Quarterly Market Commentary
Second Quarter 2023

Stocks grab a lead at the half.

- Global equity markets put up big scores in both the second quarter and the first half of 2023, amid periods of volatility. The markets were buoyed by a sharp rally in tech stocks, investors' optimism regarding generally favourable economic data, as well as the resolution of the politically charged debt-ceiling standoff in the U.S. These positive contributors offset concerns about central bank monetary policy and the stability of U.S. regional banks. Although domestic equities were positive, they trailed many other markets.
- Global fixed-income assets saw mixed performance over the quarter. Canadian and U.S. bond yields rose across the curve, most notably in the short and intermediate segments.
- SEI does not dispute the fact that inflation will continue to decelerate, especially given the current weakness in energy and goods prices. We maintain our view that inflation pressures will remain persistent in labour-intensive service industries, at least until some slack opens up in the labour markets and spending by households fades more dramatically. Canada seems to have made more progress taming inflation than most other countries.

SEI's Domestic View

Former U.S. President Harry Truman is reported to have asked for a one-armed economist so he would no longer have to listen to his advisors express their views in terms of "on the one hand, but on the other hand." While the story may be apocryphal, the sentiment is understandable and no less applicable today, given the confusing cross-currents at work in the global and Canadian economies. These domestic cross-currents persisted through the second quarter of 2023, keeping Canadian businesses, consumers and investors on edge. On the positive side, economic growth was solid even when adjusted for inflation, the labour market remained quite healthy, and there were signs that inflation may finally be easing meaningfully. However, soggy leading economic indicators, a manufacturing recession, and renewed Bank of Canada (BOC) rate hikes, alongside longstanding concerns about household debt levels and the potential for a downturn in housing activity, tempered any enthusiasm.

On the one hand, Canada's economic performance remained quite solid among advanced economies. The labour market has also remained quite healthy. Claims for employment insurance are still well below levels seen during COVID-19 lockdowns and in line with their long-term average, while the unemployment rate is still at historic lows. Further, Canada has made some of the most significant progress against inflation among advanced economies, at least for the kinds of industrial or "factory gate" materials captured in producer price indexes.

On the other hand (sorry, Harry!), Canada's manufacturing sector (like many around the world) has continued to struggle, with the S&P Global Canada Manufacturing PMI® reporting subdued demand and further declines in output and new orders in June. Leading economic indicators are suggesting there may be further trouble ahead for the Canadian economy. And while falling producer prices may bode well for the broader inflation picture eventually, demographic and wage pressures could help keep a floor under inflation pressures in more services-oriented areas of the economy. Meanwhile, prices for crude goods such as commodities may be finding a bottom at current levels. With lingering concerns around the inflation outlook, the BOC resumed its rate-hiking cycle after a several-month pause.

This has led to an even more dramatic inversion of the yield curve, which many economists view as a harbinger of recession. The recession question is obviously the one that's causing anxiety for businesses, consumers and investors. While prevailing consensus seems to be that a recession might start in the back half of this year or in 2024, it's not clear how deep (or shallow) or how prolonged (or short-lived) a downturn might be.

For investors, the name of the game hasn't changed despite the cloudy economic outlook: Ensure that your portfolio provides an appropriate level of expected risk for your financial objectives and use diversification to your advantage.

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SEI's Global View

Economists have been spending much of their time this year arguing when or if economic growth, inflation, corporate profits, interest rates and equities will peak. Optimists and pessimists alike have been confounded by the ebb and flow of the data and the gyrations of the financial markets. Waiting for a decisive break in the U.S. economy, for example, has been akin to Samuel Beckett's play, "Waiting for Godot," as the two main characters engage in discussion of a variety of topics while waiting for the eponymous Godot, who never arrives.

