

Perspectives

Quarterly economic views and asset class outlook

Summer 2024



“

The global economic outlook is improving. The headwind to growth posed by central banks is declining and broad financial conditions seem reasonably balanced.



Michael Sager, Ph.D.
Managing Director & Head,
Multi-Asset & Currency Management



Vincent Lépine
Director, Economic & Market Research,
Multi-Asset & Currency Management



Francis Thivierge, M.Sc., CFA
Senior Portfolio Manager,
Multi-Asset & Currency Management

Investment outlook remains constructive, but political risks are rising

Welcome to the 2024 summer edition of *Perspectives*.

The global economic outlook is improving. The headwind to growth posed by central banks is declining and broad financial conditions seem reasonably balanced. Early signs of recovery discussed in the [last edition of Perspectives](#) are progressing and the number of countries reporting a gradual strengthening in growth has increased. This doesn't include the US. Here evidence is consistent with a benign slowing, and growth appears to be decelerating from an unsustainably fast pace to a rate more consistent with the US economy's long-term trend. The global growth recovery will likely not prevent a further deceleration in inflation. In particular, recent data from the US service sector have softened. If maintained, this trend will likely facilitate the start of policy easing by the US Federal Reserve (Fed), while many other central banks are also expected to loosen policy further in the next 12 months.

Our constructive outlook for the macroeconomy merits continued cautious optimism for asset markets. We think that equities—particularly those markets with the strongest fundamentals and most attractive valuations—and fixed income can both do reasonably well over the next 12 months. In combination, they're expected to deliver relatively attractive returns for investors in traditional balanced portfolios.

Assessing the size and source of potential risks to this relatively constructive outlook is, as always, top of mind. Currently, political risks appear to pose a more important challenge to markets and investor sentiment than either economic data or prospective central bank policy rate decisions. Volatility related to idiosyncratic political events has already risen in a number of markets, including in Europe and Latin America. Arguably, the most significant political risks still lie ahead, with US elections in November increasingly relevant to market price action. This event is often associated with positive equity returns and higher market volatility. The starting valuation of US equity markets this time around makes an outsized gain much harder to realize. By contrast, generalized market volatility remains low and is likely to rise as we approach this event, particularly given the current polarized state of US politics.

At [CIBC Asset Management](#), we're committed to providing market insights and investment research. We hope our quarterly market and economic outlook are helpful as you find the right investment strategies that align with your portfolio goals and navigate markets during the second half of the year. If you have questions or would like to discuss our insights and commentary, please contact your advisor or CIBC representative anytime.

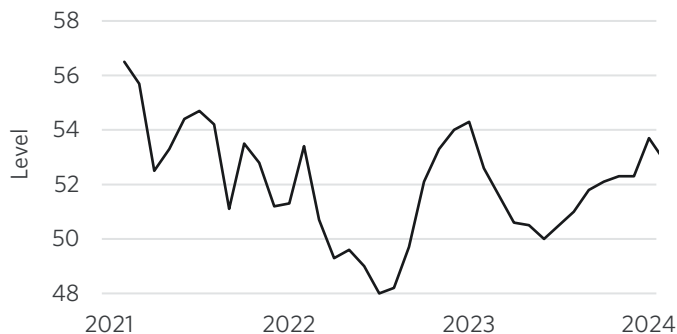
Global markets strategy

Investment outlook remains constructive, political risks increasingly important

After surprising on the upside earlier this year, the growth of global gross domestic product (GDP) has cooled a little in recent months. Much of this slowing has centered on the US, where a benign gradual reversion to trend seems to be playing out. This includes the labour market, for which supply and demand now appears to be better aligned than in past years. Concurrently, the breadth of the global growth recovery has increased, with more countries reporting a gradual improvement in economic activity. This includes Canada, although here activity data have been relatively mixed but are expected to improve.

Global growth improving at a gradual pace

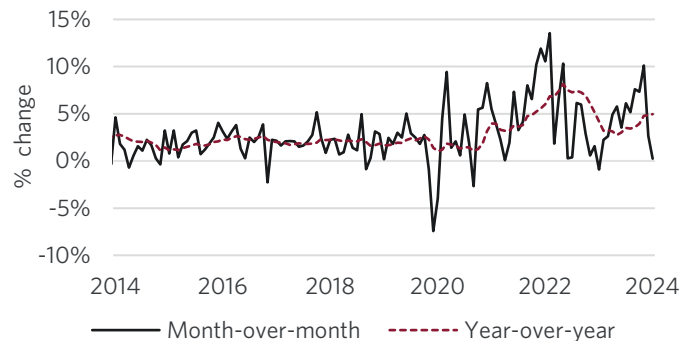
JP Morgan global composite PMI



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at May 31, 2024.

Inflation remains above central banks targets in most countries. After a sustained period of consumer price disinflation throughout 2022 and during the first half of 2023, many developed market (DM) central banks spent much of the subsequent period fretting over the extent of a renewed upswing in inflation, led by services. Canada was a noteworthy exception. Despite sustained elevated wage increases the Bank of Canada (BoC) responded in June to the moderation in Canadian consumer price inflation and became the first G7 central bank to **cut its policy interest rate** (by a quarter point to 4.75%). The inflation outlook has also recently brightened in the US with the latest consumer—and producer—price data suggesting inflation has resumed its convergence towards the Fed's 2.0% policy target. Particularly encouraging was the sharp decline in services inflation excluding shelter, which remains central to the timing and magnitude of policy easing by the Fed. Based on the available data, we continue to expect a short and shallow rate easing cycle in most DM countries, including the US and Canada.

Underlying inflation pressures still present, but improving US CPI services excluding shelter



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at May 31, 2024

Overall, the global economy is neither overheating nor particularly weak. Financial conditions are neither too easy nor unnecessarily restrictive. This benign macroeconomic environment is consistent with the *higher for longer* 12-month forecast scenario we described in the [spring edition of Perspectives](#). Accordingly, we propose only small changes to this scenario in this edition.

Equity market rally has eased financial conditions

Goldman Sachs US financial conditions index

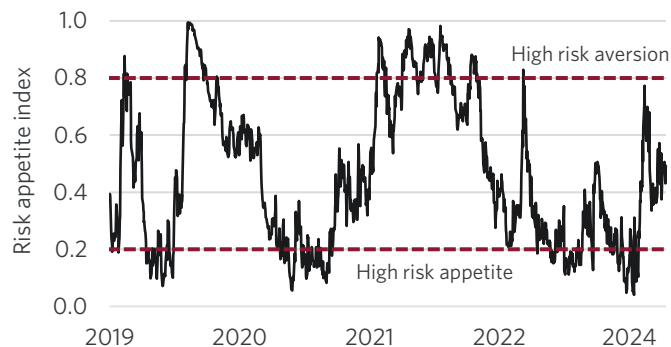


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; Goldman Sachs. Data as at June 28, 2024.

