December 2021

Market Review

Global Market Strategy @ Natixis Investment Managers Solutions

Economic & Political News

Economic data in December was mixed. Sentiment was supported by reports that the Omicron variant, while more infectious, produced less severe illness. However, this did not prevent the services Purchasing Managers' Index (PMIs) from the United States, the Euro Area, Japan, and the United Kingdom to lose part of its positive momentum.

On the labour front, Initial Jobless Claims and Continuing Claims continued to improve. However, November's job report fell short from expectations, showing that 210,000 nonfarm payrolls were added against the 545,000 expected. And, although the unemployment rate fell to 4.2% from 4.6% the month before, the large number of job vacancies continued to show a tight labour market. Similar dynamics could be seen in the Euro Area and the UK. Moreover, headline Consumer Price Index (CPI) figures, on a year-over-year basis, hit 6.8% in the US, 4.9% in the Euro Area, making a three-decade high in both regions, and 5.1% in the UK. Supply constraints and high energy prices remain largely behind price pressures.

The Federal Reserve (FED) adopted a more hawkish tone on the back of persistent inflationary pressures and labour market tightness. The central bank announced an acceleration of the tapering of asset purchases from USD15 billion to USD30 billion per month, which suggests that the tapering will conclude by March 2022. In addition, the *Dot Plot* was updated to reflect a forecast of three rate hikes in 2022. Moreover, the European Central Bank (ECB) announced that Pandemic Emergency Purchase Program will also end by March 2022, but additional purchases would be put in place to soften the transition throughout the year. As such, the central bank will use the traditional Asset Purchase Program to purchase EUR40 billion per month through Q2 2022, EUR 30 billion per month in Q3 2022 and EUR20 billion per month until rates are hike (the ECB does not expect to hike rates in 2022). The Bank of England (BoE) became the first G7 economy to increase its policy rate, from 0.15% to 0.25% and, the Bank of Japan announced it was tapering its corporate debt purchases introduced in March 2020. For its part, the People's Bank of China (PBoC) is moving in the opposite direction to try to stimulate its economic growth. After cutting the reserve requirement ratio by 50bps in early December, freeing up USD188 billion for banks, the PBoC lowered its one-year loan prime rate for the first time since April 2020 from 3.85% to 3.8%.

Equities

Following November's decline, equity markets bounced back in December supported by encouraging data regarding the severity of the illness caused by the Omicron variant. However, volatility remained elevated for most of the month. The S&P 500 gained 4.5%, the technology-heavy NASDAQ added 0.8%, the EuroStoxx 600 gained 5.2% 2000, while emerging markets continued to trail behind, advancing 1.9%. Globally, consumer staples, utilities and real estate were amongst the worst performer sectors, while consumer discretionary, communication services and information technology lagged.

Fixed Income

Core sovereign bonds were negative in December as investors digested the official announcement for a faster tapering of asset purchases and appetite for risk assets recovered from the previous month. The US 10-year government yield increased 7bps to 1.51% while the 2-year yield increased 17bps to 0.71%, leading to the flattest yield curve in over a year. This has led some observers to suggest that the curve's flattening is reflecting some investors growing concerns for a policy error by the FED that could end in a recession. Long dated European sovereign yields followed suit and moved upwards: the Bund gained 17bps to -0.18%, OATs 19bps to 0.20%, BTPs 20bps to 1.17% and Gilts 17bps to 0.97%.

Credit spreads declined in December. High yield bonds outperformed investment grade both in the US and Europe, gaining 1.9% (-54bps) and 1% (-37bps), respectively. The higher duration nature of the investment grade credit space, made both the US and Europe lose ground, retreating -0.1% (-6bps) and -1.1% (-12bps), respectively. For its part, the Emerging Markets hard currency space advanced both for the IG and HY credit ratings, increasing 0.6% (-36bps) and 1.6% (-72bps), respectively.

Emerging Markets

After dropping 4.1% in the previous month, emerging markets posted a 1.9% positive return in December —the largest one since last August. The announcement of several supportive monetary and fiscal policies seemed to strengthen investors sentiment following many months of negative news coming in from Chinese authorities. Since this policy shift, government yields have been trending down, suggesting more potential stimulus ahead.

Moreover, the Chilean central bank hike its policy rate to the highest level since 2014, the Mexican central bank also raised rates by most in almost five years, and the National bank of Hungary increased its required reserve rate and ended its government and corporate bond purchase program. Conversely, and despite the ongoing deterioration in inflation and the collapse of the Lira, the Turkey's central bank lowered the one-week repo rate in support of President Erdogan's desired monetary policy. The Lira hit a new all-time low, losing about half of its value against the dollar this year.

FX & Commodities

After soaring to a 16-months high in November on expectations for a faster tapering of asset purchases, the DXY Index remained flattish throughout December —when the FED officially confirmed the tapering acceleration—, declining 0.3% to 95.7. For its part, the Euro gained ground against the Yen and lost it against the Pound, which has appreciated against its major counterparties since the BoE hiked its policy rate in mid-December.

Commodities bounced back in December, the S&P GSCI Index increased 7.4% largely supported by large jumps in both WTI and Brent barrel prices, which increased 13.6% and 10.2%, respectively. On the other hand, natural gas prices continued to decline, falling 18.3% and stand now 41% off its highs back in October. Finally, precious metals prices advanced in the month, likely helped by a more stable US dollar and increased volatility within cryptocurrencies.

Developed Markets Equity - LC		Fixed Income Sectors - LC	
Top 3 Markets in December	**Return**	**Top 3 Markets in December**	**Return**
- OMX Stockholm	7.9%	- US HY	1.9%
- ISEQ Ireland	7.6%	- EM Sov HC	1.4%
- CAC 40	6.5%	- EU HY	1.0%
Worst 3 Markets in December		**Worst 3 Markets in December**	
- Hang Seng	-0.3%	- EU GOV	-1.2%
- Nasdaq	0.7%	- GLOBAL INF-LINKED	-0.7%
- OBX Norway	1.7%	- US GOV	-0.3%

Emerging Markets Equity - LC		Forex and Commodities - USD	
Top 3 Markets in December	**Return**	**Forex**	**Return**
- S&P BMV Mexico	7.4%	- DXY Index	-0.3%
- Thailand	5.7%	- USD/EUR	0.3%
- S&P Merval	5.3%	- USD/GBP	1.8%
Worst 3 Markets in December		**Commodities**	
- Moex Russia	-3.2%	- Gold	3.1%
- KSE-100 Pakistan	-0.4%	- WTI	13.6%
- PSEi Philippines	1.5%	- Bitcoin	-18.9%

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