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December 2023 market update

Economic hurdles: a global tango of challenges

Jan. 4, 2024

Introduction

Investor sentiment improved in December on rising expectations that major central banks, including the U.S. Federal Reserve Board ("Fed"), may begin cutting interest rates in 2024. In response, global equity markets moved higher over the month. The Fed, Bank of Canada ("BoC"), European Central Bank ("ECB") and Bank of England ("BoE") all held their policy rates steady at their December meetings. Inflation continued to subside, helping to open the door to interest rate cuts. Global economic activity remained relatively muted, with tight financial conditions weighing on households and businesses.

In Canada, the S&P/TSX Composite Index advanced, led by the Health Care and Real Estate sectors. U.S. equities, as measured by the MSCI USA Index, also rose. Yields on 10-year government bonds in Canada and the U.S. fell. Gold prices inched higher, while the price of oil finished lower.

Canada’s economy hurt by slower spending

Canadian consumers exhibited weakness in the third quarter of 2023, challenged by tight financial conditions, and the slowdown in consumer spending weighed on Canada’s economic growth. Canada’s gross domestic product (“GDP”) shrank at an annualized pace of 1.1% over the third quarter, which follows a revised 1.4% expansion in the previous quarter. The main detractors from growth were lower exports and slower consumer spending. Exports dropped by 1.3% over the quarter, driven by a 25.4% decline in shipments of energy products, where muted demand amid weaker economic activity provided a headwind for energy product shipments from Canada. While Canada’s economy benefited from a strong Canadian consumer coming out of the pandemic, that momentum is losing steam as many households struggle with high inflation and rising borrowing costs. After the quarterly drop in growth, the threat of a technical recession persists. Statistics Canada reported there was no change in Canada’s GDP in October.

Fed signals possible interest rate reductions

At its last meeting of 2023 in December, the Fed held the target range of its federal funds rate steady at 5.25%–5.50%. While market participants widely expected the rate hold, comments from the Fed resonated with investors and raised expectations the Fed could begin reducing interest rates in 2024. With the U.S. economy slowing and inflation continuing to moderate, Fed officials indicated there could be three interest rate reductions in 2024. This confirmed expectations widely held by market participants, but the acknowledgement by the Fed helped lift equity markets higher after the meeting.

The story was much the same from other central banks, except for the comments about reducing interest rates. Inflation worldwide has dropped partly due to aggressive central bank actions. The Organisation for Economic Co-operation and Development reported that inflation fell to 5.6% in October from 6.2% in September. The BoC held its benchmark overnight interest rate steady at 5.00% at its December meeting, noting that inflation and economic activity are slowing. The BoC didn’t rule out another interest rate increase should inflation persist, while Governor Tiff Macklem said it might be too early to discuss interest rate cuts. Across the Atlantic, the ECB and BoE both held steady and expressed that restrictive interest rates are needed for longer, with inflation remaining well above target.

U.S. labour market sends mixed signals

While broad-based indicators show the U.S. labour market remains strong and relatively tight, several underlying indicators point to the market cooling off. The U.S. Bureau of Labor Statistics reported that the U.S. economy added 199,000 jobs in November, topping expectations and exceeding the 150,000 job additions in October. November's job gains helped push the unemployment rate lower to 3.7%. On the surface, these robust job numbers could appear to keep the pressure on the Fed to leave interest rates at current levels. However, other data pointed to the labour market losing momentum. ADP reported private businesses in the U.S. added fewer jobs in November than in October. Furthermore, job openings fell considerably in October to 8.7 million, the lowest figure since March 2021. Job openings in the health care and finance industries dropped considerably during the month. Finally, announced job cuts increased in November, most notably in the retail trade and tech industries. The mixed signals over October and November have left many market participants wondering how this will impact inflation, central bank actions and the overall health of the U.S. economy.

China sees surprise increase in exports

A critical component of China's economy finally came to life in November, suggesting the economy might be stabilizing. Exports from China rose by 0.5% year-over-year in November, surprising economists expecting no growth (0.0%). November's increase marks the first for China since April 2023. A rise in shipments of steel products and aluminum contributed to the increase. Shipments to the U.S. increased in November, but this was partially offset by a drop in exports to Japan and the European Union. Conversely, imports fell by 0.6% year-over-year in November. The changes resulted in China's trade surplus widening in November. Strong exports are good for China's economy, which also posted relatively strong results elsewhere, pointing to healthier economic conditions. Retail sales and industrial production rose annually at a relatively strong pace in November compared to October. China's economy has shown signs of improvement in recent months, helped by support from Beijing. In December, the People's Bank of China ("PBOC") injected short-term cash into the market using reverse repos, its first such action since September. The PBOC has looked to help grow economic activity in China.

Market performance - as at Dec. 31, 2023

Equity Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
S&P/TSX Composite Index C$	20,958.44	3.57%	**3.57%**	8.12%	**8.12%**	8.12%	**8.12%**
MSCI USA Index US$	4,552.01	4.58%	**1.67%**	25.05%	**22.06%**	25.05%	**22.06%**
MSCI EAFE Index US$	2,236.16	5.24%	**2.31%**	15.03%	**12.29%**	15.03%	**12.29%**
MSCI Emerging Markets Index US$	1,023.74	3.71%	**0.83%**	7.04%	**4.49%**	7.04%	**4.49%**
MSCI Europe Index US$	2,020.40	4.93%	**2.01%**	16.68%	**13.89%**	16.68%	**13.89%**
MSCI AC Asia Pacific Index US$	169.39	4.41%	**1.51%**	8.76%	**6.17%**	8.76%	**6.17%**

Fixed Income Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
FTSE Canada	1,121.47	3.43%	**3.43%**	6.69%	**6.69%**	6.69%	**6.69%**

Universe Bond Index C$							
FTSE World Investment Grade Bond Index US$	215.24	4.20%	**1.30%**	6.44%	**3.90%**	6.44%	**3.90%**

Currencies	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
CAD/USD	0.7551	2.51%	-	2.45%	-	2.45%	-

Commodities	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
West Texas Intermediate (US$/bbl)	71.65	-5.67%	-	-10.73%	-	-10.73%	-
Gold (US$/oz)	2,062.98	1.30%	-	13.10%	-	13.10%	-
Silver (US$/oz)	23.80	-5.84%		-0.66%		-0.66%	

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