# Current Market View

**Investment Markets**

The global share markets finished mixed in local currency terms over January 2024 supported by the belief that interest rates and inflation are heading lower but investors may be getting ahead of expectations. Investors cashed up with ETF and trust distributions went looking for bargains which were few are far between. The US market surged to record highs and confidence for a soft landing grew.

What is supporting the confidence is the belief that the **Federal Reserve Bank hiking cycle is over** and interest rate cuts are just around the corner. With reporting season underway, investors are keen to see evidence of the recovery in earnings and profits in the company’s results.

**The US Federal Reserve Bank held the target range for the federal funds rate steady at 5.25%-5.0% at the FOMC meeting held on the 31st of January 2024**, indicating that the **target rate may end 2024 at around 4.6% (down around 0.75% from current level.** Interest rates pulled back (higher in yield) believing that the market may be getting ahead of itself, and inflation data was not as strong as expected. Investors focussed on the second half of 2024 and the potential for monetary policy easing once the real impact of all the interest rate hikes if felt by consumers in Q1 and Q2 of 2024.

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Source data: Lonsec as of 31st January 2024

From the chart above, you can gain an understanding of why investors over the past year have tilted their exposures towards shares over bonds given the higher risk score resulting in higher returns in most cases.

*The risk measure is simply the one-year annualised standard deviation of the monthly total return time series for each category. The total return is the share or bond price movement monthly including any cash dividends and coupons payable.*

The S&P/ASX200 volatility (VIX) pushed lower closing at 11.12 as of 31st January 2024. It is currently trading at 11.87 as at close of business 14th February 2024 (Source: S&P/ASX200 VIX). Looks like the market is expecting an uplift in volatility in the month ahead.

Expectations for further interest rate hikes now appears to be far from Central Banks thoughts as the recent inflation numbers reflect the potential for an easing bias in the months ahead. The latest inflation print in the US has revealed that the annual inflation rate fell to **3.1% in January 2024 down from 3.4% last month.** This added fuel to the belief that a soft landing is possible given the direction of inflation and the potential for interest rates to fall later in the year**.**

The issues at the forefront of investors thoughts included:

* Political conflict – the ongoing war in the middle east for Israel and Humas, along with Ukraine and Russia, has unsettled investors. While not panicking, the underlying impact of these events put doubt into expectations for any economic recovery.
* Global growth – for our region China is the focus with property developers in the spotlight. The ramifications are that if China stumbles then Australia will be impacted given, they are our biggest trading partner.
* Inflation now showing signs of abating however stubbornly above the target ranges of Central banks. The impact of monetary policy changes typically takes 12 to 18 months to be felt and so markets are watching the economic data closely for signals that will challenge growth expectations.
* Bond markets and their response to the latest inflation print and Central banks keeping the cash rates on hold, is helping settle the debt markets.
* risks: market valuations are challenging along with economic indicators flagging downside risks; however, **investors are encouraged to hold their resolve**, navigate this period of uncertainty, and expect better conditions to prevail in the 2nd and 3rd quarter of 2024.

Locally the domestic house prices continued to stabilise and drift higher after the brunt of the interest rate rises as confidence returned to stressed market sectors. This year will be challenging however, **the broader economy is weathering the storm very well** given the mixed support from high immigration levels, commodity markets and the strong level of employment with unemployment sitting at 4.1% in January 2024.

The latest inflation print for the fourth quarter of 2023 in Australia was 4.1% which was down from the 5.4% in the third quarter of 2023 but still elevated. Despite the elevated level of inflation, the RBA voted to **hold the target cash rate at 4.35%** at this month’s board meeting on the 6th of February 2024.

Despite the political conflict and volatile interest rate markets, the investment fundamentals are still supportive of longer-term recovery but not without short-term downside risk. Investors have adjusted their risk appetite to **“cautiously optimistic”** short term and **“optimistic”** medium term as they await the next round of inflation data and Central Bank activity however, the signals are getting better and **opportunistic buying** is still on the agenda despite the threat of an economic slowdown is likely to occur at some future point but the severity is now seen as limited. We are looking for a **soft landing** for Australia.