In general, input-price inflation has decelerated dramatically. Canada's industrial producer price index has registered an outright decline in its price level, with a year-over-year change of -6.3% through May. The Eurozone's producer-price index (PPI) has witnessed the sharpest deceleration, falling from a peak year-over-year rate of 43% through August 2022 to an April 2023 reading of just 1%. By contrast, the improvement in producer prices has been less dramatic in Japan (still rising at a 5.1% year-over-year pace as of May), although the country has logged a steep deceleration from earlier this year. These year-over-year inflation PPI readings should continue to show improvement in the months immediately ahead as extremely high monthly readings a year ago fall out of the calculation. .

The good news at the corporate level is feeding only slowly down to the consumer. This is especially true for core inflation, which excludes food and energy prices. Inflation is still accelerating in both the U.K. (reaching 7.1% in May) and in Japan (+2.7%). Improvement in the U.S. and the euro area has been modest, with annual core inflation running at 5.3% and 6.1%, respectively, in May. Only Canada has recorded significant progress in its core inflation rate, declining from 6.0% in June 2022 to 3.7% as of May 2023.

On a longer-term basis, we believe that demographic shifts are likely to keep labour markets tighter than has been the case at any point since the baby boomers–who were born between 1946 and 1964–first made their presence felt in the workforce in the 1970s. The new focus on supply-chain resiliency, reduced dependence on China as a manufacturing hub, the transition away from relatively cheap fossil-fuel energy to greener but more expensive sources of power, and the likelihood of significantly higher corporate taxes and financing costs in the years ahead, all suggest to us that inflation will tend to settle at 3% or more in advanced industrial economies instead of the previous norm of 2% or less.

Persistent inflation and ongoing labour-market tightness have forced most major developed-country central banks to keep raising their benchmark interest rates. The U.S. Federal Reserve (Fed), the Bank of Canada, and the European Central Bank (ECB) already have benchmark rates that match or exceed the peak recorded in 2008. We think it's likely that the Bank of England will soon join this group.

Although the Federal Open Market Committee (FOMC) chose to keep the funds rate unchanged at its June 2023 meeting, the central bank warned that it may well raise the federal-funds rate by another 25 basis points (0.25%) at its next meeting in July. It also left open the possibility of yet another rate hike after that, which Fed Chair Jerome Powell underscored during his recent Congressional testimony. It wasn't too long ago that markets were pricing in a June 2023 peak in the federal-funds rate, followed by at least three rate cuts before the end of 2023. Those cuts have now been taken out of the equation. As of the end of June, the CME Group's FedWatch Tool implied an 87% probability of a 25-basis point increase, into the 5.25%-to-5.50% range, at the next FOMC meeting on July 26. The odds of the first rate cut have now been pushed out to January 2024, with a year-end 2024 implied rate at roughly 4%.

SEI does not dispute the fact that inflation will likely continue to decelerate, especially given the current weakness in energy and goods prices. It is only a question of timing and end point. We continue to think that inflation pressures will remain persistent in labour-intensive service industries, at least until some slack opens up in the labour markets and spending by households fades more dramatically.

The rally in U.S. equities did, in fact, broaden in June, but the valuation in the market again is a problem. The price-to-earnings ratio of the broad-market S&P 500 Index has been on the rise this year, now almost reaching 19 times analysts' estimated earnings for the next 12 months. This expansion in the multiple on forward earnings has occurred despite the additional monetary tightening by the Fed and other central banks and a rebound in bond yields from the dip that took place following the mid-March bank panic.

There is some good news: Forward earnings estimates have ticked higher lately. The bad news: This upturn in expected forward earnings over the next 12 months is not likely to last if a recession materializes later this year or in 2024. The overall market also appears to be overvalued relative to today's bond yields. If earnings experience a substantial contraction, history suggests that stock valuations also will fall.

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Economic Backdrop

Global equity markets put up big scores in both the second quarter and the first half of 2023, amid periods of volatility. The markets were buoyed by a sharp rally in tech stocks, investors' optimism regarding generally favourable economic data, as well as the resolution of the politically charged debt-ceiling standoff in the U.S. These positive contributors offset concerns about central bank monetary policy and the stability of regional banks. Developed markets outperformed emerging markets during the quarter.

