January 20, 2023

Stocks Give Ground in Technical Trading

A review of the week's top global economic and capital markets news.

Investment Solutions Group

For the week ending 20 January 2023

As of noon on Friday, global equities fell back this week after the S&P 500 Index failed to overcome strong technical resistance around the 4,000 level, which is close to the 200-day moving average and a downtrend line that has been tested multiple times over the past year. In addition, for the first time in a while, investors interpreted soft US economic data as bad news for equities rather than as a sign that the

US Federal Reserve will soon turn more dovish. Compared with last Friday, the yield on the US 10-year Treasury note was slightly lower at 3.45%, having fallen as low as 3.32% earlier in the week, while the price of a barrel of West Texas Intermediate crude oil added $2.50 to $81.25. Volatility, as measured by the Cboe Volatility Index (VIX), rose to 20.6 from 19.3.

MACRO NEWS

US hits debt ceiling

The US Department of the Treasury estimates that it reached its statutory debt limit on 19 January. However, the department estimates it can use extraordinary measures to allow the government to meet its obligations through the middle of the year. In exchange for raising the limit, Congressional Republicans want to exact spending reductions from the White House, something the administration of US President Joe Biden has forcefully resisted. Though debt ceiling negotiations may become contentious, Senate Republican Leader Mitch McConnell said the United States will never default.

China's economy held up better than expected in December

China's economy held up better than expected in December despite a massive surge of COVID infections. Industrial production beat forecasts, growing 1.1% year over year, though it grew at a slower pace than in November. Retail sales declined a less-than-expected 1.9% after sales plunged 5.9% the month before. For the quarter, GDP grew 2.9% year over year, setting the stage for a continued rebound in the first quarter. On Thursday, officials from the International Monetary Fund forecast a sharp economic recovery in China beginning in Q2, based on current infection trends. China's president Xi Jinping this week called the COVID outbreak "fierce" but said that with perseverance "dawn is just ahead."

Lagarde challenges view that hiking will slow

European Central Bank President Christine Lagarde said investors would be well advised to adjust bets that the central bank will hike rates more slowly beginning in March. Press reports earlier this week suggested the ECB would downshift to quarter-point hikes after a half-point hike in February. Speaking at the World Economic Forum in Davos, Lagarde said that eurozone inflation remains too high and that the central bank will "stay the course." Markets anticipate about 130 basis points of additional tightening from the ECB by midyear before a pause.

US data softens, except for labor

The bulk of the US economic data released this week were soft, though labor data continue to defy expectations. Retail sales were a good deal weaker than forecast in December, falling 1.1% month over month, and November sales were revised lower. Industrial production declined as well, down 0.7% in December, with November revised lower too. Housing starts and building permits both declined in December, though homebuilder sentiment showed the first uptick in over a year in January. In a sign that the labor market remains robust, weekly jobless claims fell to 190,000, the lowest reading since late September.

QUICK HITS

Fed Vice Chair Lael Brainard, one of the more dovish members of the Federal Open Market Committee, said on Thursday that policy will need to be sufficiently restrictive for some time, adding that time and resolve will be required to lower inflation to the Fed's 2% target.

According to the World Population Review, India may have overtaken China to become the world's most populous country at the end of 2022. India's population was estimated at 1.417 billion, about 5 million more than China's.

New Zealand's prime minister, Jacinda Ardern, announced she will step down from her post in early- February rather than lead her party into the upcoming the general election.

According to Freddie Mac, US mortgage rates dropped to 6.15% this week, the lowest since September, after peaking at 7.08% in November. A year ago, the average rate was 3.56%. The sharp rise in rates led to a dramatic decrease in home affordability.

The Federal Reserve Bank of New York's recession model, which relies on the spread between the 3- month Treasury bill yield and the yield on the 10-year note, implies a 47% chance of recession over the next 12 months, the highest probability since 1982.

Retail sales in the United Kingdom dropped 6.1% in December, finishing the worst year on record. Consumer confidence took a tumble as the measure compiled by GfK fell to -45 in January from -40 in December, close to the lowest level since the survey began in 1980.

Core inflation in Japan rose 4% in December from a year earlier to a fresh 41-year high, double the Bank of Japan's target. The BOJ refrained from adjusting its yield curve control band this week, which suggested to investors that there will be no further adjustments until a new governor takes office in April.

Market confidence in the Brazilian government was shaken this week after President Luiz Inácio Lula Silva questioned the independence of the nation's central bank, calling it nonsense, adding that the current inflation target hinders economic growth. However, later in the week, a spokesman appeared to backtrack, saying the government does not plan to change its relationship with the central bank.

US existing homes sales continued to decline in December, falling 1.5% from November's downwardly revised 7.9% fall. Economists had expected a steeper 3.4% December decline.

EARNINGS NEWS

With about 11% of the constituents of the S&P 500 Index having reported for Q4 2022, blended earnings per share (which combines reported data with estimates for those that have yet to report) shows that earnings declined 4.9% while sales rose about 3.7% compared with the same quarter a year ago, according to data from FactSet Research. If earnings finish the quarter in the red, it would be the first decline since the third quarter of 2020.

Stay focused and diversified

In any market environment, we strongly believe that investors should stay diversified across a variety of asset classes. By working closely with your investment professional, you can help ensure that your portfolio is properly diversified and that your financial plan supports your long-term goals, time horizon and tolerance for risk. Diversification does not guarantee a profit or protect against loss.

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Sources: MFS research, Wall Street Journal, Financial Times, Reuters, Bloomberg News, FactSet Research, CNBC.com.

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