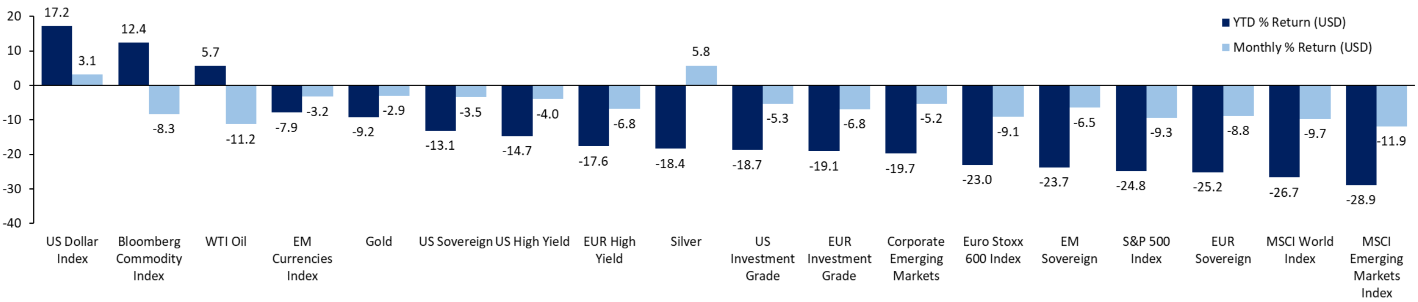
October 7, 2022

Monthly Market Wrap, September 2022

Narratives are slowing adjusting to our view, from high inflation to recession risk and systemic risk. The BoE intervention last week on the back of solvency issues at UK pension funds (margin calls that could not be met) is just an example rising systemic risks in the market. We are entering a critical phase of the bear market in risk assets. Real estate prices are starting to roll over in highly levered regions, senior financials CDS spreads are trading at a 9-year high, and financial conditions are at their tightest in well over a decade, echoing to 2007-2008. Considering the elevated level of leverage across the system, other epicentres of stress will emerge.

Chart 1. Asset Class Return YTD (USD Base)



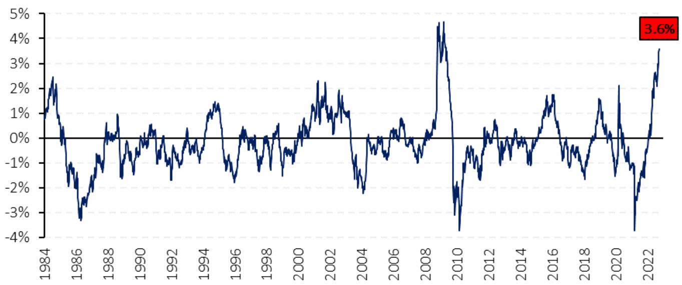
Equities

September marked the end of the summer lull. After a relatively decent start to the month on the back of short coverings and a wave of back-to-school optimism, markets rolled over to finish in the red across regions. The negative inflation pint mid-month was the catalyst to accelerate the declines. The Fed re-iterating its hawkishness and commitment to bringing down inflation and companies beginning to issue profit warnings were some of the additional factors forcing global markets lower. The MSCI World closed down -9.30% (-25.4% YTD).

As consensus was expecting a strong deceleration in inflation in August, the surprise tick up in core CPI caught a lot of investors offside leading to a swift decline in prices and US stocks having their worst month in over two years. The S&P 500 was down 9.2% (-23.9% YTD). The Nasdaq continued to underperform, down -10.6% (-32% YTD). Healthcare outperformed, down 2.6%. Meanwhile, real estate suffered the most from Powell's rhetoric that housing "may have to go through correction", down -13.3% MoM (-29.3% YTD). On the back of the recession narrative and lower consumer, the energy sector paired more of its YTD gains, down -10.5% in September (+29.8% YTD).

