ASSET MANAGEMENT

# Economic and market update

**Bob Cunneen, Senior Economist**
**August 2023**

## Key events in August 2023

- Global share prices fell in August with central banks suggesting higher interest rates for longer as well as concerns over China's sluggish economy and weak property market.
- Wall Street's benchmark indexes declined in August. While optimism on 'Artificial intelligence' (AI) is still prominent, investors have become more cautious after the recent strong share price gains. The US central bank warned that it was "*prepared to raise*" interest rates given inflation remains "*too high*". US consumer price annual inflation came in at 3.2% in July which is still above the US central bank's 2% inflation target.
- European share markets also retreated with continuing worries over rising interest rates as well as the Russia-Ukraine conflict.
- Chinese share markets delivered sharply negative performances in August. The MSCI China Index fell given concerns over subdued results for retail spending and continued weakness in the property sector. Notably the financial woes of China's large property developers dominated the headlines. Evergrande filed for US bankruptcy proceedings on foreign debt while Country Garden recorded a large financial loss and requested a delay in debt repayments.
- Australian shares disappointed in August with a mild decline given concerns over China's prospects as well as the Australian consumer. Utilities (-3.9%) and Consumer Staples (-3.2%) led the market declines given concerns about the consumer's ability to absorb higher electricity and gas prices as well as rising mortgage interest rates and rents. Information Technology (-2.1%) declined in line with a more cautious view after their recent strong gains. Despite a rebound in the iron ore price to above US$110 per tonne, the Resources sector posted a -1.8% negative return with concerns over China's economic prospects. There were some positives with surprisingly strong gains for Consumer Discretionary (5.7%) and Property Securities (2.2%) on hopes that the Reserve Bank of Australia (RBA) has ended the cycle of raising interest rates.

## Asset class summary

**Asset class returns in Australian dollars – periods to 31 August 2023**

| | CYTD % | 1 month % | 3 months % | 1 year % | 3 years pa % | 5 years pa % | 10 years pa % |
|---|---|---|---|---|---|---|---|
| Australian shares | 6.7 | -0.7 | 3.9 | 9.6 | 10.7 | 7.0 | 8.0 |
| Global shares (hedged) | 14.3 | -2.2 | 6.2 | 11.4 | 7.2 | 6.7 | 9.5 |
| Global shares (unhedged) | 20.2 | 1.1 | 6.5 | 20.6 | 12.1 | 9.9 | 12.1 |
| Emerging markets (unhedged) | 9.5 | -2.4 | 3.4 | 7.2 | 3.1 | 3.2 | 6.3 |
| Australian property securities | 9.9 | 2.2 | 6.1 | 5.9 | 7.7 | 4.4 | 8.7 |
| Global property securities (hedged) | 1.4 | -2.7 | 3.2 | -7.0 | 2.1 | -0.9 | 4.4 |
| Global listed infrastructure (hedged) | -4.6 | -4.7 | -1.6 | -9.5 | 3.9 | 3.6 | 7.2 |
| Australian bonds | 2.8 | 0.7 | -0.7 | 1.8 | -3.1 | 0.6 | 2.5 |
| Global bonds (hedged) | 1.8 | -0.3 | -0.5 | -1.2 | -3.8 | 0.1 | 2.5 |
| Global high yield bonds (hedged) | 5.1 | 0.0 | 2.4 | 5.0 | 0.2 | 2.3 | 4.5 |
| Australian Inflation-linked bonds | 4.9 | 0.8 | -0.2 | 5.4 | 1.4 | 2.5 | 3.0 |
| Cash | 2.5 | 0.4 | 1.0 | 3.4 | 1.2 | 1.2 | 1.7 |
| AUD/USD | -4.5 | -3.9 | 0.1 | -5.5 | -4.3 | -2.2 | -3.1 |

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 August

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 been countered by investor's enthusiasm for AI related shares. Global shares (hedged) delivered a very strong 6.2% return for the three months to August while unhedged global shares benefitted from a weaker Australian dollar with a 6.5% return.

Wall Street's benchmark S&P 500 Index has delivered a remarkable 8.1% 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 July's 3.2% annual result. US economic activity appears solid with robust jobs growth and more resilient consumer spending.

European shares (MSCI AC Europe) made a strong quarterly gain of 3.8% despite the Russia-Ukraine conflict on their doorstep.

Asian share markets have been improving. The MSCI China Index has rebounded by 5.3% in local currency terms but is being buffeted by property market concerns. Japan's Nikkei 225 Index also delivered strong returns given assurance from the central bank of low interest rate and bond yield settings.

Global bonds (hedged) delivered a mildly negative -0.5% quarterly return with inflation concerns still prominent.

Global high yield bonds (hedged) made a solid gain with a 2.4% 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 August

Australian shares delivered a strong 3.9% return with a mixed performance across industry sectors. The Energy sector led the market gains with a 11.5% return on the back of higher oil and gas prices recently. Consumer Discretionary was a positive surprise with a 11.3% return on the back of hopes that Australian interest rates were peaking which would allow consumers to have more purchasing power. Resources (5.0%) benefitted from hopes for a stronger Chinese economy. However, there was weakness in Health Care (-9.0%) and Consumer Staples (-1.4%) with disappointments over their recent profit performances.

Australia's economy shows significant slowdown signs with real retail spending declining over the nine months to June. Essentially, consumers are struggling to keep spending as the squeeze from higher goods and services prices, rising mortgage interest rates as well as rents takes their toll. Employment also marginally fell in July with the unemployment rate edging up from 3.5% to 3.7%. There was some mild relief as annual consumer inflation moderated from 5.4% in June to 4.9% in July according to the new Australian Bureau of Statistics monthly measure. The RBA has held the cash interest rate steady at 4.1% since June but has maintained guidance that further interest rate rises "*may be required*" to get inflation back in their 2% to 3% target range.

## Global prospects

Global share prices have positively surprised this year by making very strong gains. The mania for AI and anything with a technology flavour has been the key driver. Investors are also 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 Russian-Ukraine conflict and consumers' resilience to high interest rates are concerns. 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.