelling risk/rewards.
U.S. Large Cap (S&P 500 Index)		The U.S. large cap space represents some of the highest quality businesses in the world, with strong competitive attributes, high-levels of profitability, and strong enduring growth profiles. However, valuations still remain elevated relative to history and versus other markets globally, while earnings expectations still remain far too high for 2023. Together, these factors support our neutral stance towards U.S. large caps.
U.S. Small-Mid Cap (S&P 600 and S&P 400 Index)		We see compelling relative valuations and attractive risk/rewards across the U.S. small-mid caps space. As recession risks grow, we see the current discount valuation of U.S. small-mid caps relative to the past 20-years (which are trading in the 10th percentile of historical valuations) and their lower earnings expectations as largely discounting many of the uncertainties ahead.
Canadian Large Cap (S&P/TSX 60 Index)		We see a compelling risk/reward profile for the broad Canadian market relative to large cap equities in the U.S. and across several global markets. In particular, we have a favourable view on high-quality equities across sectors/industries trading at reasonable valuations with lower earnings risk/downside revisions given the late stage of the current business cycle.
Canadian Broad Market (S&P/TSX Composite Index)		We see a compelling risk/reward profile for the broad Canadian market relative to large cap equities in the U.S. and across several global markets. In particular, we have a favourable view on high-quality equities across sectors/industries trading at reasonable valuations with lower earnings risk/downside revisions given the late stage of the current business cycle.
Developed (MSCI Europe, Australasia, and the Middle East (EAFE) Index)		We have become more constructive on the region as we move past the peak in USD strength/Fed-hawkishness, and see broad based improvements in China including a material pivot away from its economically destructive zero-COVID policies. As a result, we have shifted our tactical allocation from very underweight over the past quarter back to a slight overweight. While we continue to see risks ahead for the EAFE region in general, attractive relative valuations and a low bar for earnings expectations offer compelling risk/rewards for investors in 2023.
Emerging (MSCI Emerging Market (EM) Index)		We have become more constructive on the region as we move past the peak in USD strength/Fed-hawkishness, and see broad based improvements in China including a material pivot away from its economically destructive zero-COVID policies. As a result, we have shifted our tactical allocation from very underweight back to neutral. While we continue to see risks ahead for the EM region in general, attractive relative valuations and a low bar for earnings expectations offer a compelling risk/reward setup for investors in 2023.
Fixed Income		With growing risks that this central bank tightening cycle will end in a recession, we suggest investors maintain a neutral stance to fixed income. We see the most attractive opportunities in longer duration bonds, particularly in the 7-10 year segments of the curve.
U.S. Government (Bloomberg U.S. Treasury Total Return Index)		We suggest investors increase weighting to an overweight allocation to U.S. government bonds as the risk of a recession have increased. However, we would avoid the shorter end of the curve (1-3 years) and begin to add U.S. government bonds between 7-10 years.
U.S. Corporate (Bloomberg Barclays U.S. Corporate Bond Index)		U.S. investment grade corporate bonds continue to offer fair risk/reward characteristics especially as credit spreads have widened out more recently. However, with the risk of a recession increasing, we suggest reducing credit risk to underweight. We suggest investors maintain exposure to bonds with a duration profile between 3-7 years.
Canadian Government (FTSE Canada All Government Bond Index)		We suggest investors increase weighting to an overweight allocation to Canadian government bonds as the risk of a recession have increased. However, we would avoid the shorter end of the curve (1-3 years) and begin to add Canadian government bonds from 7-10 years.
Canadian Corporate (FTSE Canada All Corporate Bond Index)		Canadian investment grade corporate bonds continue to offer fair risk/reward characteristics especially as credit spreads have widened out more recently. However, with the risk of a recession increasing, we suggest reducing credit risk to an underweight stance. We suggest investors maintain exposure to bonds with a duration up to 2-years.
Cash		Maintaining a neutral allocation to cash.

Source: Raymond James Ltd.; Data as of December 31, 2022.

Global Economic Outlook – The Recession Cheer Grows

From the first pitch until the seventh inning stretch, no two baseball games are alike, with many jaw-dropping, nerve-racking and climactic moments for both players and fans alike. This is akin to investing, as no two economic or market cycles are exactly the same, with investors rotating through a range of emotions from anxiety, optimism, and pessimism during the various stages of the cycle.

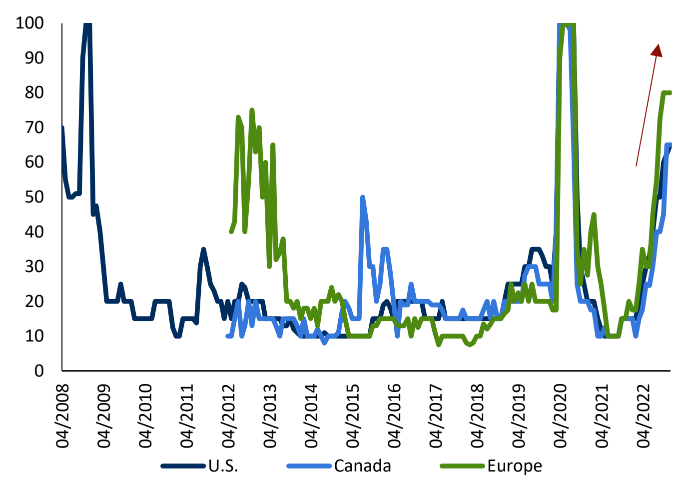
But similar to the seventh inning stretch, which marks the 80 per cent-point of a baseball game, we believe several economic and market indicators suggest today that most of this economic expansion cycle is behind us. This is perhaps why most strategists and economists are suggesting a recession will begin at some point in 2023. While we are in agreement that a recession is likely ahead for several advanced economies including Canada, the U.S. and the U.K. in 2023 or early 2024, we believe it will come down to the bottom of the ninth inning in terms of the black swan event that will eventually push the global economy into a slowdown.

What we can say with a high degree of certainty is that the U.S. Federal Reserve (Fed) along with its global central bank peers including the Bank of Canada (BoC), have aggressively and in a coordinated manner removed stimulus at a record pace to fight inflationary pressures to prevent those pressures from being entrenched in society. While this was necessary to avoid a repeat of the runway inflation and double-dip episode of the 1970s/'80s, we believe that in 2023, investors will begin to feel the "real" impacts of all the policy tightening completed in 2022. Interest rates are a powerful tool and arguably one of only a few tools that global central bankers have at their disposal to help stimulate and/or, in this case, slow down their respective economies.

As we sit here in early January and comb through all the data, we can confidently say that global economic growth has substantially weakened from the highs of 2021, which was expected as a result of all the policy tightening efforts. However, since policy changes typically work with a delay (approx. 12-18 months) in terms of the full impact on the real economy, we believe that there is a possibility that the sheer magnitude and pace of tightening over the past 10 months could result in current consensus expectations falling further before they trough and begin to improve.

Real GDP Growth Faces Mounting Headwinds [LHS]; Probability of a Recession in 2023 Continues to Rise [RHS]

5-Jan-23	Average 2000-2020	Real GDP Growth Forecasts 2021	2022	2023	2024
World	**3.2%**	**6.8%**	**2.2%**	**1.5%**	**3.7%**
Advanced Economies	**1.4%**	**5.3%**	**2.6%**	**-0.1%**	**1.1%**
US	***1.8%***	***5.9%***	***2.0%***	***0.3%***	***1.2%***
Canada	***1.8%***	***5.0%***	***3.5%***	***0.0%***	***2.3%***
Euro	1.0%	5.3%	3.3%	-0.5%	1.0%
UK	1.2%	7.6%	4.1%	-1.5%	1.2%
Japan	0.6%	2.2%	1.2%	0.5%	0.7%
Australia	2.6%	5.2%	3.6%	1.0%	1.1%
Emerging Economies	**4.7%**	**7.8%**	**2.0%**	**2.4%**	**5.2%**
Emerging Asia	6.1%	8.8%	1.5%	3.3%	6.5%
China	7.3%	8.4%	2.5%	3.0%	6.5%
India	6.4%	8.3%	6.8%	6.0%	5.8%
Russia	3.6%	4.7%	-2.5%	-2.3%	1.8%
Brazil	2.1%	5.0%	3.0%	1.0%	1.5%
Mexico	1.6%	4.7%	3.0%	0.8%	1.8%



Source: Capital Economics; FactSet; Bloomberg; Raymond James Ltd.; Data as of December 31, 2022.

Raymond James Ltd. – Recession Monitor Suggests We Are Getting Closer to the End of the Game

One of the commonly watched indicators of a possible recession on the horizon is the shape of sovereign yield curves for a particular region, which is currently inverted and near an extreme of 54 bps and 75 bps, respectively, in the U.S. and Canada. We note that while all of the past recessions have been preceded by a yield curve inversion, not all inversions have ended in a recession.

Given this, we opted to improve our batting average by leveraging a list of leading, coincident and lagging economic and market indicators, which over the past 20 years have correctly signalled a recession in the U.S. and Canada. Today, many of those indicators have deteriorated, with 67 per cent and 58 per cent of the indicators we monitor suggesting recessionary conditions are present in the U.S. and Canada, respectively.

