December 2022

Monthly Market Update

A challenging year with interest rates likely to remain high

INFORMATION CONTAINED IN THIS REPORT CURRENT AS AT 16 JANUARY 2023

Financial markets were weaker across the board in December having ended November on a stronger note. The unwinding of extremely loose monetary policy globally, easy fiscal policy, the invasion of the Ukraine by Russia which forced energy prices higher, overhanging supply chain issues and inflation all continued to influence movements across all assets. In November the Australian share market ended on a high and spent December in retreat. The S&P/ASX 200 Total Return index decreased 3.21% over the month following the lead from global share markets which decreased 5.49% as represented by the MSCI World Index. Bond and property markets also gave up ground as Interest rate rises continued to be front page news. The US Federal Reserve raised the official interest rate again by 0.5% in December to 4.1% whilst the Reserve Bank of Australia increased our rate another 0.25% to 3.10%. This was the eighth month in a row that the RBA hiked. Whilst the RBA has not ruled out further rate hikes there is an expectation by market analysts that the tightening cycle is close to a peak. It may be a bit too soon to be forecasting a peak in the interest rate cycle, but at the very least, we expect a longish pause by the RBA.

This was reinforced in RBA Governor Mr Lowe's speech. The Governor stated, "the Board expects to increase interest rates further over the period ahead, but it is not on a pre set course. It is closely monitoring the global economy, household spending and wage and price setting behaviour. The size and timing of future interest rate increases will continue to be determined by the incoming data and the Board's assessment of the outlook for inflation and the labour market".

In Australia GDP expanded by 5.9% over the year to September 2022. A drag of -0.2% came from the real estate sector where Ownership Transfer Costs (turnover) plunged by 11.2% as a result of higher interest rates. Household spending growth slowed with motor vehicles sales, hotels, cafés, restaurants and transport services contributing most of the 1.1% growth in household consumption. While not as strong as in the June quarter, the reopening up effect was once again apparent as a key driver of consumer spending.

In the US investors were encouraged by statements from Federal Reserve Chair Powell that the pace of interest rate hikes will likely slow this year. However, investors were left slightly disappointed by clear signs from the minutes that the central bank would need to keep interest rates higher for longer to tame inflation. The Governor seemed at pains to address any misunderstandings by the market, stating that it was "important to clearly communicate that a slowing in the pace of rate increases was not an indication of any weakening of the Committee's resolve to achieve its price stability goal".

Emmanuel Calligeris
Chairman of the Investment Committee

Although inflation remains centre stage, the focus continues to shift towards more core measures of inflation.

Over the coming months, the base effects from the sharp rise in commodity prices in 2022 will push headline inflation lower. However, it is the core inflationary pressures, such as wages and the labour market, that will likely dominate the reaction function of the central bank over the coming months. Recent labour market data in the US is not showing clear signs of slack, with stronger-than forecast private job creation, lower initial jobless claims and above expected non-farm payrolls. Wage pressure data was mixed, with the average hourly earnings below expectations yet the quit rate from the Jolts survey remaining high, typically resulting in employees changing jobs for higher wages.

In China, it is surprising how quickly policy has moved from 'zero covid" to reopening and lifting most restrictions.

As China re-opens, the impact on the domestic and global economy could be significant.

In the short term the rapid spread of COVID-19 is likely to be a negative for activity as cases and mortalities rise. The experience from other countries is that once the virus has passed through the population, and especially if vaccination levels can become more effective, then economic activity will rise strongly. This should be seen on numerous levels – higher consumption and private sector investment, increased volumes of foreign trade and travel, and a potential recovery in China's property market. There will be higher demand for fuel and commodities which could see upward pressure on prices and inflation in the middle to latter part of 2023.

As mentioned last month, the US Federal Reserve has not finished tightening policy this cycle, however, is likely to be less aggressive as we head into 2023. The Reserve Bank of Australia has become more cautious in its policy settings and the global economy is already near recession because of the strong U.S. dollar and a weak Chinese economy. As mentioned above, China has to backed away, from the policies that have been depressing activity. The near-term outlook is challenging however markets are forward looking and sensing a pause in the interest rate cycle, have rallied strongly at the time of writing. We are likely to see further strength in early 2023 before a more turbulent second half.

Returns

31st December 2022

ASSET CLASS RETURNS ARE BASED ON

Australian Cash
RBA Bank accepted Bills 90 Days

Australian Bonds
Bloomberg AusBond Composite 0+ Yr TR AUD

International Bonds Hedged
BarCap Global Aggregate TR Hdg AUD

Australian Listed Property
S&P/ASX 200 A-REIT TR

International Property Hedged
FTSE EPRA/NAREIT Dv REITS TR Hdg AUD

Australian Shares
S&P/ASX 200 TR

International Shares
MSCI World Ex Australia NR AUD

Emerging Market Shares
MSCI EM GR AUD

RETURNS TO THE 31ST DECEMBER 2022

	1 Month	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Australian Cash	0.27	0.76	1.36	1.63	0.64	1.04	1.66
Australian Bonds	-2.06	0.38	-0.27	-9.71	-2.87	0.54	2.33
International Bonds Hedged	-1.31	0.64	-3.17	-12.28	-3.17	-0.22	2.33
Australian Listed Property	-4.09	11.50	4.01	-20.46	-1.45	3.29	8.14
International Property Hedged	-4.11	4.51	-6.23	-23.93	-4.25	1.00	5.95
Australian Shares	-3.21	9.40	9.82	-1.08	5.55	7.11	8.66
International Shares	-5.49	3.95	4.31	-12.52	6.22	9.26	13.75
Emerging Market Shares	-2.63	4.01	-1.63	-14.33	-1.52	1.46	5.85

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