**Monthly Market Commentary**
November 2022

# Markets celebrate Fed's interest in slowing rate hikes.

- Most equity markets ended November in positive territory, with emerging markets outperforming their developed-market counterparts. Stocks globally received a major boost on the last day of the period given news that the U.S. Federal Reserve will likely begin slowing the pace of interest-rate hikes in December.
- Fixed-income asset classes also posted gains over the month as bond yields moved lower (yields and prices have an inverse relationship).
- While the collective effort of major central banks to tame inflation may prove successful, a global recession may still occur—with Europe and the U.K. more vulnerable than the U.S. and Canada to a downturn.

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**Economic Backdrop**

Most equity markets finished November in positive territory following a strong rally during the previous month. Emerging-market stocks outperformed their developed-market counterparts, led by mainland Chinese equities. Regionally, emerging markets in Asia and Europe generated the world's strongest equity returns in November, while the Asia-Pacific region also performed well. North America lagged as U.S. stocks posted relatively smaller gains.

Yields on U.S. Treasury securities with maturities of two years or greater fell in November (yields and prices have an inverse relationship). However, the 2-to-10-year yield curve remained inverted (short-term rates exceed long-term yields) and widened by 0.29% to 0.70%. U.K. gilt yields declined in the intermediate and long segments of the curve; they moved modestly lower for maturities of less than three years. Eurozone government bond rates decreased for all maturities of five years or greater, while yields rose for maturities of four years or less—thereby inverting the 2-to-10-year curve.

Fixed-income asset classes posted gains in November as intermediate- and long-term interest rates moved lower. U.S. investment-grade corporate bonds led the rally as investors turned to high-quality securities; mortgage-backed securities (MBS) and U.S. Treasurys—the most rate-sensitive areas of the market—also garnered positive returns.

Regarding the commodities market, Brent and West Texas Intermediate crude-oil spot prices were down in November by 6.3% and 6.9%, respectively, on fears that China may reinstate COVID-19 restrictions and trigger a decline in demand for oil in that country. The NYMEX natural gas price rose by 9.0% amid concerns that existing supply constraints caused by Russia's ongoing aggression toward Ukraine will intensify once the colder winter weather sparks a surge in demand. Wheat prices decreased by 9.8% as Russia agreed to renew a deal brokered with the United Nations (UN), Ukraine, and Turkey that allows for the shipment of Ukrainian grain through the Black Sea, alleviating concerns about an international food shortage.

Rishi Sunak faced his first domestic crisis as U.K. prime minister and Conservative Party leader just weeks after succeeding Liz Truss in late October, when tens of thousands of health care workers employed by the National Health Service (NHS) voted for industrial action. The Royal College of Nursing (RCN) trade union announced that nurses plan to strike on December 15 and 20—the union's first such action in its century-long existence—over compensation, working conditions, and patient safety. This came as the U.K. government failed to meet their demands for pay increases of 5% over inflation (which surpassed 11% in October). Members of trade unions that represent ambulance workers—including emergency call handlers, technicians, and paramedics—voted to strike over similar issues. Negotiations with the unions have proven especially challenging given that U.K. Chancellor Jeremy Hunt is seeking to reduce the government's £55 billion (roughly US$66 billion) deficit through drastic spending cuts. Under the current fiscal austerity plan, a gross domestic product (GDP) growth rate of 2% would result in savings of approximately £23 billion (about US$27.6 billion) for the U.K. government by the 2027-to-2028 fiscal year.

Ukraine's military regained control of the southern city of Kherson as Russian Defense Minister Sergei Shoigu ordered his troops to retreat from what had been sole regional Ukrainian regional capital that Moscow held since invading earlier this year. This is a major setback for Russian dictator Vladimir Putin.

Chinese President Xi Jinping's administration faced anti-government demonstrations across the country in response to its zero-tolerance policy regarding COVID-19. Local police forces moved quickly to diffuse the protests, which China's National Health Commission (NHC) blamed on local governments; a spokesperson for the NHC stated that some local authorities "take a one-size-fits-all approach, and take excessive policy steps that have neglected the demands of the public." Xi's administration announced an initiative to accelerate vaccinations for elderly citizens in an effort to ease the COVID-19-induced restrictions.

In Latin America, Luiz Inácio Lula da Silva (Lula) of the progressive Workers' Party won Brazil's presidential election by a narrow margin over the conservative incumbent, President Jair Bolsonaro. Lula previously served two terms as Brazil's president from 2003 to 2011.

**Central Banks**

- The Bank of Canada (BoC) raised the policy interest rate by 0.50%, to 4.25%, on December 7 and continued reducing the amount of bonds it holds on its balance sheet—a policy known as quantitative tightening. This was the seventh consecutive rate hike, bringing the cumulative increase for 2022 to 4.00%. The BoC's Governing Council noted that core inflation levels appeared to be easing but were still too high. Further, the council reiterated its commitment to bring inflation down to 2%.

- In early November, the Federal Open Market Committee implemented another 0.75% increase in the federal-funds rate—bringing it to a range of 3.75% to 4.0%, which will result in higher borrowing costs for consumers and businesses. Fed Chair Jerome Powell indicated at the end of the month that he believes the central bank will likely begin to slow the pace of interest-rate hikes in mid-December as recent data point to easing inflation. However, he also said there remains uncertainty with regard to inflation and that "History cautions strongly against prematurely loosening policy."

- The Bank of England's (BOE) Monetary Policy Committee raised its benchmark interest rate by 0.75% to 3.0% in early November, yet cited the need to reduce the U.K.'s historically high inflation rate. The BOE also noted, "The labour market remains tight and there have been continuing signs of firmer inflation in domestic prices and wages that could indicate greater persistence."