Ukraine and Israel conflict is still a major concern for investors however, we are a long way from the conflict zone and the global economic data is improving slowly but the main influence on our market remains from offshore, especially China. China is experiencing issues relating to growth and Property developers which is holding back the improving underlying market conditions in the region.

**The following total returns across the asset classes are as of 31st January 2024:**



Source data: Lonsec as of 31st January 2024

The developed markets asset classes finished mixed for the month. The AUD/USD finished sharply lower as well (-3.89%) in the month which benefitted unhedged holdings.

With **reporting season getting underway in the US,** much now will depend on how companies faired over the fourth quarter in the lead up to the festive season. Analysts expect mostly positive results, but consumption will be a key indicator.

**Asset Class Performance**



Data Source: Lonsec as of 31st January 2024 & Fox Asset Management

**Investment Climate**

The underlying investment climate has now changed to **“cautiously optimistic”** in the short term as investors consider the recent impacts of the pull back in interest rates and the European and middle east conflict.

The risk is that the conflict may escalate and involve neighbours which could then inflame the situation. While this situation continues, investors will be cautious however and fall in interest rates will spur buying in asset classes that have been oversold in recent months (property)**.**

Consumption is showing signs of a slowdown which will impact demand in the short-term and while it will take time to settle, the world will pull through this period of uncertainty supported by the deep pockets of Central Banks and strong allies of the conflicted countries.

The **medium-term view remains positive** for returns overall although headwinds will prevail, now that the US Fed has effectively **signalled a pivot for their interest rates**, this is a strong indicator for interest rate expectations and clear a path going forward for investors.

**Longer term investors are optimistic** for a goldilocks period ahead. Global Central Banks continue to indicate a resolve to get inflation under control however, the economic data is showing signs of an easing in inflation and every indication is for future easing in monetary policy expectations for the latter part of 2024. Remember **markets are forward looking** so the support now is reflecting the expectations for conditions in October 2024.

**The following commentary is based on month-end closing prices as of 31st January 2024:**

Global markets results were mixed over January as global property suffered a pullback following the Chinese property developer Evergrande suffering liquidity issues and global infrastructure eased which is confusing. Infrastructure companies are better positioned to retain margins compared to most general market equities, given that not only interest costs, but also other operating cost items, can be considered “pass-through” within a regulatory construct so costs simply flow through to users.

The changing economic conditions along with interest rates retreating from the lower yield levels dented investor confidence. The situation in Russia/Ukraine conflict remains unchanged however the latest conflict between Israel and Hamas has prompted investors to avoid that region. Unfortunately, a resolution to the regional conflict is a way off currently however, the underlying economies elsewhere are emerging with a more growth orientated momentum after such an extended period of uncertainty.

As mentioned, the Fed left the target cash rates at **5.25% - 5.50%** on the 31st of January 2024 FOMC meeting:

*“The Committee does not expect it will be appropriate to reduce the target.*

*range until it has gained greater confidence that inflation is moving sustainably toward 2 percent. In addition, the Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities, as described in its previously announced plans.*

*The Committee is strongly committed to returning inflation to its 2 percent objective. (Source: Federal Reserve Press Release January 31, 2024).*

Other measures agreed to at the Fed meeting include:

* In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals.
* The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments. (Source: Federal Reserve Press Release January 31, 2024).

**The next Fed meeting is scheduled for 19/20 March 2024**. Most officials see US interest rates ending at 5%-5.5%.

**Investor Focus**

For Australia, investors focussed on the following issues:

* Cost of living expenses and the impact on **consumer spending**.
* **Company profits** given the expected slowdown in consumer activity post the festive season.
* The level of **interest rates** and the delicate position of the RBA given the elevated inflation print.
* **Inflation** remains stubbornly high at 4.1% although easing from 5.4% in the third quarter of 2023 which although heading in the right direction, infers higher interest rates for longer.
* China growth prospects – the PBOC efforts to boost the economic growth by adding liquidity to the market to offset the property developers’ losses however, boosted a little with the GDP annual growth rate rising to 5.2% in the fourth quarter of 2023 up from 4.9% previously.

