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November 2023
Market Pulse

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MARKETS REBOUND AS RATE CUTS PRICED IN

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Global bond and equity markets rallied strongly in November, as investors welcomed signals that rates had peaked and that slowing inflation and economic activity could lead to monetary easing in 2024. Economic data showed slowing US activity compared to somewhat improving data in the Eurozone. Major central banks, especially the Federal Reserve (Fed) and the European Central Bank (ECB), continued to emphasise the need to keep policy restrictive for longer to tame inflation. However, some monetary policy committee members noted the potential for lower rates amid slower inflation.

Macro

While global macroeconomic data remained healthy, there were signs of slowing, particularly in the US. Data in Europe was somewhat mixed, while China continued to recover. Global inflation also fell further, lending credence to the peak rates narrative.

US economy

US labour-market data suggested some loosening of conditions. While September job openings rose to 9.55m from 9.50m in August, October data showed the addition of 150K non-farm payrolls compared to consensus expectations of 180K (and down from 297K in September). August and September payroll figures were also revised down by a cumulative 101K. Unemployment rose to 3.9%, which is the highest level since January 2022; in November, weekly initial jobless claims rose as high as 231K, the highest since August.

US activity data was also suggestive of a slowdown. October retail sales fell by 0.1% month-on-month (m/m), driven by the fall in gasoline sales. October durable goods orders declined by 5.4% m/m, driven by a 49.6% fall in aircraft orders, which are often volatile. Excluding this and defence, orders were still down by 1.3%, accelerating from a 0.8% fall in September. However, the November composite PMI indicated an ongoing rise in economic activity. The index was unchanged from October, at an expansionary 50.7 (a PMI above 50 indicates economic expansion).

Meanwhile, October consumer prices rose by a headline rate of 3.2% year-on-year (y/y) and a core rate of 4.0%, both below market expectations. Falls in energy and gasoline prices drove the former and the latter was the lowest level since September 2021.

US policy

The Fed maintained the federal funds rate at a range of 5.25-5.50%, as expected, at its November meeting. Chair Powell's comments were viewed as somewhat dovish as he stated the central bank was pleased with the progress on inflation and that "it's just clear that inflation expectations are in a good place." This was suggestive of a peak in the policy rate in the near term.

Moreover, Fed Governor Waller stated that "policy is currently well positioned to slow the economy and get inflation back to 2%", and that "something appears to be giving, and it's the pace of the economy." The Fed's third-quarter Senior Loan Officer Opinion Survey (SLOOS) supported this statement, showing continued tightening of lending standards and reduced loan demand. Waller also stated that the Fed "could start lowering the policy rate just because inflation is lower." Given lower inflation data, this led rate markets to price in the first Fed rate cut for May 2024.

However, some senior Fed members seemed to push back against the more dovish rhetoric and have emphasised data dependence. At the IMF in November, Powell stated: "If it becomes appropriate to tighten policy further, we will not hesitate to do so."

Europe

In the Eurozone, third-quarter GDP fell by 0.4% quarter-on-quarter (q/q) annualised, below consensus forecasts of no change. This was down from a 0.6% rise in Q2 and was driven by falls in Germany (-0.3%) and Ireland (-6.9%) over the period. Eurozone industrial production fell by 1.1% m/m in September.

However, there were some signs of positive momentum in sentiment in Q4. The Eurozone composite PMI increased, rising from 46.5 in October to 47.1 in November, though it remains in contractionary territory (below 50).

Meanwhile, inflation continued to fall. Headline prices were up by 2.4% y/y in November, the slowest rise since July 2021 and down from 2.9% in October. Core price rises decelerated to 3.6% y/y in November from 4.2% in October. This, along with the still-soft economic backdrop, led rate markets to price in monetary easing from the ECB as early as April 2024.

