Economic and market update

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Key events in July 2023

- Global shares made solid gains in July. Optimism over 'Artificial Intelligence' (AI) and encouraging signs that global inflation is moderating continue to outweigh concerns over rising interest rates and bond yields.
- Wall Street's benchmark S&P 500 Index made strong gains. The promise of AI boosting productivity and profit margins for technology companies remains the key positive for US shares. Further encouraging signs of consumer inflation moderating to 3% annual change in June also boosted investor sentiment. The Federal Reserve raised US interest rates again by 0.25% to 5.25% - 5.50% range in July but signalled that future decisions will be guided by the data.
- European share markets made mild gains even with continuing worries over the Russia-Ukraine conflict and another 0.25% rise in interest rates by the European Central Bank (ECB).
- Asian share markets also delivered positive performances. The MSCI China Index, in local currency terms, rebounded strongly with hopes for further stimulus measures by China's central bank and government. Japanese shares delivered milder gains given the central bank signaled "*more flexibility*" on the current low interest rates.
- Australian shares made strong gains given lower inflation and hopes that China will pursue more stimulus. The Energy sector led the market with an 8.8% monthly return given a rebound in oil prices. Financials (4.9%) made a strong rebound with optimism that the Reserve Bank of Australia's (RBA) interest rate hiking cycle was coming to an end. Information Technology (4.5%) was boosted by the mania for AI-related shares. Resources (2.3%) made solid gains given China's stimulus hopes. However, there was some weakness in Consumer Staples (-1.0%) and Health Care (-1.5%) with concerns that the consumer was struggling.
- Australia's economy is giving mixed signals with robust jobs growth and moderating inflation being countered by weak retail spending. Consumer price pressures also moderated in the June quarter with annual inflation coming in at 6%. However, consumers still confront a 'painful squeeze' on budgets. Retail sales disappointed in June with a sharp fall. The RBA again held the cash interest rate steady at 4.1% but maintained guidance that further interest rate rises "*may be required"*.

Asset class summary

Asset class returns in Australian dollars – periods to 31 July 2023

	CYTD %	1 month %	3 months %	1 year %	3 years pa %	5 years pa %	10 years pa %
Australian shares	7.5	2.9	2.0	11.7	12.0	7.5	8.3
Global shares (hedged)	16.8	3.1	8.1	10.5	10.0	7.4	9.6
Global shares (unhedged)	18.9	2.4	6.4	16.9	12.7	10.4	11.8
Emerging markets (unhedged)	12.1	4.9	6.3	12.2	3.6	3.7	6.5
Australian property securities	7.5	3.9	1.9	-0.1	9.7	4.5	8.4
Global property securities (hedged)	4.2	3.2	2.0	-9.9	3.8	-0.1	4.2
Global listed infrastructure (hedged)	0.1	1.4	-1.6	-6.0	5.5	4.4	7.4
Australian bonds	2.0	0.5	-2.6	-1.5	-3.5	0.6	2.4
Global bonds (hedged)	2.0	0.0	-0.8	-3.6	-4.0	0.2	2.5
Global high yield bonds (hedged)	5.0	1.1	1.3	2.0	0.4	2.5	0.0
Australian Inflation-linked bonds	4.1	0.7	-1.4	2.9	1.3	2.5	2.9
Cash	2.1	0.4	1.0	3.1	1.1	1.2	1.7
AUD/USD	-0.6	1.2	2.0	-3.4	-2.1	-1.9	-2.8

Past performance is not a reliable indicator of future performance. **Sources:** Australian shares - S&P/ASX 200 Total Return Index; Global shares (hedged) - MSCI All Countries World (A$ hedged, Net); Global shares (unhedged) - MSCI All Countries World in A$ (Net); Emerging markets - MSCI Emerging Markets in A$ (Net); Australian property securities - S&P/ASX 300 A-REIT Accumulation Index; Global property securities - FTSE EPRA/NAREIT Developed (A$ hedged, Net); Global listed infrastructure - FTSE Global Core Infrastructure 50/50 (Hedged $A); Australian bonds - Bloomberg AusBond Composite 0+ Yr Index; Global bonds (A$ hedged) - Barclays Global Aggregate (A$ hedged, Gross); Global high yield bonds (A$ hedged) - Barclays US High Yield Ba/B Cash Pay x Financials ($A Hedged); Australian inflation-linked bonds - Bloomberg AusBond Inflation Government 0+ Yr Index; Cash - Bloomberg AusBond Bank Bill Index; AUD/USD - WM/Reuters Daily (4 pm GMT).

Key events in global markets over the last three months to July

Global share prices have continued to climb a wall of worries this year. High inflation, rising interest rates, banking stresses and the conflict in Ukraine have not yet curbed investor's enthusiasm. Global shares (hedged) delivered an exceptionally strong 8.1% return for the three months to July. The stronger Australian dollar has partly dented gains with the unhedged global shares providing a milder 6.4% return.

Wall Street's benchmark S&P 500 Index has delivered a remarkable 10.4% return in local currency terms. These strong gains come despite the US central bank continuing to raise interest rates. Investors appear to have gained solace from milder consumer inflation with June's 3% annual result being the lowest in the past two years. US economic activity appears resilient with robust jobs growth countering milder retail spending.

European shares made a strong quarterly gain of 2.6% despite the Russia-Ukraine conflict on their doorstep.

The performance of Asian share markets is improving. The MSCI China Index has rebounded by 5.5% in local currency terms with hopes that China will pursue more stimulus to support their subdued economy. Japan's Nikkei 225 Index delivered an exceptionally strong return of 15.1%, in local currency terms, given the low interest rate and bond yield settings.

Global bonds (hedged) delivered a mildly negative -0.8% quarterly return with inflation concerns still prominent.

Global high yield bonds (hedged) made a positive gain with a 1.3% return. Investors have regained their appetite for high yield with optimism that the global economy is proving resilient to the wall of worries.

Key events in Australia over the last three months to July

Australian shares delivered a solid 2% return with a mixed performance across industry sectors. Information Technology (20.6%) led the market gains in line with the global mania for AI. There were also strong gains for the Energy (11.1%) sector given a rebound in oil prices. Resources (2.8%) also did reasonably well with hopes for a stronger Chinese economy. However, there was sharp weakness in Health Care (-8.0%) and Consumer Staples (-2.8%) with concerns over the financial health of the Australian consumer.

Australia's economy is struggling judging by weak retail spending and housing construction activity. Consumers are understandably reluctant to spend given the budget challenges of high inflation and interest rates. The RBA's surprise 0.25% interest rate hike in both May and June to a 4.1% cash interest rate has only added to the worry list. Housing is providing a very complex profile with a rebound in house and apartment prices over recent months but a dramatic slide in new housing approvals and rise in insolvencies amongst builders. There are some positive signs amidst this gloom. The labour market remains strong with June recording a 32,600 surge in jobs and the unemployment rate close to 50 year lows at 3.5%. Inflation pressures have also moderated with June's 6% annual rise being materially lower than last year.

Global prospects

Global share prices have positively surprised this year by making strong gains. The mania for AI and anything with a technology flavour has been the key driver. Investors also appear to be hoping that central banks have completed their interest rate tightening cycle and achieved a 'soft landing' of continued economic growth with falling inflation.

However, there are still some significant risks that investors should be cautious on. Clearly the Russia-Ukraine conflict and consumer's resilience to high interest rates are factors that are formidable. For investors, assessing these considerable risks is very challenging. Given that there are multiple positive and negative outcomes possible over coming months, investors should maintain a disciplined and diversified strategy.