September 2022 market update

Canada's labour market is running out of steam – how about inflation?

Oct. 7, 2022

Introduction

Global equity markets fell sharply over September in response to ongoing monetary tightening by global central banks, who also signaled their intentions to increase rates further. The prospect of higher rates raised concerns about how aggressive monetary tightening may negatively affect global economic activity and trigger a worldwide recession.

The U.S. Federal Reserve Board ("Fed"), Bank of Canada ("BoC"), European Central Bank ("ECB") and Bank of England ("BoE") all raised their key interest rates during the month. But business activity across many major economies posted relative weakness in September, prompting more recessionary worries. As reported in September, inflation cooled in Canada and the U.S. in August but remained elevated. Inflation in Europe and the U.K. continue to tick higher. China's economy struggled under the weight of lockdown restrictions, supply chain challenges and slower global economic activity.

In Canada, the S&P/TSX Composite Index declined, hindered by weakness in the Communication Services sector. The S&P 500 Index dropped over 9%, while the tech-heavy NASDAQ Composite Index fell over 10%. Yields on 10-year government bonds in Canada and the U.S. both moved higher. The price of oil and gold both dropped over the month.

More rate hikes on the way

The BoC and the Fed continued their aggressive measures in September, and despite signs of cooling inflation, the central banks suggested more rate increases were likely. The BoC raised its benchmark overnight interest rate by 75 basis points ("bps") to 3.25%. It was the BoC's fifth consecutive rate hike. Despite Canada's inflation rate easing to 7.0% in August, BoC Deputy Governor Paul Beaudry commented it was still too high, and the BoC remained committed to bringing it down to its 2% target. The story was much the same in the U.S. The Fed raised the target range of its federal funds rate by 75 bps to 3.00%-3.25%. As inflation persisted, Fed officials indicated they expected the federal funds rate to climb above 4% by year-end. The comment sent equity markets into a tailspin with rising concerns that further rate hikes could push the U.S. economy into a recession.

Not to be outdone, the BoE raised its Bank Rate by 50 bps to 2.25%, its seventh consecutive increase. At the same time, the ECB raised its key interest rate by 75 bps to 1.25% at a second consecutive meeting. In the U.K. and Europe, inflation has shown little signs of abating, prompting these central banks to predict further rate hikes in 2022. Meanwhile, the People's Bank of China ("PBOC") headed in the opposite direction this year. In September, the PBOC reduced the borrowing costs of 14-day reverse repos by ten bps to 2.15%. With China's economy weakening, the PBOC hopes this move will help to revive credit and support growth.

Strong labour market cooling

After Canada's labour market tumbled at the onset of the pandemic, it quickly improved as lockdown restrictions eased and economic activity picked up. As conditions improved, the labour market tightened, and wages surged higher. However, wage growth trailed Canada's inflation rate, putting pressure on Canadian consumers. According to Statistics Canada, job vacancies in Canada reached a record 997,000 at the end of the second quarter. Since then, jobs in Canada have scaled back. For the third consecutive month in August, the Canadian economy lost jobs. Almost 40,000 were shed during the month, with most of the losses in full-time employment. The largest number of job losses were posted among public sector employees. The losses pushed Canada's unemployment rate up to 5.4% in August, its highest level since February 2021 and first monthly increase since January 2021. With economic conditions coming under pressure, Canada's labour market may continue to face challenges in the coming months. While slowly working its way into the labour market, the BoC path of aggressive tightening might bring the labour force back into balance.

Real estate heat subsiding

The U.S. housing market heated up with the onset of the pandemic but now has begun to cool. Existing home sales fell 0.4% in August to 4.8 million homes. It marked the seventh straight monthly decline pulling existing home sales to the lowest level since May 2020. Home prices remained elevated, but growth slowed. On a year-over-year basis, the median selling price of a home rose 7.7% to $389,500 in August. However, it was the slowest pace of annual growth since June 2020. Demand for housing has been constrained by higher prices and rising mortgage rates, propelled higher alongside moves by the Fed. Those mortgage rates climbed to their highest level since 2008. The Mortgage Bankers Association of America reported the rate on a 30-year fixed-rate mortgage rose to 6.52% over the week ended September 23. The pain of higher prices not only hurt buyers but builders too. According to the NAHB Housing Market Index, confidence among builders fell to its lowest level since May 2020 as high costs of inputs and waning demand created a challenging environment. Building permits fell 10.0% to 1.5 million units in August, the lowest number since August 2020.

Moving to the safety of the greenback

Over September, currency markets posted large swings due to rising rates, high inflation, volatile commodity markets and economic uncertainty. The U.S. dollar was the main beneficiary. The DXY Currency Index, which tracks the U.S. dollar against other major world currencies, rose more than 3% over the month. It also climbed to its highest level since 2002. As the Fed aggressively lifted rates and the outlook for the global economy remained uncertain, investors piled into the relative safety of the greenback. The Canadian dollar moved to its lowest level against the greenback since 2020, largely in response to its close link with commodity prices, particularly oil, which fell over the month.

In the U.K., financial market stability was challenged. The British pound fell to its lowest level ever against the U.S. dollar late in the month after the new U.K. government announced sweeping tax cuts, raising concerns that inflation may tick even higher and push the economy into a deep recession. The yield on 10-year U.K. government bonds surged higher. In response, the BoE announced it would begin purchasing long-term government bonds at any quantity necessary to avoid unwanted tightening of financial conditions and ensure ongoing credit flow. This approach helped stabilize the U.K. dollar. Still, with so much uncertainty about global economic conditions, currency markets may be volatile.

Market performance - as at Sept. 30, 2022

Equity Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
S&P/TSX Composite Index C$	18,444.22	-4.59%	**-4.59%**	-13.09%	**-13.09%**	-8.10%	**-8.10%**
S&P 500 Index US$	3,585.62	-9.34%	**-4.56%**	-24.77%	**-18.01%**	-16.76%	**-9.56%**

Dow Jones Industrial Average US$	28,725.51	-8.84%	**-4.03%**	-20.95%	**-13.85%**	-15.12%	**-7.78%**
MSCI EAFE Index US$	1,661.48	-9.73%	**-4.97%**	-28.88%	**-22.49%**	-27.17%	**-20.87%**
MSCI Emerging Markets Index US$	875.79	-11.90%	**-7.26%**	-28.91%	**-22.53%**	-30.11%	**-24.06%**
MSCI Europe Index US$	1,454.90	-8.80%	**-3.99%**	-30.50%	**-24.25%**	-26.78%	**-20.44%**
MSCI AC Asia Pacific Index US$	138.92	-12.37%	**-7.75%**	-28.07%	**-21.60%**	-29.56%	**-23.47%**

Fixed Income Markets	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
FTSE Canada Universe Bond Index C$	1,050.08	-0.53%	**-0.53%**	-11.78%	**-11.78%**	-10.48%	**-10.48%**
FTSE World Investment Grade Bond	194.05	-5.24%	**-0.24%**	-20.48%	**-13.34%**	-21.50%	**-14.42%**

Index US$							

Currencies	Level	Month to date	Month to date (C$)	Year to date	Year to date (C$)	1 year	1 year (C$)
CAD/USD	0.7231	-4.02%	-	-7.63%	-	-7.32%	-

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)	79.49	-11.23%	-	5.69%	-	5.94%	-
Gold (US$/oz)	1,660.61	-2.95%	-	-9.22%	-	-5.48%	-