We remain in a broadly constructive investment environment. We expect equity markets to make further progress to the upside, albeit perhaps more limited than seen in the past year for the US. Credit markets are also expected to continue to perform relatively well under our *higher for longer* scenario. Our two alternative economic scenarios are also relatively benign for investment portfolios. They have somewhat more inflation or less growth than under our main scenario, but no great danger for investors who, consistent with our outlook, remain relatively constructive. The more important challenge to markets in the next 12 months could come from political events rather than economic data or central bank decision making. The long list of potential political risks includes November's US election, additional European elections and Chinese relations with the US and Europe.

Investors have embraced the improving outlook

CIBC AM risk indicator



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at June 28, 2024.

The relatively favourable environment we expect is not sufficient to currently warrant a tactical overweight equity position. Normal equity returns should dictate portfolio positioning that's in line with an investor's [long-term strategic asset](#) allocation. Abnormally

attractive returns would be needed to justify a tactical overweight. Although we remain constructive, we don't expect equity markets to realize abnormal returns. Furthermore, relative to fixed income, expected equity outperformance is likely small over the next 12 months. The economic outlook we project for the next year is also expected to be relatively helpful to fixed income returns. Although this outlook doesn't offer a high conviction tactical opportunity, it does represent good news for balanced portfolio investors who can expect solid returns in the next year on the two main asset classes in their portfolios.

Rather than looking for opportunities between equities and fixed income, our tactical thinking remains focused on relative strategies within asset classes. In equities, we're focused on an overweight in Canadian equities versus underweight in EAFE®. Among other things, this reflects more attractive valuations in Canada. In fixed income, we're focused on a tactical overweight in global fixed income versus underweight the FTSE Canada Universe. This tilt is motivated by relatively attractive yields currently available in global bonds of a similar (and often superior) quality to their Canadian equivalents.

Multi-asset outlook

Asset class	Current 28-Jun-24	Most likely range for the next 12 months	
		Minimum	Maximum
Canada 3 Month T-Bills rate	4.75%	3.50%	4.25%
Canada 2 Year government bond yield	3.99%	3.15%	3.85%
Canada 10 Year government bond yield	3.50%	2.95%	3.60%
US 10 Year government bond yield	4.40%	3.50%	4.75%
Germany 10 Year government bond yield	2.50%	1.50%	3.00%
Japan 10 Year government bond yield	1.05%	0.65%	1.50%
Canada Investment Grade corporate spreads	1.17%	0.90%	1.25%
US High Yield corporate spreads	3.17%	2.73%	3.65%
EM Sovereign (USD dominated) bond spreads	344	250	500
S&P/TSX price index	21,876	20,850	25,200
S&P 500 price index	5,460	4,775	5,825
Euro Stoxx 50 price index	4,894	4,600	5,600
Japan Topix price index	2,810	2,600	3,175
MSCI Emerging Markets	67,433	61,700	74,800
USD/CAD	1.368	1.315	1.390
EUR/USD	1.071	1.040	1.120
USD/JPY	160.88	148.00	168.00
USD/CNH	7.30	7.15	7.45
Gold	2,327	2,200	2,500
Oil price, WTI	81.54	60.00	92.00

Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party provider: Bloomberg. Data as at 29 June 2024.

Global equities: Still cautiously constructive, focused on attractive fundamentals

The performance of global equity markets was mixed over the past quarter. Some markets continued to generate strong returns. This included the US (the Nasdaq rose by 8.15% in Q2 2024 and the S&P500 increased by more than 4%), Hong Kong (7.12%), China (the HSCEI was up 9.2%), and Taiwan. Other markets were adversely impacted by political uncertainty. Unexpected election results towards the end of the second quarter in Mexico, India, South Africa and Europe all triggered a marked rise in market volatility. The CAC 40 index in France fell by 7% in response to European election results in early June and the Mexican equity market fell by more than 4% in the month in response to a surprisingly strong election performance by the governing Morena party. By contrast, South African equities rose by 7% in June, with an important impetus being the announcement of a Government of National Unity.

Equity valuations range from neutral to expensive, depending on the region. Canada is relatively attractive, with a Forward Price/Earnings (P/E) ratio broadly consistent with its historical average. This partly explains our current tactical overweight in this market.

Canada equity valuation rising, but not expensive

TSX forward PE

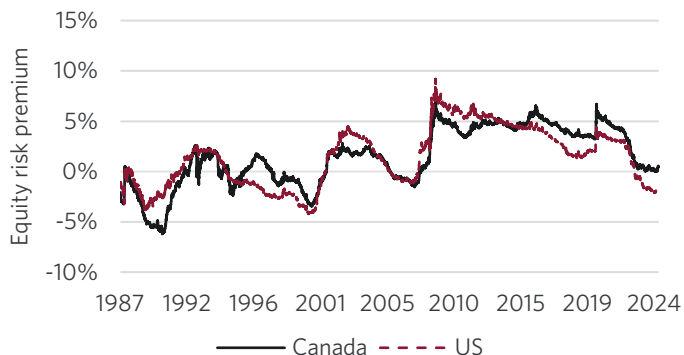


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at June 28, 2024.

Another key valuation metric we monitor is the gap between the earnings yield and the short-term risk-free interest rate. This represents a simple estimate of the equity risk premium. Central bank policy tightening over the last few years narrowed this gap to levels that suggest many equity markets are overvalued—including US large-cap. The expected reduction of policy rates back towards a level consistent with a neutral policy setting will improve the equity risk premium. But most equity markets won't subsequently screen as cheap. This partly explains our continued cautious optimism.

Equity risk premiums are tight, but will improve as central banks ease

Earnings yield minus risk free short rates

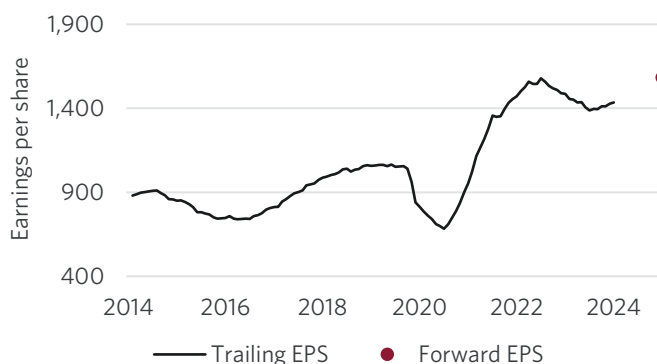


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at June 28, 2024.

The bottom-up market consensus is expecting earnings to grow in a range of 7% (in Europe) to 18% (in emerging markets), depending on the region. This expected range is high compared to the average growth of the last 40 years. Historically, earnings tend to grow above average only when the economy is growing above potential. For the next 12 months, our economic forecasts imply that global GDP will grow slightly below potential. More reason for caution alongside optimism.

Earnings are expected to continue to recover

TSX earnings

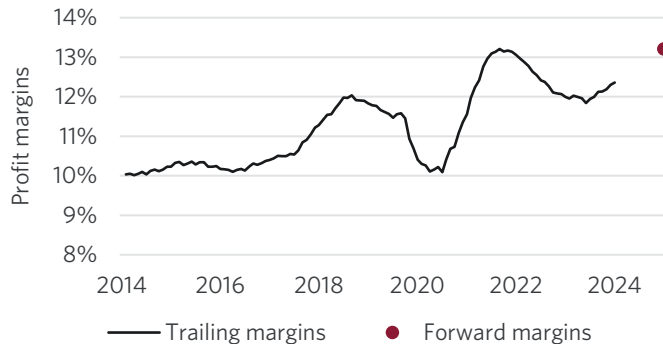


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at June 28, 2024.

