Monthly Market Update

Market volatility will likely increase amid the U.S. debt ceiling standoff

INFORMATION CONTAINED IN THIS REPORT CURRENT AS AT 11TH MAY 2023

April was again a very eventful month for the Australian share market which increased by 1.85% over the month to be 2.83% higher over the year. The domestic market was supported by a stronger-than-expected US reporting period which saw the US share market increase by 1.46%. At the end of the month, investors witnessed fading concerns about a run on the US banking system after the US Federal Reserve injected over USD 350 billion. This was short lived, however. In early May, a number of US regional banks saw their share prices sell off considerably as concerns about default increased again. First Republic Bank's depositor flight, amounted to over 40% in the first quarter – much more than had been expected, causing the share price to plummet. Australian bond prices were flat over the month whilst international bond prices increased by 0.41%. Listed property (REITS) increased strongly (5.29%) given a more sedate bond market outlook.

Economic data in the US, remains strong although cracks are appearing including consumer confidence and weaker GDP. . The labour market remains tight, fuelling high job gains and modest income growth. The recent non-farm payrolls report was stronger than expectations with the unemployment level hitting a low of just 3.4%. Annual wage gains slowed but still exceeded the Federal Reserve's 2% inflation target and was the 12th consecutive month that employment growth was better than expected. The report suggests that the Federal Reserve will increase rates further. US durable goods orders rose more than expected in March. The market was also buoyed by some positive technology sector earnings releases for the first quarter, with Microsoft, Meta Platforms, Amazon, and Alphabet all beating analyst estimates. Consumer confidence in the US fell to a nine-month low in April, while first-quarter GDP was lower than expected.

The ongoing political brinkmanship over the US debt ceiling is likely to keep markets on edge. As is the case each time, there will be some political point scoring to be had as politicians posture for their own benefit. It will go to the 11th hour, then the government will print more bonds after the debt ceiling is approved by congress because if its not raised, people, particularly those on food stamps will starve. However, the US Federal Reserve (that has been the buyer of these bonds during Covid) will see elevated risk to economic stability and controlling inflation and may not participate in the Government's bond issuance this time. When the Federal Reserve prints money, inflation usually and eventually occurs. This is an undesirable scenario particularly in light of the fact that the Fed is trying desperately hard to bring the level down currently. That means that sovereign and pension funds and insurance companies will be the buyers and they will see elevated debt as risky. That will likely result in a higher borrowing cost for

Emmanuel Calligeris
Chairman of the Investment Committee

the government. Which means that taxes will have to increase as governments get money through utilities and taxes. Given that the economy is slowing, the US government will not want to compound the slowing by increasing tax or upping utility bills. The volatility of the market will likely increase as politicians posture and the media reports whether congress "will / won't" pass legislation to increase the debt ceiling. The US debt ceiling will ultimately be raised.

In Japan, the Bank of Japan stated that its long-standing ultra-easy monetary stance would continue for the foreseeable future. The recent fall in headline inflation towards 3% from a 41-year high of 4.3% in January 2023 gave the central bank ammunition to keep the loose monetary policy stance unchanged and the vote to do so at the April policy meeting was unanimous. However, the BoJ removed all reference in its statement to keeping rates at "present or lower levels", paving the way for a potential change to its policy further down the line. The central bank raised its inflation forecast for financial year 2023 from 1.6% to 1.8% and mildly lowered its GDP outlook from 1.7% to 1.4%. The Tokyo consumer price index, which was released after the BoJ's statement, showed core inflation in Japan's capital reaccelerating to 3.5% in April from 3.3% in February.

In Australia the government wasted its time and taxpayer money in an attempt to fix what isn't broken – namely the setting of monetary policy. Following an independent review culminating in 51 recommendations, Treasurer Chalmers is preparing to restructure the Reserve Bank of Australia (RBA) into two separate boards, a policy board and a governance board. It will be interesting to see if anything changes from the current experience. I suspect not. The RBA raised the cash rate by 0.25%. Crucial to this decision was the Board's interpretation of the first quarter's CPI report, focussing on the strength of inflation amongst service components despite the moderation in the headline and trimmed mean measures running ahead of the Board's expectations. With inflation rightly noted as being uncomfortably high, there was a greater emphasis on "the importance to returning inflation to target within a reasonable timeframe". In domestic data, nominal retail sales have only made a partial recovery so far this year, rising 0.4% in March to effectively be flat on a quarter-average basis. Given the persistence of price rises, a material contraction in inflation-adjusted sales over the first quarter of the year is likely and is therefore pointing to downside risk to household consumption. Lastly, the budget position has improved materially given higher-than-anticipated commodity prices, inflation and strength in the labour market. Given the ongoing pressures facing households, there will be some flexibility to deliver targeted spending, however the Government is expected to show restraint by retaining the bulk of the windfall revenue gain.

The gap between near term growth expectations and elevated inflation levels persists and been supportive for safe-haven assets such as gold. We continue to believe that we are towards the tail end if interest rate increases in Australia and the US but do not anticipate an easing this year.

Returns

30th April 2023

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 30TH APRIL 2023

	1 Month	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years
Australian Cash	0.30	0.83	1.60	2.37	0.81	1.11	1.68
Australian Bonds	0.19	1.99	4.23	2.06	-2.28	1.38	2.64
International Bonds Hedged	0.41	0.69	3.86	-2.28	-3.17	0.43	2.35
Australian Listed Property	5.29	-2.11	7.38	-9.90	10.71	4.94	7.36
International Property Hedged	2.02	-5.46	3.06	-16.36	4.29	0.52	3.19
Australian Shares	1.85	-0.80	8.71	2.83	13.99	8.26	7.90
International Shares	3.16	9.40	8.61	11.12	12.71	11.11	13.91
Emerging Market Shares	0.20	1.57	12.59	0.53	4.00	1.62	6.51

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