North America was the top-performing region among developed markets for the quarter due primarily to strength in the U.S. Pacific ex Japan was the primary market laggard due to weakness in New Zealand and Singapore. Eastern Europe led the emerging markets, benefiting mainly from strong performance in Hungary, Poland, and Greece. Latin America also performed well during the period. Conversely, emerging markets in the Far East posted negative returns, hampered by a downturn in China amid investors' worries about relatively weak economic data.

President Joe Biden and Kevin McCarthy, Speaker of the U.S. House of Representatives, reached an agreement on raising the $31.4 trillion debt ceiling during the last week of May. Both the U.S. House of Representatives and the Senate passed the legislation–the Fiscal Responsibility Act–by wide margins, with strong support from Republicans and Democrats. The bill suspends the debt ceiling through January 1, 2025, maintains non-military spending close to current levels for the 2024 fiscal year, which begins in October, and implements a 1% cap on increases in non-military spending for the 2025 fiscal year. The fast-track approval of the legislation, which Biden subsequently signed into law, enabled the government to avoid a potential default on its debt on June 5, the "X-date" on which Treasury Secretary Janet Yellen had warned that the U.S. would no longer be able to meet its financial obligations.

The Fed maintained the federal-funds rate in a range of 5.00% to 5.25% following its meeting in mid-June. During an appearance before the U.S. House of Representatives Committee on Financial Services the following week, Fed Chair Jerome Powell stated, "Nearly all [Federal Open Market Committee] participants expect that it will be appropriate to raise interest rates somewhat further by the end of the year…We will continue to make our decisions meeting by meeting, based on the totality of incoming data and their implications for the outlook for economic activity and inflation, as well as the balance of risks. We remain committed to bringing inflation back down to our 2 percent goal and to keeping longer-term inflation expectations well anchored."

Powell attended the Banco de Espana Fourth Conference on Financial Stability in Madrid, Spain, toward the end of June to discuss the instability in the U.S. banking sector earlier this year. The Fed chair commented, "The banking system remains sound and resilient, deposit flows have stabilized, and strains have eased." He acknowledged that the failures of several regional banks "were painful reminders that we cannot predict all of the stresses that will inevitably come with time and chance. We therefore must not grow complacent about the financial system's resilience."

U.S. regional bank stocks continued to experience significant volatility during the second quarter, and ended the period with notable losses. U.S. regulators took control of California-based First Republic Bank. The California Department of Financial Protection and Innovation–which oversees the operations of state-licensed financial institutions, including banks and credit unions–issued a statement announcing that it had taken over the bank and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. The FDIC subsequently accepted J.P. Morgan Chase Bank's bid "to assume all deposits, including all uninsured deposits, and substantially all assets of First Republic Bank." The KBW Regional Banking Index, which tracks the performance of publicly traded U.S. regional banks and thrifts, fell 6.7% in the second quarter, and was down more than 27% for the year to date.

The performance of global fixed-income assets was mixed over the second quarter. High-yield bonds recorded positive returns and were the top performers within the U.S. market for the period. Corporate bonds, mortgage-backed securities (MBS) and U.S. Treasurys ended the quarter in negative territory. U.S. Treasury yields moved sharply higher across the curve during the quarter. Between late April and late May, yields on 1-month U.S. Treasury bills (T-bills) with maturities close to the U.S. government's "X-date" of June 5 for the default on its financial obligations climbed 167 basis points (1.67%) to 6.02%—the highest level since the introduction of the 1-month T-bill in July 2001—before tumbling to 5.28% over the last two days of the month following the announcement of a potential agreement on raising the debt ceiling. The yield on the 1-month T-bill ended the quarter at 5.24%. Investors had demanded higher yields as compensation for the additional risk that the U.S. government could default on its debt in early June. The yields on 2-, 3-, 5-, and 10-year Treasury notes climbed 0.81%, 0.68%, 0.53%, and 0.33%, respectively, over the second quarter. The spread between 10- and 2-year notes widened from -0.58% to -1.06% during the three-month period, further inverting the yield curve.