We can disaggregate expected earnings growth into the outlook for sales and profit margins. The market consensus expects sales to grow by 5% in the US, 1% in Canada and 7% in the emerging markets (EM) as a whole over the next 12 months. This seems generally reasonable, and even conservative in the case of Canada. The gap between elevated expected earnings growth and more reasonable expectations for sales growth is explained by the outlook for profit margins—which the market consensus expects to widen. The pace of expected improvement appears to be optimistic. Profit margins tend to follow the economic cycle—they rise and fall as economic activity accelerates.

The behaviour of margins is also a reflection of the pricing power of companies and their ability to raise prices faster than input costs. Since labour is the most important input to production and wage costs tend to be stickier than headline inflation, our expectation for further gradual disinflation across the global economy should represent a headwind to profit margins. Putting all these factors together, we don't expect significant support for equity returns to come from either expanding valuations or rising profit margins. More likely, the main driver of returns in the next year will be resilient revenue growth.

The market consensus expects profit margins to rise to previous peaks
S&P 500 profit margins



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at June 28, 2024.

Cautious optimism, with a focus on strong fundamentals and relatively attractive valuations, remains key to successfully navigating markets in the coming year. Canadian equities underperformed significantly over the last two years. As a result, valuation looks more attractive and momentum isn't as overbought as it is in other markets. This sets the stage for a period of catch-up performance as economic activity recovers from the recent slowdown.

EAFE® equities have fared relatively well in recent quarters, particularly Value sectors led by Financials. Corporate profits in Europe have been more resilient than expected in the context of a weak economy, with banks benefiting from higher interest rates as well as a re-rating from very low P/E multiples. As such, the potential for further good performance is limited in relative terms. Japan offers a more constructive outlook based on structural reforms being implemented to improve corporate competitiveness. But with the Nikkei being up over 50% since early 2023, a lot is already in the price.

Japanese equities have benefited from the depreciation of the Japanese yen, which now screens as deeply undervalued. The Bank of Japan (BoJ) is slowly moving away from its ultra accommodative policy stance at a time when as the Fed will likely start to cut rates soon. While we don't see an immediate catalyst for a reversal in the currency, these conditions make further depreciation less likely—and thus less supportive of equities.

Most of our indicators point toward near-term relative underperformance of US equities. However, S&P500 performance continues to be concentrated in a few companies that have displayed a lack of sensitivity to the cyclical economic outlook. The risk is this situation will persist for the foreseeable future.

The Emerging Markets (EM) index has changed substantially over the last 15 years. Historically, it was concentrated in manufacturing and commodity producing countries. From 2008 until recently, it became increasingly dominated by China and consumer related sectors. However, China has performed poorly in recent years and its weight has substantially declined as a result. Taiwan and India have become more prominent. Positive signs on the global semiconductor cycle should support Taiwan, although valuation is a concern. An important question for India is whether its domestic growth will remain robust enough to support this market's high valuation. Our base case is that it will. However, given how far valuation has moved, a lot of good news has been priced. Although the outlook for China matters less than it did in the past for the EM index, it's still important. We expect recent Chinese policy initiatives to provide only a limited boost to growth in the next couple of quarters. Without additional stimulus, their impact on growth will fade moving into 2025. This presents a headwind for this market.

Overall, therefore, the EM index combines countries with good fundamentals but expensive valuations, and cheap countries with less appealing growth prospects. A keen focus on fundamentals remains paramount.

Global fixed income: Wait before extending duration, buy emerging market bonds now

Global bond market performance was slightly negative in the second quarter of 2024, the WGBI index (Canadian dollars hedged) decreased by 0.45% during the period. Yields moved higher in the first half of the quarter but finished the period almost unchanged. Among relevant factors, bond markets were impacted by the beginning of interest rate cutting cycles by the BoC and a day later by the European Central Bank (ECB). The Fed and the Bank of England have both expressed a bias to easing policy stance as long as the gradual trend lower in inflation does re-assert itself. By contrast, the BoJ continues to march to its own beat and is looking to cautiously raise its policy rate as well as taper quantitative easing (QE). These moves are expected to lead to a gradual move higher in Japanese government bond (JGB) yields in coming quarters.

Across developed markets and reflecting a combination of policy expectations and cyclical economic trends, government bond yields are trading close to our estimate of long-term, structural equilibriums. Given our expectation for a continued gradual improvement in global economic growth, yields will likely fluctuate within a relatively narrow band in the next 12 months. For instance, we expect 10-year US Treasury yields to move in a range of 3.50% to 4.75%, centered around a long-term equilibrium yield of 4.15%. As such, Treasury bond returns in the next year will likely be dominated by interest income.

In terms of portfolio strategy, since the current 10-year US Treasury yield (4.40% on June 28, 2024; according to Bloomberg) is trading only a little above our equilibrium level, we recommend a slight overweight duration position. We'll extend this overweight on any substantive back-up in yields, assuming there's no meaningful change in our economic outlook.

Our EM bonds portfolio strategy remains positively tilted and pro-cyclical. During Q2 2024, idiosyncratic event risk negatively impacted performance in several EM markets. This included the election-related volatility in Mexico and South Africa noted above as well as renewed fiscal concerns in Brazil. Going forward, the global growth outlook remains sufficiently robust to allow a decent portfolio exposure towards higher beta names in the EM bond universe, including Brazil and South Africa, as well as Chile. This outlook will be helped a little further if the Chinese government announces additional measures to stimulate economic activity. Also, with starting yields elevated in many countries, valuations remain relatively appealing. Moreover, many EM central banks will likely continue easing monetary policy in response to a trend weakening in inflation data. This easing is expected to trigger capital gains across the EM bond universe.

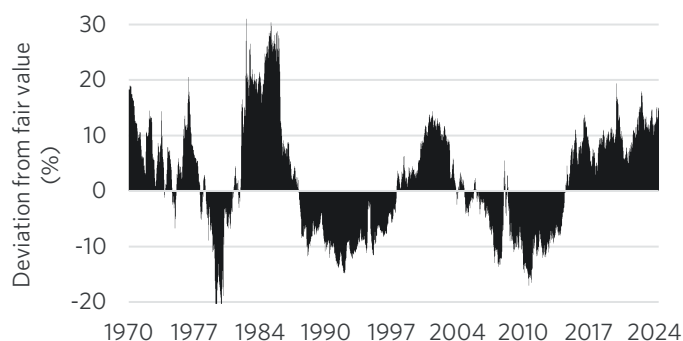
Currencies

US Dollar: Still expensive

The US dollar (USD) continued to defy gravity in the second quarter of 2024, gaining further ground for a cumulative Year-to-Date (YTD) appreciation of more than 4% on a trade-weighted basis. The strength of the greenback was consistent with the US economy's continued cyclical growth leadership that kept the Fed on the sidelines. It was also broad-based, with the most noteworthy gains against the Japanese yen and several emerging currencies, including the Brazilian real. Already overvalued by 10% at the start of the year, USD's overvaluation on a trade-weighted basis reached nearly 15% by the end of Q2.

