



Time is on my side

Atul Bhatia, CFA – Minneapolis

Too often, we find investors focusing on what the press puts before them instead of concentrating on issues relevant to their goals. We explain why investment time horizon should be a key focus of portfolio thinking.

Most investors, in our experience, have an intuitive understanding of their individual risk tolerance and a robust filter to ignore news stories that are outside their universe. They have little trouble, for example, skipping over discussions regarding the volatility surface of swaptions or the most recent moves in a double-knockout USD/JPY option combo.

When it comes to investment time horizon, though, we find the situation reversed, with investors overly focused on issues that we think are irrelevant to their portfolio goals when measured over the appropriate time span. Too few investors, in our view, read the financial press with a focus on how their individual investment time horizon differs from that of active institutional traders and the typical reporter.

In it for the long haul

Most investors, in our experience, say they have a long-term perspective. That view, we think, makes sense. Individuals tend to save for major life events such as children's college tuition or retirement that are frequently years in the future. Many even take an intergenerational approach, looking to provide for grandchildren or more distant heirs.

That mindset is very different from active institutional traders, who we find tend to think in terms of quarterly earnings reports and annual bonus payments. Moreover,

most institutional traders cannot really determine their own holding period. They tend to rely significantly on borrowed money—in some cases, positions are funded with as much as 90 percent debt. This forces traders to take a short-term outlook; if they cannot meet the margin call from their lenders, it doesn't matter if their long-term view was correct—they still end up losing money.

The financial press, unsurprisingly in our view, tends to reflect the short-term perspective of more active traders. Partly because it makes for better copy—an article headlined “Quarterly portfolio rebalance comes off without a hitch” is not likely to draw a lot of clicks. But it also helps with reporters' need to explain daily market moves; short-term predictions let reporters and the press get a jump on the news cycle.

Ignore the obvious?

This difference in time horizon has significant implications for how investors should approach their consumption of financial data.

Take, for instance, all the discussion about the timing of Fed rate cuts. Rather than getting sucked into a discussion of will they, won't they, or when they move, we think investors should start by asking if the outcome really matters to them. For many, if not most, individual investors, we think the answer is likely no.

For perspectives on the week from our regional analysts, please see [pages 3–4](#).

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Let's start with bond prices. If the Fed delayed rate cuts by a year, the impact on 5-year Treasury rates would be approximately 20 basis points, assuming the central bank then implemented the policy path embedded in interest rate futures pricing from the start of March. That's less than the yield change from Feb. 7 to Feb. 13 of this year. So, all of the analysis, all of the discussion, and all of the forecasting on the Fed boils down to the equivalent of some random week in February. If we didn't lose sleep over the latter, why is there such an intense focus on the former?

Equity price moves are also sensitive to interest rates, and Fed policy could have a meaningful impact on where stocks go in the short term. But it's important to put interest rate policy into context. If rates are staying high, but corporate earnings and economic growth are solid, then we think there is little reason to expect a sustained loss of value to stock prices. In its recent rate hike campaign, the Fed took interest rates up by 5.25 percent, and equity markets are at or near record highs; do we really think a small delay in rate cuts is a meaningful threat over a multiyear time horizon?

We think it's very clear why short-term traders care about the timing and number of cuts—they're playing with borrowed money and need to make sure that margin calls don't push them into forced sales. But for a cash investor—or one with the moderate leverage typical in individual accounts—the likely impacts of May versus June versus September for the first cut are blips in performance that will likely be long forgotten when retirement rolls around.

Best case or worst case?