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Global commodity prices moved lower during the second quarter. The West Texas Intermediate (WTI) crude-oil spot price and the Brent crude oil price fell 6.6% and 5.6%, respectively, in U.S. dollar terms, hampered by investors' concerns about waning demand for oil. The 25.1% rise in the New York Mercantile Exchange (NYMEX) natural gas price for the quarter was attributable to investors' expectations that a hot summer season and the possibility of hurricanes in the U.S. will boost demand. The wheat price was down 6.0% over the quarter, as Ukraine and Russia renewed an agreement that allows the shipment of Ukrainian grain through the Black Sea, increasing supply. The wheat price rallied briefly in late June after the Wagner Group, a Russian paramilitary organization that had been fighting in Ukraine on behalf of the Russian government, organized a mutiny against Russian President Vladimir Putin's regime. The group occupied Rostov-On-Don in southern Russia, a significant command center for the Russian government's invasion of Ukraine. The wheat price subsequently fell near the end of the month when the Wagner Group's leader, Yevgeny Prigozhin, agreed to be exiled to Belarus, and the mercenaries retreated from Rostov-On-Don. The gold spot price declined 2.9% during the quarter, hampered by the Fed's outlook for more interest-rate hikes in the near future; the resolution of debt ceiling in the U.S., which reduced demand for the precious metal as a "safe-haven" asset; and U.S. dollar strength.

The Wall Street Journal reported that, according to several intelligence agencies in Western countries, Yevgeny Prigozhin's plans for a rebellion included capturing numerous Russian military leaders. Western intelligence officials also noted that Prigozhin had informed several high-ranking Russian military officers, possibly including Gen. Sergei Surovikin, commander of the Russian aerospace force, about his plans for mutiny. A spokesman for the Russian government subsequently denied the reports about Surovikin in a press conference towards the end of June. The Wagner Group had been fighting in Bakhmut, Ukraine, since the summer of 2022, and retreated from Bakhmut between late May and early June. The withdrawal from the city occurred after Prigozhin claimed that Russian Defense Minister Sergei Shoigu and Valery Gerasimov, Chief of the General Staff, had intentionally withheld ammunition from Wagner Group fighters.

Central Banks

- Following a two meeting pause, the Bank of Canada (BoC) resumed its interest rate-hiking cycle following its meeting on June 7. The overnight rate increased 0.25% to 4.75%, while the Bank continued reducing the amount of bonds it holds on its balance sheet—a policy known as quantitative tightening. Recent reports for both consumer prices and GDP were above expectations, providing ample justification for the resumption of rate increases. The BoC's Governing Council noted that it continues to monitor a number of factors including excess demand, inflation expectations, wage growth, and corporate pricing behaviours. The next scheduled meeting is on July 12.

- The Fed's so-called dot plot of economic projections, released in June, indicated a median federal-funds rate of 5.6% at the end of 2023, up from its previous estimate of 5.1% issued in March, implying that the central bank could implement two more 0.25% rate increases in the coming months. The Fed also raised its estimate for personal-consumption-expenditures (PCE) price inflation by 0.3% to an annual rate of 3.6% as of the end of this year. The PCE price index is the Fed's preferred gauge of inflation, as it tracks the change in prices paid by or on behalf of consumers for a more comprehensive set of goods and services than that of the CPI.

- In a split 7-2 vote, the Bank of England (BOE) raised its benchmark rate by 0.50% to 5.00% on June 21. The BOE's Monetary Policy Committee (MPC) expects U.K. GDP to tick up 0.25% in the third quarter of this year. However, it anticipates that there will be a modest increase in underlying economic output in the second half of 2023. Additionally, the MPC projects that the UK's inflation rate, as measured by the consumer-price index, will fall significantly over the remainder of this year attributable mainly to lower energy costs. The central bank anticipates that core inflation, which excludes volatile food and energy prices, will decline later this year due to lower costs in the supply chain. Additionally, the MPC believes that food-price inflation will decelerate over the next several months.