USD remains expensive

US dollar valuation

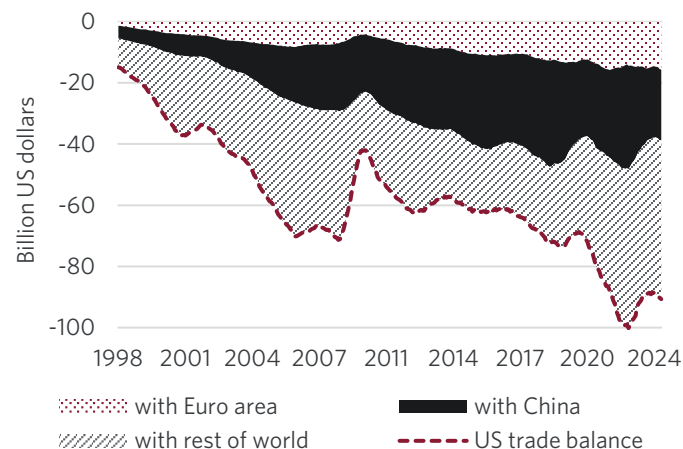


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

As highlighted in [our previous quarterly outlook](#), USD's overvaluation isn't something new. The currency has screened as expensive for nearly a decade. This certainly hasn't helped the US economy reap the full competitive benefits of the substantial productivity gains it has realized over recent years, particularly against the likes of Canada and the Eurozone. As a result, the US trade deficit with the rest of the world is now much bigger than it was 10 years ago. With US elections looming, US trade imbalances will likely take center stage again with increased prospects of another trade war and important implications for market volatility and currency valuations.

The US trade balance continues to widen despite strong productivity

US trade balance



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

Further out, one of the more important risks to USD comes from fiscal policy. US government debt as a percentage of GDP is projected by the Congressional Budget Office (CBO) to continue to rise in coming years well beyond previous highs. How this unprecedented situation resolves will be particularly important in the context of USD's continued status as the global economy's pre-eminent reserve currency.

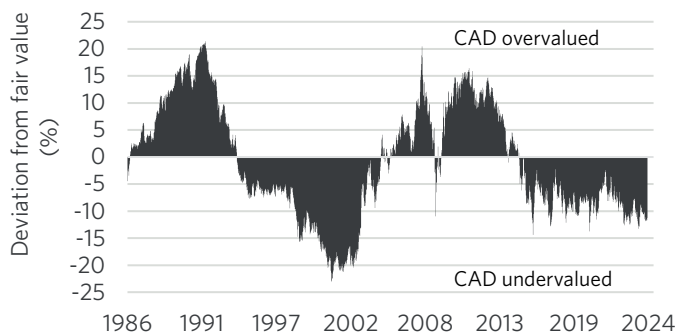
In the meantime, USD—just like the US economy—is expected to stay resilient in coming quarters.

Canadian dollar: Rangebound and weak

The Canadian dollar (CAD) remained stuck in the doldrums against USD through the second quarter of 2024, hovering around US\$0.73. This is close to the bottom of its trading range of the last two years and a long way from our fair value estimate of (US\$0.85, equivalent to an undervaluation versus USD of 15%).

CAD is undervalued but unlikely to strengthen in the near term

Canadian dollar valuation



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

CAD has screened as undervalued for nearly a decade. Similar to USD, Canada's productivity performance has been a key determinant of the currency's weakness. Canada is experiencing a multi-year *negative* productivity shock, in absolute terms and relative to the US. In addition, we remain downbeat on the short-term outlook for the price of several of Canada's key commodity exports, including crude oil. Monetary policy is likely to be broadly neutral but, as noted above, political risks might begin to exert downward pressure on CAD if trade war speculation becomes increasingly prevalent. The CAD/USD bilateral rate is expected to remain weak over the next 12 months, trading in a range between US\$0.7200 and US\$0.7600 (US\$0.7310 as of June 28, 2024, according to Bloomberg).

Euro: A more volatile range

The euro (EUR) moved in a broad range against USD in the second quarter of 2024 as a whole. It struggled in June in the face of two important headwinds. First, the ECB joined the BoC and announced its first quarter point interest rate cut early in the month. In our opinion, elevated European unit labour costs—primarily reflective of persistently poor Eurozone productivity, similar to Canada—will limit the extent of further ECB easing. This means monetary policy differentials will likely play little role in EUR's behaviour in coming months.

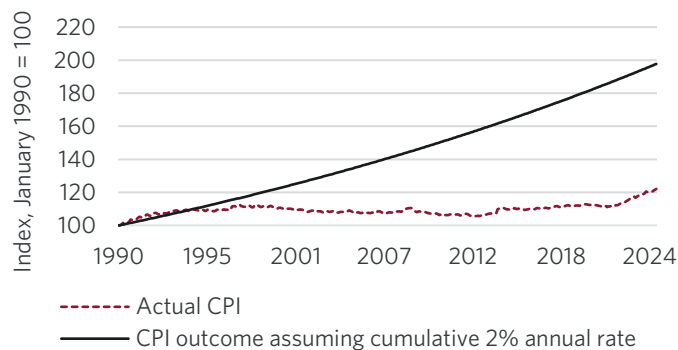
Second, following European elections in early June and the subsequent snap parliamentary elections called by French President Macron, political risk has resurfaced in Europe. The immediate impact was a weakening of EUR, and a widening of French and other country sovereign bond spreads. We don't expect significant additional EUR weakness as a result of political risk. The ECB remains credible and independent. The outcome of French elections appears unlikely to trigger seismic negative changes in domestic fiscal policy. The deficit is already stretching the bounds of possibility as defined by European fiscal rules. And results of the early June European parliamentary elections actually resulted in a broad continuation of the status quo, despite being largely overshadowed by French politics. However, political risk does have the potential to encourage more volatility and so does the risk of renewed trade tensions with the US and China. Accordingly, we expect a more volatile EUR/USD bilateral exchange rate over our 12-month forecast horizon that trades between US\$1.0400 and US\$1.1200 (US\$1.0713 as of June 28, 2024, according to Bloomberg).

Japanese yen: Balance of risks suggests a stronger yen

The Japanese yen's four-year depreciation against USD persisted through the second quarter of 2024. The exchange rate reached ¥160 at the end of the period—a level last seen in 1986 prior to the subsequent sustained deep Japanese economic malaise. During this period, Japan experienced a spectacular decline in GDP per capita relative to the US and an equally spectacular shortfall in inflation. This malaise has recently motivated the Japanese government to adopt wide-ranging corporate reforms intended to encourage a renewed focus on corporate profitability and shareholder value creation, and ultimately a normalization of the Japanese economy that encompasses stronger wealth creation and GDP growth, as well as persistent achievement of the BoJ's 2% inflation target. As part of these efforts, the BoJ and the Japanese government have quietly embraced yen weakness as an integral element of economic normalization. It drove the initial upturn in Japanese inflation in the absence of domestic economic strength and has also been an important driver of the strong performance of Japanese equity markets.