- The European Central Bank's (ECB) applicable rates for its third targeted longer-term refinancing operation (TLTRO III,) aligned with its deposit-facility rate on November 23. The lending facility was originally established to foster credit availability but has essentially enabled bank subsidies as interest rates have risen, prompting the ECB's action.

- The Bank of Japan (BOJ) did not meet in November. At its meeting in late October, the central bank maintained its short-term interest rate at -0.1%, and the 10-year Japanese government-bond (JGB) yield target held near 0%. The BOJ has continued to offer purchases of 10-year JGBs at 0.25% in an effort to keep yields within its acceptable range.

**Economic Data (unless otherwise noted, data sourced to Bloomberg)**

- According to Statistics Canada, the rate of inflation decelerated (as measured by the change in the Consumer Price Index (CPI)) to 0.7% for October, and 6.9% for the one-year period. Although the year-over-year increase matched September's rise, the one-month jump in prices was the largest since June. Gasoline prices—despite some weakness in prior months—were up over 9%, as price increases eased in other sectors. Consumer prices remain elevated and well above the preferred BoC range for inflation. Producer prices had been easing, but once again turned higher. The Industrial Product Price Index (IPPI) was up 2.4% in October, while the Raw Materials Price Index (RMPI) rose 1.3%. On a year-over-year basis, the IPPI climbed 10.1% and the RMPI increased 9.0%. Prices for petroleum and crude energy product were generally higher. The labour market added a meager 10,000 jobs in November, while the unemployment rate ticked down to 5.1%.

- The Commerce Department's Personal Consumption Expenditures (PCE) Index—the Federal Reserve's (Fed) preferred inflation measure as it excludes volatile food and energy prices—slowed in October to 0.3% from 0.6% for the month and to 6.3% from 6.6% for the 12-month period. The U.S. employment situation remained robust. The U.S, Department of Labor reported that payrolls expanded by a larger-than-expected 263,000 during November, while the unemployment rate was unchanged at 3.7%. In October, average hourly earnings gained 0.6% for the month and 5.1% over the 12-month period. The U.S. economy continued to improve in the third quarter, expanding at an annualized rate of 2.9% (up from the Commerce Department's initial estimate of 2.6%)—after contracting at annualized rates of 1.6% in the first quarter and 0.6% in the second quarter. The Institute for Supply Management's manufacturing purchasing managers' index (PMI) declined in November by 1.2% to 49.0%, ending 29 consecutive months of expansion as it reached its lowest level since May 2020. A PMI reading below 50% indicates contraction.

- Consumer prices in the U.K. increased in October by 2.0% for the month and by 11.1% for the 12-month period—the highest year-over-year inflation rate since the National Statistics series began in January 1997. According to the Office for National Statistics, U.K. GDP decreased 0.2% over the three-month period ending September, up slightly from the 0.1% decline in the second quarter of this year. U.K. manufacturing activity contracted for the fourth consecutive month in October after growth began to slow in May. Activity in the U.K. services sector contracted for the second straight month in November after expanding at a modest-but-healthy pace through the summer and leveling off in September.

- Eurozone consumer prices dipped in November by 0.1%, the first decline since mid-2021, and slowed to a 10.0% year-over-year increase from a 10.7% gain in the 12-month period ending October. A contraction in eurozone manufacturing activity that began in July continued in November, though there was modest improvement from the previous month. Eurozone services activity declined for the fourth consecutive month in November after expanding for 17 straight months between March 2021 and July 2022. Eurozone economic growth slowed in the third quarter to 0.2% from 0.8% over the three-month period and to 2.1% from 4.3% in the year over year.

**Market Impact (Referenced Index Returns are in CAD)**

Global developed equity markets posted strong gains led by emerging markets (in particular China) and developed markets in Europe and Asia. Domestic equities lagged, but still produced solid performance as materials and information technology set the pace, while utilities and healthcare lagged. Canadian smaller companies modestly outperformed larger companies. Despite ceding their recent market leadership, U.S. equities were also firmly positive.

Fixed-income markets rallied on the expectations that central banks may be nearing the end of the current rate hiking regime. Corporate bonds, real-return bonds and government debt all posted strong gains, meanwhile, short-term bonds and residential mortgage securities were also positive. Riskier U.S. high-yield bonds were up modestly. The gains in fixed-income markets were a welcome reprieve for investors struggling with what may wind up being the worst calendar year for bonds on record.

**Index Data (November2022)**

- The S&P/TSX Composite Index was up 5.54%.
- The FTSE Canada Universe Bond Index returned 2.81%.
- The S&P 500 Index, which measures U.S. equities, gained 4.94%.
- The MSCI ACWI (Net) Index, used to gauge global equity performance, rose 7.10%.
- The ICE BofA U.S. High Yield Constrained Index, representing U.S. high-yield bond markets, returned 1.83% (currency hedged) and 1.24% (unhedged).
- The Chicago Board Options Exchange Volatility Index—a measure of implied volatility in the S&P 500 Index that is also known as the “fear index”—decreased from 25.88 to 20.58.
- WTI Cushing crude oil prices—a key indicator of movements in the oil market—moved lower from US$86.53 to US$80.55 a barrel to end November.
- The Canadian dollar was little changed at C$1.36 per U.S. dollar. The U.S. dollar was generally weaker versus the world’s other major currencies; it ended November at US$1.03 versus the euro, US$1.19 against sterling and at 139.54 yen.

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