U.S. & Canadian Economic & Market Indicators Continue to Weaken into Recessionary Territory

Indicator	Recession Signals	Dot-com Bubble (03/2001 - 11/2001)	Financial Crisis (12/2007 - 06/2009)	COVID-19 Pandemic (02/2020 - 04/2020)	Year End - 2021 U.S. & Canada	Current (U.S.)	Current (Canada)
Leading Indicators							
10yr-2yr Spread	10yr-2yr yield curve has inverted prior to every recession (i.e., the spread has turned negative)	✓	✓	✓	✗	✓	✓
Leading Economic Index (LEI)	The YoY change in the LEI has turned negative prior to every recession	✓	✓	✓	✗	✓	N/A
Consumer Confidence Index	Consumer confidence has collapsed before every recession in the U.S., & similarly prior to most recessions in Canada	✓	✓	✓	✓	✓	✓
Initial Claims for Unemployment Insurance	The number of initial claims typically reaches an inflection point (i.e., troughs) and begins to rise prior to a recession	✓	✓	✓	✗	✗	✗
Purchasing Manager Index (PMI)	PMIs, which measure the level of economic activity of the economy tends to fall below 50 into a contraction territory before a recession (> 50 = expansion; < 50 = contraction)	✓	✓	✓	✗	✓	✓
Coincident Indicators							
Real GDP Growth	Real GDP growth has declined for at least two consecutive periods (QoQ/MoM) during every recession	✓	✓	✓	✗	✗	✗
Disposable Personal Income	The U.S. disposable income level tends to decline prior to entering a recession and falls further during a recession	✓	✓	✓	✗	✓	✗
Savings Rates	Savings rates tend to decrease prior to a recession and increase during a recession	✓	✓	✓	✓	✓	✓
Lagging Indicators							
CPI	Inflation typically peaks before/during a recession	✓	✓	✓	✗	✓	✓
Financial Conditions Index	Financial conditions tend to tighten aggressively and reach a peak prior to a recession	✓	✓	✓	✓	✓	✓
Corporate Profits	The YoY growth in profits typically turns negative prior to every recession	✓	✓	✓	✗	✗	✗
Unemployment Rate	The unemployment rate signals a recession when the 3-month moving average rises 0.5% or more versus the prior 12-month low	✓	✓	✓	✗	✗	✗

Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

Interest Rates Set To Move to 3rd Base in 2023. Then What?

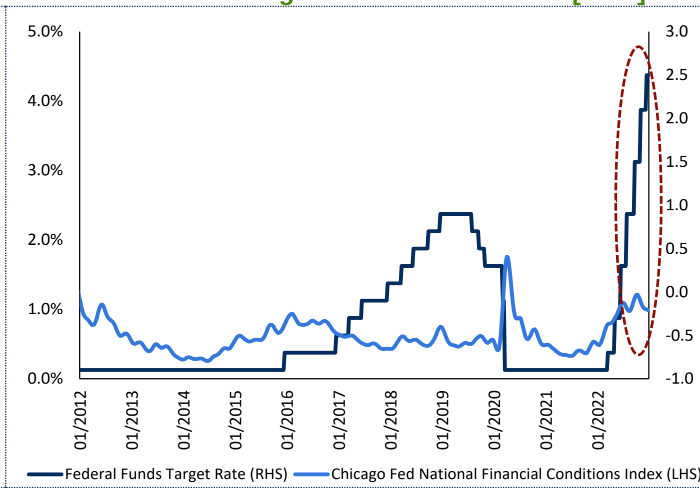
Last week, we read through the release of the minutes from the December Federal Open Market Committee (FOMC) meeting, which showed that the committee was concerned about “an unwarranted easing in financial conditions” that “would complicate the Committee’s effort to restore price stability”, especially if the easing in financial conditions came from investors not understanding how the Fed is prepared to respond (our interpretation). As we demonstrate below, the Financial Conditions Index moved higher (tighter financial conditions) ahead of, and alongside, the Fed’s tightening regime and has been moving lower of late.

Financial conditions remain fairly easy as they are below zero. According to the Chicago Fed, they are influenced by money markets, debt and equity markets as well as the traditional and “shadow” banking systems. The discounting of a continued economic slowdown by financial markets that would lead to an eventual rate cut is probably the biggest contributor to the “unwarranted easing of financial conditions” the Fed mentioned. So, the Fed is telling the markets to cool it for now. To confirm that signal, Kansas City Fed President Esther George said the release raised her “forecast over 5%” well into 2024 and that she sees “staying there for some time, again, until we get the signals that inflation is really convincingly starting to fall back toward our 2% goal”. On the other hand, Atlanta Fed President Raphael Bostic said that inflation is “way too high” and “there is still much work to do”. Minneapolis Fed President Neel Kashkari indicated he expects the Fed “pausing at 5.40%, but wherever that end point is, we won't immediately know if it is high enough to bring inflation down to 2% in a reasonable period of time". A move to 5.40 per cent would be two more hikes in 2023 than the market has currently priced in.

BoC Governor Tiff Macklem in his final public appearance of 2022 re-emphasized that getting inflation back to the two per cent target (down from 8.1 per cent as of June 2022) was the bank’s main goal. Moreover, he noted that the world looked a lot different now than it did during the past 30 years. Greater geopolitical tensions and a backlash in some areas against globalization will make it harder to bring inflation down and keep it there. But similar to the recent comments from the FOMC committee, the objective for the bank was crystal clear in that while a recession is a near-term risk, persistently high inflation expectations from households and businesses were an even greater risk. These comments followed the bank’s decision to hike rates for the seventh time in 2022, this time by 50 bps to 4.25 per cent, while continuing its policy of quantitative tightening.

Policy Rate Forecasts [LHS]; Divergence between a Hawkish Fed & Loosening Financial Conditions [RHS]

5-Jan-23	Interest Rate Forecasts			
	Current	2022	2023	2024
Advanced Economies				
US	4.50%	4.38%	4.13%	2.88%
Canada	4.25%	4.25%	3.25%	2.50%
Euro	2.50%	2.00%	3.00%	2.50%
UK	3.50%	3.50%	4.50%	3.00%
Japan	-0.10%	-0.10%	-0.10%	-0.10%
Australia	3.10%	3.10%	3.60%	3.10%
Emerging Economies				
China	3.65%	2.00%	1.80%	1.80%
India	6.25%	6.25%	6.40%	6.40%
Russia	7.50%	7.50%	7.00%	6.50%
Brazil	13.75%	13.75%	11.00%	7.50%



Source: Capital Economics; Bloomberg; Raymond James Ltd.; Raymond James Financial; Data as of December 31, 2022.

U.S. Economic Outlook: From Easy Policy to Aggressive Tightening

What a difference a year can make! From living in a world with global synchronized monetary easing just a year ago to ending 2022 with most central banks tightening their monetary policies at unprecedented speeds. The Fed raised rates by 425 bps in less than a year, and despite that, the U.S. economy remained strong. But it's likely to moderate as the impact of the tightening influences the real economy. On the other hand, the U.S. labour market continues to be strong and beat expectations, adding an average of 329,000 jobs per month in 2022, which historically is a very strong number. Barring unexpected external shocks, inflation is on a clear disinflationary trajectory, and we expect it to continue on this path as shelter costs are likely to start declining in the upcoming quarters. Despite the current resilience of the U.S. economy and our expectations that inflation will continue to decline through next year, we expect the restrictive stance of monetary policy to push the economy into a mild recession, with three quarters of negative growth starting in the second quarter followed by a weak recovery in 2024. We expect 0.0 per cent growth in 2023 and a modest 0.8 per cent upturn in 2024.

A Pulse Check on the U.S. Economy

Economic Indicator	Status	Comments
Growth	Neutral	GDP growth is expected to continue to moderate in the 1Q23, and to enter negative territory over the following three quarters.
Employment	Neutral	Nonfarm payrolls have slowed but are still very strong. Expectations are for nonfarm payrolls to weaken in 2023 while the unemployment rate increases.
Consumer Spending	Neutral	Despite inflation trending lower, prices remain elevated, and as excess savings from the pandemic continue to dwindle, consumer spending is likely to weaken next year.
Business Investment	Neutral	Interest rates will continue to negatively impact the strength of business investment in 2023.
Manufacturing	Concerning	Manufacturing was supported by strong export demand in 2022, but it has started to decline over the last few months, and we expect this trend to continue in 2023.
Housing and Residential Construction	Concerning	The housing market is and will remain in recession as the strong increase in mortgage rates impacts affordability. We should continue to see weaker housing and further declines in home prices.
Inflation	Neutral	Inflation remains the biggest risk for the economic outlook, but, barring any external shock (such as energy prices increasing again), we believe the worst is behind us and we should see inflation below 3% by the end of 2023.
Monetary Policy	Concerning	The Fed has slowed the pace of rate increases, and we believe they'll slow it further in the first half of 2023. However, we estimate the terminal rate at 5%, and this restrictive level is likely to lead to a recession in 2023.
Long-Term Interest Rates	Neutral	The yield curve ended the year near its deepest inversion in over four decades, but bond yields have retracted considerably since their highs. We expect long-term interest rates to decline further, especially towards the end of the year or in 2024 as the curve will likely remain inverted until the Fed pivots to an easier monetary policy stance.
Fiscal Policy	Neutral	Contributions to GDP from government spending next year are unlikely to change significantly as it is improbable that with next year's gridlock scenario in Washington, Congress will be able to agree on items that will expand spending.
The Dollar	Neutral	The US dollar should remain strong relative to other currencies as the Fed maintains its hawkish stance and the global economy falls into recession. However, the US dollar has weakened recently, and should weaken further if and when the Fed pivots to an easier policy setting.
Rest of the World	Neutral	The ongoing conflict in Ukraine continues to have a bigger impact on Europe's economy than on the US. Lower energy prices have eased concerns about the immediate future, but risks remain high.

Source: Raymond James Financial; Raymond James Ltd.; Data as of December 31, 2022.

Almost all petroleum forecasts we have seen lately predict oil prices would go back to $100 or higher. It is clear that the Fed is trying to be ahead of the curve in case this forecast comes to fruition and pushes inflation higher once again.

