Weekly Market Update

Central banks spark global equity rally

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- U.S. and European stocks surge on prospects for further QE in Europe and additional stimulus from China.
- Dovish ECB commentary sends Eurozone bond yields and the euro lower.
- A continued “risk-on” climate dents demand for U.S. Treasuries and supports corporate bonds.
- Housing and labor market conditions are bright spots in a light week for U.S. data releases.
- In our view, Q3 U.S. economic weakness is ebbing, paving the way for a stronger Q4.
- We believe U.S. stocks may extend their recent gains into year-end, although not in a straight line

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After a cautious start to the week, global equity markets received two late-week lifts: First, European Central Bank (ECB) President Mario Draghi indicated that the ECB would consider expanding its quantitative easing (QE) program at its December meeting to spur the region’s recovery and inflation rate, both of which are potentially vulnerable to slowing growth in the emerging markets.

This was followed by an announcement from China’s central bank that it was cutting its one-year lending rate, one-year deposit rate, and reserve requirements for banks. These measures followed Beijing’s mid-week injection of 105.5 billion yuan ($16.6 billion) to the financial system in order to boost liquidity for banks and encourage lending to small businesses.

Equities

In the U.S., the S&P 500 Index gained 2.1% for the week, with strong corporate earnings reports contributing to the advance. Since hitting a low of 1,867 on August 25, the index has climbed about 11% through October 23, propelling it back into positive territory (+2.5%) for the year-to-date period.

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In Europe, the STOXX 600 Index jumped 4% for the week in local currency terms, although that gain was reduced to just 0.82% when translated into U.S. dollars, reflecting the euro's substantial weakening (from about 1.14 to 1.10) versus the U.S. currency.

Despite the concerns that prompted the ECB's dovish signals, recent data releases show that the region's lending conditions continue to improve, credit standards have eased for both business and consumer loans, and loan demand has picked up. In addition, Eurozone manufacturing and service-sector activity topped forecasts in October, suggesting that the region's modest recovery hasn't yet been weakened by the economic slowdown in China. The possibility of further deceleration in China, which reported third-quarter GDP growth of 6.9% (its slowest pace since 2009), and in other large emerging-market economies, was among the ECB's primary concerns.

Chinese equities were up modestly during the past week, posting their biggest daily loss since mid-September before surging at the end of the week. There are encouraging signs for China's economy, including robust sentiment from real estate developers and buyers, and double-digit growth in auto sales. Emerging-market stocks as a whole lost ground for the week through October 22 amid sagging commodity prices. Although we continue to have longer-term concerns about China, in the near term it remains the one market that could ignite a rally across the developing world by surprising to the upside.

Fixed income

U.S. Treasury yields edged higher during the week as "risk-on" sentiment continued to pervade the market. The yield on the bellwether 10-year U.S. note, which began the week at 2.04%, rose to 2.09% on October 23. (Yield and price move in opposite directions.) The market's better sentiment was supported by the ECB's soothing remarks, rising stock prices, a number of better-than-expected U.S. earnings releases, and some solid U.S. economic data. Meanwhile, the prospect of further support from the ECB energized the Eurozone sovereign bond market, as yields on German, Italian, and Spanish bonds fell sharply, and stabilized spreads for emerging market-debt.

In contrast to U.S. Treasuries, "spread" sectors (higher-yielding, non- Treasury securities) benefited from investors' improved mood. Investment-grade and high-yield corporate bonds led the way, buoyed by positive fund flows.

Current updates are available here. For additional insights on commodity markets from TIAA-CREF portfolio manager Navaneel Ray, view our Weekly Market Perspective Video.

Housing releases highlight a quiet week for U.S. economic data

The past week's data releases showed fresh evidence of the healthy U.S. jobs and housing markets. Among the reports:

- **First-time unemployment claims,** which had fallen sharply in the prior two weeks, inched up to 259,000, while the less-volatile four-week moving average dipped slightly, to 263,250, its lowest level since 1973.

- **Homebuilder sentiment** reached its highest level since 2005 in September, according to the National Association of Home Builders/Wells Fargo index.
- **Housing starts** touched a nearly eight-year high in September**,** while **existing home sales** easily topped forecasts, supported by low mortgage rates, steady jobs growth, and a slight improvement in credit availability.
- **Home prices** rose 0.3% in August, according to the FHFA. For the 12 months ending in July, prices were up 5.5%.
- The index of **leading economic indicators** published by The Conference Board fell 0.2% in September but still suggest that the U.S. economy is on track for moderate growth.

Outlook

With the S&P now having almost fully recovered the losses sustained in the recent correction, we believe the U.S. equity market is unlikely to revisit its August lows. In fact, we would not be surprised if the S&P 500 is able to reach a new high by year end—although further pauses are likely along the way. Encouragingly, even before the week's ECB-fueled boost, more economically sensitive cyclical stocks and value shares led the market's advance. This buttresses our view that the U.S. economy's third-quarter weakness is ebbing, and the market is discounting improved fourth-quarter activity.

Corporate earnings have been a further support: with more than 30% of companies reporting so far, well over 70% have beaten expectations, despite a period of weaker economic activity.