- The European Central Bank (ECB) increased its benchmark interest rate by 0.25% to 4.00% following its meeting on June 15. In a statement announcing the rate hike, the ECB's Governing Council noted, "Indicators of underlying price pressures remain strong, although some show tentative signs of softening. Staff have revised up their projections for inflation excluding energy and food, especially for this year and next year, owing to past upward surprises and the implications of the robust labour market for the speed of disinflation."

- The Bank of Japan (BOJ) left its benchmark interest rate unchanged at -0.1% at its meeting on June 15. The central bank noted that it "will purchase a necessary amount of Japanese government bonds (JGBs) without setting an upper limit so that 10-year JGB yields will remain at around zero percent." Additionally, the BOJ indicated that it will maintain its yield control program, allowing 10-year JGB yields to fluctuate in the range of around +0.5% to -0.5% from the 0% target.

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

- According to Statistics Canada, the rate of inflation moderated (as measured by the change in the Consumer Price Index (CPI)) to 3.4% for the year ending May—the smallest annual increase since June 2021. Consumer prices increased by 0.4% May. Base-year effects—the rolling off of exceptionally robust price increases from the first half of 2022 in the annual data—played a significant role in the moderation of price increases. Mortgage interest costs soared 29.9% over the 12-month period, representing the most significant contributor to rising prices. Excluding mortgage interest, the CPI would have risen by 2.5%. Producer prices declined in May, and were significantly lower from year-ago levels. The Industrial Product Price Index (IPPI) fell 1.0% in May, while the Raw Materials Price Index (RMPI) was down 4.9%. On a year-over-year basis, the IPPI slid 6.3% and the RMPI plunged 18.4%. Prices for many commodities, especially for energy and metals, were notably weaker. The Labour Force Survey remained mostly positive—the unemployment rate was up 0.2% to 5.2% as the number of people searching for work increased while the economy added 60,000 jobs in June.

- According to the third estimate from the Department of Commerce, U.S. gross domestic product (GDP) grew at a better-than-expected annualized rate of 2.0% in the first quarter of 2023, up significantly from the second estimate of 1.3%, but down from the 2.6% rise in the fourth quarter of 2022. The largest increases for the first quarter of this year were in consumer spending, exports, and federal government spending. These gains offset reductions in private inventory investment (a measure of the changes in values of inventories from one time period to the next) and residential fixed investment (purchases of private residential structures and residential equipment that property owners use for rentals). The government attributed the increase in the GDP growth rate relative to the previous estimate to upward revisions to exports, consumer spending, state and local government spending, and residential fixed investment. These offset downward revisions to nonresidential fixed investment (purchases of both nonresidential structures and equipment and software) and federal government spending. The U.S. employment outlook remains resilient, with robust hiring and notable increases in job openings. The Department of Labor reported that U.S. payrolls expanded by a greater-than-expected total of 338,000 in May, though the unemployment rate rose 0.3 percentage point to 3.7%. The professional and business services, government, and health care sectors saw the largest employment gains during the month. Average hourly earnings rose 0.3% in May and 4.3% year-over-year. The 12-month increase was marginally lower than the 4.4% annual rise in April. Furthermore, according to the Department of Labor's Job Openings and Labor Turnover Survey (JOLTS), the number of job openings in the U.S. rose by 358,000 (3.7%) to 10,103,000 in April (the most recent reporting period)—well above the pre-pandemic level of 7 million in February 2020. Higher mortgage rates continue to weigh on the U.S. housing market. The National Association of Realtors (NAR) reported that sales of existing homes rose 0.2% in May, but were down 20.4% versus the same period a year earlier. The median existing-home sale price fell 3.1% year-over-year to $396,000. The inventory of unsold existing homes increased 3.8% month-over-month to 1.08 million, equivalent to a three-month supply at the current monthly sales pace. According to the NAR, a six-month supply of homes historically has indicated a "balanced market," in which prices rise modestly. Inventories of greater than six months typically favour buyers, while a supply of homes that will be depleted in less than six months constitutes a "seller's market." The Conference Board's Leading Economic Index® (LEI), which is designed to signal peaks and troughs in the business cycle in the U.S., fell 0.7% to 106.7 in May, following a 0.6% decline in April. The LEI retreated 4.3% over the previous six-month period. The downturn in the index in May resulted from consumers' tempered expectations for business conditions, a decline in the Institute for Supply Management (ISM®) New Orders Index—which tracks new-order volumes for 18 manufacturing industries—the inverted U.S. Treasury yield curve, and deteriorating credit conditions. The LEI has declined for 14 consecutive months, indicating weaker economic activity.