We can see in the heat map below the different inflation paths and the time we need for the Fed to attain the 2.0 per cent inflation target going forward. Remember that these are very simple scenarios that assume that inflation changes at a constant rate per month in order to observe what would happen to the year-over-year rate of inflation for both the consumer price index (CPI) and the personal consumption expenditures (PCE) price index, which is the favoured inflation number targeted by the Fed.

By looking at this “inflation heat map”, we clearly see that what markets are expecting – for the Fed to pivot before the end of 2023 – is akin to expecting several monthly deflationary (i.e., negative rates of inflation) readings for both the CPI and the PCE price index. Although this is not impossible, it is very unlikely, as things stand today. And the reason has to do with, as we indicated above, the possibility for oil prices to, once again, cross the $100 per barrel threshold.

Markets Are Expecting the Fed to Pivot before the End of 2023

Year-Over-Year CPI Percentage Change	Month-Over-Month CPI Percentage Change							
	-0.1%	0.0%	0.1%	0.2%	0.3%	0.4%	0.5%	0.6%
Nov-22	7.1%	7.1%	7.1%	7.1%	7.1%	7.1%	7.1%	7.1%
Dec-22	6.4%	6.5%	6.6%	6.7%	6.8%	6.9%	7.0%	7.1%
Jan-23	5.6%	5.8%	6.0%	6.2%	6.5%	6.7%	6.9%	7.1%
Feb-23	4.7%	5.0%	5.3%	5.6%	5.9%	6.3%	6.6%	6.9%
Mar-23	3.3%	3.7%	4.1%	4.5%	4.9%	5.4%	5.8%	6.2%
Apr-23	2.8%	3.4%	3.9%	4.4%	4.9%	5.4%	6.0%	6.5%
May-23	1.7%	2.4%	3.0%	3.6%	4.2%	4.8%	5.5%	6.1%
Jun-23	0.3%	1.0%	1.7%	2.4%	3.2%	3.9%	4.6%	5.3%
Jul-23	0.2%	1.0%	1.9%	2.7%	3.5%	4.3%	5.2%	5.9%
Aug-23	-0.4%	0.5%	1.4%	2.4%	3.3%	4.2%	5.2%	6.1%
Sep-23	-0.9%	0.1%	1.1%	2.1%	3.1%	4.2%	5.2%	6.3%
Oct-23	-1.1%	0.0%	1.1%	2.2%	3.3%	4.5%	5.6%	6.8%
Nov-23	-1.1%	0.0%	1.1%	2.2%	3.3%	4.5%	5.6%	6.8%
Dec-23	-1.1%	0.0%	1.1%	2.2%	3.3%	4.5%	5.6%	6.8%

Year-Over-Year PCE Percentage Change	Month-Over-Month PCE Percentage Change							
	-0.1%	0.0%	0.1%	0.2%	0.3%	0.4%	0.5%	0.6%
Nov-22	6.1%	6.1%	6.1%	6.1%	6.1%	6.1%	6.1%	6.1%
Dec-22	5.4%	5.5%	5.6%	5.7%	5.8%	5.9%	6.0%	6.1%
Jan-23	4.7%	4.9%	5.1%	5.3%	5.5%	5.7%	6.0%	6.2%
Feb-23	4.0%	4.4%	4.7%	5.0%	5.3%	5.6%	5.9%	6.2%
Mar-23	3.3%	3.7%	4.2%	4.6%	5.0%	5.4%	5.8%	6.2%
Apr-23	2.2%	2.8%	3.3%	3.8%	4.3%	4.8%	5.4%	5.9%
May-23	1.9%	2.6%	3.2%	3.8%	4.4%	5.0%	5.7%	6.3%
Jun-23	1.2%	1.9%	2.7%	3.4%	4.1%	4.8%	5.6%	6.3%
Jul-23	0.1%	0.9%	1.7%	2.6%	3.4%	4.2%	5.0%	5.9%
Aug-23	0.2%	1.1%	2.0%	2.9%	3.8%	4.8%	5.7%	6.6%
Sep-23	-0.2%	0.8%	1.8%	2.8%	3.9%	4.9%	5.9%	7.0%
Oct-23	-0.6%	0.5%	1.6%	2.7%	3.8%	5.0%	6.1%	7.3%
Nov-23	-1.2%	0.0%	1.2%	2.4%	3.7%	4.9%	6.2%	7.4%
Dec-23	-1.2%	0.0%	1.2%	2.4%	3.7%	4.9%	6.2%	7.4%

Source: Raymond James Financial; Raymond James Ltd.

Washington Policy: Regulatory Action, China Policy and an Early Look at 2024

We view the 2022 midterm election outcome as a positive result for the markets, with Democrats exceeding expectations and expanding their Senate majority by one vote (51-49) and Republicans capturing a nine-seat House majority – a pick-up below historical averages. The markets have historically favoured split government as it reduces the policy uncertainty coming from D.C. and produces an incentive to pass bipartisan legislation on compromise issues.

However, there is also a high likelihood of gridlock and elevated headline risk around must-pass legislation. The Democrats’ 51-seat Senate majority will boost their ability to confirm officials for key regulatory/judicial posts and tilt committee assignments in their favour. However, losing the House means the vote margin given any pursuit of reconciliation legislation will be off the table. In the House, the GOP will govern with a slim 222-seat majority, which will prove challenging for the Speaker of the House in gathering support for bills – especially as the small majority could give individual lawmakers significant leverage or stalling ability in negotiations.

Turning attention to the 2023 agenda, we would focus on three things: must-pass legislation, potential areas of bipartisan compromise and Senate confirmations (which have a significant impact on President Biden's regulatory agenda). We will also be monitoring external factors, especially the increased attention on geopolitical risk, the Fed's monetary policy decisions and the 2024 presidential election. We expect a "tough on China" bill to lead the list of potential bipartisan compromises.

The debt ceiling is primed to be one of the most contentious must-pass issues facing the new Congress in 2023, with Republicans poised to take a hard line in negotiations in exchange for Democrats' concessions on social spending and entitlements. While this may cause a period of headline risk for markets, we ultimately expect Congress will settle on a compromise solution to avert a debt ceiling breach that threatens the credit rating of U.S. government securities.

China will also be a prominent issue and serve as a key area for bipartisan compromise with a slight tilt toward more hawkish policy decisions. Years of escalating tensions have raised market concern, but recent signals point to a flattening of the escalation potential that raises the possibility of constructive progress – though we caution that the political setup in both countries will continue to support frictions in 2023. Anti-trust, cryptocurrency and oversight will likely also feature as core themes in 2023. We expect that Ukraine-related policy and spending will continue to enjoy bipartisan support, but "noise" should be expected from certain political factions. Similarly, tech-related anti-trust policy has overall bipartisan backing, but specifics on content moderation and consumer protection will be where fracture lines and legislative delays may emerge. Cryptocurrency will see heightened legislative attention following the ongoing fallout around FTX.

Given the gridlock in the new Congress, supercharged regulatory actions should be expected as a key mechanism to advance the priorities of the Biden administration in areas such as financial regulation, consumer protection, labour as well as climate and competition policy. However, recent judicial trends that have acted as a check on regulatory power will likely dampen the ultimate impact of any new rules.

Eyes in D.C. have already turned to the 2024 presidential election, with several prominent names in the running to lead both parties in what will likely be competitive primaries. However, at this stage, it is hard to accurately predict who will emerge as a front-runner, and we would caution that conventional wisdom regarding potential presidential candidates shortly post-midterm is often wrong.

Canadian Economic Outlook: Base Case is a Mild Recession

Click for Full Report

Following a strong economic showing in 2022, real GDP growth is expected to grind to a halt in 2023 and show no growth as the economy enters a mild recession. Higher rates will continue to weigh on domestic demand, while exports (e.g., crude) likely contract amid a broader and global slowdown.

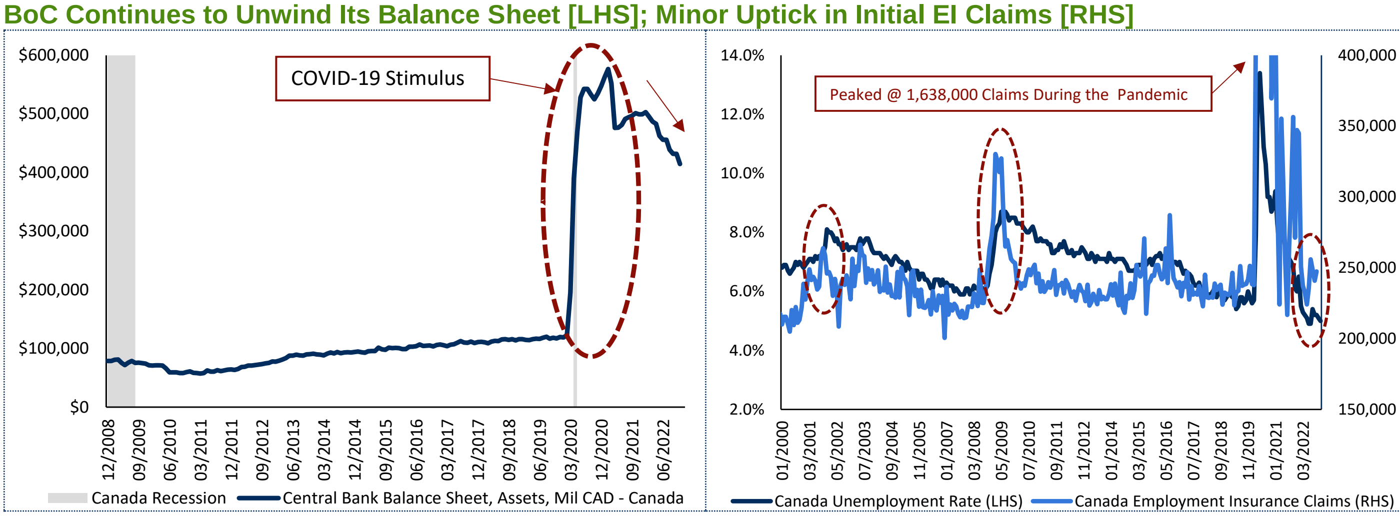
Overnight rates have already risen by 4.0 per cent in the past 10 months, the fastest pace in 26 years, while the BoC has continued to unwind its balance sheet – the BoC reduced its bond holdings by ~$85 billion since January 2022 – also known as quantitative tightening.

