MARKETS & ECONOMY | NOVEMBER 3, 2023

Global Markets Weekly Update

Highlighted Regions

U.S.

Stocks see best gain since November 2022 on falling yields

The S&P 500 Index recorded its strongest weekly gain in nearly a year, as signs of a slowing economy and a policy statement from the Federal Reserve that was generally perceived as dovish led to a sharp decrease in long-term bond yields. Growth stocks and the technology-heavy Nasdaq Composite Index outperformed somewhat, but the gains were broad-based and led by the small-cap Russell 2000 Index, which scored its best weekly gain since October 2022.

It was the second-busiest week of earnings season, and T. Rowe Price traders noted that markets also appeared to be moved in part by trades made by institutional investors to recognize tax losses before their fiscal year ended on October 31. Index rebalancing and “window dressing” before month-end holdings disclosure may also have been at work.

Along with earnings, the week brought a slew of policy statements, economic reports, and geopolitical developments for investors to digest. A primary driver of sentiment appeared to be the Fed’s policy meeting that concluded Wednesday. The Fed left rates steady, as was widely expected, but investors appeared encouraged by the post-meeting statement, which signaled that the recent runup in long-term Treasury yields had achieved some of policymakers’ intended tightening in financial conditions. Fed officials also seemed comfortable with the recent upside surprises in economic data, merely tweaking their description of the pace of economic growth from “solid” to “strong.”

Unemployment rate reaches highest level since early 2022

Friday's closely watched payrolls report seemed to confirm that the labor market was cooling, with wage pressures hopefully—in the eyes of investors, at least—soon to follow. Employers added 150,000 jobs in October, below expectations and the lowest level since June, and September's strong gain was revised lower. Meanwhile, the unemployment rate rose to 3.9%, its highest level since January 2022.

Average hourly earnings rose 0.2%, less than expected, although September's gain was revised higher to 0.3%. The 12-month gain fell to 4.1%, its lowest level in over two years but still above the roughly 3% level that policymakers are often believed to consider compatible with their overall inflation target of 2%. The Labor Department's quarterly employment cost index, released Monday, surprised modestly on the upside, indicating an annual increase in wages and benefits of 4.3%.

Encouragingly for both workers and investors, preliminary estimates of productivity growth in the quarter were better than expected, with unit labor costs declining. The 4.7% gain in productivity was the best showing since businesses began to reopen in the early stages of the pandemic in the third quarter of 2020.

Treasury funding fears abate somewhat

A final factor boosting overall market sentiment appeared to be the U.S. Treasury's announcement that it would sell USD 112 billion of longer-term securities at its quarterly refunding auctions the following week, slightly below its original projection of USD 114 billion. Our traders noted that downward revision seemed to remove a large overhang on the bond market, as worries have intensified recently that demand for Treasuries would be unable to keep up with the expanding supply necessary to fund swelling federal debt levels.

The above factors combined to result in a plunge in long-term Treasury yields over the week, with the yield on the benchmark 10-year U.S. Treasury note tumbling from 4.88% to an intraday low on Friday of around 4.48%, its lowest level since late September. (Bond prices and yields move in opposite directions.) The municipal bond market enjoyed the tailwind of falling Treasury yields and also benefited from relatively light primary issuance.

Credit-sensitive bond sectors also performed well, especially following the Fed's announcement on Wednesday. Heavy issuance in the investment-grade corporate market was met with solid demand, while the high yield bond market benefited from a lack of new issues and the upgrade of Ford debt to investment grade, which will soon move it out of the high yield indexes.

Index	Friday's Close	Week's Change	% Change YTD
DJIA	34,061.32	1643.73	2.76%
S&P 500	4,358.34	240.97	13.51%
Nasdaq Composite	13,478.28	835.27	28.78%
S&P MidCap 400	2,478.34	151.52	1.97%
Russell 2000	1,760.71	125.39	-0.03%

This chart is for illustrative purposes only and does not represent the performance of any specific security. ***Past performance cannot guarantee future results.***

Source of data: Reuters, obtained through Yahoo! Finance and Bloomberg. Closing data as of 4 p.m. ET. The Dow Jones Industrial Average, the Standard & Poor's 500 Stock Index of blue chip stocks, the Standard & Poor's MidCap 400 Index, and the Russell 2000 Index are unmanaged indexes representing various segments of the U.S. equity markets by market capitalization. The Nasdaq Composite is an unmanaged index representing the companies traded on the Nasdaq stock exchange and the National Market System. Frank Russell Company (Russell) is the source and owner of the Russell index data contained or reflected in these materials and all trademarks and copyrights related thereto. Russell® is a registered trademark of Russell. Russell is not responsible for the formatting or configuration of these materials or for any inaccuracy in T. Rowe Price's presentation thereof.

