# 3-Month Market Review

(as at March 31, 2023)

## Banking Sector Turmoil Reduces Rate Fears, Helps Stocks

### Latest Developments

After a topsy turvy three months, stocks ended the quarter with healthy gains and recovered a generous portion of the losses incurred in 2022.

- Concerns over the health of the banking sector traversed through the markets following the collapse of Silicon Valley Bank (SVB), Signature Bank, and other regional lenders in March. Strangely enough, this was an impetus to push up stock prices.
- SVB and Signature Bank were the second and third-largest bank failures in US history, with combined assets of $319 billion, according to the U.S. Federal Deposit Insurance Corporation.
- Nevertheless, global stocks, measured by the MSCI World Index, gained 7%. U.S. stocks and European 500 stocks both rose by 8% and 9% respectively.
- These gains were led by shares in Big Tech, reflected in the Nasdaq Composite index rising by 17%, its strongest quarterly performance since 2020. The likes of Microsoft and Apple are seen as less exposed to a potential downturn in bank lending if the recent turmoil in the regional banking sector were to continue.
- Elsewhere in major markets, we saw positive developments in European and Chinese growth indicators.
- The spike in energy prices from the war in Ukraine was expected to send Europe into recession over the winter, but growth has remained positive. Europe has benefited from the unusually warm winter and consumers are benefitting from job gains, improving real incomes and falling energy prices.
- The *Financial Times* reported that in March, activity in China's non-manufacturing sectors grew at its fastest rate in more than a decade as business confidence rocketed and demand grew steadily. Investors aren't too euphoric about this, however, since much of the immediate boost from dismantling Covid-19 restrictions has already passed and the recovery is likely to moderate over the coming months.
- Even bonds got in on the action and showed a muted but positive return of 3% (for core U.S. bonds).

### What this Means

- Investors are concerned that the collapse of SVB may trigger a financial crisis, like 2008. While there are major differences, SVB's fall-from-grace is due to the bank's poor risk management. Irrespective, the banking system is ultimately supported by trust, so regulators acted quickly to restore confidence. Still, the ripple effect of SVB's failure tightened financial conditions, which has the effect of slowing down the economy and reducing the risk of inflation.
- Market movements can often appear counterintuitive. While the turmoil in the banking sector is, in itself, very bad, the stock market took the view that the silver lining could be that these troubles may prevent the US Federal Reserve from additional rate hikes.
- To be fair, the failure of SVB was due to mismanagement of its interest rate exposure. Fed chair Jerome H. Powell remarked that SVB's collapse would have a comparable (wider economic) impact of an extra interest rate hike.
- The Fed maintains that interest rates could go higher, stating: *"If we need to raise rates higher, we will."* Investors may be overly optimistic as consensus believes that rates have peaked and anticipate rate cuts by the year-end. Time will tell who is right.

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