The Japanese economy has experienced decades of anemic inflation

Actual inflation vs cumulative 2% annual rate



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at 28 June 2024.

We estimate that the yen is now significantly undervalued against many currencies, including USD and the Chinese renminbi (CNH). This undervaluation is being reflected in external trade balances, with Japanese bilateral surpluses rising strongly against both the US and China. Consequently, we're likely most of the way through this extended period of yen weakness. The balance of risks over the next 12 months favour a stronger yen as the BoJ gradually raises its policy interest rate and continues to slowly reduce the extent of QE, concurrent to at least some policy easing by the Fed and the People's Bank of China (PBoC) and a further reduction of EM policy rates that will reduce the attractiveness of the carry trade. And yet there's little evidence to suggest a sustained reversal in the yen is imminent, given the continued lackluster performance of the domestic economy and continued negative real wage growth.

We expect the yen to trade between ¥148 and ¥168 against USD in the next 12 months (¥160.88 as of June 28, 2024, according to Bloomberg).

Commodities

Oil: Still rangebound, despite volatility

The price of oil has been choppy over the past few months, trading from a peak US\$87/bbl at the beginning of April to as low as US\$73/bbl in early June before bouncing back to US\$80 by the end of the month. There have been several contributory factors. On the supply side, confusion followed the June OPEC+ meeting in Riyadh. The group extended the current required production cuts through 2025, but also provided a schedule for bringing 2.2mbbls/d of voluntary cuts back to the market starting in October 2024. OPEC+ subsequently clarified its position and highlighted that any production decision will continue to depend on market conditions. We expect supply side discipline to remain in place. In North America, publicly traded companies continue to focus on balance sheet strength and shareholder returns after funding current operations. Growth remains a lower priority.

One of the leading indicators of crude oil output we monitor is onshore drilled but uncompleted wells (DUCs) in the US. This metric provides a picture of the available inventory that US producers can readily bring to the market in short order. DUCs peaked during the 2020 pandemic and have subsequently steadily dropped to a level not seen in 10 years. As a result, incremental capital being committed to operations will be required just to sustain output at current levels and it won't be sufficient to fund additional growth.

The fall in DUCs limits available US oil supply US onshore oil wells drilled but uncompleted

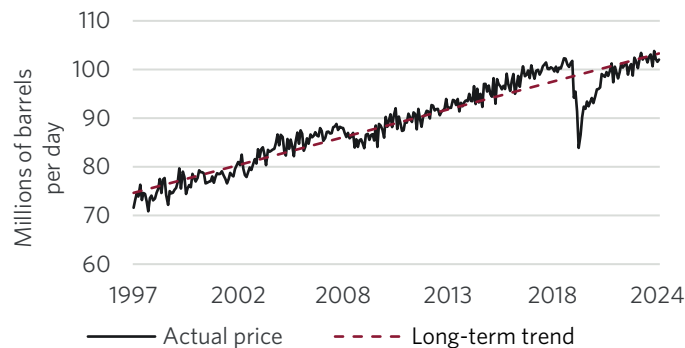


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers Bloomberg. Data as at 30 April 2024.

On the demand side, the start of the Northern Hemisphere summer travel season will be important to monitor for signals on the short-term outlook for energy demand. Over the medium to longer term, we expect oil demand to continue to grow with global population and GDP. This is consistent with the trend seen over the last 30 years.

Long-term rising trend in oil demand

Annual oil demand



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: US Department of Energy. Data as at June 28, 2024.

Combining these various factors, we expect oil to largely trade between US\$60 and US\$92/bbl during coming quarters with temporary deviations outside this range dictated by the ebb and flow of geopolitical risks and macroeconomic data. This range represents a healthy price for Canadian producers who will likely continue to generate meaningful free cash flow at these levels. Cash flows that can be used to support further deleveraging efforts and capital returns to shareholders.

Copper: Gradual price appreciation ahead

Copper experienced a wild ride in the second quarter of 2024. From a low of US\$4.05/lb at the start of April, the price ran to an all-time high of US\$5.00/lb in mid-May, driven by financial positioning, before falling back to a fundamentally more reasonable price of US\$4.40/lb by the end of June.

On the supply side, global copper inventories ticked higher in recent months driven by warehouses in China. This is somewhat unusual for this time of year because we're in peak construction season in the Northern Hemisphere. It's likely that the observed price volatility pushed some buyers to the sidelines to await more certainty and stability. The growing inventory level could also signal that global demand—for copper, and more generally—isn't as robust as expected. We'll be watching the data closely over the next few quarters to see if more normal seasonal inventory patterns re-emerge.

Rising copper inventories

Global copper inventory



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LME. Data as at 28 June 2024.

On the demand side, the data from China have disappointed in recent months raising concerns about copper demand from this key end user. Growth in China remains uneven, with exports and energy transition related sectors strong, offset by weakness in consumer spending and the property sector. We continue to watch for additional targeted stimulus to support the Chinese economy in the coming months.

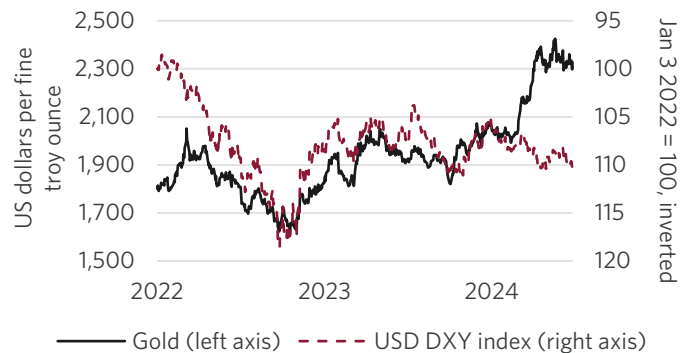
Over the medium term, we see a compelling case for copper price appreciation. The transition to a lower carbon economy will be copper intensive as a result of the manufacture of renewable energy producing assets and in the distribution networks necessary to deliver low carbon electricity to end users. The impact of this transition demand will outweigh slowing demand from traditional sources, including Chinese housing. As a result, copper prices will have to move higher to incentivize the next generation of copper supply projects into the market to satisfy demand.

Gold: Remains attractive

Gold moved sideways through the second quarter, trading between US\$2,300/oz and US\$2,400/oz for most of the period. This price action was consistent with the behaviour of USD, which also moved in a range through the period. But the correlation between gold and USD has loosened substantially in recent quarters. Gold traded well above the level implied by USD as a result of ongoing geopolitical risks, continued central bank buying and expectations of at least some US interest rate cuts in the coming months.

Gold's correlation with USD recently weakened

Gold Versus USD Index



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg. Data as at 28 June, 2024.

In the near term, the risk of a wider conflict in the Middle East and the ongoing conflict in Ukraine could lend further support to gold. Should cooler heads prevail and the situation in these regions stabilizes, some of the risk premium currently built into gold could start to come out.

Fundamentally, expectations of interest rate cuts will likely be supportive of gold. We also expect gold's traditional inverse correlation with USD to continue to re-emerge, which should lend support to the price when rates come down.

