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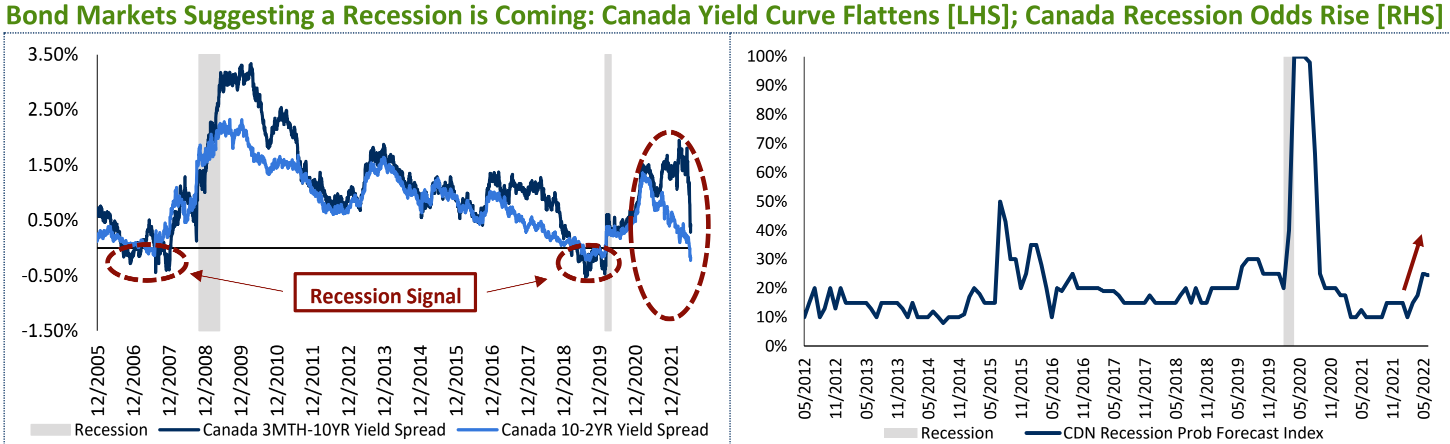
"Winter Is Coming"

It was House Stark of Winterfell that ruled the North from their fortress in Winterfell, in the hit fantasy TV series Game of Thrones. Ned Stark, also known as the Lord of Winterfell and Warden of the North, popularized the term "winter is coming", which became a common phrase used throughout the series to suggest that tougher times were ahead. While we too expect the upcoming winter to be a harsh one here in the North, in a similar vein, we believe investors should be prepared for a more challenging, volatile, and unpredictable economic and market climate heading into 2023.

Moreover, as we discussed in detail in our latest **Quarterly Asset Allocation report: Stop! Hammer Time**, we continue to anticipate the level of uncertainty to remain elevated as central banks continue to tighten policy despite the growing risks of a hard-landing/recession on the horizon. Canada's inflation rate continues to run hot and remains elevated with the latest reading of the Consumer Price Index (CPI) for June rising +8.1% year-over-year (YoY). We expect CPI readings for the remainder of the year to hover around +7% which is ~2-3x above the neutral range of ~2% that the Bank of Canada (BoC) has historically targeted - the level of inflation which is neither expansionary nor restrictive for the economy. But with the level of inflation well above this target range and labour markets still extremely tight, aggressive policy tightening efforts are currently the only tool the BoC can use to help bring down inflation towards more reasonable levels. However, we remind investors that changes in monetary policy (i.e., rate increases/decreases) not only have a delayed impact on the real economy, but they also do very little to help alleviate temporary and/or structural inflationary impulses associated with China lockdowns, Saudi/Texas drilling, quarantines, refining capacity, war, supply-chain on shoring, etc. We expect this aggressive pace of tightening to weigh heavily on domestic demand, with measures of spending growth falling sharply including with residential investment, which we believe will fall back to pre-pandemic levels.

The bond market, which historically has been a fairly accurate predictor of recessions, is currently signaling a higher risk of a recession for the Canadian economy over the next 12 months. We see the odds of a recession increasing from here, especially if the BoC continues to tighten monetary policy aggressively into year-end.

Bond Markets Suggesting a Recession is Coming: Canada Yield Curve Flattens [LHS]; Canada Recession Odds Rise [RHS]

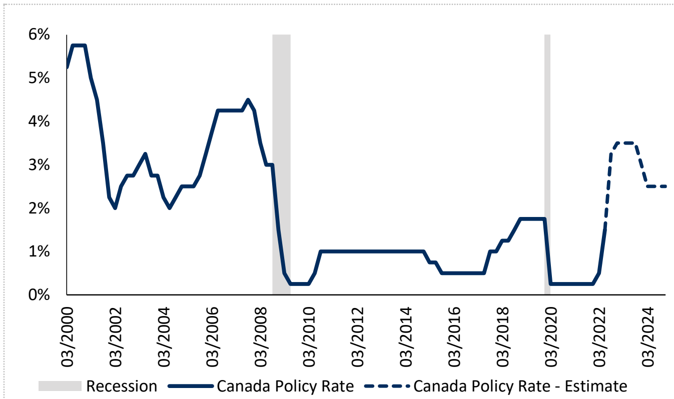


Source: FactSet; Raymond James Ltd.; Yield spread data as of July 22, 2022; Canada Recession Probability as of June 30, 2022.

