MARKET RECAP

September 2022

Rotman Commerce Trading Group

CONTENTS

GLOBAL MARKETS INSIGHT

IN THIS ISSUE

- Fixed Income Markets – Historically high levels of inflation saw central banks continue to commit to hawkish monetary policy with the FED and BOC both hiking rates by 75bps this month. Credit spreads continue to widen as elevated geo-political risk and pandemic related supply chain issues increase uncertainty in the markets.

- Commodity Markets – Escalations in the Russia-Ukraine war continues to add challenges in production and led to pressure on prices. Weaker energy demand and extending contractionary monetary policies led to a decline in energy prices for the 4th consecutive months. Gold prices are also down for a record number of months and volatile due to fluctuations in dollar and interest rate expectations.

- Equity Markets – Decline in equity prices across global indices were driven by extended interest rate hikes resulting in lower customer discretionary spending and profitability expectations. The British Pound and Euro plummeted to a record low against the dollar lowering investor confidence Asian markets such as Thai and Indonesia remained strong and experienced positive returns.

- Industry Overview – telecommunications underperform relative to the market, while promising minimal growth of 0.1% by year-end. Acceleration of 5G network deployments and increased competition in wireless broadband market remain relevant industry trends, and seismic shifts in the Canadian telecom landscape are on the horizon.

FIXED INCOME

Month in Review

The Fed ended September with a 75 bps rate hike amid high inflation. Liquidity in the bond market hit historical lows due to huge sell-offs caused by uncertainty in the current high rate environment. UK markets experienced significant net-selling as a result of the new Chancellor’s sudden announcement indicating steep tax cuts on the horizon. The Bank of England stepped in promising to purchase 65 billion GBP of long-dated securities. Investment grade corporate bonds suffered record low prices since 2004. Market volatility has caused US 10-Year and 2-Year Treasury Yields to end this month at 3.829% and 4.279% respectively, continuing the massive inversion of the curve and adding to market pressure.

Rates

Interest rates continue to reach historical highs this month, with the Fed predicting rates of 4.4% by December 2022. In addition to the 75 bps hike in September, Fed officials have indicated their intention of hiking until the funds level hits a terminal rate of 4.6% in 2023. Stocks wavered and the Dow Jones Industrial Average fell slightly following this announcement. Furthermore, PCE-measured inflation is predicted to reach 2.8% in 2023, 0.2% more than what was originally projected in June 2022.

The Bank of Canada increased their overnight rate to 3.25% earlier this month while proceeding with quantitative tightening. Amidst supply disruptions, COVID-19 outbreaks, and the war on Ukraine continuing to impact growth and prices, inflation rates will continue to rise in the months to come.

As of September 28th, the Bank of England announced plans of quantitative easing, bringing optimism to the market in hopes that affliction from central banks is coming to an end. Massive tax cuts in England at the end of this month also show signs of increasing interest rates in order to tame already high levels of inflation.

Credit

The current hiking cycle leaves credit markets under pressure due to widening credit spreads and the lack of issuance at higher yields. Bank of America labelled credit stress in the “borderline critical zone" by month-end, and future economic tightening threatens market stability.

Globally, September saw the highest number of cancelled or delayed bond deals since June. Both junk and investment grade debt had the largest fund withdrawal and spread widening since 2020, and the average high grade spread hit 164 bp. CCC rated bonds are down almost 17% this year, and investors are moving away from high risk bonds due to fear of economic downturn, causing the risk premium gap between BB and B rated debt to further widen.

COMMODITIES

Agriculture

As of 30th September, wheat futures are trading at $9.20 per bushel, +15.8% MTD, after quite a geopolitical intensive month that affected prices across the industry. h Despite Russia's announcement of a record wheat crop this month, the reluctance of Russian bankers, insurers and shippers to do business due to economic sanctions has caused numerous issues, driving wheat prices up. As the #1 exporter of wheat, Russian sanctions have caused major supply issues at a time in which the US is reporting lower than expected production. Recent escalations in the Russia-Ukraine conflict have also bolstered prices, as Putin threatens to break up the Black Sea Grain agreement. While the deal allows Ukraine to continue maritime trade of grain during war through the Black Sea, Putin has been criticising the exports, threatening to cut off trade and remove supply.

Soybean prices have experienced extreme volatility, ending on a loss after strong price action in both directions. Mid-year production in Brazil disappointed after harvest numbers topped at 126 million tonnes-down 9.7% YoY due to drought-causing prices to soar intra month. High prices and lacklustre demand throughout the month caused a 6.2% YoY drop in imports across China and a subsequent fall in prices. Suppliers forced to cut production due to a shortage caused by increased demand, indicates the potential for recovery in imports. Another contributor to rising prices stems from massive spikes in the cost of fertilizer. The rising cost of gas-a primary ingredient in fertilizer-is making it unreasonable to buy or produce large amounts of the chemical, thus squeezing an already tight supply.

