

Keys to the market

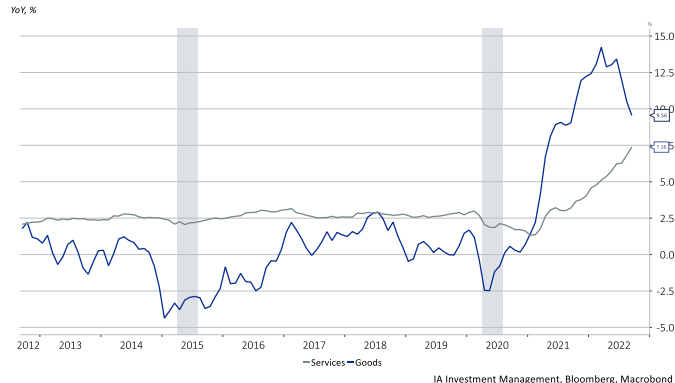
What happened last week

October 14, 2022

Volatility was the buzzword on the financial markets this week as asset prices fluctuated violently. The Bank of England's decision to stop supporting gilt prices, stronger PPI data and a higher CPI print in the United States all caused stock prices to tumble and bond yields to spike. Even so, investors in short-covering mode staged a strong rally on Thursday. The UK Prime Minister's decision to abandon the corporate tax cuts introduced three weeks ago disappointed the markets, which were expecting a full cancellation of the budget.

Unexpectedly high inflation in the United States sealed the case for a 75-bps rate hike in November, and the probability of a 100-bps move is increasing. It's now clear that inflation has become more entrenched in services in the US economy, fuelled by housing and transportation, whereas goods inflation continues to moderate. The hopes of a Fed pivot were decisively dashed on the news. As the IMF downgraded its 2023 global growth outlook, citing punishing interest rates and chronic inflation, the probability of a recession scenario has increased.

U.S.: Inflation in Goods vs Services



The prevailing mantra for the global bond markets is now "expect the unexpected." In that context, the higher US inflation print drove 10-year Treasury yields up 10 bps to about 4%. Canada bonds mostly sat on the sidelines, with the 10-year yield edging up only 5 basis points. The focus will shift to the US labour market next week, when we will see whether higher rates and slowing economic activity are starting to take a bite. We would be remiss not to mention the craziness that is now the UK bond market, as zig-zagging government policy and central bank intervention once again had 2-year and 30-year gilts yields gyrating by

Highlights

- The UK government cancelled the corporate tax cuts introduced three weeks ago.
- Strong CPI numbers in the US dashed hopes of a Fed pivot.
- The IMF downgraded the 2023 global growth outlook, citing punishing interest rates and chronic inflation.

On our radar

- In Canada: September CPI and August retail sales
- In the US: September industrial and manufacturing production, and housing starts; October initial and continuing jobless claims

25 basis points during the week, albeit to declining global impact as investors got used to the noise.

Despite the short covering in equities and the UK government's changes to its budget, the stock market is on track to end the week lower. The main headlines concerning stocks were new export controls announced by the Biden administration to restrict China's access to artificial-intelligence and semiconductor chips. We think this move will have a negative impact on the Chinese economy, specifically on AI supercomputing industries and military advancement. We expect retaliation targeting US companies doing business in China, and major brands such as Nike and Apple could be at risk.

Third-quarter results will switch into a higher gear next week, with 16% of the S&P 500 companies reporting. Given the economic uncertainty and a material increase in negative pre-announcements, third-quarter earnings estimates have fallen 7% in the past three months. Earnings for the energy sector were revised upward while 9 of the 11 sectors in the S&P 500 had downward revisions to earnings. We see an increased probability that earnings targets will be missed because the economic slowdown, the strong US dollar and continued supply-chain delays are putting pressure on profitability.

Markets

(Total Return, in CAD)

As at October 13, 2022	WTD %	MTD %	YTD %	1Y %	3Y %	5Y %
Equities						
S&P 500	2.25	3.45	-14.33	-4.77	10.93	11.80
S&P/TSX	0.17	1.03	-10.23	-7.04	7.45	6.50
NASDAQ	1.34	1.58	-25.72	-16.75	13.94	15.03
MSCI ACWI	1.15	2.45	-16.89	-10.12	6.83	7.56
MSCI EAFE	-1.12	0.42	-20.36	-16.91	-0.51	0.86
MSCI EM	-3.47	-1.41	-21.60	-21.91	-1.22	-0.62
Commodities (USD)						
Gold	-1.68	0.35	-8.90	-7.06	3.82	5.03
CRB	0.20	0.14	-3.12	-0.19	12.71	5.42
WTI	-3.81	12.10	18.48	10.78	17.66	11.61
Fixed Income						
FTSE TMX Canada Universe	-0.51	-1.85	-13.41	-11.69	-2.83	0.16
FTSE TMX Canada Long	-1.38	-3.74	-23.91	-19.95	-6.74	-0.94
FTSE TMX Canada Corporate Overall	-0.30	-1.33	-11.94	-10.60	-1.58	0.89
Currencies						
DXY	-0.38	0.22	17.45	19.43	4.56	3.83
USDCAD	0.10	-0.55	8.83	10.53	1.37	1.98
USDEUR	-0.32	0.26	16.33	18.62	4.14	3.87
USDJPY	1.29	1.64	27.84	29.91	10.75	5.64
USDGBP	-2.13	-1.39	19.44	20.61	3.74	3.24

	CA	US
Yields		
2Y	4.11	4.46
5Y	3.59	4.20
10Y	3.42	3.94
30Y	3.34	3.92
Spreads		
IG corporate bonds	179	171
HY bonds	368	525

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ROOTED IN HISTORY. INNOVATING FOR THE FUTURE.

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