- According to the Office for National Statistics, consumer prices in the U.K. rose 0.6% month-over-month in May, matching the 0.6% increase in April. The inflation rate rose 7.9% over the previous 12-month period, up 0.1% from the 7.8% annual increase in April. Food and non-alcoholic beverages, as well as restaurants and hotels, were the most notable contributors to the annual increase in prices. Core inflation, which excludes volatile food and energy prices, rose at an annual rate of 6.5% in May, an upturn from the 6.2% year-over-year increase in for the previous month. The Office for National Statistics also reported that U.K. GDP ticked up 0.1% over the three-month period ending April 30, 2023. Construction and production increased 1.6% and 0.2%, respectively, versus the previous three-month period, while the services sector dipped 0.1%. The S&P Global/CIPS Flash UK Manufacturing Output Index was unchanged at 47.7 in June due to a decrease in orders, along with customer destocking (a planned reduction in stock or inventory). A reading below 50 indicates contraction in the manufacturing sector. The S&P Global/CIPS Flash UK Services PMI Business Activity Index declined 1.5 to 53.7 in June, but indicated expansion for the fourth consecutive month. The slowdown in the rate of growth relative to the previous month resulted mainly from a reduction in consumer spending, as well as weaker demand in the construction and real estate sectors.

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- Eurostat estimated that the inflation rate in the eurozone fell 0.6% to 5.5% for the 12-month period ending in June. Energy prices decreased 5.6% year-over-year in June, following a 1.8% decline in May. While prices for food, alcohol and tobacco, as well as industrial goods, led the upturn in the annual inflation rate in June, the pace of acceleration slowed. Core inflation, which excludes energy and food, rose 5.4% for the month, up from 5.3% in May. Eurozone manufacturing remained in contraction territory in June, with the HCOB Flash Eurozone Manufacturing PMI Output Index falling 1.8 to an eight-month low of 44.6. Services activity in the eurozone expanded in June, but the HCOB Flash Eurozone Services PMI Business Activity Index was down 2.7 to a five-month low of 52.4. According to Eurostat's third estimate, eurozone GDP dipped 0.1% in the first quarter of 2023, down 0.2% from the initial estimate of a 0.1% increase. Eurozone GDP also declined 0.1% in the fourth quarter of 2022. GDP increased 1.0% over the 12-month period ending in March 2023. Poland's economy was the strongest performer, expanding 3.8% in the first quarter, while Ireland's GDP decreased at an annual rate of 4.6% year-over-year.

Index Data (Q2 2023)

- The S&P/TSX Composite Index gained 1.10%.
- The FTSE Canada Universe Bond Index returned -0.69%.
- The S&P 500 Index, which measures U.S. equities, gained 6.32%.
- The MSCI ACWI (Net) Index, used to gauge global equity performance, was up 3.82%.
- The ICE BofA U.S. High Yield Constrained Index, representing U.S. high-yield bond markets, returned 1.40% (currency hedged) and -0.62% (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," fell from 18.70 to 13.59.
- WTI Cushing crude-oil prices, a key indicator of movements in the oil market, moved from US$75.67 to US$70.64 a barrel to end the quarter.
- The Canadian dollar strengthened to C$1.32 per U.S. dollar. The U.S. dollar was mixed versus the world's other major currencies. It ended June at US$1.09 versus the euro, US$1.27 against sterling, and at 144.54 yen.