Corn prices have been rising steadily after hitting an 8-month low back in July, with the commodity slowly decoupling from oil pricing as supply concerns have outweighed low demand concerns. Output for the US is estimated at 13.9 billion bushels in the next year, a 415 million decline from prior estimates as yields struggle throughout the world. Summer droughts in the US have devastated production this year while La Nina effects have been terrorizing South American harvests, creating further supply issues.

Energy

Oil prices have been on a steady decline for a 4th consecutive month, as markets sell off due to weak energy demand and continued contractionary monetary policy. WTI futures traded at about $79-80 per barrel, with the surging US dollar adding to overall bearish sentiment as the commodity becomes more expensive to foreign nations. Russian exports also declined by more than 250,000 barrels/day this month, further revealing the effects of lessening demand. A potential surge in prices is expected in the coming weeks as the upcoming October OPEC meeting could result in supply cuts over the concerns of weak demand. Other factors such as the Nord Stream Pipeline leak and the uplifting of China's lockdown could further boost prices, but such factors leading to surges in oil prices are hypothetical at best.

Precious Metals

Metal markets finished the month off mixed on the back of dollar and rate movements, deterioration in the global economic backdrop, and geopolitical tensions.

Over the course of Q3, gold prices have fallen 7.7%. September also marked the bullion's sixth consecutive monthly drop, creating the biggest streak of monthly decreases in four years. Movements in gold have been largely influenced by changes in the dollar and the interest rate outlook. In particular, fears surrounding imminent large interest rate hikes from the U.S. Federal Reserve have made investors less keen on holding the bullion due to the increase in opportunity cost from the non-yielding asset.

> **We're still essentially in a pretty weak environment for gold with an aggressive Fed and some Fed speakers throughout the week likely to hammer home the point that rates are going to be higher for longer," and added that "we could see prices fall below the $1,600 level.**
>
> *Ryan McKay (TD Securities, Commodity Strategist)*

Silver is on track to reach a second straight quarterly decline. However, given struggles in the global electronics sector and deterioration in the global economic backdrop, silver prices may also find themselves under pressure.

Other metals such as palladium, aluminum, nickel have gained sharply following geopolitical tensions that have added weight on their availability. Moreover, limitations in mine supply from South Africa have placed more pressure on these commodities.

EQUITIES

Month in Review

The month of September saw heightened volatility across all asset classes. Despite recent data indicating a strong labour market and a low unemployment rate, equity markets globally continued to move in favour of the bears. Many of the concerns highlighted by investors in recent months including shifts in geopolitics and the unravelling of macroeconomic policies adopted during the COVID-19 pandemic have become even more pronounced. Towards the end of the month, events such as the mobilisation of Russian troops in response to Russia's shortcomings in the Russia-Ukraine conflict and leaks in the Nordstream pipelines—a system of pipes that transports liquified natural gas directly from Russia to the EU—signal the possibility of an escalation in geopolitical tensions. These concerns have translated over to the CBOE Volatility Index [$VIX] which broke its 30 point ceiling, an indication of high levels of volatility, towards the latter end of the month. Since the time of reporting, it has remained above 30 points.

Figure 1:VIX for September 2022

Moreover, as Central Banks across the world attempt to reign in on inflation by aggressively hiking interest rates, investors have come to realize the necessary sacrifices that these policies have on economic output. Nonetheless, there remains an air of certainty among Central Banks in developed economies that they are still capable of achieving "modest" levels of economic growth before year-end. Overall, investors remain speculative as they try to navigate the potential future effects of current changes to macroeconomic policy and the geopolitical landscape.

U.S. & Canada

Figure 2: S&P 500 Chart for September 2022

Stock market indices in the United States and Canada decreased sharply over the month of September. More specifically, the Nasdaq fell 1% or 109.97 points from 11,740.56 to 11063.64. The S&P 500 declined 1.1% or 43.96 points from 4005.80 to 3836.21. The Dow Jones Industrial Average [DJIA] decreased 1% or 313.45 points from 31,328.07 to 30,824.65. The high volume trading and declining trend across markets indicates a negative sentiment among investors. Notwithstanding the geopolitical tensions affecting global supply chains, volatility in the markets can be attributed to the uncertainty among investors in the extent of interest rate hikes by the FOMC. The volatility in North American markets has been noticeable since the month of August as stocks rose and then abruptly fell the next month. Stock prices depend on the FOMC and the FOMC is still in the process of taming inflation. The hiking of interest rates leading to higher borrowing costs is in turn causing discretionary consumer spending to decrease. Equity prices inevitably decline as a result of a loss in investor confidence in firms' ability to generate profits. It is recommended for investors to save cash on hand in case there are better investments to be made in the future. An additional factor of the pessimistic sentiment is the continued supply chain crunch as a result of the Russia-Ukraine war. The war is halting the flow of goods, causing high product inflation, and increasing product shortages, negatively affecting the value of equities.