We continue to see the case for a strategic portfolio allocation to gold. This encompasses heightened geopolitical risk, an expectation of higher financial and economic volatility, lower interest rates and a residual risk of recession. Gold is expected to represent a relatively consistent hedge to a wide range of tail risks.

Economic analysis

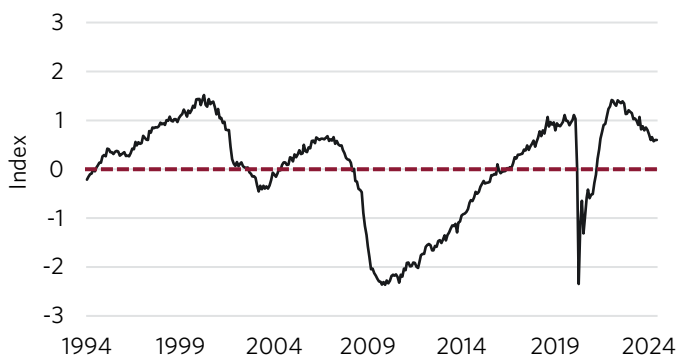
US: Growth decelerating to trend

The US economy is cooling from the surprisingly strong growth it delivered over the last several quarters. This slowdown will likely prove benign as activity readjusts towards its historical trend rate, around 1.8% year-over-year (Y/Y). Growth is expected to be supported by three sectors: household consumption, business investment, and government spending.

Household consumption appears resilient, underpinned by an increasingly healthy jobs market in which the demand and supply of labour are quickly realigning into balance. Business investment is likely to accelerate as pent-up demand for machinery and equipment responds positively to the imminent start of a shallow Fed easing cycle. And government spending is expected to remain robust, with neither political party seemingly in the mood to embrace a more restrictive fiscal stance ahead of November elections. Net exports are likely to be a drag on growth—continued USD strength and the risk of a broad expansion of tariff policies don't bode well for a strong US trade performance.

The US labour market continues to rebalance

Kansas City Fed labour market conditions level of activity indicator

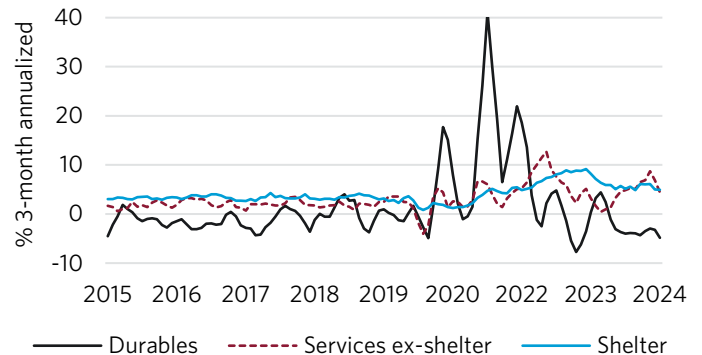


Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; Kansas City Federal Reserve. Data as at 28 June 2024.

We expect US inflation to gradually slow back towards the Fed's 2% policy target. This will likely be driven by a pullback in durable goods inflation. Service sector inflation excluding shelter has also resumed its slowdown, aided by weaker wage growth and strong productivity growth. Some stickiness is expected to persist in shelter inflation (notwithstanding progress evident in the latest data print). This component accounts for 15% of the Fed's preferred measure of shelter inflation, the Personal Consumption Expenditure (PCE) deflator. The persistence in shelter inflation is likely due to an historically low rental vacancy rate, strong household formation and unusually low housing affordability driven by reaccelerating property prices and still-elevated mortgage rates.

US CPI expected to gradually decline

US headline CPI



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

Sticky shelter inflation is not likely an impediment to Fed rate cuts, but it does play to our narrative that the easing cycle will be relatively short and shallow.

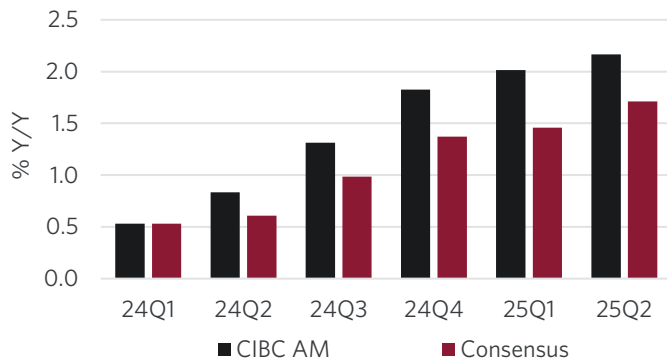
With US politics taking center stage later this year, the main risks to the economic outlook likely lie beyond our 12-month forecast horizon. These risks include the public debt load. This remains on an upward trajectory even under the CBO's most benign economic assumptions on growth and interest payments. Without corrective action—which we don't expect regardless of the outcome of November's elections—rising debt suggests a widening term premium and higher equilibrium bond yields. Nevertheless, the impacts of fiscal policy won't be felt for some time, leaving us comfortable with the view of a US economy growing close to potential.

Canada: Inflation risks remain, despite substantial progress

The Canadian economy rebounded solidly in the first quarter of the year after three quarters of soft growth. Household consumption was the main driver of the recovery and remained resilient in response to solid gains in household real disposable income. In turn, robust income growth reflects continued strong wage and employment growth. We expect GDP growth to remain resilient. On the one hand, continued relatively tight labour market conditions should sustain household income and consumer spending. On the other hand, the start of policy easing by the BoC will likely fuel pent-up housing demand as well as residential and business investment spending.

The Canadian economy is expected to gain strength

Canadian real GDP growth forecast



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

Inflation continues to make substantial progress in its journey back to the BoC's 2% policy target. The BoC's preferred measure—the headline Consumer Price Index (CPI)—ended the period at 2.9% Y/Y. This progress mainly reflected further improvement in the function of supply chains that has dampened goods price inflation. Service sector inflation remains sticky, due to elevated rent and mortgage interest cost inflation. Against this backdrop, the BoC guided markets to expect additional cuts in the second half of 2024 if inflation pressures continue to dissipate—as it expects they will. We see moderate upside risks to the BoC's inflation outlook that will likely limit the extent of rate cuts. These risks—elevated wage growth and shelter inflation—share a common factor: rapid population growth.

Canada's labour market continued to rebalance back towards equilibrium during the second quarter. This rebalancing was mainly driven by a rapid rise in the supply of labour resulting from population growth. A supply-driven labour market rebalancing unfolds differently to a more traditional demand-driven adjustment. The latter occurs in the context of weakening demand for goods and services, which leads to falling employment and rising unemployment that both exert downward pressure on wage growth. By contrast, the Canadian economy has recently experienced a moderate increase in unemployment concurrent to continued employment *growth*, as well as elevated wage gains and robust demand for goods and services.

Strong wage growth has been sustained by two factors. First, newcomers to Canada take time to assimilate into the labour force. This means that the benefit of additional labour supply in limiting wage inflation, and boosting output, is delayed. In the meantime, these newcomers are consumers and put immediate upward pressure on the demand for goods and services. Over the past 12 months, there were approximately two extra consumers for each addition to the workforce.