However, with inflation still running above the BoC's target of two per cent, with the latest reading of headline and core CPI for November rising by 6.8 per cent and 5.4 per cent YoY, respectively, rates could move higher by an additional 50-75 bps in H1/2023. This will effectively take overnight rates to 4.50-5.00 per cent even though we are seeing clear signs that inflationary impulses are cooling rather quickly. As mentioned above, depending on the fallout from the recession, including the impacts on the still tight labour markets, rates may either stay higher for longer, or we may see cuts as the economy moves into a recession, and inflation cools, barring unexpected external shocks (e.g., Russian invasion of Ukraine).

What is quite evident today is that higher rates are already weighing on domestic demand, including interest rate-sensitive parts of the Canadian economy such as housing. After more than two decades of falling interest rates, the popularity of variable rate borrowing has risen and has left households vulnerable to higher borrowing costs and, as a result, interest rate shocks on par with those of the 1980s and mid 2000s. Signs of these higher-cost pressures are already evident with residential spending declining in Q3 of 2022 along with the consumer confidence index, which is hovering at a recession lows.

The silver lining amid what appears to be a deteriorating economic backdrop remains the strength in the labour markets - the Canadian unemployment rate is at a record low of 5.1 per cent. However, we note that should labour markets weaken more substantially than what we currently expect – unemployment rising to the mid-6.0 per cent-levels under a mild recession scenario – the downside could get ugly given the level of debt among Canadian households.

BoC Continues to Unwind Its Balance Sheet [LHS]; Minor Uptick in Initial EI Claims [RHS]



Source: FactSet; Raymond James Ltd.; Raymond James Financial; Bank of Canada balance sheet asset as of November 30, 2022. Canada unemployment rate as of December 31, 2022. Canada employment insurance claims as of October 31, 2022.

Global Equities: Risks? Yes, but Compelling Rewards

Major global equity markets have put up a mixed showing in 2022 as headwinds for some markets have resulted in tailwinds for others. Large-cap, blue-chip and value-oriented indices globally (e.g., FTSE 100, Nikkei 225, S&P/TSX Composite, etc.) outperformed their more growth-oriented and expensive peers (e.g., Nasdaq 100, S&P 500, etc.) as interest rates have risen from record lows this year.

As a reminder, asset prices (including the price of equities, bonds, housing, art, antiques, crypto, etc.) typically fall as rates rise. The exception has been the MSCI China Index, which is being hit by several headwinds, not to mention zero-COVID-19 policies for most of 2022, which have since ended.

For 2023, despite the weakening and rather uncertain outlook, we see good value across the global equity complex where stocks have rerated and reflect a lot of the risks on the horizon. Across North American equities, Canadian equities broadly speaking (i.e., the S&P/TSX 60 and S&P/TSX Composite) still look attractive, while in the U.S., we see a more compelling risk/reward profile for U.S. mid- and small-caps (i.e., S&P Mid Cap 400 and S&P Small Cap 600) versus large caps (S&P 500). Outside of North America, we are increasingly more positive on markets across the Europe, Australasia and the Middle East region (i.e., MSCI EAFE), and we are becoming more constructive on Emerging Markets following a difficult 2022, especially as China does away with its unsuccessful zero-COVID policy.

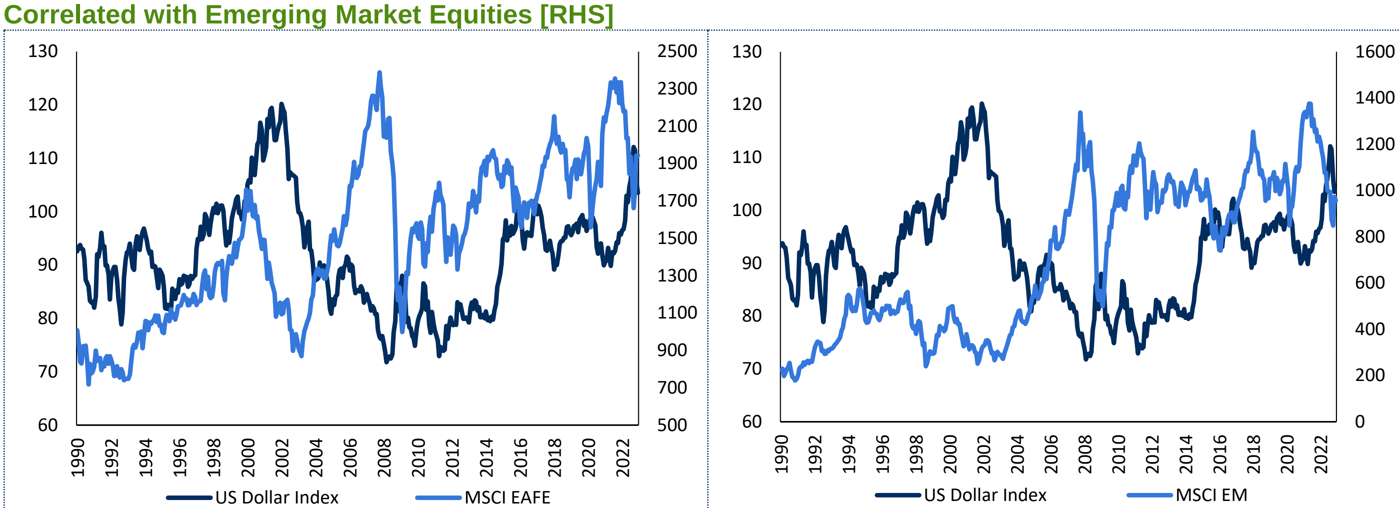
Despite the Uncertainty, We See a Compelling Risk/Reward for Global Equities

Equities	3Mo (in USD)	3 Mo (in CAD)	YTD (in USD)	YTD (in CAD)	Current PE NTM	Historical PE Median (Since 2000)	Premium (RED) / Discount (GREEN)
Canada							
MSCI Canada Value (Canada)	2.1	1.0	-5.3	1.6	9.7	12.3	-2.6
S&P/TSX Composite (Canada)	2.6	1.6	-12.2	-5.8	12.3	14.6	-2.3
S&P/TSX 60 (Canada)	2.4	1.4	-12.6	-6.2	12.2	14.4	-2.1
S&P/TSX Small Cap (Canada)	4.1	3.0	-15.4	-9.3	12.1	16.9	-4.8
MSCI Canada Growth (Canada)	3.7	2.6	-19.8	-14.0	17.9	18.0	-0.1
U.S.							
S&P Composite 1500 Value (U.S.)	7.5	5.8	-5.5	-0.9	15.1	13.9	1.2
S&P Mid Cap 400 (U.S.)	4.1	3.1	-13.1	-6.7	12.8	13.7	-0.9
S&P Small Cap 600 (U.S.)	3.1	2.1	-16.1	-10.0	12.3	15.8	-3.6
S&P Composite 1500 (U.S.)	2.1	1.0	-17.8	-11.8	16.3	15.7	0.6
S&P 500 (U.S.)	1.9	0.9	-18.1	-12.2	16.7	15.9	0.8
S&P Composite 1500 Growth (U.S.)	-3.5	-4.7	-28.7	-24.2	17.7	18.5	-0.8
NASDAQ Composite (U.S.)	-5.9	-6.9	-32.5	-27.6	22.4	22.1	0.2
Europe							
FTSE 100 (U.K.)	13.0	11.9	-10.4	-3.9	9.9	12.5	-2.6
CAC 40 (France)	17.4	16.2	-12.4	-6.1	12.1	13.3	-1.2
Euro STOXX 50 (Europe)	19.2	17.9	-17.2	-11.2	12.0	13.3	-1.3
DAX (Germany)	20.5	19.2	-17.4	-12.5	11.4	12.8	-1.5
Asia Pacific							
Hang Seng (Hong Kong)	10.2	9.0	-12.6	-6.3	9.6	12.1	-2.5
Nikkei 225 (Japan)	5.8	4.7	-19.1	-14.3	14.7	16.4	-1.8
MSCI China (China)	8.5	7.4	-21.8	-16.1	10.7	10.9	-0.1
Major Aggregates							
MSCI EAFE (Developed Markets ex U.S. & Canada)	13.0	11.9	-14.0	-7.8	12.1	13.6	-1.5
MSCI World (Global)	4.5	3.5	-17.7	-11.8	15.0	15.6	-0.6
MSCI EM (Emerging Markets)	5.7	4.6	-19.7	-13.9	11.6	11.6	0.0

Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

Our constructive view on global equities (excluding North American equities) is primarily based on relative valuations and on our expectation that we are past the peak of USD strength/Fed-hawkisness. We expect the U.S. dollar to weaken as China re-opens, and for developed and emerging equity markets outside the U.S. to modestly outperform, especially later in the year as China's re-opening becomes more impactful.

USD Negatively Correlated with Developed Market Equities (ex. U.S. and Canada) [LHS]; USD Negatively Correlated with Emerging Market Equities [RHS]



Source: FactSet; Bloomberg; Raymond James Ltd.; Data as of December 31, 2022.

