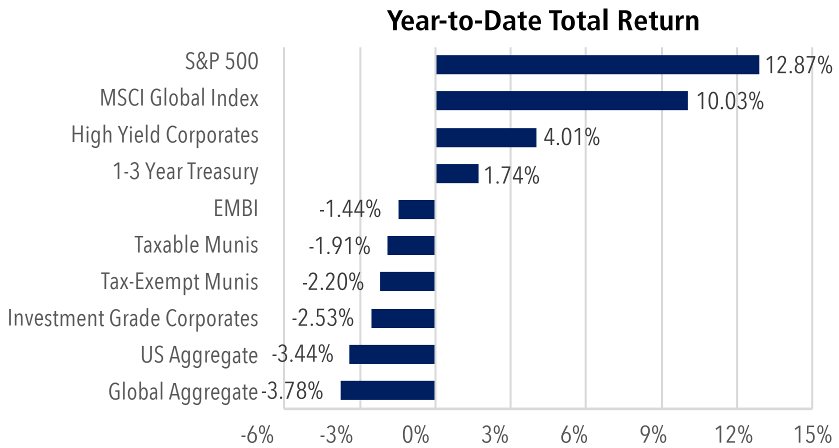
Week Ending: **October 20, 2023**

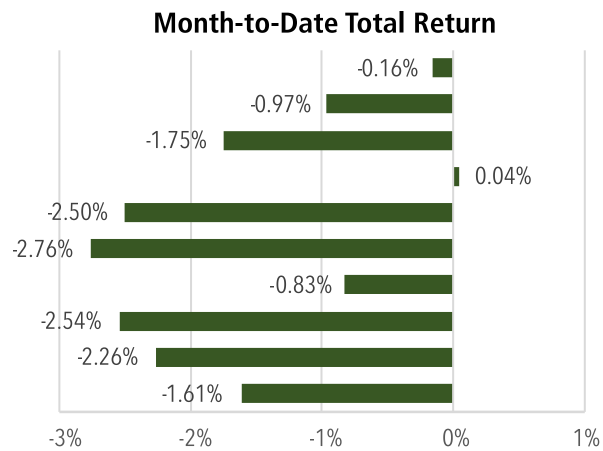
Out Of Control

Economic Overview:

Data this week revealed that U.S. retail sales in the so-called "control group," which excludes autos, gasoline, building materials, and food services, surged 0.6% in September and 3.8% versus a year ago to a new series high. In brief: bet against the U.S. consumer at your own peril. Less heralded, though no less consequential, were developments on the goods production side of the economy. Famously, goods production stalled, then boomed, and then busted during the Covid Era (2020-2022). Of late, weak manufacturing sector readings underpinned many bearish economic outlooks. However, quietly, goods production appears to be forming a bottom. The manufacturing purchasing managers' index (PMI), though still below 50, rose to 49 in September from a low of 46. And this week's data showed Industrial Production rose sharply in September and is now up versus a year ago. If the goods sector of the economy recovers and the consumer remains strong, will the case for a near-term economic downturn evaporate? Yes, we say.

Total Returns by Asset Class





Source: Bloomberg

Highlights of the Week:

High Yield: The size of the US high-yield bond market has fallen by 28% since the peak in 2021, primarily due to an abundance of high-yield issuers receiving investment grade upgrades over the past several years. The scarcity effect of fewer high-yield bonds outstanding should provide a technical tailwind for the asset class.

Corporates: This week, primary issuance totaled $25 billion, predominantly from banks post-earnings. In addition to three of the "Big Six" banks, PNC Financials Services Group issued new debt this week, leading the way for regional banks. However, amidst a softer market tone, almost all new deals were cheaper post-issuance, with interest rates spiking higher and investment-grade corporate spreads rising five basis points to an option-adjusted spread (OAS) of 129.

Municipals: This week, Governor Pritzker asserted that he would veto any legislation in Chicago that would impose a financial transaction tax since it could encourage Chicago exchanges to leave the state. The tax legislation question was raised as Mayor Johnson unveiled his 2024 budget for the City earlier in the week, which includes some optimistic special tax projections to fill a $538 million budgetary hole. Nevertheless, Fitch upgraded the City's rating to BBB+/Stable from BBB/Stable yesterday despite the structural imbalance. Municipal market fund outflows for September totaled $4.4 billion, the highest of any month in 2023. September's levels increased year-to-date outflows to $12 billion.

Equities: The U.S. equity market fell for the week as higher interest rates and escalating geopolitical risk in the Middle East drove a risk-off tone. The consumer discretionary, real estate, and technology sectors led markets lower, while the consumer staples, energy, and communications sectors were the best performers.

Securitized Products: Softness in risk markets and a better outlook for new issuance in the European Collateralised Loan Obligations market have led to slight upward pressure on spreads over the last few weeks. Despite higher spread levels, secondary market trading has fallen considerably following a period of above-average volumes. Overall, demand for high-quality bond profiles remains. However, market participants with such holdings are reluctant to sell, hence the fall in secondary market activity.