## Asset Class Returns

Returns across the various asset classes ended mixed over the month:



Source data: Lonsec as of 31st January 2024

## Global Share Returns

For share markets, the focus remains on **inflation** and the potential for Central Banks to look at interest rate **easing programmes** over the longer time should inflation data continue to drift lower. Unhedged global shares fared better with the USD/AUD weakening (0.6574 down from 0.6840) which had a positive impact of (+3.89%) on AUD returns over the month for unhedged investors.

The markets are looking to stabilise and regain a level of confidence. Investors welcome the obvious signs that Central Banks have “**pivoted”** now and future interest rates moves are likely to be down not up which will underpin company valuations and support markets.

Asia and the Emerging Markets fell behind as the slowdown in the global markets and China weighed on investors’ minds.

Most investors are content to **stay invested and ride out any volatility** and selectively add to their holdings which has proven the correct strategy over the last period.



Source data: Lonsec as of 31st January 2024

In AUD terms, the global share markets posted one month return of (+4.54%). The US posted returns of (+4.96%), Asia ex Japan (-1.71%), Japan (+7.99%), the UK (+1.84%), Europe (+3.12%) and the Emerging Markets (-1.56%).

**Australian Shares**

Australian shares posted positive returns pulled along by the global trend and improving economic conditions. Shares finished (+1.19%) for the month and (+14.0%) over the last three months. The focus for investors was:

* **Cost of living expenses** and the impact on consumer spending.
* **Company profits** given the expected slowdown in consumer activity post the festive season.
* **Consumer confidence** post the interest rate increases.
* **Mortgage stress** and the impact on domestic house prices and banks.
* **Inflation** and the welcome response by the RBA to hold the target cash rate at 4.35%.

Commodity markets ended mixed with Iron Ore closing at US$135.13 per tonne at the end of January 2024 with a monthly loss of (-0.91%) and gains of (+13.64%) for the previous three months. Oil (WTI) closed higher at US$75.85 a barrel at the end of January 2024 resulting in a gain of (+5.86%) for the month and down (-6.38%) over the last three months. China remains our main export market followed by Japan.

## Australian Industry Returns

Industry sectors posted mixed results for December 2023. The industry sector performance results for the last month were:



Source data: Lonsec as of 31st January 2024

Over the last month, Energy was the best performing sector posting gains of (+5.22%).

Materials was the worst performing sector finishing (-4.80%) for the month.



Source data: Lonsec as of 31st January 2024

## Debt Market Returns

Bonds and Fixed Interest markets finished mixed as global bond prices eased (up in yield) as Central Bank hold on the cash rates in the developed countries and rhetoric that suggested caution as an indication that perhaps markets had run ahead of themselves caused investors to consider a longer-term timeframe for cash rates to come down. In Australia, the short-dated 2-year Government bonds trading at **3.78%** on the 15th of February 2024 and longer dated 10-year bonds trading at **4.156%.**

Global Bonds ended down (-0.45%) and Australian Bonds ended up (+0.21%) for the month of January 2024 and up (+5.55%) and up (+5.96%) respectively for the previous three months.

The RBA left the **target cash rate at 4.35%** following the 6th of February 2024 board meeting and stated that:

*“While recent data indicate that inflation is easing, it remains high. The Board expects that it will be some time yet before inflation is sustainably in the target range. The path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe will* ***depend upon the data*** *and the evolving assessment of risks, and a further increase in interest rates cannot be ruled out. The Board will continue to pay close attention to developments in the global economy, trends in* ***domestic demand, and the outlook for inflation and the labour market****. The Board remains resolute in its determination to return inflation to target and will do what is necessary to achieve that outcome.” Michelle Bullock, Governor, RBA Monetary Policy Board meeting, 6th February 2024.*

The US Federal Reserve Bank (the Fed) kept their monetary policy measures on hold by maintaining the target range for **federal funds at 5.25% to 5.50%** on the 31 January 2024 meeting. In addition, the Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities.

The US 10-year Government bonds closed at (3.918%) for the month up in yield (+0.052%) from the previous month close of (3.866%).

The Australian Government 10-year bonds finished higher in yield in January 2024 at (4.074%) up in yield (+0.107) from (3.967%) in December 2023.



Source data: Lonsec as of 31st January 2024

## Currency

The $A closed weaker AUD/USD 0.6574 at the end of January 2024 which benefitted investors who held offshore assets unhedged (+3.89%) over the month and (-3.59%) over the last three months.