More demand for goods and services will likely provide a further boost to labour demand. And higher labour demand will make it difficult for wage growth to slow enough to be compatible with the BoC's inflation target. This effect is compounded by the second factor: the high proportion of unionized workers in Canada. One

way to measure this effect is to track wage settlements with cost of living allowances. These settlements continue to rise too fast to be consistent with achieving the BoC's inflation target, given Canada's persistent lackluster productivity. Poor productivity has been accentuated, temporarily at least, by the recent rapid population growth. By contrast, the US also experienced strong immigration and population growth in the past couple of years, but at the same time realized a vigorous resurgence of labour productivity. This indicates that Canada's problem is driven by deep-seated issues such as low private sector investment.

High wage inflation has persisted despite rising unemployment

Canadian wage inflation & unemployment



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

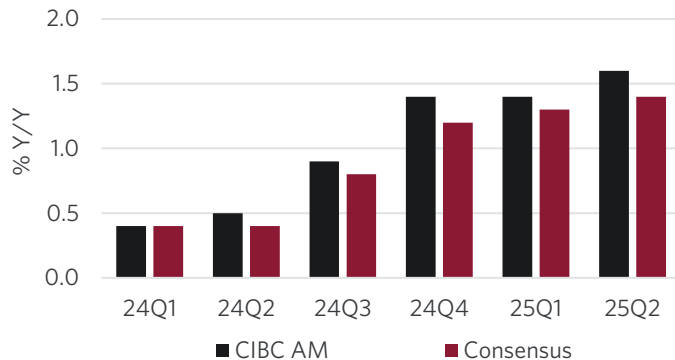
The sustained decline in productivity implies an increased demand for labour and higher unit labour costs (ULCs). In turn, higher ULCs sustain inflationary pressures as firms seek to pass at least some of the additional costs they face on to customers in an effort to maintain profit margins. The BoC has a difficult road to navigate. Higher for longer than the market consensus expects seems to be its most likely path forward.

Eurozone: Recovery gathers pace, inflation challenges remain

We continue to expect a moderate recovery in the eurozone economy, with GDP likely to grow by 1.6% in the next year. This is broadly in line with its long-term trend rate and compares to annualized growth in the first half of 2024 closer to 0.4%. The main driver of the recovery will be consumer spending: the labour market remains resilient, savings are plentiful, and financial conditions eased during the first half of 2024. Net exports are projected to provide an additional boost to growth, consistent with the broadening global economic recovery. We expect a much smaller contribution from investment spending and a significant drag from inventories. The economic recovery is projected to be increasingly broad-based across eurozone countries. Until recently, the main source of growth was the south, including Spain and Italy. Now, growth is finally resuming in Germany, and likely to run at a similar rate to the eurozone aggregate.

Eurozone growth is expected to strengthen further

Eurozone real GDP growth forecast



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

Significant progress has also been made on inflation since the start of 2024. By May, headline and core Harmonized Index of Consumer Prices (HICP) yearly inflation rates had decelerated to 2.5% and 2.9%, respectively, increasingly adjacent to the ECB's 2% target. This backdrop gave the ECB enough leeway to deliver its first quarter point rate cut in early June. Its main refinancing rate now stands at 4.25%.

More rate cuts are expected in this easing cycle. But the ECB's room for maneuver is likely more limited than the market consensus expects. Similar to other DM central banks, we continue to expect the eurozone easing cycle to be relatively short and shallow. This outlook appears broadly consistent with the view of the ECB, which recently revised up its own inflation projections for 2024 and 2025, and also ensured the commentary that accompanied its first rate cut had a hawkish tone.

But even the ECB appears a little too optimistic on inflation. We agree that it will succeed in returning inflation back to target—our 10-year **annualized expected inflation** rate for the eurozone is 1.9%. But the remaining journey may be a little harder than it expects. In particular, and similar to Canada, the main driver of above-target inflation is elevated growth in ULCs. And also similar to Canada, this reflects a combination of continued strong wage growth—ECB data report that negotiated wages rose 4.7% Y/Y in Q1—and falling labour productivity. The ECB assumes productivity growth in the next two years will be double the average rate observed over the past two decades. Without substantive supply side reforms, and in the context of trend-like growth, we think this assumption is too aggressive. This represents an important challenge to the ECB's projection of a sharp deceleration in ULCs in 2025.

Unit labour costs represent a challenge to the ECB

Eurozone unit labor costs & productivity growth



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: LSEG Datastream. Data as at 28 June 2024.

China: More stimulus required to support growth; government response unlikely to be sufficient

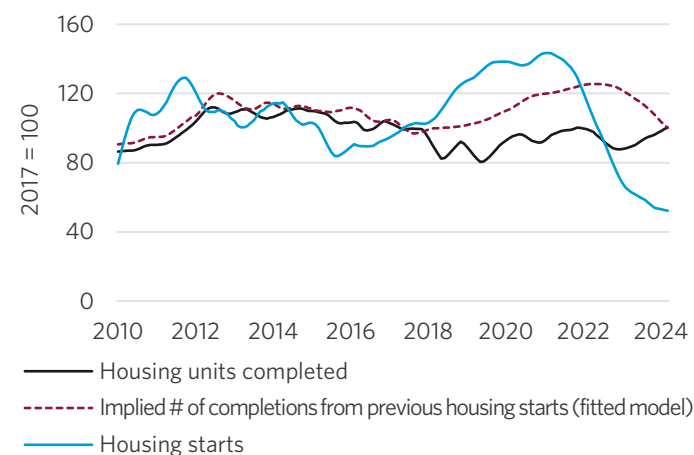
Chinese growth remains weak, consistent with our expectation. The persistent downturn in residential construction remains a major obstacle to growth. Other parts of the economy are also struggling despite the injection of substantial stimulus in sectors such as technology and renewable energy. Economic slack, housing uncertainty and an inadequate policy response have all worsened the decline in housing demand and prices.

More stimulus is needed, but policymakers face major constraints. The housing sector is unlikely to drive long-term growth due to an accelerating population decline. This is a rare occurrence for a country at China's stage of economic development. Low interest rates are hurting bank profitability. With local government indebtedness already high, large-scale infrastructure stimulus (similar to those launched in the past) is not on the cards. In any case, it would likely worsen oversupply issues and financial challenges that authorities have been trying to resolve for some time.

A major challenge facing the Chinese economy is the substantial volume of unfinished residential construction. Reduced housing demand and a government-led crackdown limiting easy access to credit have forced cash-strapped developers to halt construction on many projects. This has caused completion rates to drop well below levels suggested by housing starts. We estimate that the stalled construction stock accounts for at least 5% of GDP. This is a major impediment to a healthier economic outlook.

A massive amount of stalled housing projects

Chinese housing activity



Source: The information is provided by CIBC Asset Management Inc. using data from the following third-party providers: Bloomberg; LSEG Datastream. Data as at 28 June 2024.