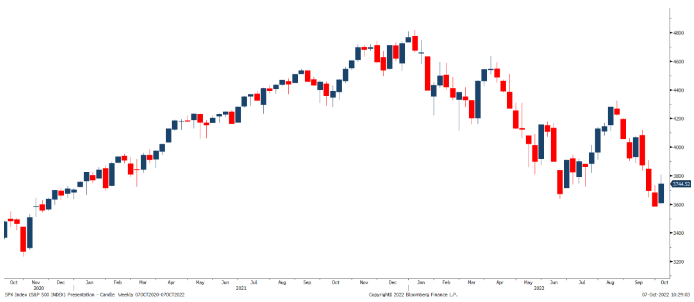
European equities faced similar headwinds. Inflation continued to accelerate, Eurozone CPI reached double digit (+10% YoY). German PPI hit a new high at 45% YoY. Consumer confidence continued to erode, reaching new lows at -42.5. Spain was one of the worst performing regions, down -6.6% (-13.6% YTD). On a sector basis, real estate was the biggest underperformer, down -17.6% (-42% YTD). Other rate sensitive sectors such as Telecom and utilities lagged, down a respective -12.7% and -8.9% last month (-14.2% an -17.4% YTD).

Chart 2. GS Financial Conditions YoY



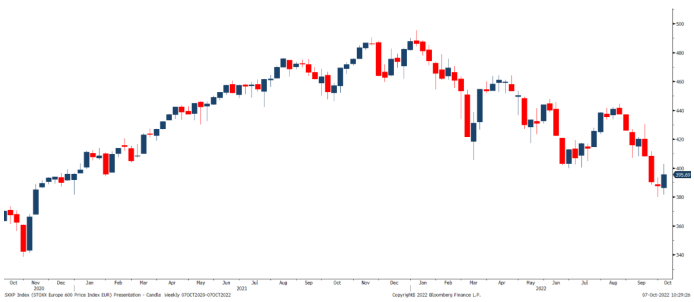
Source. MAM Research, Bloomberg

Chart 3. S&P 500 Index (Weekly)



Source. Bloomberg, MAM Research

Chart 4. EuroStoxx 600 Index (Weekly)



Source. Bloomberg, MAM Research

Fixed Income

US economic data continues to display a contracting economy. Inventories keep building up for the 23rd consecutive month. Rate sensitive consumption is falling with existing homes sales down -27% YTD and mortgage purchase applications down 36% YoY. "Trust me, our tightening will be enough to bring inflation down to 2%. It will be enough". Powell's hawkish comments at the last Fed meeting helped push the 2-Year Treasuries yields up towards 4.28%, now reaching 2007s highs. The 10-2 Year spread further declined to -54bps before slightly retracting to end the month near August lows at -45bps.

In Europe, record-high double digits inflation figures continue to hurt consumer confidence. The German Zew Economic Sentiment for September came in at -60.7, which is the lowest level since 2008 and the depths of the Great Financial Crisis. The ECB raised interest rates by 75bps in September – its largest rate hike in history, pushing the 10-Year Bund yields to 2.11%. Interestingly, however, the ECB anticipates only one quarter of negative growth (4Q22). We believe this stance is overly optimistic and expect revisions to come.

In the UK, inflation woes coupled with finance minister Kwasi Kwarteng tax cuts package pushed the 10Y Gilts yield to 4.09%, back to 2008 levels.

Currencies

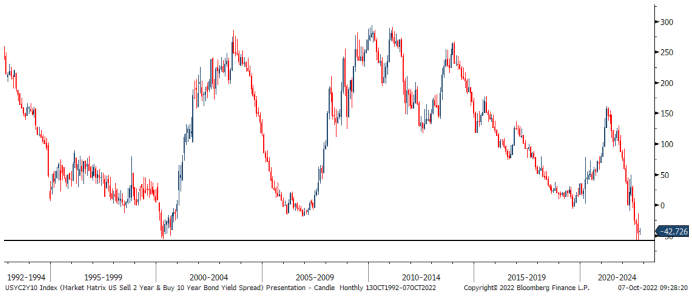
The dollar strengthened for the fourth straight month in September, reaching a new year-to-date high at 111.15. As usual, Powell's hawkish rhetoric supported by a re-accelerating inflation continued to support the greenback meanwhile trade balances and relative growth expectations continued to weigh in the balance. The dollar was up 3.1% MoM, now up by more than 17.2% YTD.