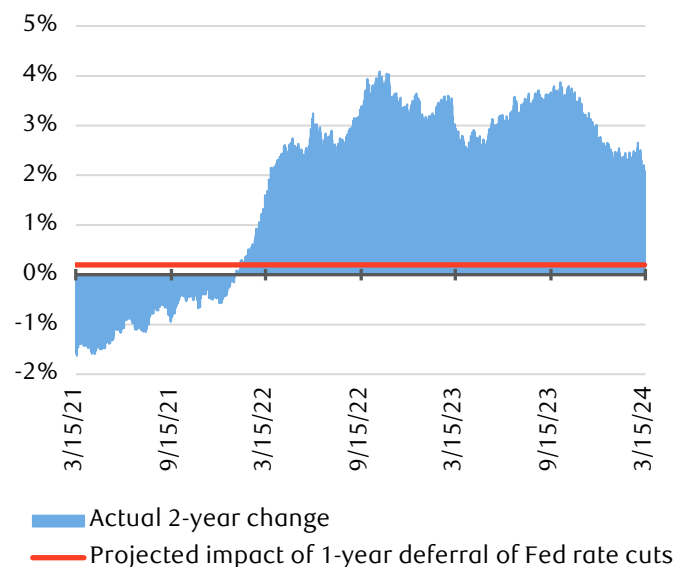
The informational bias toward short-term results can even turn perceived outcomes from negative to positive. Most regular readers of the financial press, for instance, probably worry about a potential market selloff caused by the Fed's failure to cut when expected. That may be a bad outcome for a hedge fund, but the economics look very different for a retirement saver.

A selloff means 401k or other routine contributions will buy more assets, so any Fed-induced pullback likely means more money when it matters. Higher interest rates also mean better reinvestment rates on upcoming portfolio cash flows; coupons and dividends will earn more, boosting realized yields. Finally, lower security prices allow investors to optimize their tax profile, swapping losing positions into new securities to delay or even eliminate taxes, subject to IRS restrictions.

The bottom line is that we believe there's only one account valuation that really matters—the valuation on the day the investment is liquidated. Intermediate readings are potentially important markers, but focusing on those data points is letting the tail wag the dog.

Rate cut timing is barely discernible against longer-term rate shifts

Change in 5-year U.S. Treasury yield



Note: Projected impact is based on fed fund futures-implied rates as of 3/1/24.

Source - RBC Wealth Management, Bloomberg

The Fed matters, but so do you

This is not to say that monetary policy is irrelevant or that macroeconomic conditions don't matter. The ideal blend of equities and fixed income will vary with prospects for a recession, and for investors with shorter time horizons—such as those in retirement or with a high emphasis on money market investments—rate cut timing may be important to their portfolios. Individuals may also have significant exposure to interest rate policy through their employment or personal business.

Our point isn't that everyone should ignore the Fed. Instead, our view is that the degree and type of attention paid to particular inputs varies with the individual. Just as a moderate risk investor is probably not going to be looking too deeply into exotic option pricing, a long-term investor can likely look past the first rate cut debate.

Not dead yet

John Maynard Keynes famously observed that “in the long run, we're all dead,” while Burton Malkiel and other economists have told us that short-term asset price moves are random. Knowing where you sit on the spectrum from quantum uncertainty to the inevitable future is a first step toward knowing what to focus on when thinking about markets.

UNITED STATES

Michael Roedl – Minneapolis

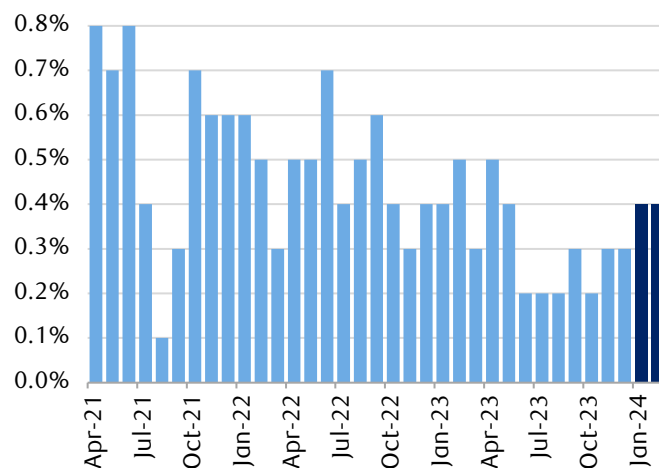
■ Inflation in the U.S. gained momentum in February for the second month in a row, reinforcing the Federal Reserve's cautious stance on rate cuts this year.

Headline inflation rose 0.4% in February, mostly led by higher gasoline prices, whereas food prices came in flat. Core inflation, which excludes food and energy prices, also advanced 0.4%, up from the 0.3% rise in January. Shelter and gasoline prices accounted for over 60% of the overall monthly increase, while prices for vehicles, airfares, and apparel posted their largest monthly advances since May 2022. After an already brisk inflation report from January, higher prices in February add more evidence that inflation remains persistent across the economy even as policy rates sit at 5.25%–5.50%, the highest levels in over 20 years.

