

Charting a Course: **Managing Tailwinds and Headwinds in Today's Economy**

Last week, Halifax, Nova Scotia hosted SailGP's first ever event in Canada. According to organizers, the event was a success, with some of the biggest crowds the circuit has seen watching the races. The impressive F50 catamarans move at speeds of up to 100 km/h and are akin to F1 racing cars on water with athletes who resemble fighter pilots rather than wind-swept adventurers of the seas. The global circuit now heads to New York City before the final race in San Francisco.

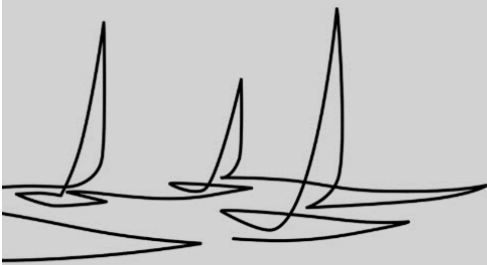
Tailwinds and headwinds play a major factor in these high intensity races as teams seek to position themselves to capture as many tailwinds in flight as possible, while battling the challenges of the headwinds in each race.

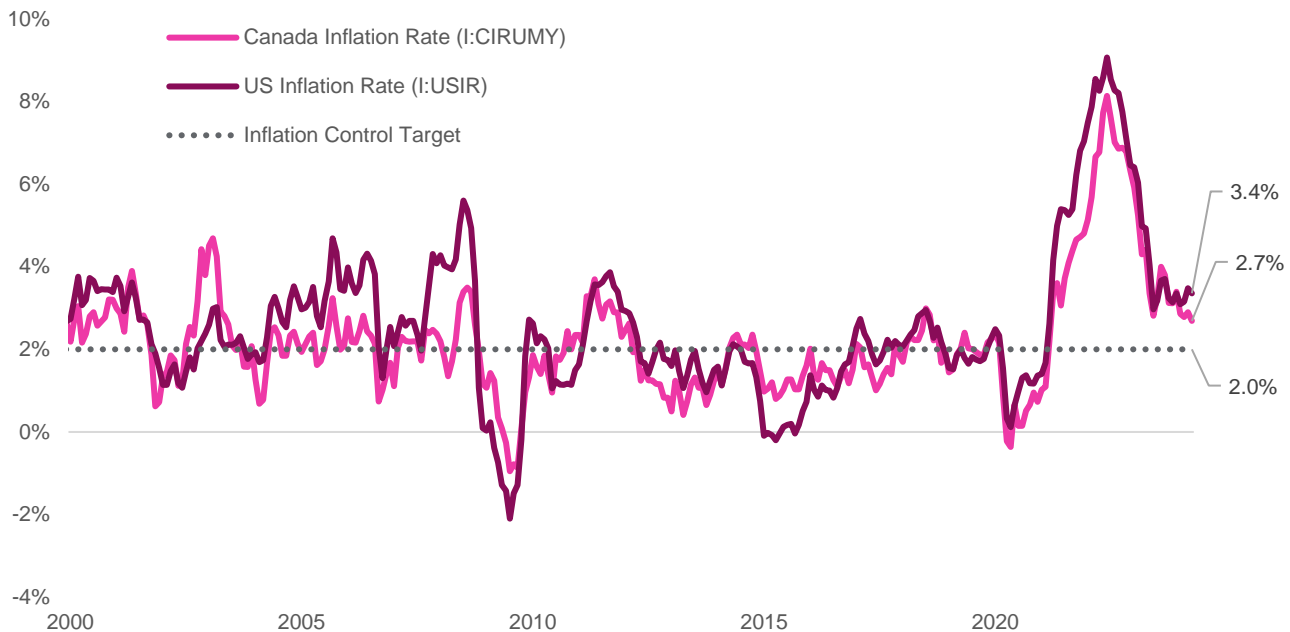
Much like in sailing, market tailwinds are factors that enhance investor confidence, drive market trends upwards, and generally support an environment conducive to rising stock prices. The all-too-familiar headwinds slow market sentiment, pose threats, and increase caution. For investors, it is our job to position portfolios to maximize the benefit of market tailwinds while limiting the dangers that market headwinds pose.

We highlight three key tailwinds pushing markets forward and three headwinds that must be taken into consideration.

Tailwind: Falling Inflation

Inflation in the US fell from a high of 9.1% to 3.4% in April, while in Canada, it is lower at 2.7%. Falling inflation allows central banks to cut rates and reduce the cost of capital. Although neither level has met the central banks' targets, signs suggest a likely rate-cutting regime in Canada and other parts of the world. Lower rates mean cheaper capital for companies and real estate developers, spurring investment, jobs, and growth.





Source: Y-Charts

Tailwind: Healthy Labour Markets

Labour markets remain healthy and resilient globally, with unemployment rates within acceptable levels. Along with moderating inflation, this suggests continued strength in consumer demand. This is likely to persist due to structural factors causing labour demand to outstrip supply. On the supply side, subdued growth in the working-age population and changes in labour force participation are significant factors. On the demand side, uncertain supply has led employers to hoard labour, creating a cycle of tightness. Consumer spending is the largest driver of developed economies.

Tailwind: Growth in Manufacturing

The Purchasing Managers' Index (PMI) increased to 50.3 last month, indicating growth in manufacturing (readings above 50 indicate growth). This ended 16 straight months of contraction in manufacturing. Supply chain constraints, a major issue after COVID, have subsided, with no significant delays from Houthi militant attacks on international shipping. Manufacturing is important as it signals future demand and serves as a major source of employment across many sectors.

Headwind: Tight Monetary Policy

Despite central banks around the world starting to cut rates, interest rates have been at their highest levels since 2001 for nine months. This is causing stress in interest rate-sensitive markets like Canadian housing, where over two-thirds of mortgage holders will renew by 2026. High rates raise concerns about underlying market weakness before a potential breakdown, similar to 2008 when rates were only 0.25% lower than today, leading to a \$2 trillion loss in global economic growth.

Headwind: Expansionary Fiscal Policy

The positive effects of recent monetary tightening could be undermined by ongoing fiscal spending, which is expected to persist through the US election period. This continued spending is likely to sustain higher inflation levels in the US, creating uncertainty about when rate cuts might begin. The conflicting pressures generate uncertainty in financial markets, as mixed signals complicate predictions about future economic conditions and policy direction, leading to increased market turbulence.

Headwind: Rising Geopolitical Tensions

While the conflicts in Palestine, Ukraine, Yemen, and the South China Sea may seem distant from the safety of our Canadian shores, they significantly impact global geopolitical stability. These conflicts result in increased security measures, trade disruptions, sanctions, and supply chain issues, alongside the tragic loss of lives and displacement of families. As we strive for lasting peace, these challenges hinder growth and prosperity for all, making confident investment difficult.

As investors, understanding and navigating the tailwinds and headwinds is crucial for strategic portfolio positioning. With falling inflation, healthy labor markets, and a recovering manufacturing sector providing momentum, there are positive signs for market growth. However, the challenges of tight monetary policies, expansionary fiscal measures, and rising geopolitical tensions cannot be overlooked. By staying informed and adaptive, we can better manage these factors to foster stability and confidence for our clients.

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