Europe

European markets have been under strenuous pressure since the beginning of the year. Higher than expected inflation was not well received by equity markets that priced in the anticipation of aggressive future rate hikes. The main European index (STOXX 600) fell by 4.86% in September after gains in July and August which now seem to have been a temporary bear market bounce.

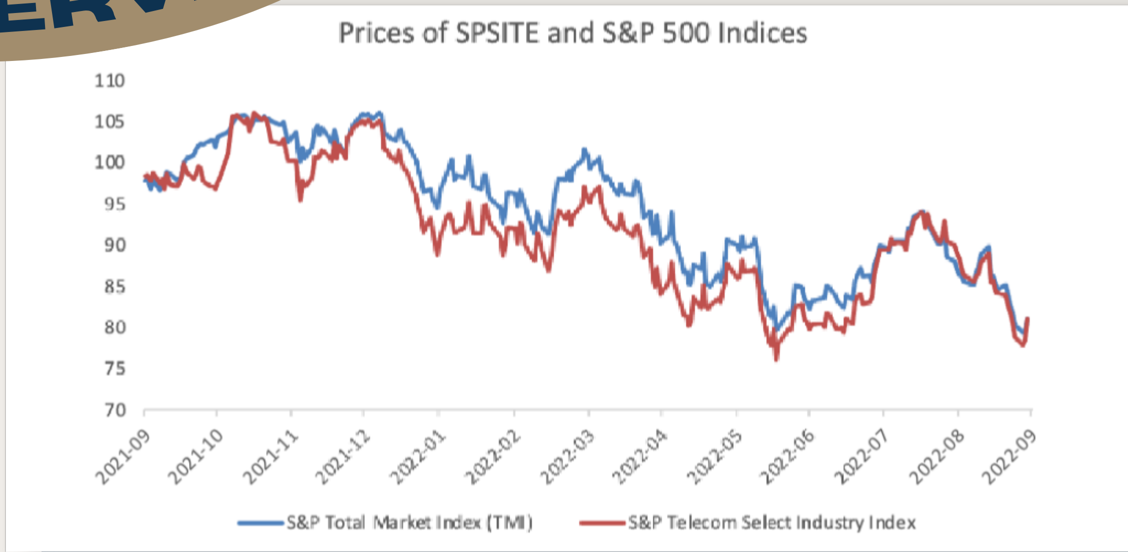
Currency dynamics in the eurozone have also had a negative impact on equities this month. The Euro and the pound are at their lowest value relative to the US dollar in over two decades. European investors saw their relative purchasing power slashed which led to a tumbling risk sentiment in the region.

Asia

Similar to equity markets across Europe and North America, Asian equity markets also experienced declines in response to current geopolitical conflicts and interest rate hikes. The MSCI Asia Pacific Index declined 1.1% while the Japanese index (Nikkei 225) was down by 7.55% in September. Despite global pessimistic sentiment, investors in the ASEAN region remained optimistic with Indonesian and Thai indices demonstrating positive returns. This is driven by the re-opening of regional economies and high energy prices that have played into the hands of the nations whose exports primarily focus on commodities. Looking forward, the Chinese equity market is worth paying attention to. In September, Chinese growth continued to subside with the lack of confidence among consumers under the strict COVID-19 policy and a deteriorating real estate market. As the 20th Party Progress nears, many measures will be reassessed including the COVID-19 policy. These changes will potentially have a paramount influence on the Chinese equity markets as well as global equity markets.

INDUSTRY OVERVIEW

TELECOMMUNICATIONS



The S&P Telecom Select Industry Index (SPSITE) is comprised of stocks in the S&P Total Market Index (TMI) that fall into the communications equipment, integrated telecom services, and wireless telecom services sub-industries.

INDEX NAME	1 YR RETURN
S&P Telecom Select Industry Index (SPSITE)	-17.65%
S&P Total Market Index (TMI)	-17.20%

Industry Trends and Performance

The Telecommunications sector consists of products such as telephone, internet, and satellite. The major players based on IBISWorld market share are China Mobile (12.2%), Deutsche Telekom (8.9%), Verizon Communications (8.5%), and AT&T (7.5%).

Industry growth by the end of this year is expected to be minimal at an annualized rate of 0.1%, with key drivers including the acceleration of 5G network deployments, higher penetration rates for mobile devices and increasing average revenue per user. Population, and thus telephone subscriptions in urban areas has been on the rise, creating the opportunity for increased wireless subscribers and revenue generation.