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Glossary of financial terms

The **debt ceiling** is the total amount of money that the U.S. government is authorized to borrow to meet its existing legal obligations, including Social Security and Medicare benefits, military salaries, interest on the national debt, tax refunds, and other payments. Failing to increase the debt limit would cause the government to default on its legal obligations.

Yield is the income returned on an investment, such as the interest received from holding a security. The yield is usually expressed as an annual percentage rate based on the investment's cost, current market value, or face value.

Mortgage-backed securities (MBS) are pools of mortgage loans packaged together and sold to the public. They are usually structured in tranches (a slice or portion of a structured security) that vary by risk and expected return.

Yield curve represents differences in yields across a range of maturities of bonds of the same issuer or credit rating (which is used to assess the risk of default of companies or countries). A steeper yield curve represents a greater difference between the yields. A flatter curve indicates the short- and long-term yields are closer together.

An **inverted yield curve** occurs when short-term yields exceed long-term yields. While an inverted yield curve historically has predicted economic recessions, it is an indicator—not a forecast.

The **federal-funds rate** is the interest rate charged to lending institutions on unsecured overnight loans. It is set by the U.S. Federal Reserve's Federal Open Market Committee. The rate is increased when the Federal Reserve wants to discourage borrowing and slow the economy and decreased when the Federal Reserve wants to spur economic growth.

Economic output comprises a quantity of goods or services produced in a specific time period.

Monetary policy refers to decisions by central banks to influence the amount of money and credit in the economy by managing the level of benchmark interest rates and the purchase or sale of securities. Central banks typically make policy decisions based on their mandates to target specific levels or ranges for inflation and employment.

A **recession** is a significant and prolonged downturn in economic activity.

U.S. Treasury bills are short-term debt obligations backed by the U.S. Treasury Department with a maturity of one year or less.

Input price inflation measures changes in the prices of materials and fuels purchased by manufacturers for processing.

Index definitions

The **MSCI All Country World Index (ACWI)** is a market capitalization-weighted index that tracks the performance of over 2,000 companies, and is representative of the market structure of 48 developed and emerging-market countries in North and South America, Europe, Africa, and the Pacific Rim. The index is calculated with net dividends reinvested in U.S. dollars.

The **ICE BofA U.S. High Yield Constrained Index** is a market capitalization-weighted index which tracks the performance of U.S. dollar-denominated below-investment-grade (rated BB+ or lower by S&P Global Ratings and Fitch Ratings or Ba1 or lower by Moody's Investors Service) corporate debt publicly issued in the U.S. domestic market.

The **KBW Regional Banking Index** tracks the performance of U.S. regional banks and thrifts that are publicly traded in the U.S.

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Consumer-price indexes measure changes in the price level of a weighted-average market basket of consumer goods and services purchased by households. A consumer price index is a statistical estimate constructed using the prices of a sample of representative items whose prices are collected periodically.

A **purchasing managers' index (PMI)** tracks the prevailing direction of economic trends in the manufacturing and service sectors.

The **S&P Global/CIPS Flash UK Manufacturing Output Index** measures the activity level of purchasing managers in the manufacturing sector of the U.K. A reading above 50 indicates expansion in the sector; below 50 indicates contraction.

The **S&P Global/CIPS Flash UK Services PMI Business Activity Index** measures the activity level of purchasing managers in the services sector. A reading above 50 indicates expansion in the sector; a reading below 50 indicates contraction.

The **HCOB Flash Eurozone Manufacturing PMI Output Index** measures the activity level of purchasing managers in the manufacturing sector of the eurozone. A reading above 50 indicates expansion in the sector; below 50 indicates contraction.

The **HCOB Flash Eurozone Services PMI Business Activity Index** measures the activity level of purchasing managers in the services sector of the eurozone. A reading above 50 indicates expansion in the sector; below 50 indicates contraction.

Producer-price indexes (PPI) measure the average change over time in selling prices received by domestic producers of goods and services.

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