Currency forecasters see the AUD/USD range between 0.6250 and 0.7250 cents in the medium term and most likely to trade within the 0.5500 to 0.7500 range in the longer term.

## Australian Economy

Australia’s latest GDP data for the third quarter of 2023 revealed an **annual growth rate of 2.1%** which was unchanged from the second quarter of 2023. Unemployment increased to 4.1% in January 2024 from 3.9%. The **core Inflation rate fell to 4.2%** in the fourth quarter of 2023 which is above the Reserve Bank’s targeted 2% to 3% target range. The **inflation rate eased to 4.1%** in the fourth quarter of 2023 down from 5.4% in the third quarter 2023.

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## Current Market View

### Domestic View

The Australian share market continued to trend higher over January 2024 as Global interest rates paused following the lead given by Central Banks that **interest rates have peaked** but cautioned about getting **too excited, too early** with longer term periods expected before looking at easing monetary policy.

The latest inflation numbers indicated an easing in inflation related prices however the focus remained on the potential for Central Banks to ease monetary policy in the months ahead. Pre-empting this move, **markets need to assess the economic data** for indicators on the path going forward. Falling interest rates should lead to rising company valuations however, consumer spending is showing signs of slowing.

More aggressive investors are taking advantage of any pullback in markets to buy oversold companies in industries and entering **selective risk-on trades**. This activity is likely to be in response to conservative earnings guidance being achieved and future guidance being marginally positive.

The overall investment feeling for shares in the short-term is **“cautiously optimistic”** but remains **optimistic** **over the long run** as interest rates ease along with inflation.

### Global View

Global markets returns were mixed over January 2024 in AUD terms despite the tailwinds of a weakening AUD/USD exchange rate which benefitted (+3.89%) on the performance results for unhedged investors. Inflation, interest rates and the political uncertainty remain the key focus. For China, it is a wait and see brief as domestically they wait to see any indication of global growth falling before looking to commit to expand their markets.

Reporting season always proves to be an interesting period as company results filter through the markets. Early signs are positive, so expectations are supportive of markets currently.

Despite the uncertain geopolitical situation with the Russia-Ukraine, Israel-Hamas conflict, and economic slowdown concerns, we expect the **medium-term outlook to reflect better opportunities for investors**. Short-term, we expect the start of 2024 to reflect subdued investor appetite as interest rates search for equilibrium, companies release results and consumers tighten their belts.

**Where to From Here?**

**For Australia**, what is happening in the global markets is directly impacting our markets as there is alignment in trade terms, but the fallout remains mitigated given our immigration, agricultural and resource assets. All eyes are focussed on the **Middle East political unrest.** Let us hope the situation will be contained and a solution that ceases further aggression and violence is forthcoming.

The latest rhetoric from Central Banks now **confirms the change to monetary policy thinking but cautions about getting ahead of the game**. We may not have seen the real impact of the interest rate rises just yet, but the first half of 2024 should provide a strong indication of where we are heading in terms of soft or hard landing for the global economies.

Markets have already weathered tough conditions over 2023 and now there is economic evidence pointing to a potential mild global recession in the US and Europe down the track. **Markets are forward looking**, so it is likely they have **found a bottom and consolidating** before starting to recover longer term. We suspect we have just seen the start of that recovery process.

Fingers crossed that this latest changes to monetary policy direction in the developed countries, will lead to a moderation in prices and the start of a more stable growth platform.

**Footnote**

This market update written by Graham Fox for and on behalf of HNW Planning on 15/02/2024. Graham Fox is an external asset consultant and consults to the HNW Investment Committee. Graham has enjoyed a career in financial services covering several private, corporate and investment banking institutions including, Genesys Wealth Advisers (research), Standard & Poor’s Australia (fund ratings), Westpac Private Bank (research, strategy and product), Gold Link Capital (sales and marketing), Challenger Financial Services Group (COO asset management), Deutsche Funds Management (head of treasury), Canadian Imperial Bank of Commerce (regional head of FX), Banque Nationale de Paris, (F/X) and Commercial Bank of Australia (International and Treasury). Graham references material made available from HNW Planning’s' contracted research houses including Lonsec and Morningstar.