10 Year Correlation Matrix – USD, Yen, Yuan, CAD, Negatively Correlated with Developed and Emerging Equity Market Indices

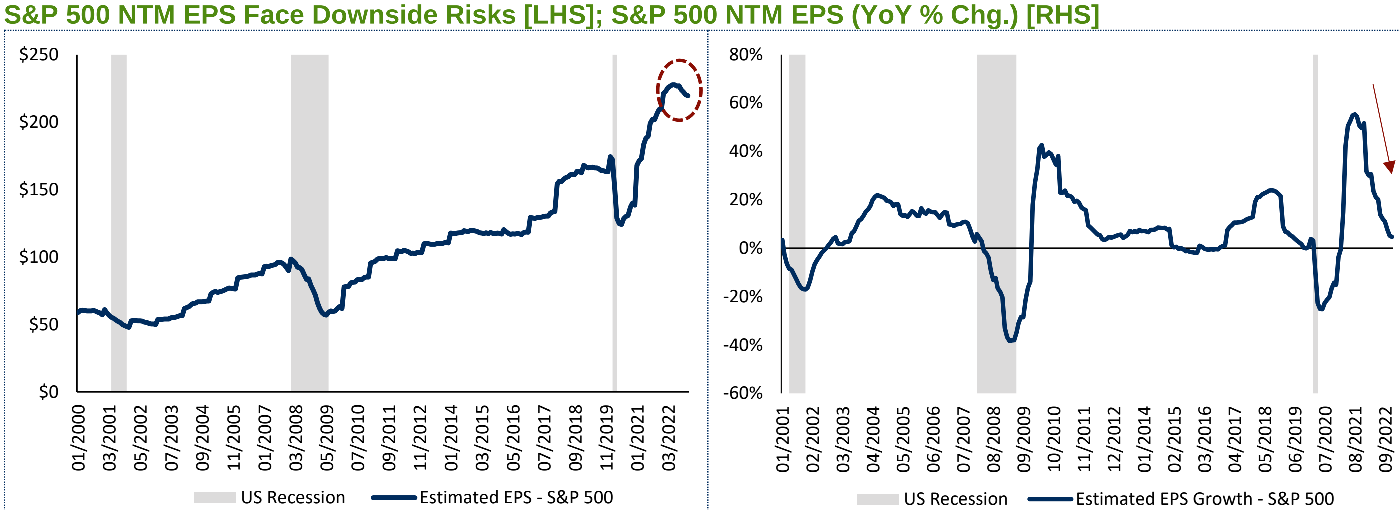
	U.S. Dollar	Japanese Yen	British Pound	Euro	Chinese Yuan	Canadian Dollar	MSCI EM*	MSCI EAFE**	Hang Seng***
U.S. Dollar	1.00	0.57	-0.73	-0.96	0.39	0.57	-0.32	-0.43	-0.21
Japanese Yen	0.57	1.00	-0.26	-0.44	0.22	0.20	-0.03	0.00	0.04
British Pound	-0.73	-0.26	1.00	0.61	-0.37	-0.49	0.38	0.52	0.27
Euro	-0.96	-0.44	0.61	1.00	-0.33	-0.46	0.24	0.36	0.17
Chinese Yuan	0.39	0.22	-0.37	-0.33	1.00	0.34	-0.41	-0.32	-0.39
Canadian Dollar	0.57	0.20	-0.49	-0.46	0.34	1.00	-0.51	-0.53	-0.35
MSCI EM*	-0.32	-0.03	0.38	0.24	-0.41	-0.51	1.00	0.78	0.86
MSCI EAFE**	-0.43	0.00	0.52	0.36	-0.32	-0.53	0.78	1.00	0.62
Hang Seng***	-0.21	0.04	0.27	0.17	-0.39	-0.35	0.86	0.62	1.00

Source: Bloomberg; FactSet; Raymond James Ltd.; Data as of December 31, 2022. *MSCI Emerging Markets; **MSCI Developed Markets ex U.S. and Canada; ***Hong Kong stock market.

U.S. Equities – Avoid Stealing Bases in 2023

In 2022, we have got used to a world where consumer demand in the economy was resilient (8-9 per cent nominal consumer spending growth most of the year), while inflation, unfortunately, was also resilient and only showing modest improvement after peaking in the summer. The good news for the year was that corporate EPS was resilient as well, with EPS for the S&P 500 in 2022 likely coming in around ~$218, only down slightly from where consensus EPS stood at the beginning of the year ($222) despite the twin disruptions of the Russian war with Ukraine and material lockdowns in China. Both the war and China's lockdowns likely increased the peak of inflation and delayed it into the summer. As well, they likely made the decline frustratingly slow so far, with inflation only improving from a peak of ~9 per cent in June to ~7 per cent at year end.

S&P 500 NTM EPS Face Downside Risks [LHS]; S&P 500 NTM EPS (YoY % Chg.) [RHS]



Source: FactSet; Bloomberg; Raymond James Ltd.; Data as of December 31, 2022.

Our view for 2023 is that it will likely also be a volatile year for equities, but for the exact opposite reasons compared to 2022. We expect inflation to moderate substantially through

2023. Consumer demand should slow substantially as savings rates, which are currently historically low, revert closer to normal levels, forcing consumers to slow their spending. On top of this, rates increase, student loan payments resume, COVID benefits continue to taper and the labour market should soften. The headwinds to consumer spending are substantial entering 2023. At the same time, supply chains appear to be improving, and we suspect this should continue through 2023 and 2024, creating increases in aggregate supply while slowing aggregate demand meaningfully. This combination of slowing demand and rising supply should allow inflation to ease meaningfully and long-term rates to decline from current levels, which should cause P/Es to move modestly higher on equity indexes.

S&P 500 2022 Drawdown in NTM EPS vs. Historical Recessions (Peak to Trough)

Index/Sector	Dot-Com Bubble	Financial Crisis	COVID-19	Average	2022 Sell-off	Difference	1-mo rev to EPS NTM	3-mo rev to EPS NTM
S&P 500	-15%	-36%	-21%	-24%	-4%	20%	-0.6%	-3.0%
Communication Services	--	-18%	-17%	-18%	-12%	5%	1.4%	0.3%
Consumer Discretionary	-37%	-41%	-43%	-40%	-1%	39%	0.9%	5.6%
Consumer Staples	5%	-2%	-6%	-1%	-1%	0%	0.0%	-1.4%
Energy	-6%	-64%	-93%	-54%	6%	60%	-13.3%	-42.1%
Financials	5%	-60%	-32%	-29%	2%	31%	1.7%	7.1%
Health Care	9%	0%	-5%	2%	-5%	-7%	-0.9%	-4.2%
Industrials	-1%	-38%	-41%	-26%	0%	26%	-1.1%	-6.2%
Information Technology	-58%	-25%	-3%	-29%	-8%	20%	-0.5%	-3.7%
Materials	-42%	-55%	-23%	-40%	-19%	21%	-1.1%	-7.2%
Real Estate	--	-43%	-9%	-26%	-1%	25%	-1.2%	-5.4%
Utilities	-7%	-8%	0%	-5%	3%	8%	1.0%	1.7%

Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

However, as that moderation in inflation occurs, we suspect S&P 500 consensus EPS expectations for 2023 – which have already declined from ~$250 in June to ~$230 today – will slip further as the economy slows and labour market conditions soften, down to the ~$200-$220 range for the next two years, which is our current estimate.

S&P 500 2023 EPS Sensitivity Analysis

EBIT Margin \ Sales Growth	5.0%	4.0%	3.0%	2.0%	1.0%	0.0%	-1.0%	-2.0%	-3.0%	-4.0%	-5.0%	-6.0%
17.90%	249	246	243	240	237	234	231	228	225	222	219	216
17.70%	246	243	240	237	234	231	228	225	222	219	216	213
17.50%	243	240	237	234	231	228	225	222	219	216	213	210
17.30%	240	237	234	231	228	225	222	219	216	213	210	207
17.10%	237	234	231	228	225	222	219	216	213	210	207	204
16.90%	234	231	228	225	222	219	216	213	210	207	204	201
16.70%	231	228	225	222	219	216	213	210	207	204	201	198
16.50%	228	225	222	219	216	213	210	207	204	201	198	195
16.30%	225	222	219	216	213	210	207	204	201	198	195	192
16.10%	222	219	216	213	210	207	204	201	198	195	192	189
15.90%	219	216	213	210	207	204	201	198	195	192	189	186
15.70%	216	213	210	207	204	201	198	195	192	189	186	183
15.50%	213	210	207	204	201	198	195	192	189	186	183	180

2023 Consensus EPS Estimate In 6/2022

2023 Consensus EPS Estimate Today

2022 Consensus EPS Estimate

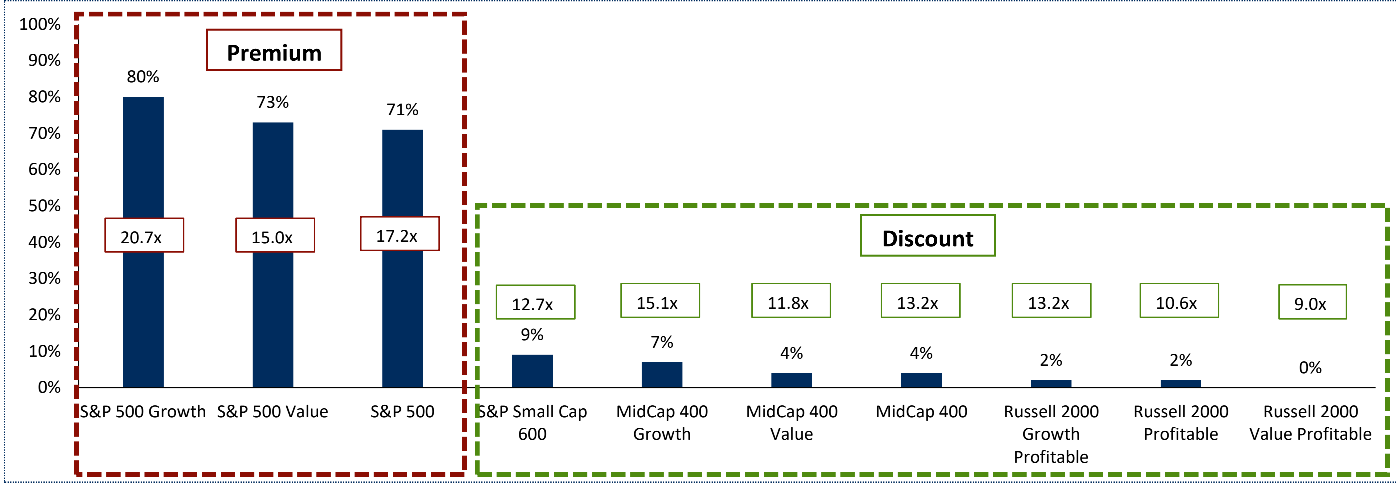
Mid Recession Scenario

Severe Recession Scenario

Source: Raymond James research; Raymond James Ltd.