■ **High-risk fixed income assets are extending gains on the year** as preferred shares lead the way returning 3.4% as of Wednesday's close, followed by leveraged loans and high-yield corporate bonds returning 2.2% and 1%, respectively. Even though markets continue to price in Fed rate cuts this year, it appears to us that investors remain optimistic considering how low-risk assets, such as Treasuries, investment-grade (IG) corporates, and municipal bonds, are underperforming in 2024. Apart from municipals barely scratching out positive gains this year, returns for Treasuries and IG corporates remain in negative territory as yields continue to drift higher from early January. Heavy issuance of Treasuries and IG corporate debt likely contributed to weaker performance, in our view, although IG corporate spreads (excess yield vs. Treasuries) still hover around the tightest levels in

U.S. inflation gained momentum in first months of 2024

Monthly change in the U.S. Consumer Price Index, excluding food and energy costs



Source - RBC Wealth Management, Bloomberg; data through 2/29/24

about two years at +93 basis points. Regardless, **we think the overall performance picture will eventually tilt toward low-risk assets in 2024**, but until then policymakers will be watching for more evidence that inflation is on a sustainable path toward 2%.

CANADA

Matt Altro & Richard Tan – Toronto

■ **The Canadian economy added 41,000 jobs in February, doubling consensus expectations. However, the labour force grew by 83,000, and thus the unemployment rate increased by 0.1% to 5.8%.** In our view, high interest rates and tepid economic growth could remain headwinds to hiring trends in the near term. Put differently, we believe the marginal worker will experience longer lead times before securing a job compared to the past one to two years. On a related note, wage growth has declined as bargaining power has begun to shift away from workers and towards employers, according to RBC Economics. Overall, **softening labour market conditions support the market's expectation that interest rates should decline throughout 2024.** RBC Economics believes the Bank of Canada will pivot towards rate cuts in the second half of the year and forecasts an overnight rate of 4.00% by year's end.

■ According to RBC Economics, **home sales picked up in February**, notably in Vancouver, Edmonton, Hamilton, and Montreal, driven in part by softening recessionary risks and improved optimism surrounding the Canadian economy. Meanwhile, the MLS Home Price Index climbed higher in February, with Toronto prices rising on a month-over-month basis for the first time in seven months. Montreal saw home prices rise as well, with median prices for both single-family homes and condo apartments increasing in February by 2.8% and 1.3% m/m, respectively. Overall, RBC Economics thinks **a substantial recovery in activity is unlikely to take place until interest rates fall more meaningfully**, potentially in the second half of 2024.

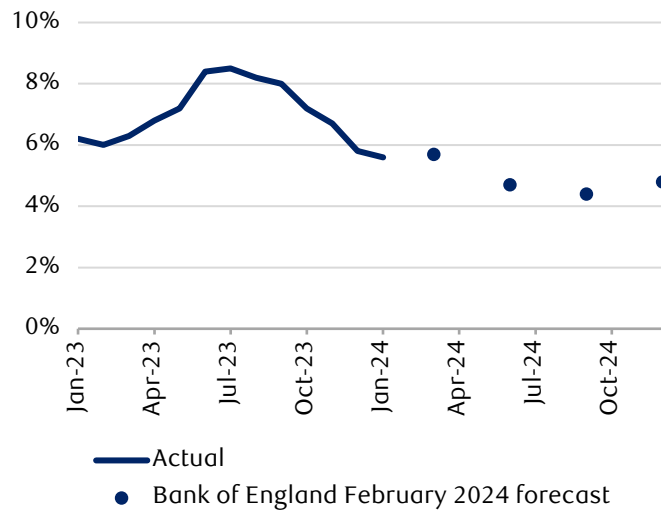
EUROPE

Rufaro Chiriseri, CFA – London

■ **UK GDP rebounded following two consecutive quarters of negative growth in H2 2023.** GDP expanded by 0.2% y/y in January, in line with economist consensus expectations. The largest contributor to GDP is attributed to the output in services, while industrial production was a notable laggard. RBC Capital Markets now estimates Q1 GDP growth of 0.2% from flat previously. We think growth is likely to be supported by the fall in utility bills when prices are reset in April, improved real incomes, and easing financing conditions.