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Europe

In local currency terms, the pan-European STOXX Europe 600 Index rebounded from the previous week's loss and ended 3.41% higher. Major stock indexes also rallied, lifted by expectations that interest rates may have peaked. Italy's FTSE MIB surged 5.08%, France's CAC 40 Index jumped 3.71%, and Germany's DAX climbed 3.42%. The UK's FTSE 100 Index added 1.73%.

European bond yields broadly declined as expectations rose that major central banks have completed their monetary policy tightening cycles. The yield on the 10-year German sovereign bond fell to its lowest levels in more than two months. Swiss and French bond yields also declined, as did the yield on the UK 10-year government bond.

BoE keeps rates at 15-year high, sees stagnant economy in 2024

The Bank of England (BoE) held interest rates at a 15-year high of 5.25% for the second consecutive meeting but warned that rates would have to stay at a restrictive level for "an extended period of time." BoE Governor Andrew Bailey said the bank "will be watching closely to see if further interest rate increases are needed, but even if they are not needed, it is much too early to be thinking about rate cuts."

The central bank's latest projections showed the inflation rate halving by year-end and dropping below the 2% target at the end of 2025, which is later than previously forecast. The BoE estimated that the economy would expand 0.1% for the rest of this year and remain flat in 2024.

Meanwhile, the UK housing market remained weak. The BoE reported that lenders approved 43,328 mortgages in September, the lowest level since January.

Eurozone inflation slows sharply, economy shrinks; German jobless rate rises

Inflation in the eurozone slowed more than expected to an annual rate of 2.9% in October—its lowest level since July 2021—from 4.3% in September. The European Union statistics agency said a decline in energy and food prices were the main reasons for the decline. The slowdown probably reflected weaker economic growth in the bloc as well; gross domestic product contracted 0.1% sequentially in the third quarter. The German economy, the largest in the eurozone, shrank by the same magnitude relative to the second quarter. Meanwhile, Germany's Federal Labor Office reported that the seasonally adjusted jobless rate in October increased by more than expected to 5.8%. By comparison, the unemployment rate came in at 5.7% in September.

Norges Bank holds rates steady

Norway's central bank kept its key interest rate unchanged at 4.25% but said it would probably increase the cost of borrowing in December, unless inflation continued to abate.

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Japan

Japan's stock markets gained over the week, with both the Nikkei 225 Index and the broader TOPIX Index returning around 3%. Although the Bank of Japan (BoJ) tweaked its yield curve control framework, monetary policy remained highly accommodative, supporting sentiment. The central bank's dovish stance weighed on the yen, however, which briefly weakened past the 151 level to the U.S. dollar. The Japanese currency has remained under pressure given the interest rate differential between Japan and the U.S.

BoJ tweaks monetary policy to allow yields to rise more freely, raises inflation forecasts

The BoJ remained committed to its ultra-loose monetary policy stance at its October meeting, leaving its short-term lending rate unchanged at -0.1%. However, the central bank adjusted its yield curve control framework for the second time in three months to allow yields to rise more freely—it will now regard its 1.0% ceiling for 10-year Japanese government bond (JGB) yields as a reference, rather than strictly capping interest rates at that upper bound. However, the BoJ said it can announce unscheduled bond purchases or fixed rate operations at its discretion, dependent on the path of global yields. Over the week, the JGB yield rose to 0.91% from 0.87%, hovering around its highest level in over a decade.

In the Outlook for Economic Activity and Prices, BoJ policymakers raised their consumer price index (CPI) forecasts substantially for fiscal years 2023 and 2024, both to 2.8% year on year, above the central bank's 2% target. They said that the outlook for price growth depends on the assumptions regarding crude oil prices and the government's economic measures, as well as asserting that underlying CPI inflation is likely to increase gradually toward achieving the price stability target.

