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MARKET COMMENT (As of end of Nov. 2023)

Financial markets had an early Christmas in November. On the first day of the month, the Federal Reserve meeting has suggested the end of interest rate hikes. Throughout the month, Governors' speeches reinforced the idea that further rate hikes may not be necessary, prompting investors to bring forward their expectations for the first rate cut. Similarly, ECB governors echoed this sentiment, confirming that major central banks believe their policies are well positioned to return inflation back to the 2% target.

As a result, G10 10Y rates plummeted between -50bps and -65bps over the month, a remarkably rare shift similar to the months of Nov08 and Dec08 during the financial crisis. The 'Fed pivot' may not be the only explanation; the rapid unwinding of certain CTA strategies and macro bets also contributed. Meanwhile, a positioning for an economic hard landing and an aggressive Fed easing next year has gained traction, and active investors in interest rate markets are currently as bullish as ever, according to a JP Morgan survey.

U.S. economic indicators remain mixed. While consumers has remained resilient so far, there are signs of fatigue. The labor market remains robust with historically low unemployment rates. However, the ISM manufacturing index remains in contraction territory and the ISM services index is declining, in line with the negative trajectory of the US Conference Board's leading index. In Europe, Germany is facing a potential recession with a slightly negative Q3 GDP, sluggish factory orders and an IFO Business Climate indicator that remains at levels similar to 2008/09 or 2020, following a decline in household spending. France's Q3 GDP also unexpectedly fell to -0.1%. China's real estate sector remains under scrutiny; efforts to stem the housing slump include banks offering unsecured short-term loans to qualified builders, although non-performing loans continue to rise. China's manufacturing and non-manufacturing PMIs turned down, with the Composite PMI hovering near contraction.

Ultimately, equity markets opted for optimism and greeted the end of rate hikes with an exuberant rally that gained nearly 10% over the month, as reflected in the MSCI World Index. The "7 Magnificent" rose nearly 15% in November, for a total return of over +100% YTD in the Bloomberg Magnificent 7 Total Return Index. However, this year's equity market performance is one of the narrowest on record. The overwhelmingly positive sentiment in the equity markets may seem disconnected from interest rate market expectations and economic indicators, especially in light of high valuations and slowing earnings growth, as investors see cooling inflation as supportive of price/earnings multiples. As expected, analysts rushed to revise their forecasts for the S&P 500 during the month, with many seeing the index surpassing the 5000 level within the next 12 to 18 months. It's worth noting that the AI narrative continues to draw attention and support positive sentiment.

Risk parameters such as the VIX or V2X indices reached remarkably low levels not seen since the pre-COVID era. Credit spreads tightened significantly, averaging -30bps for 5-year investment grade benchmarks over the month. However, they are still pricing in comparatively more risk than the Equity Volatility Index. In summary, geopolitical tensions such as the war in Ukraine, the Israel-Hamas conflict and other global issues have temporarily taken a back seat. Debt has also been somewhat sidelined, although the colossal amount of sovereign debt around the world could potentially cause turbulence again in the future with new interest costs.

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