Signs of further easing in UK wage growth

Average change in weekly earnings (whole economy)



Source - Bloomberg, Bank of England, UK Office for National Statistics; actual data through 1/31/24

■ **The unemployment rate rose slightly in January to 3.9% from 3.8% in December, though low response levels distort the data quality.** The labour market still seems tight, with signs of cooling. The private sector wage growth slowed to 6.1%. If the current trend in wage growth deceleration persists, it could undershoot the Bank of England's February Monetary Policy Report Q1 projection. While the pieces of the central bank puzzle in focus (labour market tightness, private sector pay growth, and services inflation) are trending positively, we expect the Monetary Policy Committee to remain cautious when it meets on March 21, but to acknowledge fading labour market risks.

■ **Markets have modestly shifted and are now expecting the Bank Rate to reach 4.53% from 4.47% at year-end 2023.** After a strong rally, Gilt yields drifted higher with the 10-year yield moving 8 basis points higher to settle at 4.04%.

■ **Eurozone industrial production slumped by 3.2% m/m in January and largely reversed December's 2.6% m/m expansion, thus exerting pressure on Q1 GDP and increasing risks of stagnation.** The decrease was largely driven by usually volatile data from Ireland which contracted 29% m/m in January after expanding 19.1% m/m in December. While there are chances of recovery later in the year, this may put the hopes of a bottoming out in economic activity at risk, in our view.

ASIA PACIFIC

Emily Li – Hong Kong

■ **South Korea is committed to ending the long-standing undervaluation of its stock market, according to the country's top financial regulator.** Its recently announced "Corporate Value-Up Program" aims to promote the participation of retail investors and encourage companies to rely on equities for wealth and capital generation. The government's focus on improving corporate valuation could mitigate the financial consequences associated with economic downturns and slowing growth. Key to the program's success, in our view, will be support from controlling shareholders of the major corporations, known as chaebols. In addition to the measures announced so far, the government is contemplating reducing taxes on distributed income as a means of advancing the development of capital markets and possibly increasing chaebol support.

■ **JPMorgan Chase & Co. has said it intends to maintain hiring in China to support the growth of its asset management business in the country.** The CEO of JPMorgan Asset Management (JPMAM) China stated in an interview that China's mutual fund industry continues to be a key market for global asset managers and provides a high level of growth certainty. JPMAM made a notable start to 2024 by launching an exchange-traded fund that tracks the new CSI A50 Index, attracting a substantial investment of two billion yuan in less than 10 days.

■ Shares of Xiaomi (1810 HK) experienced their largest intraday surge in over a year on March 12, following the company's announcement that it will commence sales of its highly anticipated electric vehicles (EVs) this month. **The Beijing-based electronics firm, known for its smartphones, has made a substantial investment with the goal of entering China's EV market,** which is currently dominated by Tesla (TSLA US) and BYD (1211 HK). Xiaomi announced it will introduce its SU7 series for purchase in 29 cities on March 28, without disclosing prices. The competitive EV landscape has become less appealing recently, as Tesla and BYD are engaged in a price war to attract Chinese consumers, and the industry as a whole is experiencing declining profit margins and slower growth.