"There is only one thing we say to ~~death~~ recession: Not today."

While there has been much talk of a recession already underway in Canada, we tend to disagree with this view, though as we noted above, the odds have risen considerably over the past several months. In fact, investors are currently pricing in that the BoC will continue to raise overnight rates to 3.5% (up from 2.5% today), pause, and then begin slashing rates beginning in 2023 as the recession arrives.

What's Priced In - BoC to Slash Rates in 2023 as the Recession Arrives



Source: Capital Economics; Raymond James Ltd.; Date as of July 24, 2022.

Confusing investors further on whether or not a recession has arrived is the sell-off in the S&P/TSX index since the April 2022 peak. This decline has been rather swift with the broad market down -13.3% as of July 22. Comparing this performance to the past two recessions as defined by C.D. Howe Institute, the recent performance of the S&P/TSX has been much larger and has occurred more quickly than during both the 2008/2009 recession and the COVID-19 recession in 2020.

S&P/TSX Performance From 2022 Peak vs. Recessions

Performance	Financial Crisis (Oct 2008 - May 2009)	COVID-19 (Feb 2020 - Apr 2020)	2022 Sell-off from Peak (April 2022 - Current)
Canada S&P/TSX Composite	**8.7%**	**-8.5%**	**-13.3%**
Communication Services	-17.3%	-4.5%	-10.5%
Consumer Discretionary	-6.7%	-10.7%	-4.8%
Consumer Staples	3.7%	-1.0%	-2.0%
Energy	9.5%	-21.9%	-6.3%
Financials	-0.4%	-16.9%	-13.1%
Health Care	-5.1%	-16.6%	-48.2%
Industrials	-7.0%	-5.5%	-6.6%
Information Technology	34.6%	16.8%	-26.9%
Materials	52.0%	19.7%	-29.5%
Real Estate	-5.8%	-23.6%	-13.4%
Utilities	-9.9%	-6.2%	-2.8%

Source: FactSet; Raymond James Ltd; Data as of July 22, 2022. Financial Crisis: October 2008 - May 2009; COVID-19: February 2020 - April 2020; 2022 Sell-off: April 2022 – July 22, 2022.

Moreover, according to the C.D. Howe Institute – considered Canada's most influential and independent think tank **- they define a recession as broadly speaking, a pronounced, persistent, and pervasive decline in aggregate economic activity. In other words, to identify a recession three dimensions need to be considered simultaneously: amplitude, duration, and scope – or how widespread is the downturn.**

While markets have sold off aggressively, with signs of weakness/cracks emerging across several corners of the economy, we do not believe factors present today meet this broad definition of a recession **yet**. That said, we find it interesting that markets and investors have gotten ahead of themselves with investors already discounting a recession. We note, valuations for the broad S&P/TSX index is trading in line with valuations observed during the past two recessions.

Sector Forward P/E: Current vs. Recessions

Median PE NTM (Absolute)	Current (7/22/2022)	Recession*	Premium (+) / Discount (-) vs. Recession
Canada S&P/TSX Composite	**11.5**	**11.2**	**0.3**
Communication Services	17.9	11.7	6.2
Consumer Discretionary	13.0	11.1	1.9
Consumer Staples	16.3	13.6	2.7
Energy	7.9	14.4	-6.5
Financials	9.6	8.3	1.2
Health Care	15.7	12.6	3.0
Industrials	24.2	10.1	14.0
Information Technology	32.2	13.7	18.5
Materials	9.5	15.5	-6.0
Real Estate	15.2	11.7	3.5
Utilities	24.0	15.2	8.7

Source: FactSet; Raymond James Ltd.; Date as of July 22, 2022; *Recession: recession periods identified by C.D. HOWE. October 2008 - May 2009; February 2020 - April 2020.

As we have noted since the beginning of the year, staying **selective**, especially during this period (mid-to-late cycle) in the broader economic cycle, is extremely important. **We continue to prefer sectors that are trading at a discount (green) over those trading at a premium (red) as noted in the above chart.** Moreover, identifying good quality stocks within these sectors may offer investors lower risk to the downside from further valuation declines/multiple compression and/or from downward revisions to earnings as the economy and even global economies slow in the months ahead. On a stock-specific level we continue to prefer high-quality businesses trading at attractive valuations, with durable earnings and flows, which are led by strong and reputable management teams. **Stay vigilant, opportunistic, and long-term focused……………………………………………. as winter is coming!**

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