Government announces new fiscal stimulus amid falling voter support

Japan's government announced a new fiscal stimulus package worth more than USD 110 billion, aimed at boosting growth and helping households cope with the rising cost of living. The measures include cuts to income and residential taxes as well as cash handouts to low earners. Boosting growth is also a key part of the package. The announcement comes at a time when support for Prime Minister Fumio Kishida's administration appears to be fading, with many voters disappointed by the impact of rising inflation on their purchasing power.

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China

Stocks in China gained as speculation that U.S. interest rates may have peaked offset broader concerns about the country's slowing growth. The Shanghai Composite Index rose 0.43%, while the blue chip CSI 300 advanced 0.61%. In Hong Kong, the benchmark Hang Seng Index added 1.53%, according to FactSet.

China's factory activity returned to contraction in October. The official manufacturing Purchasing Managers' Index (PMI) fell to a below-consensus 49.5 in October, down from 50.2 in September, as production growth slowed. The nonmanufacturing PMI slowed to a lower-than-expected 50.6 from 51.7 in September. (Readings above 50 indicate expansion.) Separately, the private Caixin/S&P Global survey of manufacturing activity fell to a below-forecast 49.5 in October from September's 50.6. The private survey of services activity edged slightly higher but also lagged the consensus estimate.

More evidence of China's property slump underscored investor concerns about a key growth driver for the economy. New home sales by the country's top 100 developers fell 27.5% in October from a year earlier, easing from the 29.2% drop in September, according to the China Real Estate Information Corp. In a further sign of the sector's downturn, real estate loans declined to RMB 53.19 trillion in September from the prior-year period, according to the central bank. The level of loans was RMB 100 billion less than a year earlier and marked the first year-on-year decline since the data became available in 2005.

China's ongoing housing market decline remains a serious drag on its growth outlook for many investors despite recent indicators suggesting a demand recovery after Beijing rolled out a flurry of stimulus measures. Although China is widely expected to attain its goal of 5% gross domestic product (GDP) growth in 2023, many observers appear to believe that the economy remains vulnerable given insufficient governmental support for the housing sector. According to S&P Global Ratings, under a bear case scenario, China's GDP growth could slow to as low as 2.9% next year as property sales fall as much as 25% from 2022.

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Other Key Markets

Brazil

On Wednesday, Brazil's central bank reduced its key interest rate, the Selic rate, by 50 basis points, from 12.75% to 12.25%, as was widely expected. According to the post-meeting statement, policymakers characterized the global environment as "adverse, due to an increase in longer-term interest rates in the United States, the persistence of high core inflation in many countries, and new geopolitical tensions." Domestically, they viewed economic activity as being "consistent with the scenario of deceleration over the next quarters." They also noted that headline inflation remains "in a path of disinflation," while other measures of price pressures are still above the central bank's target for inflation.

As for possible future rate cuts, policymakers "anticipate further reductions of the same magnitude" at the next few monetary policy meetings. This, however, is based on the assumption that the economy and inflation evolve in line with their projections.

Colombia

On Tuesday, Colombia's central bank decided to keep its overnight interest rate at 13.25%, which was also widely expected. The decision was not unanimous, however, as two of the seven policymakers on the Board of Directors voted for a quarter-point rate cut, as they did at the previous policy meeting in September.

According to T. Rowe Price emerging markets sovereign analyst Aaron Gifford, the tone of the post-meeting statement and the subsequent press conference were cautious, as policymakers expressed concerns about sticky inflation and inflation expectations that have recently risen. Tellingly, in its quarterly monetary policy report released this week, the central bank increased its forecast for inflation to 9.8% for this year versus 9.0% previously. While the growth outlook is still weak, the technical staff revised up its forecast for this year slightly as well to 1.2% from 0.9%.

Although most policymakers believe that "the prudent course of action is to refrain from commencing an interest rates reduction process" at this time, Gifford believes that the central bank could begin cutting rates by the end of the year. However, that could depend greatly on the next two inflation readings being in line with or lower than expectations.

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