The housing sector is not expected to serve as a long-term growth driver. But implementing stimulus measures designed to kick-start stalled construction projects presents a key opportunity to provide cyclical support to the Chinese economy. This could prevent a vicious cycle that damages confidence, exacerbates the housing downturn and increases financial stability risks. The measures we

expect to see are likely to include housing upgrade initiatives similar to those implemented in the latter half of the 2010s, only now with a larger focus on President Xi's social housing objectives. Given that self-built homes represent about 15%-20% of the total housing stock, converting low-quality private properties into state-subsidized housing could advance Xi's vision of "common prosperity" and foster a more equitable society—while absorbing housing supply. Between 2015 and 2019, the PBoC financed housing upgrades equivalent to about 3% of GDP through its Pledged Supplementary Lending (PSL) facility. We expect the PSL to be restarted.

Announced and prospective policy stimulus will likely represent tailwinds to Chinese GDP growth during the remainder of 2024. But the aggregate growth impulse will subsequently wane and eventually turn negative. This loss of momentum is expected to be compounded by unintended fiscal tightening by local governments, who derive around one-third of their revenue from land sales that will be challenged by the subdued outlook for new housing construction. GDP growth is forecasted to peak at 4.9% in Q4 and to average 4.4% over the next four quarters as a whole. This growth rate is much weaker than the norm of only a few years ago and it will be insufficient to significantly narrow the sizeable excess supply output gap in the Chinese economy. Therefore, inflation is likely to remain low.

In this context, we expect the PBoC to become less averse to allowing CNH to depreciate more freely against a broad range of currencies.

Economic forecasts (next 12 months)

Region	Current GDP	GDP - consensus	GDP - CIBC AM view	Current inflation	Inflation - consensus	Inflation - CIBC AM view	Policy rate - CIBC AM view
Canada	0.5%	1.5%	1.8%	2.9%	2.2%	2.8%	-0.75%
United States	2.9%	1.8%	1.8%	3.3%	2.7%	3.0%	-1.00%
Eurozone	0.4%	1.2%	1.3%	2.6%	2.2%	2.5%	-0.75%
China	5.3%	4.5%	4.4%	0.3%	1.2%	1.2%	
Japan	-0.1%	1.1%	1.3%	2.9%	2.2%	2.5%	0.40%
World	2.7%	2.7%	3.2%	3.5%	3.0%	3.4%	

Source: The information is provided by CIBC Asset Management Inc. Inflation refers to CPI.

Alternative economic scenarios

Higher for longer (50% probability): Under this scenario, inflation will likely prove to be a little stickier than expected by the market consensus, forcing central banks to move to the sidelines earlier than expected. The DM central bank easing cycle will be relatively short and shallow. The Fed will likely deliver 100 basis points (bps) of rate cuts across the entire cutting cycle. In terms of balance sheet policy, the Fed will likely play safe by keeping excess reserves abundant. Tapering of quantitative tightening that began in May 2024 will likely end later this year. The US economy is expected to grow by 1.9% Y/Y in early 2025 and at a Y/Y average of 1.8% over the next four quarters. Global growth is projected to average 3.0% Y/Y over the 12-month forecast period. Core PCE inflation is expected to be 2.6% in early 2025. Long-term inflation expectations will remain well anchored, but the term premium is projected to drift higher. The 10-year US Treasury yield is expected to drop to 4.0%.

Second wave inflation (25% probability): Under this scenario, global monetary policy stance isn't sufficiently restrictive, allowing the economy to grow above potential over the forecast horizon. US real GDP growth will remain elevated in Q1 2025, at 2.8% Y/Y with global growth running above 3.0% Y/Y. Abundant central bank liquidity and a lack of fiscal discipline will allow inflation to re-accelerate, forcing DM central banks to keep policy rates unchanged. Under this scenario, 10-year US Treasury yields will rise to 5.0% in the context of a rising term premium and higher long-term inflation expectations.

Global slowdown (25% probability): Under this scenario, global monetary policy stance turns out to be too restrictive. Combined with a larger fiscal drag than expected, the global economy downshifts into a lower gear and inflation decelerates sharply. This gives central banks leeway to cut policy interest rates more aggressively to cushion the economic downturn. Bond markets will rally more convincingly with 10-year US Treasury yields projected to drop to 3.1% and the yield curve to flatten.

Authors



Michael Sager, Ph.D.
Managing Director & Head,
Multi-Asset & Currency Management



Daniel Greenspan, MBA
Director, Equity Research,
Global Fixed Income & Equities



Francis Thivierge, M.Sc., CFA
Senior Portfolio Manager,
Multi-Asset & Currency Management



Vincent Lépine
Director, Economic & Market Research,
Multi-Asset & Currency Management



Eric Morin
Senior Research Analyst,
Multi-Asset & Currency Management



About CIBC Asset Management

At CIBC Asset Management, we believe that every customized investment solution begins with research and rigour. We specialize in a variety of investment solutions such as equities, fixed income, currency management, liability-driven investments, asset allocation, and responsible investments.

Across a spectrum of investment solutions, we commit to in-depth research. Dedicated sector and regional analysts focus on industry research and security-specific idea generation. Our investment professionals leverage deep and diverse expertise by sharing proprietary research across asset-class teams. By sharing insight across asset class teams, we maximize opportunities to add value to our client portfolios.

Contact us any time

To learn more about CIBC Asset Management and our investment solutions, please contact your advisor or your CIBC representative. For more insights, connect with us on [LinkedIn](#).

The views expressed in this material are the views of CIBC Asset Management Inc., unless otherwise indicated, and are subject to change at any time. CIBC Asset Management Inc. does not undertake any obligation or responsibility to update such opinions. This material is provided for general informational purposes only and does not constitute financial, investment, tax, legal or accounting advice nor does it constitute an offer or solicitation to buy or sell any securities referred to.

Forward-looking statements include statements that are predictive in nature, that depend upon or refer to future events or conditions, or that include words such as "expects", "anticipates", "intends", "plans", "believes", "estimates", or other similar wording. In addition, any statements that may be made concerning future performance, strategies, or prospects and possible future actions taken by the fund, are also forward-looking statements. Forward-looking statements are not guarantees of future performance. These statements involve known and unknown risks, uncertainties, and other factors that may cause the actual results and achievements of the fund to differ materially from those expressed or implied by such statements. Such factors include, but are not limited to: general economic, market, and business conditions; fluctuations in securities prices, interest rates, and foreign currency exchange rates; changes in government regulations; and catastrophic events.

The above list of important factors that may affect future results is not exhaustive. Before making any investment decisions, we encourage you to consider these and other factors carefully. CIBC Asset Management Inc. does not undertake, and specifically disclaims, any obligation to update or revise any forward-looking statements, whether as a result of new information, future developments, or otherwise prior to the release of the next management report of fund performance. Past performance may not be repeated and is not indicative of future results.

Bloomberg® is a service mark of Bloomberg Finance L.P. and its affiliates, including Bloomberg Index Services Limited ("BISL"), the administrator of the indices (collectively, "Bloomberg") and have been licensed for use for certain purposes by CIBC Asset Management Inc. Bloomberg is not affiliated with CIBC Asset Management Inc., and Bloomberg does not approve, endorse, review, or recommend any CIBC Asset Management Inc. products.

"EAFE" is a registered trademark of MSCI Inc., used under license.

CIBC Asset Management and the CIBC logo are trademarks of Canadian Imperial Bank of Commerce (CIBC), used under license.

The material and/or its contents may not be reproduced without the express written consent of CIBC Asset Management Inc.