Looking Back at the Markets in November and Ahead to December 2022

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This entry was posted on Dec 6, 2022 2:56:32 PM

and tagged Commentary

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The October bounce continued in November, with the S&P 500 up 5.59 percent and the Dow Jones Industrial Average (DJIA) up 6.04 percent, while the Nasdaq trailed with a respectable gain of 4.51 percent. Internationally, the news was even better, with developed markets up 11.26 percent and emerging markets leading the pack with a 14.85 percent gain. It was a good month across the board and surprisingly so for international markets after an extended period of underperformance.

Looking Back

A recurring rebound. November's rebound came from continued improvement in inflation news and increasing conviction that the Fed would slow rate hikes. With the shift in investors' expectations, the 10-year U.S. Treasury yield fell from 4.07 percent at the start of November to 3.68 percent by month-end. The fall in yields helped drive the Bloomberg U.S. Aggregate Bond Index to a 3.68 percent return. The fall in U.S. yields also started to pull the dollar back down, and the combination drove the outperformance of international markets.

Impressive third-quarter reports. The third-quarter earnings reporting season ended with an overall gain of 4.49 percent for the S&P 500, which was well above the initial expectations. These better-than-expected earnings reports also helped support the markets. And with earnings higher and valuations adjusting upward as rates pulled back, the market received two tailwinds during the month.

Declines in data. Although last month's data showed improvement, inflation was still high. Additionally, the recent jobs report and the service sector confidence survey suggested that improvement may not continue. And at the most recent Fed meeting, Chair Powell emphasized that a pivot was not in the Fed's plans anytime soon, suggesting that the market might be too confident—again.

Looking Ahead

Assessing the risks. The Covid-19 pandemic in China, which may prompt more lockdowns and supply chain disruptions, and the war in Ukraine may rattle markets in December. So, despite the strong market performance over the past couple of months, many risks remain, and we can expect more volatility in December. But, looking forward to the end of the year, there are also reasons to be cheerful.

This is typically a positive season for markets (the term “Santa Claus rally” is there for a reason). Many of the recent risks, such as the midterms, have now passed. And while international risks in Ukraine and China could get worse, signs show that they are under control, at least for the moment.

Stabilized markets. Even though midterm years have often been volatile, markets have tended to rally after the elections. Additionally, the reduced uncertainty around inflation, the Fed, and the economy should help support the markets. And with slower growth and inflation, we could see valuations stabilize and improve further. We may even see some appreciation as fears about earnings growth moderate.

Economic slowdown. Despite the current good news on earnings, concerns about fourth-quarter earnings continue to mount and will likely continue to weigh on markets. Housing construction, a significant component of overall investment, continues to drop sharply, and both consumer and industrial confidence are in downtrends. A slower economy typically leads earnings down, and analysts’ estimates of future earnings continue to decline.

Looking forward, even if we don’t get another month as good as the past two, the prospects for the rest of the year look pretty good. The upside of the weak year to date is that much of the damage to the markets and economy may have already been done. And for the economy, slower growth should help contain inflation.

Markets Rallied as Risks Decreased

We saw the markets rally in November as risks subsided. While some of those risks may return, others are gone for good. On the economic side, there’s still growth, which will help both earnings and the market. Many sources of uncertainty continue to show signs of improvement, and while risks remain, most of them are likely incorporated into markets, so further effects should be limited.

November was a solid month for financial markets, and while the chances are good, we may not see that again in December. But we could see continued progress with many of the risks that shook the markets in 2022—and that’s a good way to close out the year.

Happy holidays!