

April Market Insights



Yung-Yu Ma, Ph.D., Chief Investment Strategist, BMO Wealth Management - U.S.

Outlook: More back and forth

Stress in the banking sector has added to the economic uncertainty associated with the Fed hiking short-term interest rates by over 4% during the past 12 months. While the housing market responded quickly to those interest rate increases, other areas of the economy responded with a lag as credit became more costly and less available. We do not believe the banking sector suffers from insolvency concerns writ large, but the recent events are likely to tighten credit conditions further in the coming months.

On the positive side, interest rates and future interest rate expectations have come down notably, which has stabilized the equity market in the near term. The Fed's next meeting is on May 3rd, and the market currently expects a toss-up between no rate hike and a quarter percent rate hike. The market is also hopeful that the Fed will reverse course and cut interest rates later in the year as the economy slows and inflation cools. We expect inflation to decline in the coming months, but how nimbly the Fed will respond to changing conditions is unclear and a potential source of risk.

The labor market has shown very early signs of softening around the edges, which is both healthy and welcome for the economy. Weekly initial unemployment claims remain at historically low levels around 200k/week, but should these readings jump toward 300k/week and beyond then downward momentum could develop in the economy. Similarly, should high-yield credit spreads rise above the levels reached in mid-March that would indicate greater economic and market risk.

Positioning

We recommend a balanced approach to risk-taking and believe that 2023 will produce returns more in line with historical averages for both stocks and bonds. The technology sector has recently outperformed, which is typical when interest rate expectations fall sharply and the market quickly reprices areas of potential growth. On net, both stocks and bonds have experienced a favorable, albeit volatile, first quarter. Given the backdrop of a slowing

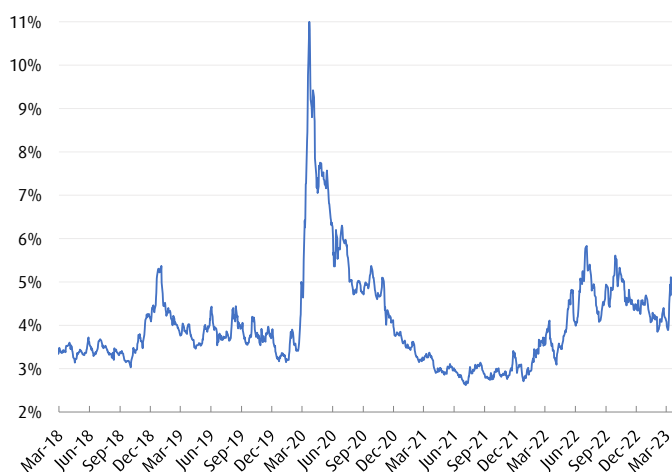
economy and expected falling inflation and interest rates, it's advisable to be neither too enthusiastic nor too pessimistic.

On the Horizon

The earnings season for the first quarter of 2023 is approaching. Expectations for this and future quarters have come down modestly, but we are less confident that corporate outlooks will exceed those already priced into the market.

We continue to believe there is sufficient economic stability to limit the downside momentum in both the economy and markets. Unlike the severe recessions of 2001 and 2008 where economic imbalances were extreme, the present slowdown can be largely alleviated by falling interest rates when the Fed eventually changes course.

Bloomberg Corporate High Yield Debt - Credit Spread



Source: Bloomberg L.P. (2023), BMO Wealth Management (2023)



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