MARKET Scorecard

Equities (local currency)	Level	MTD	YTD	1 yr	2 yr
S&P 500	5,165.31	1.4%	8.3%	34.0%	22.9%
Dow Industrials (DJIA)	39,043.32	0.1%	3.6%	22.7%	18.5%
Nasdaq	16,177.77	0.5%	7.8%	44.6%	26.0%
Russell 2000	2,071.71	0.8%	2.2%	18.8%	4.6%
S&P/TSX Comp	21,970.11	2.8%	4.8%	12.2%	2.4%
FTSE All-Share	4,243.71	1.9%	0.3%	3.1%	6.4%
STOXX Europe 600	507.33	2.6%	5.9%	14.6%	17.7%
EURO STOXX 50	5,000.55	2.5%	10.6%	22.1%	35.6%
Hang Seng	17,082.11	3.5%	0.2%	-13.3%	-16.9%
Shanghai Comp	3,043.84	1.0%	2.3%	-6.9%	-8.0%
Nikkei 225	38,695.97	-1.2%	15.6%	39.0%	53.8%
India Sensex	72,761.89	0.4%	0.7%	24.9%	31.0%
Singapore Straits Times	3,160.72	0.6%	-2.5%	0.9%	-2.7%
Brazil Ibovespa	128,006.05	-0.8%	-4.6%	24.1%	14.6%
Mexican Bolsa IPC	55,848.72	0.8%	-2.7%	5.4%	4.8%
Gov't bonds (bps change)	Yield	MTD	YTD	1 yr	2 yr
U.S. 10-Yr Treasury	4.190%	-6.0	31.1	61.7	219.8
Canada 10-Yr	3.424%	-6.6	31.4	65.5	143.1
UK 10-Yr	4.021%	-10.3	48.4	65.1	253.0
Germany 10-Yr	2.366%	-4.5	34.2	10.7	211.7
Fixed income (returns)	Yield	MTD	YTD	1 yr	2 yr
U.S. Aggregate	4.82%	0.8%	-0.9%	2.3%	-4.4%
U.S. Investment-Grade Corp	5.30%	1.0%	-0.7%	5.9%	-1.4%
U.S. High-Yield Corp	7.74%	0.7%	1.0%	12.9%	7.8%
Commodities (USD)	Price	MTD	YTD	1 yr	2 yr
Gold (spot \$/oz)	2,174.41	6.4%	5.4%	13.6%	9.4%
Silver (spot \$/oz)	25.01	10.3%	5.1%	14.7%	-3.3%
Copper (\$/metric ton)	8,560.70	1.9%	1.1%	-4.0%	-15.7%
Oil (WTI spot/bbl)	77.56	-0.9%	8.2%	3.7%	-29.1%
Oil (Brent spot/bbl)	83.97	0.4%	9.0%	4.0%	-25.5%
Natural Gas (\$/mmBtu)	1.66	-10.9%	-34.0%	-36.4%	-64.9%
Currencies	Rate	MTD	YTD	1 yr	2 yr
U.S. Dollar Index	102.7980	-1.3%	1.4%	-0.8%	3.7%
CAD/USD	0.7424	0.8%	-1.7%	1.9%	-5.4%
USD/CAD	1.3471	-0.8%	1.7%	-1.9%	5.7%
EUR/USD	1.0950	1.3%	-0.8%	2.0%	0.3%
GBP/USD	1.2799	1.4%	0.5%	5.1%	-1.8%
AUD/USD	0.6621	1.9%	-2.8%	-0.7%	-9.2%
USD/JPY	147.6600	-1.5%	4.7%	10.8%	25.9%
EUR/JPY	161.7000	-0.2%	3.8%	13.1%	26.4%
EUR/GBP	0.8556	0.0%	-1.3%	-2.9%	2.2%
EUR/CHF	0.9621	0.7%	3.6%	-1.7%	-5.6%
USD/SGD	1.3321	-1.0%	0.9%	-1.0%	-2.3%
USD/CNY	7.1868	0.0%	1.2%	4.9%	13.4%
USD/MXN	16.6676	-2.3%	-1.8%	-11.9%	-20.3%
USD/BRL	4.9720	0.0%	2.4%	-5.2%	-2.0%

Equity returns do not include dividends, except for the Brazilian Ibovespa. Bond yields in local currencies. Copper Index data and U.S. fixed income returns as of Tuesday's close. Dollar Index measures USD vs. six major currencies. Currency rates reflect market convention (CAD/USD is the exception). Currency returns quoted in terms of the first currency in each pairing.

Examples of how to interpret currency data: CAD/USD 0.74 means 1 Canadian dollar will buy 0.74 U.S. dollar. CAD/USD -1.7% return means the Canadian dollar fell 1.7% vs. the U.S. dollar year to date. USD/JPY 147.66 means 1 U.S. dollar will buy 147.66 yen. USD/JPY 4.7% return means the U.S. dollar rose 4.7% vs. the yen year to date.

Source - Bloomberg; data as of 3/13/24

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			Count	Percent
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