



## A Month



## in the Markets

**NOVEMBER 2023**

In this latest edition our Multi Asset Solutions Team look at the challenges investment markets faced in October. Global stock markets fell for a third month in October<sup>1</sup> after a sharp increase in bond yields triggered volatility across financial markets.<sup>2</sup>

### Market Overview

Yields on 10-year US government bonds soared to 16-year highs during the month<sup>3</sup>, while those on 30-year UK government bonds hit levels not seen since 1998. Yields on European and Japanese bonds also rose.

The yield represents the income an investor expects to receive from a bond. The sharp increase in yields recorded in October made bonds more appealing than stocks because they offer good returns with less risk.

With signs that stubborn inflation will keep interest rates higher for longer, investors have been demanding higher yields to protect their returns from being eroded.<sup>4</sup>

However, higher yields also mean borrowing costs for companies and households increase, potentially hampering investment, slowing economic growth, and burdening highly indebted companies and individuals. It also means governments have to pay more to borrow and cover the cost of their debt.<sup>5</sup>

The S&P 500 recorded three-months of consecutive losses for the first time since the onset of the COVID-19 pandemic in March 2020. The index, which measures the biggest listed companies in the US, fell by more than 10% near the end of October from its most recent high on 31 July – this is known as a ‘market correction’. The Dow Jones Industrial Index also fell in October, wiping out its gains this year.<sup>6</sup>

The Stoxx Europe 600, which measures European shares including the UK, had its worst October performance since 2020. While the month has typically ended with positive returns over the past 25 years, that pattern was undone this month due to surging bond yields, war between Israel and Hamas and underwhelming quarterly earnings reports.<sup>7</sup>

Concern that the conflict in the Middle East could escalate and spread to other parts of the region drove

the price of gold, considered a haven during times of uncertainty, to a five-month high.<sup>8</sup>

### **Baffled by bonds?**

It may be worth taking some time to learn the basics to help you better understand how they work. Visit our [Basics on Bonds page](#) for more information.

### **UK and Europe**

The Bank of England (BoE) is expected to keep interest rates at a 15-year high despite growing signs of a recession, defined as two successive quarters of negative growth.<sup>9</sup>

Britain's economy is on course for a contraction in the fourth quarter after a survey of business leaders reported another decline in activity, with the S&P Global UK Purchasing Managers' Index (PMI) falling to its lowest level since January.<sup>10</sup>

Consumer inflation in the UK has fallen more slowly than its developed-market peers, with the effects of 14 consecutive interest rate increases between late 2021 and August this year reverberating across the housing market, jobs and consumer spending.<sup>11</sup>

In the Eurozone, data released on the last day of the month showed that inflation across the region dropped to a two-year low in October, better than economists had expected, increasing expectations that interest rates will remain on hold. The economy, however, shrank slightly in the third quarter when compared with the previous three months, initial estimates showed.<sup>12</sup>

A survey of business leaders indicated that the Eurozone economy may also contract in the final quarter of the year, with the S&P Global PMI for October unexpectedly dropping to a three-year low as manufacturers cut staff and hiring in the services came to a near standstill.<sup>13</sup>

On 26 October, the European Central Bank (ECB) announced that its key interest rate would remain unchanged, the first pause after 10 straight hikes. It reiterated that maintaining rates at record highs 'for sufficiently long' would help lower inflation.<sup>14</sup>

### **US**

Data released in October showed that the US economy grew at its fastest pace in nearly two years between July and September as people spent more on everything from cars to concert tickets. This is despite interest rates on mortgages, loans and credit cards being pushed up by higher bond yields.<sup>15</sup>

Consumer confidence among Americans dropped to a five-month low in October, with most worried about rising prices, especially for groceries and petrol. They were also concerned about business conditions, politics, and higher interest rates. Consumer expectations for inflation also hit a five-month high, indicating that they expect prices to get even higher.<sup>16</sup>

Signs of a potential economic slowdown can also be seen in businesses spending less on new machinery and other equipment.<sup>17</sup>