INDUSTRY OVERVIEW: TELECOMMUNICATIONS

The industry was on the decline this month resonating with the overall market performance and added market volatility due to pandemic lockdowns in China, weather disruptions in Florida and expectations of a global recession.

The S&P Telecom Select Industry Index reported a -9.63% return last month and -17.65% return YoY. Recently, the industry is becoming more competitive due to improved fixed wireless connections, and growing demand in the multi-access edge computing and private cellular networks. There is also a switch to more decentralised government broadband infrastructure funding with the $1 trillion Infrastructure Investment and Jobs Act for continued investments in broadband adoption

Industry Spotlights

US telco Verizon

On September 28th, Verizon executives revealed new product offerings and partnerships at North America's most influential connectivity event, Mobile World Congress Las Vegas. Such examples are creating the world's first 5G gaming handheld device, powerful fixed wireless broadband connectivity, and a streaming deal with National Football League. In collaboration with Razer and Qualcomm, the company introduced the new Android handheld gaming device, Razer Edge 5G, leveraging the strong demand for high-performance mobile gaming.

Additionally, they introduced the Verizon Receiver working with Qualcomm again, which will employ its powerful network technologies and Qualcomm 5G Fixed Wireless Access Platform. This product becomes industry-leading and reliable broadband connectivity with a 100% increase in upload speeds.

Seismic shifts in telcom on the Horizon?

Telcom giant Rogers Inc's (RCI.B) proposed $26-billion acquisition of Shaw Communications Inc, continues to hang in regulatory limbo as Canadian competition authorities push back on a merger announcement released 18 months ago. Shareholders of RCI.B have been left with the short end of the stick as they saw the stock recently plummet to its two-year lows and end off the month 5.87% down, underperforming its peers. Time delays combined with ongoing uncertainty are making analysts increasingly bearish on Rogers Inc, expecting prices to fall in the near future. Major industry rivals BCE Inc's Bell, and Telus Corp, are taking advantage of the delay through increased investments and capital spending to increase their share in the market.

DISCLAIMER

Any analysis or conclusions drawn in this article were developed through the use of publicly available information and resources. This document was curated solely for educational purposes and should not be constituted or substituted as professional investing advice; the Rotman Commerce Trading Group (RCTG) is not liable for use of the information or suggestions embedded in this article made by viewers.

The information contained in this report is made up of data collected by RCTG from sources considered to be reliable, but no representation or warranty, whether expressed or implied, is made by RCTG or its associates in coherence with its accuracy or correctness.

The content within this document is in no shape or form associated with the opinions or views of the University of Toronto or the Rotman School of Management.

Information or visuals within this report shall not be redistributed or replicated by any such person without the consent of the owner, RCTG and its affiliates.

SOURCES

- https://www.bbc.com/news/world-europe-63071552
- https://www.federalreserve.gov/newsevents/pressreleases/monetary20220921a.htm
- https://am.jpmorgan.com/hk/en/asset-management/per/insights/market-insights/monthly-market-review/
- https://www.federalreserve.gov/newsevents/pressreleases/monetary20220921a.htm
- https://www.federalreserve.gov/newsevents/pressreleases/monetary20220921a1.htm#:~:text=The%20Board%20of%20Governors%20of,%2C%20effective%20September%2022%2C%202022.
- https://www.nasdaq.com/articles/stock-market-news-for-sep-21-2022
- https://tradingeconomics.com/united-states/interest-rate
- https://www.bankofcanada.ca/2022/09/fad-press-release-2022-09-07/
- https://www.reuters.com/markets/europe/bank-england-buy-long-dated-bonds-suspends-gilt-sales-2022-09-28/
- https://www.cnbc.com/amp/2022/09/21/fed-rate-hike-september-2022-.html
- https://www.nytimes.com/2022/09/29/us/politics/tax-cuts-uk.html
- https://www.wsj.com/livecoverage/stock-market-news-today-09-29-2022/card/bond-market-liquidity-is-really-bad-right-now-K8Lj4cRZ8N1M550Gxawp?mod=Searchresults_pos1&page=1
- https://www.cnbc.com/2022/09/28/bank-of-england-delays-bond-sales-launches-temporary-purchase-program.html
- https://www.reuters.com/world/uk/imf-moodys-censure-uk-policy-bank-england-says-will-act-big-2022-09-28/
- https://www.wsj.com/articles/wild-moves-send-stocks-and-bonds-lower-in-third-quarter-11664514134
- https://www.bloomberg.com/news/articles/2022-09-30/credit-market-moves-toward-break-point-as-sales-flop-funds-flee
- https://www2.deloitte.com/us/en/pages/technology-media-and-telecommunications/articles/telecommunications-industry-outlook.html
- https://telecoms.com/517538/oneweb-prepares-to-launch-36-satellites-from-india/
- https://www.theglobeandmail.com/business/article-rogers-shaw-merger-telecom/