Economists argue whether this will be a soft landing, slight recession or meaningful recession. But the outcome, in any case, is likely an economic slowdown with a negative impact on corporate profitability. We expect the "soft-ish" economic conditions to likely persist into 2024 due to the lagged impact of higher Fed rates, which will likely cap some of the benefit from higher P/Es in 2023. We find ourselves squarely in a late cycle economy right now with the Fed actively trying to soften conditions, which will ultimately lead to lower inflation, lower rates and lower earnings expectations. Against this backdrop, we expect a reasonably flattish S&P 500 and slightly better small/mid-cap performance due to lower P/Es. We do not expect a material difference in performance between growth and value over the full year, but we would expect the first part of the year to favour value stocks and the back half of the year to favour growth stocks as long-term rates decline.

Index Level NTM P/E Relative to 20-Year Experience for Nine Style Boxes (R2K LTM Ex-Non-Earners)



Source: FactSet; Raymond James Ltd.; Raymond James & Associates; Data as of December 12, 2022.

From a sector perspective, real estate is our favourite one, followed by health care and staples, while we suspect consumer discretionary, industrials and financials will be the most challenging ones. That being said, those are full-year expectations, and we expect that at some point during the year the Fed will "pivot" and start messaging a potentially much lower rate outlook in 2024. When this occurs, we expect the market itself to "pivot" from the defensive sectors we favour currently to the more cyclical ones. For more details, please see our 2023 equity outlook (link to report).

S&P 500 2022 Drawdown in NTM P/E vs. Historical Recessions (Peak to Trough)

Index/Sector	Dot-Com Bubble	Financial Crisis	COVID-19	Average	2022 Sell-off	Difference	Current PE NTM	Historical PE (Since 2000)	Premium (+) / Discount (-)	YTD Return
S&P 500	-12.0	-6.7	-5.9	-8.2	-7.3	0.9	16.6	15.9	0.7	-18.1%
Communication Services	--	-9.4	-5.7	-7.6	-11.0	-3.5	14.6	17.9	-3.3	-39.9%
Consumer Discretionary	-7.6	-8.4	-7.0	-7.7	-26.8	-19.1	21.2	17.8	3.4	-37.0%
Consumer Staples	-1.9	-5.3	-4.7	-4.0	-1.1	2.9	20.7	18.0	2.7	-0.6%
Energy	-7.2	-4.8	7.4	-1.5	37.9	39.4	9.7	13.7	-4.0	65.7%
Financials	-7.2	-5.0	-5.6	-5.9	-2.7	3.2	12.0	12.4	-0.4	-10.5%
Health Care	-6.7	-7.4	-4.8	-6.3	0.5	6.8	17.5	16.1	1.4	-2.0%
Industrials	-9.2	-8.2	-6.6	-8.0	-9.3	-1.3	18.1	16.0	2.1	-5.5%
Information Technology	-40.4	-9.3	-7.3	-19.0	-8.7	10.3	19.6	17.8	1.7	-28.2%
Materials	1.4	-9.0	-6.5	-4.7	-7.2	-2.5	15.7	15.2	0.5	-12.3%
Real Estate	-1.0	-13.3	-8.1	-7.5	-4.5	2.9	16.4	18.1	-1.7	-26.1%
Utilities	-2.2	-6.3	-7.4	-5.3	0.9	6.2	18.5	14.7	3.8	1.6%

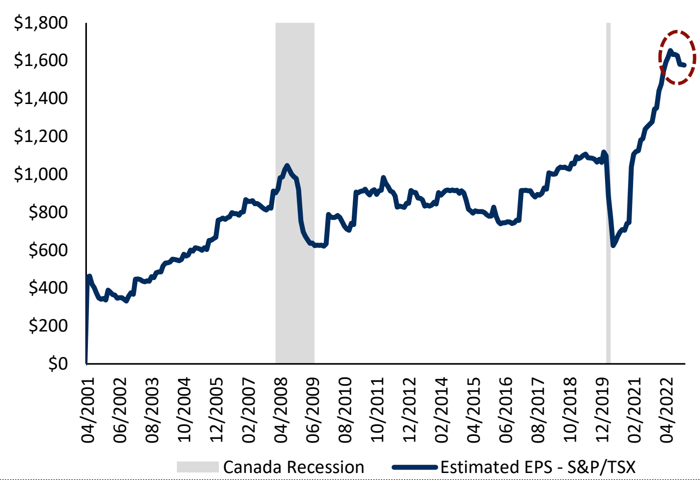
Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022. YTD returns are in USD.

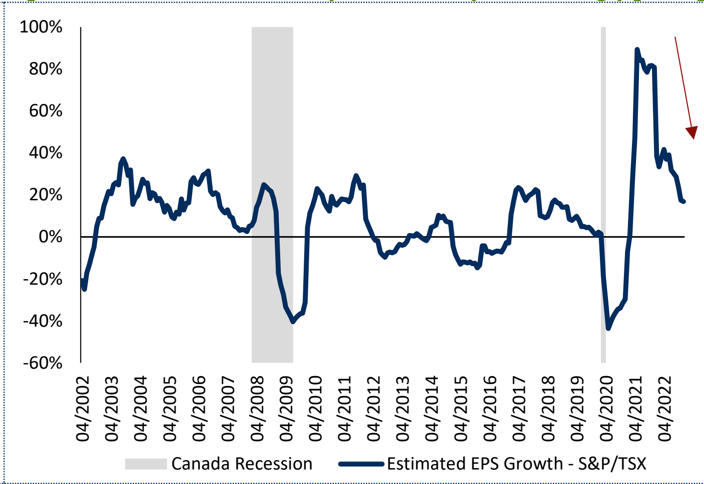
Canadian Equities – Raising Your Batting Average in 2023

On a relative basis, the S&P/TSX index has outperformed several U.S. broad markets along with many global markets in 2022 in Canadian dollar terms. Even if we exclude the impacts of the strong performance of the energy sector (18.1 per cent of the S&P/TSX Composite), which was up 30.3 per cent in 2022, the index would have posted a -11.3 per cent total return for the year, outperforming the S&P 500 index which fell 12.2 per cent in 2022.

However, as we look forward into 2023, while we continue to expect downside to earnings as we move further into the year, valuations are attractive on a historical and relative basis and have priced in a strong move in 10-year yields of +187 bps in 2022. We believe this sets up the index for a low-mid single-digit return year in 2023, especially as yields peak and move lower, while multiples expand slightly.

S&P/TSX Composite NTM EPS Face Downside Risks [LHS]; S&P/TSX NTM EPS Expectations (YoY% Chg.) [RHS]





Source: FactSet; Bloomberg; Raymond James Ltd.; Raymond James Financial; Data as of December 31, 2022.

While a recession in Canada is a likely outcome for 2023, we believe current EPS expectations for the year still remain too high. As we demonstrate below, earnings during the past two recessions have fallen by 36 per cent from the peak, while 2023 EPS expectations since the peak in 2022 have fallen only five per cent.

S&P/TSX Composite 2022 Drawdown in NTM EPS vs. Historical Recessions (Peak to Trough)

Index/Sector	Financial Crisis	COVID-19	Average	2022 Sell-off	Difference	1-mo rev to EPS NTM	3-mo rev to EPS NTM
S&P/TSX Composite	-38%	-33%	-36%	-5%	30%	-2.1%	-6.0%
Communication Services	-6%	-12%	-9%	0%	9%	-0.4%	-0.5%
Consumer Discretionary	-25%	-41%	-33%	-2%	31%	0.0%	-4.2%
Consumer Staples	1%	4%	2%	9%	7%	-0.2%	-0.1%
Energy	-60%	-107%	-84%	-9%	74%	-8.8%	-27.7%
Financials	-20%	-19%	-19%	1%	21%	0.1%	2.3%
Health Care	18%	-55%	-18%	-35%	-17%	45.0%	115.7%
Industrials	-21%	-39%	-30%	15%	45%	-3.4%	-5.1%
Information Technology	-5%	0%	-2%	-2%	1%	1.2%	5.5%
Materials	-52%	-2%	-27%	-25%	1%	-0.6%	-8.4%
Real Estate	--	-7%	-7%	-2%	4%	0.2%	-2.5%
Utilities	-15%	-4%	-10%	11%	21%	0.7%	2.9%

Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

As a moderation in inflation occurs, we suspect S&P/TSX Composite Index consensus EPS expectations for 2023, which have already declined from ~$1,670 in June to ~$1,580 today, will slip further as the economy slows and labour market conditions soften, down to ~$1,400 in 2023. This is in line with a mild recession scenario, which is our current expectations.