In the UK, the Chancellor's Autumn statement showed that increased inflation resulted in higher nominal tax receipts. This allowed the government to announce some fiscal easing, including reducing national insurance rates, while spending was left "broadly unchanged". As a result, the Office for Budget Responsibility (OBR) projects that the budget deficit will fall from 5.0% of GDP in fiscal year 2022/23 (year to 5 April 2023) to 4.5% in 2023/24. Meanwhile, the UK GfK consumer confidence barometer rose by more than expected to -24 in November, reversing most of the fall in October. The composite PMI for November also rose back into expansionary territory, at 50.1.

China

Chinese economic data for October showed healthy activity. There were upside surprises for both industrial production and retail sales, which expanded by 4.6% and 7.6% y/y, respectively. Fixed-asset investment rose by 2.9% y/y, below expectations of 3.1%.

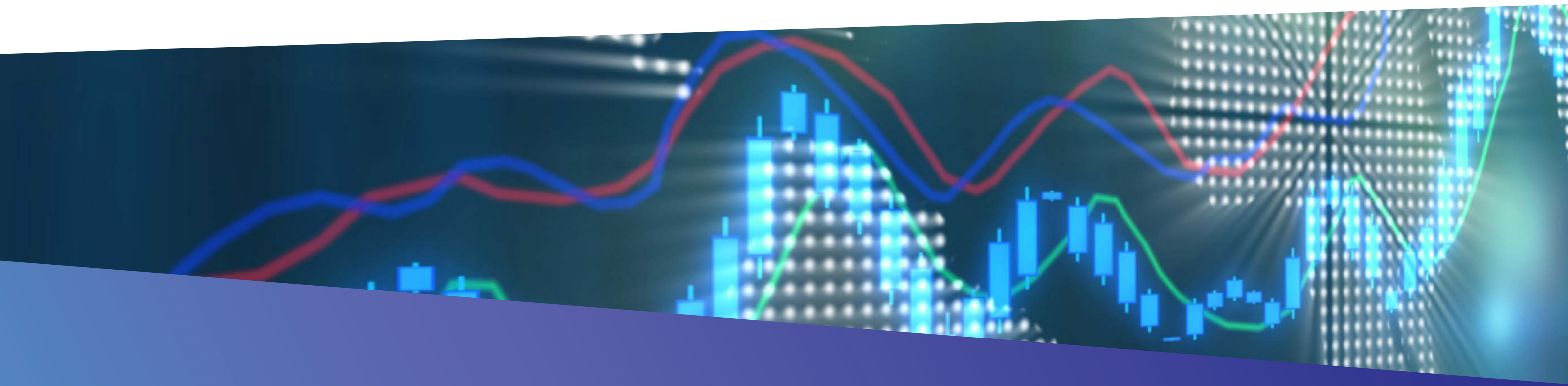
MARKET ROUND-UP

Equities

Global stock markets rebounded strongly in November, buoyed by slowing inflation and the potential for easier monetary policy in 2024. The MSCI All Country World index rallied by 8.1% (+5.9% in euro terms) over the month. The MSCI USA rose by 9.4% (+6.0% in euros), while European ex-UK equities rose by 6.9% (+7.4% in euros).

Bonds

Bond markets also rallied strongly, with yields falling as inflation fell and rate markets priced in monetary easing from the Fed and the ECB as soon as Q2 2024. The ICE BofA 5+ Year Euro Government bond index rose by 4.4% over the month. US and German 10-year yields declined significantly, by 60bps to 4.33% and by 36bps to 2.45%, respectively.



CHARTS OF THE MONTH

Global Equities

Source: ILIM, Bloomberg. Data is accurate as at 30 November 2023.

Bonds – German 10-year yield

Source: ILIM, Bloomberg. Data is accurate as at 30 November 2023.

