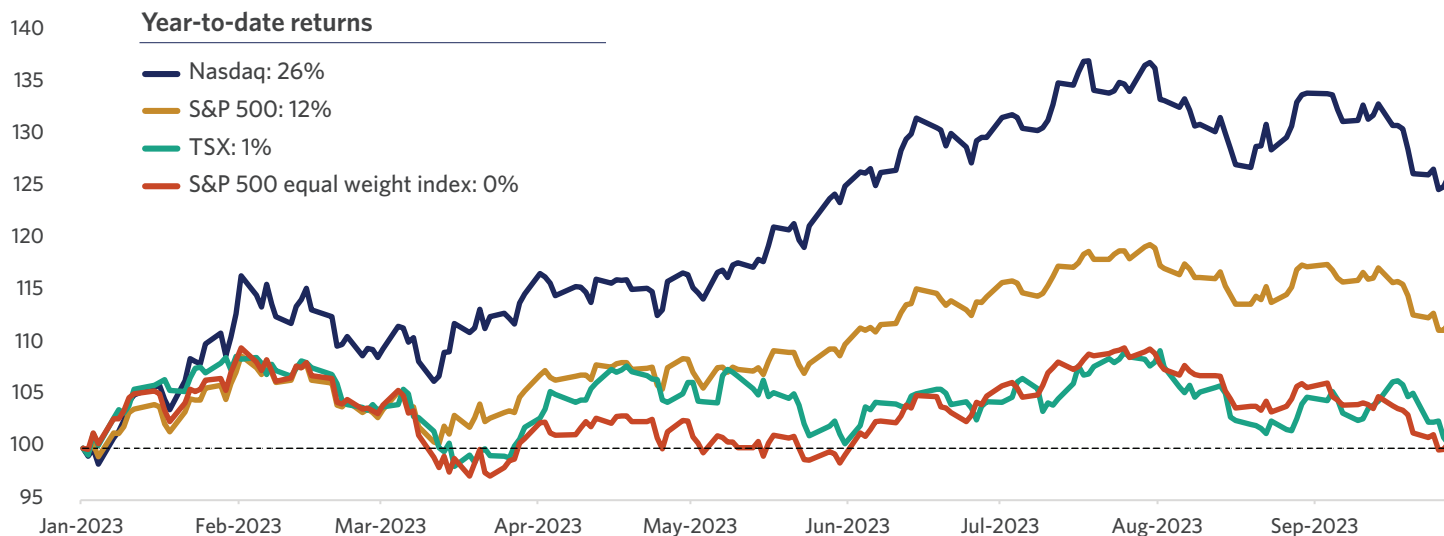


Quarterly market outlook: **Fourth quarter 2023****A few stocks have driven this year's gains, but leadership could broaden out**

Source: Bloomberg. 2023 stock market index performance as of 10/5/2023
Past performance is not indicative of future results.

Equity outlook

High interest rates on the back of determined central banks took some wind out of the market's sails in Q3. However, we believe moderating inflation, recovering corporate profits, and an approaching end to the BoC's and Fed's rate hikes can support a positive outlook for the remainder of the year, especially for parts of the equity market that have lagged.

Earnings recovery provides support — Higher material and labour costs have pressured corporate profits, with TSX and S&P 500 earnings declining about 8% from last year's peak. But this decline was not as bad as feared since corporate revenue has continued to grow, driven by a resilient economy. After three consecutive quarters of declines, Q3 will likely mark a positive inflection point, with earnings poised to increase from a year ago. We expect earnings to rebound further in 2024, validating the broader uptrend in stocks.

High interest rates pose valuation headwinds — Valuations for U.S. large-cap stocks have increased over the past year, driven primarily by mega-cap tech stocks, which have benefited from enthusiasm around artificial intelligence (AI). With interest rates likely staying higher for longer, valuations might have a hard time expanding further from here. This is why we think earnings growth will have to do the heavy lifting to drive markets higher. Domestically, unlike the U.S., TSX valuations are below historic averages but might also have a hard time expanding as Canadian economic growth softens.

Opportunities might lie beneath the surface — Outside U.S. mega-cap tech, valuations are more reasonable, presenting an opportunity for regional and sector leadership to broaden over time. The S&P 500, which is heavily influenced by the 10 largest companies based on market capitalization, has gained about 12% since the start of the year. But the S&P 500 Equal Weight Index, which assigns the same weight to all the stocks that are included, has stayed flat for the year, highlighting the narrow participation. Other lagging segments of the equity market include small-cap and overseas stocks as well as value-style investments, all of which have the potential to catch up.

► Action for investors

We recommend considering a neutral allocation in equities, staying close to your long-term strategic allocations and using pullbacks to diversify across lagging asset classes. We favour increased allocations within consumer discretionary and reduced allocations to financials.

Investing in equities involves risks. The value of your shares will fluctuate and you may lose principal.