The EUR continued to suffer, hitting 20 years lows against the USD at 0.9807, amid Putin's partial mobilization, the strength of the dollar from the hawkish Fed signals, and the harsh winter coming up for Europe as Russia has cut gas supplies. The Euro continued to decline for the 4th straight month, -2.6% MoM (-14.0% YTD).

Across the Channel, the GBP continued to suffer, hitting an ATL against the USD at 1.03, before recovering in the last few sessions of the month. The drop followed the announcement of a spending and tax plan by Britain's new Conservative government, translating into an enormous increase in the budget deficit and a worsening balance of payments. The Pound ends the down -4.3% MoM (-17.8% YTD).

In Japan, the BoJ $20bn intervention did little to support the Yen, down another -4.3% MoM (-25.6% YTD).

Chart 5. US 10-2 Treasury Spread (Monthly)



Source. Bloomberg, MAM Research

Chart 6. UK 10-Year Gilts Yield

Source. Bloomberg, MAM Research

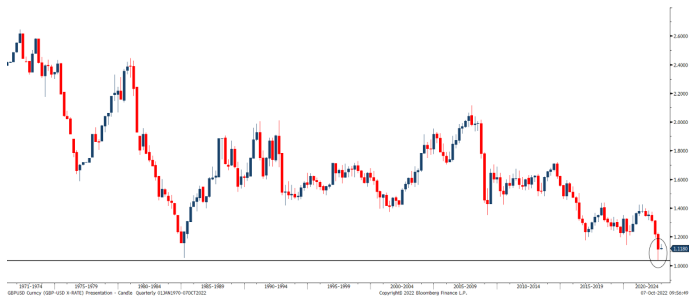
Chart 7. US Dollar Index (Monthly)

Source. Bloomberg, MAM Research

Chart 8. USD/Euro Spot Exchange Rate (Monthly)

Source. Bloomberg, MAM Research

Chart 9. USD/GBP Sport Exchange Rate (Quarterly)



Source. Bloomberg, MAM Research

Commodities

Commodities were hit hard this September, with the Bloomberg Broad Commodity Index down -8.3% MoM (+12.4% YTD).

The energy sector was hit particularly hard, down -16.6% MoM (+49.8% YTD). Natural gas prices were a key contributor to negative returns for energy being down -25.9% (+81.4% YTD), following weaker demand due to Hurricane Ian and weather-driven demand at a seasonal nadir. WTI crude oil slipped for a fourth consecutive month, down -11.2% MoM (+5.7% YTD), as recessionary fears grabbed the market's attention with China's biggest annual drop in demand in more than three decades, and the spectre of global central banks renewing their commitment to fight inflation looming large on hopes for the global economy.

Industrials were down -6.3% (-16.2% YTD) as the Fed re-iterated that a painful period of slow economic growth was ahead. Copper prices fell for a 6th consecutive month amid reduced global growth expectations, down -3.0% (-23.6% YTD).

Agriculture was down -1.7% in September (+10.8%), on concerns about demand amid fears of a global recession and higher than expected stocks.

Precious metals outperformed but were still down -0.9% (-11.7% YTD). Gold declined for the 6th consecutive month, down -3.0% MoM (-8.9% YTD), whilst Silver caught a bid at end of the month to finish up 5.5% (-18.2% YTD).

Emerging Markets

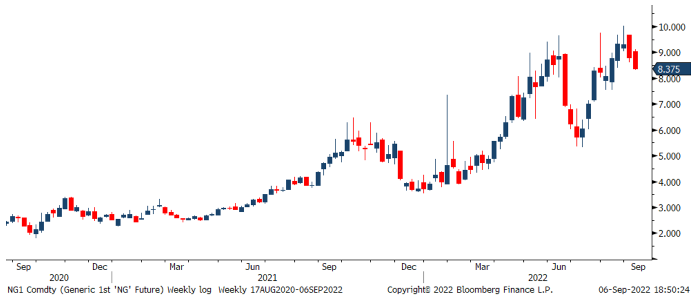
EM equities lagged last month, down -11.7% (-27.2% YTD).