S&P/TSX Composite 2023 EPS Sensitivity Analysis

EBIT Margin \ Sales Growth	9.5%	8.5%	7.5%	6.5%	5.5%	4.5%	3.5%	2.5%	1.5%	0.5%	-0.5%	-1.5%
20.00%	1800	1760	1720	1680	1640	1600	1560	1520	1480	1440	1400	1360
19.50%	1760	1720	1680	1640	1600	1560	1520	1480	1440	1400	1360	1320
19.00%	1720	1680	1640	1600	1560	1520	1480	1440	1400	1360	1320	1280
18.50%	1680	1640	1600	1560	1520	1480	1440	1400	1360	1320	1280	1240
18.00%	1640	1600	1560	1520	1480	1440	1400	1360	1320	1280	1240	1200
17.50%	1600	1560	1520	1480	1440	1400	1360	1320	1280	1240	1200	1160
17.00%	1560	1520	1480	1440	1400	1360	1320	1280	1240	1200	1160	1120
16.50%	1520	1480	1440	1400	1360	1320	1280	1240	1200	1160	1120	1080
16.00%	1480	1440	1400	1360	1320	1280	1240	1200	1160	1120	1080	1040
15.50%	1440	1400	1360	1320	1280	1240	1200	1160	1120	1080	1040	1000
15.00%	1400	1360	1320	1280	1240	1200	1160	1120	1080	1040	1000	960
14.50%	1360	1320	1280	1240	1200	1160	1120	1080	1040	1000	960	920
14.00%	1320	1280	1240	1200	1160	1120	1080	1040	1000	960	920	880

2023 Consensus EPS Estimates In 6/2022

2023 Consensus EPS Estimates Today

Mid Recession Scenario

Severe Recession Scenario

Source: Raymond James research; Raymond James Ltd.

For the S&P/TSX Composite, we believe valuation for the broad market is attractive at 12.3x next 12 months earnings versus the 20-year median of 14.6x. Sectors that offer the most favourable risk/reward today include energy, materials (e.g., golds), real estate and consumer staples, while we see further downside risks either from valuation compression or from downside earning revisions for the information technology, industrials and utilities sectors.

S&P/TSX Composite 2022 Drawdown in NTM P/E vs. Historical Recessions (Peak to Trough)

Index/Sector	Financial Crisis	COVID-19	Average	2022 Sell-off	Difference	Current PE NTM	Historical PE (Since 2000)	Premium (Green) / Discount (Red)	YTD Return
S&P/TSX Composite	-8.4	-5.0	-6.7	-9.3	-2.6	12.4	14.6	-2.2	-5.8%
Communication Services	-7.2	-4.7	-5.9	-0.5	5.4	17.4	15.7	1.7	-2.6%
Consumer Discretionary	-7.6	-5.8	-6.7	-9.5	-2.8	14.1	14.3	-0.2	-6.0%
Consumer Staples	-5.6	-4.7	-5.2	-1.0	4.2	15.9	15.8	0.1	10.1%
Energy	-9.3	0.1	-4.6	15.5	20.1	8.7	15.0	-6.4	30.3%
Financials	-5.6	-4.3	-5.0	-2.5	2.4	9.4	11.5	-2.1	-9.4%
Health Care	-7.2	-16.4	-11.8	-44.3	-32.5	16.2	16.4	-0.2	-61.6%
Industrials	-9.9	-4.7	-7.3	-11.1	-3.8	21.9	15.6	6.3	1.4%
Information Technology	-16.7	-12.4	-14.6	-19.1	-4.6	31.6	21.4	10.2	-52.0%
Materials	-12.7	-5.5	-9.1	-10.2	-1.1	14.6	17.2	-2.6	1.7%
Real Estate	--	-8.2	-8.2	0.3	8.5	14.8	14.7	0.2	-21.5%
Utilities	-6.4	-10.7	-8.6	-6.4	2.2	18.6	17.9	0.7	-10.6%

Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022. YTD returns are in CAD.

Global Fixed Income: Finally, a Worthy Competitor!

After nearly a decade of ultra-low interest rates when there was no other alternative and the only game in town was equities, the recent move in global interest rates across the yield curve – which move inversely to bond prices – has created an opportunity where the risk/reward for bonds remains quite attractive.

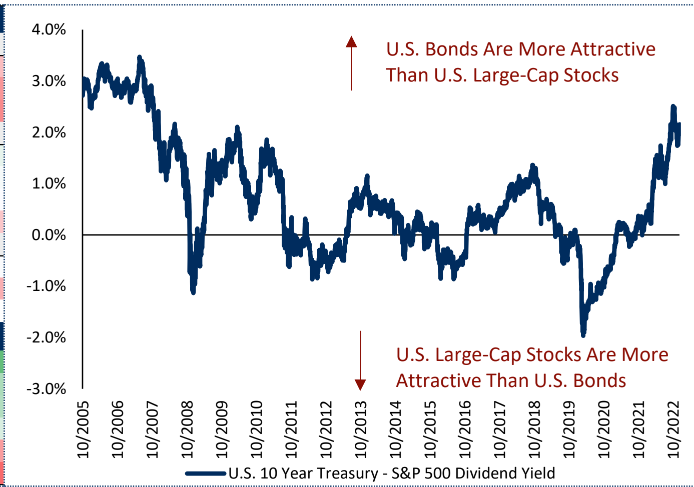
However, despite weak performance for fixed income as an asset class in 2022, we see the case for investors to be adding to global fixed income over the next year as the economic outlook slows further with several global economies entering a recession.

Though bond prices have been falling in lockstep with equities, and thus not behaving or offering the same degree of diversification benefits most investors would have expected from this asset class, we believe stubbornly high inflation and the rapid pace of interest rate hikes/tightening are the main culprits. That said, we believe the worst of these pressures for the fixed income asset class are likely behind us.

Fixed Income Markets Performance [LHS]; U.S. 10 Year Yields – S&P 500 Index Dividend Yield = Bonds > Large-Cap U.S. Equities [RHS]

Fixed Income	3Mo (in USD)	3 Mo (in CAD)	YTD (in USD)	YTD (in CAD)
Canada				
Canadian Bonds (Corporates)	2.7	1.7	-15.6	-9.5
Canadian Bonds (Aggregate)	2.0	1.0	-17.3	-11.3
Canadian Bonds (Government)	1.8	0.8	-17.8	-11.9
U.S.				
U.S. Bonds (High Yield)	2.5	1.4	-10.6	-4.1
U.S. Bonds (Government)	0.4	-0.6	-12.3	-5.9
U.S. Bonds (Aggregate)	1.3	0.3	-13.0	-6.7
U.S. Bonds (Corporates)	2.5	1.5	-15.3	-9.1
Global				
Global Bonds (High Yield)	6.2	5.1	-12.7	-6.4
Global Bonds (Aggregate)	3.9	2.9	-16.2	-10.2

Yields	3Mo (in USD)	3 Mo (in CAD)	YTD (in USD)	YTD (in CAD)
U.K. Benchmark Bond - 10 Year	3.2	3.2	12.0	12.0
U.S. Benchmark Bond - 10 Year	11.1	11.1	3.1	3.1
China Benchmark Bond - 10 Year	2.7	2.7	2.4	2.4
Japan Benchmark Bond - 10 Year	-1.5	-1.5	-2.4	-2.4
Canada Benchmark Bond - 10 Year	0.1	0.1	-11.0	-11.0
Australia Benchmark Bond - 10 Year	0.6	0.6	-13.3	-13.3



Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

Fixed Income: Adding to the Roster (i.e., Duration) in the Off-season Is an Optimal Strategy to Get Playoff Ready

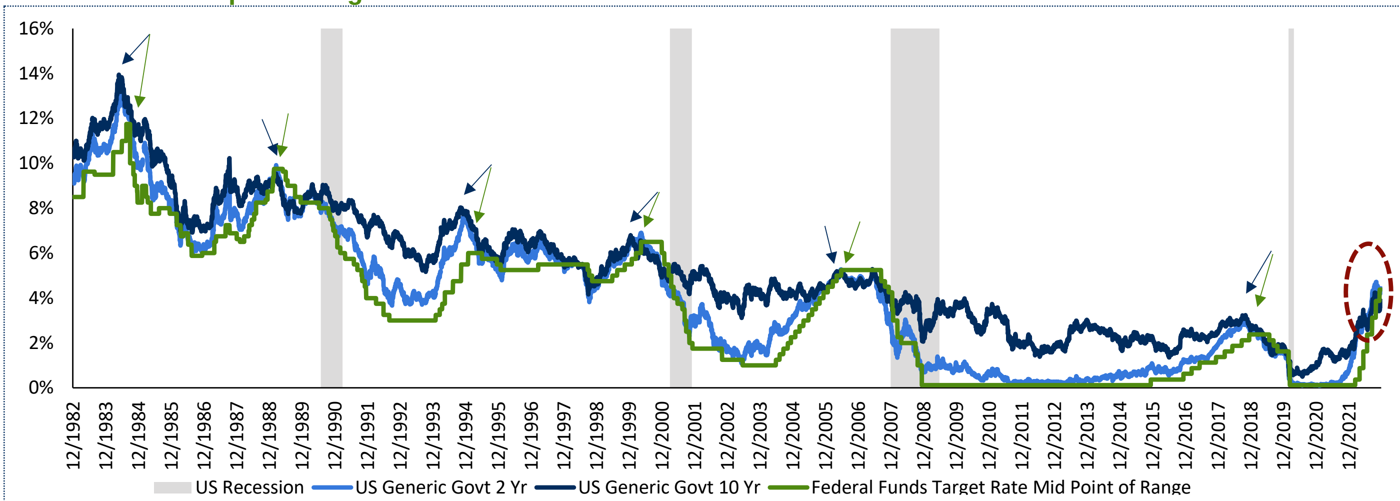
Headline inflation for Canada and the U.S. has been falling as we expected, and the respective central banks (CBs) are slowing, or are expected to slow, the pace of rate increases. The latest 50-basis-point rate hike by the Fed, while widely expected, was lower than the 75-basis-point rate increases made at the last three Fed rate decisions.