MARKET SNAPSHOT

Market returns (EUR)

Equity Markets (EUR)	MTD Return (%)	YTD Return (%)	2022 Return (%)
MSCI Ireland	3.2	14.6	-21.1
MSCI United Kingdom	3.4	6.8	1.4
MSCI Europe ex UK	7.4	14.1	-11.9
MSCI North America	6.1	18.1	-13.8
MSCI Japan	5.2	13.2	-10.8
MSCI EM (Emerging Markets)	4.6	3.8	-14.5
MSCI AC World	5.9	14.6	-12.6

10-Year Yields	Yield Last Month (%)	2022 Yield (%)	2021 Yield (%)
US	4.33	3.87	1.51
Germany	2.45	2.57	-0.18
UK	4.18	3.67	0.97
Japan	0.67	0.42	0.07
Ireland	2.83	3.13	0.24
Italy	4.23	4.70	1.17
Greece	3.69	4.62	1.34
Portugal	3.14	3.59	0.47
Spain	3.47	3.66	0.57

FX Rates	End last month	2022 Rates	2021 Rates
U.S. Dollar per Euro	1.09	1.07	1.14
British Pounds per Euro	0.86	0.89	0.84
U.S. Dollar per British Pounds	1.26	1.21	1.35

Commodities (USD)	MTD Return (%)	YTD Return (%)	2022 Return (%)
Oil (Brent)	-5.2	-3.6	10.5
Gold (Oz)	2.7	11.7	-0.3
S&P Goldman Sachs Commodity Index	-3.6	-1.0	26.0

Source: ILIM, Bloomberg. Data is accurate as at 1 December 2023.

THE ILIM VIEW – LOOKING AHEAD

Sovereign bond yields are broadly higher this year on the back of a slower-than-expected pace of moderation in inflation, resilient economic activity and an upward reset for the level and timing of peak policy rates. With inflation having clearly peaked and central banks now suggesting that the end of the tightening cycle could already have been reached, bond yields are expected to decline over the next 12 months.

On a 12-month view, our base case is that German 10-year government bond yields fall from 2.45% at end-November to around 1.75%, and that the equivalent US bonds fall from 4.33% to somewhere in the region of 3.75%. We believe bonds offer a strong risk-reward profile at this stage in the cycle and are attractive from an income perspective, while also providing potential for capital gains via falling yields. The current relatively high level of bond yields – and central banks' commitment to bring inflation down – mean the asset class should remain attractive on a multi-year basis, with high single-digit returns possible over the next 12 months in riskier segments of fixed income.

Global equities have proved resilient in 2023 as recession fears have receded and a peak in central bank policy rates has come into view. While global earnings are forecast to be only modestly higher this year – by approximately 0.4% – they have held up better than feared at the start of the year, as sales have surprised to the upside in the better economic backdrop and the margin squeeze for corporates has been less than anticipated. Earnings are expected to grow by over 10.9% in 2024.

Global equity valuations are slightly above long-term averages, trading on a 12-month forward P/E multiple of 16.2x against a long-term average of 16.0x. Equities remain expensive against both bonds and cash given the high yields currently available on these assets. Despite this, the outlook on a 12-month view is positive. Central banks are likely to pivot towards looser policy in 2024 as inflation continues to fall. An increasing probability of a soft landing with a rebound in both growth and earnings should also provide support.

Over the medium term, the rollout of AI should boost efficiencies and earnings across the whole market and allow equities to trade at higher valuation levels. The ongoing green-related capex cycle could also boost earnings over the medium term. Any short-term volatility in markets is likely to be offset by the above factors, resulting in positive returns on a 12-month time frame.

THE MONTH AHEAD

DECEMBER

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
				8 US Non Farm Payrolls US Unemployment Rate
	12 US Inflation Rate GB Unemployment Rate	13 US Fed Interest Rate Decision GB GDP	14 GB BoE Interest Rate Decision EA ECB Interest Rate Decision US Retail Sales MoM	
		20 GB Inflation Rate YoY	21 US GDP Growth Rate QoQ Final	22 US Durable Goods Orders

Source: tradingeconomics.com

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Figures referenced herein have been sourced from ILIM and Bloomberg. Forecast figures have been prepared by ILIM based on reasonable assumptions, internal data and data sourced from Bloomberg.

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