After raising interest rates 11 times in a row between March 2022 and July 2023, the Federal Reserve (Fed) chose to hold steady in September. At the time, there was talk of one more rate hike in 2023, but the higher cost of borrowing, and companies and people spending less could help keep inflation down and potentially remove the need for rates to rise again.<sup>18</sup>

### **Asia Pacific**

A survey of business leaders showed that China's factory activity shrank in October, while growth in the services and construction sector unexpectedly slowed, indicating that the recovery in the world's second-largest economy remains fragile.<sup>19</sup>

The report, released on the last day of the month, came after data revealed that China's economy deteriorated in the third quarter due to a decline in export demand and a deepening property crisis. The government has taken steps to help; including raising spending on infrastructure, cutting interest rates to spur lending, and easing criteria on home purchases, but economists have called for more comprehensive reforms to reignite growth.<sup>20</sup>

Foreign investors sold Chinese shares for the third consecutive month in October, marking the longest

streak on record, due to concerns about the economic recovery, deflation, and the allure of higher-yielding and safer assets, such as US government bonds.<sup>21</sup>

On 31 October, the Bank of Japan (BoJ) announced it would be more flexible with the way it controls bond yields, a precursor to scrapping the country's ultra-loose monetary policies.<sup>22</sup>

At the same time, the BoJ announced that it kept its key interest rate unchanged at -0.1%. It is the last major central bank to maintain negative interest rates.<sup>23</sup> As a result, the yen weakened toward a 33-year low against the dollar, while yields on 10-year government bonds rose to the highest levels in a decade.<sup>24</sup>

## Outlook

We continue to hold the view that bonds are attractively priced.

Bond yields have climbed on the back of rising interest rates and indications from policymakers that they could stay high. Bond yields and prices move in opposite directions, so bond prices have come down.

We believe that interest rates are either at or near their peak, which means that bond market prices won't fluctuate that much.

The difference in yield between government bonds and company bonds is known as credit spreads, which is a measure of the health of a business. We expect they will probably also remain little changed at current levels. We believe that highly rated companies have healthy fundamentals (analysis of a business's financial statements) and have not experienced increased debt defaults. This gives us the confidence to buy these bonds and continue to earn an extra yield over government bonds.

We expect that the global economic environment will be one of low growth, while inflation will gradually decrease. We expect oil prices to increase.

The economic climate means that there is higher risk of credit downgrades on government bonds by credit-ratings agencies, which assess the abilities of countries to repay their debts much like a bank would a customer who wants to take out a mortgage.

We believe investors will be much more cautious when buying shares and base their decisions on valuations rather than being swept up in broad market rallies.

Therefore, our outlook reflects the positions in the funds, which are overweight bonds relative to the benchmark, underweight cash, and a slight underweight in shares.

All data as at 31 October 2023.

<sup>1</sup> S&P Global BMI, 31 October 2023

<sup>2</sup> Business Insider, 8 October 2023

<sup>3</sup> CNBC, 19 October 2023

<sup>4</sup> The Guardian, 4 October 2023

<sup>5</sup> Associated Press, 23 October 2023

<sup>6</sup> Yahoo! Finance, 31 October 2023

<sup>7</sup> Bloomberg, 31 October 2023

<sup>8</sup> Reuters, 28 October 2023

<sup>9</sup> Reuters, 25 October 2023

<sup>10</sup> Reuters, 24 October 2023

<sup>11</sup> Reuters, 30 October 2023

<sup>12</sup> CNBC, 31 October 2023

<sup>13</sup> Bloomberg, 24 October 2023

<sup>14</sup> CNBC, 26 October 2023

<sup>15</sup> Bankrate, 30 October 2023

<sup>16</sup> Bloomberg, 31 October 2023

<sup>17</sup> Associated Press, 26 October 2023

<sup>18</sup> Bankrate, 30 October 2023

<sup>19</sup> Bloomberg, 31 October 2023

<sup>20</sup> Associated Press, 18 October 2023

<sup>21</sup> South China Morning Post, 31 October 2023

<sup>22</sup> Reuters, 31 October 2023

<sup>23</sup> Bloomberg, 31 October 2023

<sup>24</sup> Reuters, 31 October 2023

## **Important Information**

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