After a 75-basis-point rate hike in September, the BoC has raised its benchmark rate by 50 basis points in its last two rate decisions. Markets are currently expecting another 50 basis points to be made by the Fed by March 2023, while only one 25-basis-point rate hike by the BoC in January.

Both CBs are expected to pause through the summer to allow the tighter monetary policy effects to show up in the economy. The Fed has narrowed its focus to an easing in the tight labour market and a softening in non-housing-related services inflation, which it currently views as the primary driver of inflation.

We expect the CBs to continue to talk tough with respect to fighting inflation, saying they do not expect any rate cuts in 2023 because their job of fighting inflation has not yet been completed. That said, history shows that interest rates typically begin to fall once CBs have stopped raising rates, as we showed in our last edition.

When the Fed Stops Raising Rates – Run Fast!

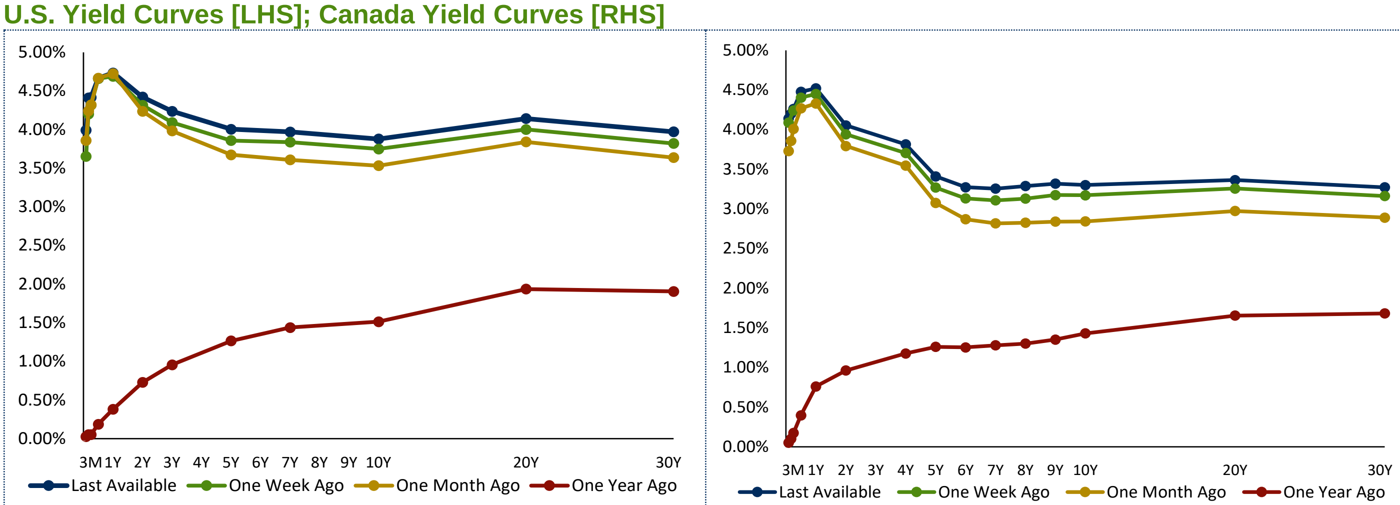


Source: FactSet; Raymond James Ltd.; Raymond James Financial; Data as of December 31, 2022.

While a slight chance of a soft landing (no recession) remains, we continue to believe a recession in North America is coming. But, whether a recession occurs, interest rates across the yield curve should fall as the CBs pause interest rate hikes, similar to what unfolded in the U.S. during the soft-landing period after the 1994 rate-hiking regime. The risk to this scenario is a sudden resurgence in inflation, which we currently do not expect.

We continue to advise clients to add duration (through longer maturities) to their portfolios to capture the current yield environment. While we like shorter-maturity yield levels for short-term cash needs, we prefer longer-duration fixed income products for a higher total return.

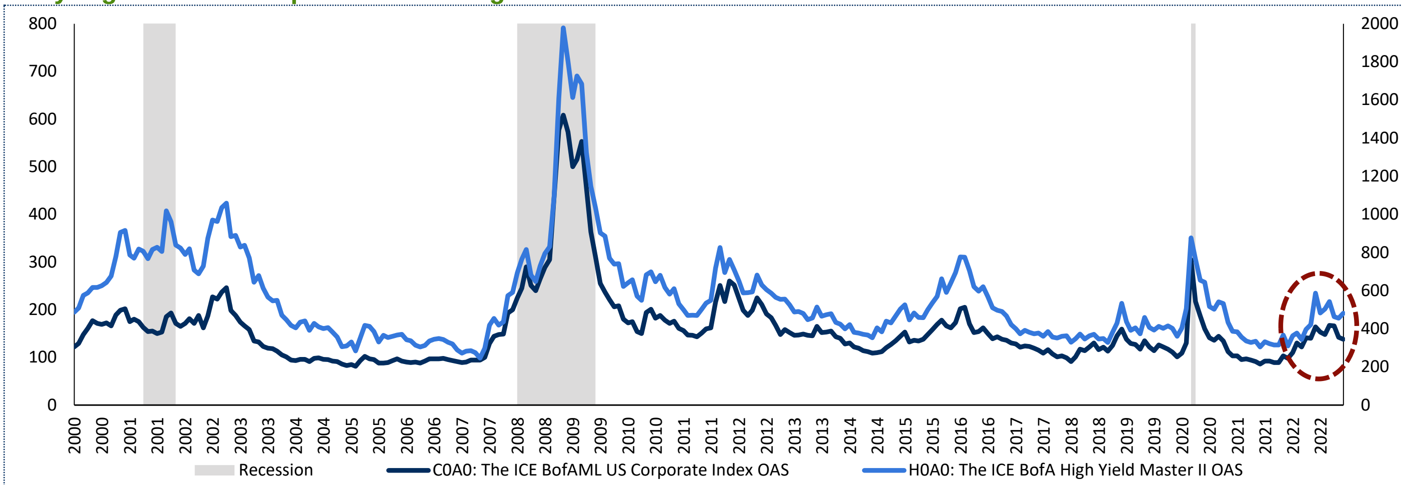
U.S. Yield Curves [LHS]; Canada Yield Curves [RHS]



Source: FactSet; Raymond James Ltd.; Raymond James Financial; Data as of December 31, 2022.

Because we remain cautious about a recession, we are concerned about an increase in credit risk, so we continue to suggest that corporate bond holdings be reduced to underweight in total alongside an increase in quality and defensive positions. In relative terms, U.S. yields are higher across the board than Canadian ones, so we prefer holding U.S. treasury over Canadian sovereign bonds.

Early Signs of Credit Spreads Widening



Source: FactSet; Raymond James Ltd.; Data as of December 31, 2022.

Asset Allocation Committee

Nadeem Kassam, MBA, CFA (Chair)
Head of Investment Strategy
Raymond James Ltd.

Tavis C. McCourt, CFA
Institutional Equity Strategist
Raymond James & Associates

Ellis Phifer, CFA, CMT
Institutional Fixed Income Strategist
Raymond James & Associates

Ed Mills
Washington Policy Analyst
Raymond James & Associates

Nicole Svec, MBA, CFA
Head of Equities, Institutional Sales Toronto
Raymond James Ltd.

Sean Boyle, MBA
Co-head of Institutional Sales
Raymond James Ltd.

Douglas Drabik
Senior Retail Fixed Income Strategist
Raymond James & Associates

Eugenio J. Alemán, Ph.D.
Chief Economist
Raymond James & Associates

Eve Zhou
Multi-Asset Analyst
Raymond James Ltd.

Important Investor Disclosures

Complete disclosures for companies covered by Raymond James can be viewed at https://raymondjames.bluematrix.com/sellside/Disclosures.action

This newsletter is prepared by the Private Client Services team (PCS) of Raymond James Ltd. (RJL) for distribution to RJL's retail clients. It is not a product of the Research Department of RJL.

All opinions and recommendations reflect the judgement of the author at this date and are subject to change. The author's recommendations may be based on technical analysis and may or may not consider information contained in fundamental research reports published by RJL or its affiliates. Information is from sources believed to be reliable but accuracy cannot be guaranteed. It is for informational purposes only. It is not meant to provide legal or tax advice; as each situation is different, individuals should seek advice based on their circumstances. Nor is it an offer to sell or the solicitation of an offer to buy any securities. It is intended for distribution only in those jurisdictions where RJL is registered. RJL, its officers, directors, agents, employees, and families may from time to time hold long or short positions in the securities mentioned herein and may engage in transactions contrary to the conclusions in this newsletter. RJL may perform investment banking or other services for, or solicit investment banking business from, any company mentioned in this newsletter. Securities offered through Raymond James Ltd., Member-Canadian Investor Protection Fund. Financial planning and insurance offered through Raymond James Financial Planning Ltd., not a Member-Canadian Investor Protection Fund.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual funds. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently, and past performance may not be repeated. The results presented should not and cannot be viewed as an indicator of future performance. Individual results will vary and transaction costs relating to investing in these stocks will affect overall performance.

Information regarding High, Medium, and Low risk securities is available from your Financial Advisor.