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Monthly Market Commentary

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US Economy

There still was little hard evidence of a broad-based slowdown in economic growth through October, as US GDP (Gross Domestic Product) grew an estimated 5.2% in the third quarter. Business surveys showing little or no growth in combined manufacturing and services through October understated strength in measures of actual activity. Consumer spending has been propelled by solid job gains – 150,000 in October – remaining on the leading edge of third quarter economic growth. Furthermore, a rebound in orders for business equipment earlier in the third quarter pointed toward a revival of business investment.

Still, signs of financially stretched consumers were apparent from slippage in disposable (after-tax) income and the lowest savings rate of the year in September. Lower-income households are relying more on credit to finance budgets absorbed increasingly by food, fuel, and other staples. CPI inflation slowed to a four-month low, led by a drop in fuel costs. However, disinflation has become stickier, largely due to shelter-cost increases holding the core rate higher in October. Still-elevated inflation is tilting the Fed's bias toward "higher for longer" interest rates – which threaten to intensify the impact of tightening financial conditions in a slowing economy.

US Markets

After hitting an intraday low on October 27th, US equity markets subsequently rebounded throughout November. Despite this volatility, which has seen the S&P 500 Index trade both below and above its 50-day and 200-day moving averages, we believe markets could continue to be range-bound as the economy weakens further in the coming months.

The factors capping it to the upside include long-term interest rates (which remain close to multi-decade highs), worsening geopolitics, and a slowing economic and corporate earnings outlook. In addition, we believe the Federal Reserve's goal of taming inflation could keep monetary policy tighter for longer than markets anticipate. Where the S&P 500 Index may trade to the downside will be a function of the length and severity of an economic slowdown, which now seems to be unfolding and could adversely impact corporate profits. As such, we believe long-term investors could have opportunities to deploy side-lined cash as we move forward.

Fixed Income

The Federal Open Market Committee (FOMC) met in November and as anticipated, kept the federal funds rate unchanged at 5.25% - 5.50%. The Fed stated that recent indicators suggest that economic activity has been expanding at a strong pace. Job gains have moderated in recent months but remain strong, and the unemployment rate has remained low. Inflation, however, remains elevated above their long-term target of 2.0%.

Looking forward, the FOMC statement confirms that the Fed will continue to take into account the cumulative tightening of monetary policy, the lags with which monetary policy may affect economic activity and inflation, and economic and financial developments in its decisions at each meeting. The Fed continues to evaluate the "extent of additional policy firming that may be appropriate to return to 2% inflation over time." We read this to mean the Fed remains in a "higher for longer" stance.

International Markets

Europe's economic slowdown worsened this fall, with a preliminary reading of third-quarter GDP indicating the Eurozone economy contracted on a quarterly basis for the first time since the pandemic in 2020. A composite index of the region's business activity fell at the fastest pace in three years in October. The Eurozone's service sector shrank for a third straight month, while its manufacturing downturn deepened amid softening global trade. Steady interest rate hikes by the European Central Bank (ECB) are translating to tightening financial conditions, denting consumer confidence, and restricting business growth. On a positive note, Eurozone inflation fell sharply in October. Overall, these readings support our view that the Eurozone is likely already in a recession, preceding our forecasted downturn in the US by early 2024.

Over in Asia, China's still fragile economy, slowing world trade, and the deflationary effects of a strong US dollar are setting the tone for Asia's struggling trade-sensitive economies. China business surveys signaled growth virtually flatlined in October due to a relapse in manufacturing and weakening gains in services. Among the main headwinds to a stronger Chinese recovery are a slumping property sector and a debt overhang limiting fiscal and monetary stimulus. Manufacturing-led weakness also has been apparent in the rest of Asia, including Japan, as the region deals with an increasingly challenging global macro environment. The silver lining to broad manufacturing weakness is in reducing global supply-chain pressures. Dollar strength is having a twofold effect on the region, by restraining commodity prices and forcing central banks to tilt away from monetary accommodation.

Commodities

Despite challenges such as minimal rainfall and high temperatures, US corn production is expected to hit an all-time record harvest in 2023, according to the US Department of Agriculture. Record US harvests matter because the US is already the largest producer of corn globally, accounting for 32% of total global production. Interestingly, US farming conditions were not ideal to start the season. Earlier in the season, high temperatures and minimal rainfall sparked fears of a drought across the corn belt. While the corn belt did experience adverse weather conditions, technological advancements in seeding and farming practices helped farmers overcome these challenges.

As a result, this strong harvest, on top of already elevated global supplies, pushed corn prices lower this year. Overall, most grains and oilseeds have been well supplied in 2023, resulting in softer prices across the board.

What Does This Mean to Me?

The US economy continues to lose steam. Overseas, the global economy has also been slowing; any additional hiccups in the US economy would likely exacerbate the trend. Yet, persistent weakening should eventually usher in a pickup in disinflation and the potential for rate cuts. Both factors historically have helped spark an economic recovery, which we believe could materialize once the slowdown is behind us. For now, we believe positioning portfolios for potential opportunities available in today's market environment and strategically adding side-lined cash is a prudent approach.

If you have any questions or concerns, please do not hesitate to reach out to us at any time.

Sincerely,

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Investing in commodities is not appropriate for all investors. Exposure to the commodities markets may subject an investment to greater share price volatility than an investment in traditional equity or debt securities. The prices of various commodities may fluctuate based on numerous factors including changes in supply and demand relationships, weather and acts of nature, agricultural conditions, international trade conditions, fiscal monetary and exchange control programs, domestic and foreign political and economic events and policies, and changes in interest rates or sectors affecting a particular industry or commodity. Products that invest in commodities may employ more complex strategies which may expose investors to additional risks, including futures roll yield risk.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility.   Investing in emerging markets accentuates these risks.

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