Every single EM region covered by our models was negative in September. Chinese equities suffered the most (-14.6% MoM, -31.2% YTD) amid a worrying growth outlook and the ever-present zero-Covid policy. The tech-heavy Hang Seng index touched an 11-year lows amid the massive global tightening as well as rising geopolitical tensions.

On the other hand, Brazilian equities were relative outperformers as the presential race between Lula and Bolsonaro tightened. Some investors wagered that Bolsonaro, while not favoured, could eke out a second-round win, allowing him to push forward pro-market reforms and privatizations. Brazilian equities were down -3.3% MoM (+11.5% YTD).

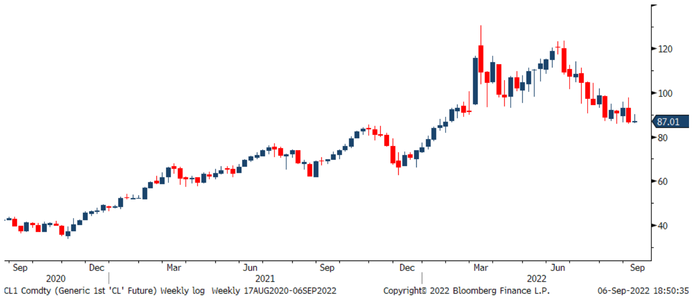
The MSCI Emerging Market Currencies Index was down -3.24% last month (-7.9% YTD). The Chinese Renminbi continued to weaken against the dollar for the 7th consecutive month, down 3.3% (-12.1% YTD). The Brazilian Real was down -4.2%, while the Mexican Peso was flat.

Chart 10. Natural Gas Continuous Futures (Weekly)



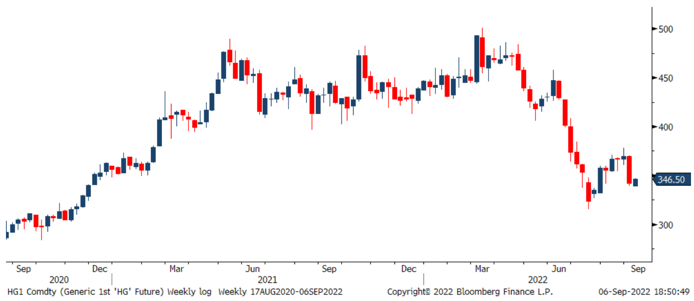
Source. Bloomberg, MAM Research

Chart 11. WTI Crude Oil Continuous Futures (Weekly)



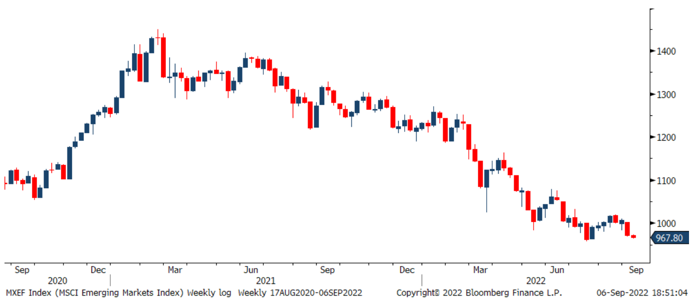
Source. Bloomberg, MAM Research

Chart 12. Copper Continuous Futures (Weekly)



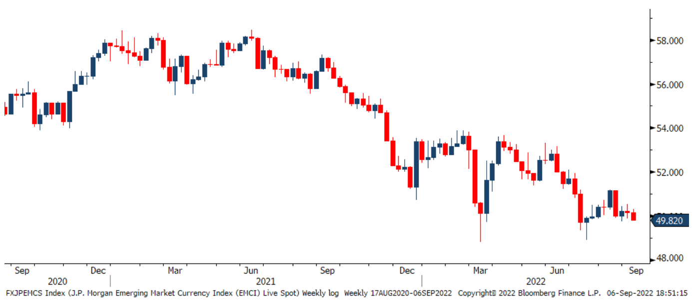
Source. Bloomberg, MAM Research

Chart 13. MSCI EM Index (Weekly)



Source. Bloomberg, MAM Research

Chart 14. MSCI EM FX Index (Weekly)



Source. Bloomberg, MAM Research

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