# Current Market View

**Investment Markets**

What a difference a month makes! Santa Claus rally to the rescue.

The global share markets finished stronger in local currency terms over November 2023 as global interest rates shifted sharply lower in what has been described as a roller coaster ride.

Investor optimism ramped up despite the **higher for longer inflation** mantra that was prevalent last month. **What caused the turnaround?** Inflation data confirming demand as measured by CPI (prices) are heading in the right direction with **falls in most developed countries** along with the **US Federal Reserve Bank holding rates steady at the December FOMC meeting held on the 14th of December 2023, indicating that the target cash rate may end 2024 at around 4.6% (down around 0.75% from current level.** Interest rates rallied as investors focussed on 2024 and the potential for monetary policy easing once the real impact of all the interest rate hikes if felt by consumers. This is likely to occur in Q3 of 2024.

****

Source data: Lonsec as of 30th November 2023

Historically bonds have had a key role to play in a multi-asset portfolio approach. The recent sell off in the bond markets saw capital losses impacting returns however, with yields in the corporate markets at or near the 5% level for short-dated maturities, this is proved attractive for the risk adverse investor. **US 10-year bonds have fallen 1% in just a month** which is extraordinary. From the chart above, you can gain an understanding of why investors over the past year have tilted towards shares over bonds given the higher risk 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 13.95 as of 30th November 2023. It is currently trading at 9.79 as at close of business 12th December 2023 (Source: S&P/ASX200 VIX). Looks like the market is expecting a quiet session 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 **3.1% in November 2023 down from 3.2% last month.** TheUS Federal Reserve Bank (the Fed) **left the target cash rate unchanged at 5.25% to 5.50%** on the 14th of December 2023, meeting.

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.
* Bond markets and their response to the latest inflation print and Central bank cash rate hold is helping settle the debt markets.
* Share market valuations are challenging along with economic indicators flagging downside risks; however, **investors are encouraged to hold their resolve, buy the dip**, navigate this period of uncertainty, and expect better conditions to prevail in the latter part of this month and early 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 3.9% in December 2023.

The latest inflation print for the third quarter of 2023 in Australia was 5.4% which was down from the 6.0% in the second 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 5th of December 2023.

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 **“risk-on, buy the on dips”** 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.

**The following total returns across the asset classes are as of 30th November 2023:**



Source data: Lonsec as of 30th November 2023

The developed markets asset classes finished strongly for the month. The AUD/USD finished sharply higher as well (+4.76%) in the month which cost unhedged holdings.

**Asset Class Performance**



Data Source: Lonsec as of 30th November 2023 & Fox Asset Management

**Investment Climate**

The underlying investment climate has now changed to **“risk-on, buy on dips”** in the short term as investors consider the recent impacts of the falling 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 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 September 2024.

**The following commentary is based on month-end closing prices as of 30 November 2023:**

Global markets rebounded strongly in November much to the relief of investors. The changing economic conditions along with interest rates peaking has supported 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%** at the 13/14 December 2023 FOMC meeting:

*“Recent indicators suggest that growth of economic activity has slowed from its strong pace in the third quarter. Job gains have moderated since earlier in the year but remain strong, and the unemployment rate has remained low. Inflation has eased over the past year but remains elevated” (Source: Federal Reserve Press Release December 13, 2023).*

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 December 13, 2023).

**The next Fed meeting is scheduled for 30/31 January 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 5.4% although easing from 6.0% in the second 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 and the slowdown in the GDP annual growth rate to 4.9% in the third quarter of 2023 down from 6.3% previously.

## Asset Class Returns

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



Source data: Lonsec as of 30th November 2023

## Global Share Returns

For share markets, the focus remains on **inflation** and the level of commitment by Central Banks to stem the rise which is showing signs of easing across the developed world. H**igher inflation means higher interest rates** usually however, in the current environment economic activity is slowing which is front running the inflation numbers. Unhedged global shares lost ground with the USD/AUD strengthening (0.6648 down from 0.6346) which had a negative impact of (-4.76%) on AUD returns over the month for unhedged investors.

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

The **volatility in markets retreated** over November 2023 in response to the falling interest rates. S&PASX200 volatility (VIX) pushed lower closing at 13.95 as of 30th November 2023. It is currently trading at 9.79 as at close of business 12th December 2023 (Source: S&P/ASX200 VIX). Most investors are content to **stay invested and ride out the storm** and add to their holdings opportunistically which has proven the correct strategy over the last period.



Source data: Lonsec as of 30th November 2023

In AUD terms, the global share markets posted one month return of (+4.48%). The US posted returns of (+4.21%), Asia ex Japan (+2.60%), Japan (+3.67%), the UK (+1.88%), Europe (+4.94%) and the Emerging Markets (+3.15%).

**Australian Shares**

Australian shares posted strong returns pulled along by the global trend. Shares finished (+5.03%) for the month and (-1.81%) 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 recent 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 stronger with Iron Ore closing at US$130.46 per tonne at the end of November 2023 with a monthly gain of (+9.71%) and gains of (+19.70%) for the previous three months. Oil (WTI) closed sharply lower at US$75.96 a barrel at the end of November 2023 resulting in losses of (-6.25%) for the month and down (-6.95%) over the last three months. China remains our main export market followed by Japan.

## Australian Industry Returns

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



Source data: Lonsec as of 30th November 2023

Over the last month, Healthcare was the best performing sector posting gains of (+11.71%).

Energy was the worst performing sector finishing (-7.41%) for the month.



Source data: Lonsec as of 30th November 2023

## Debt Market Returns

Bonds and Fixed Interest markets finished higher as global bond prices firmed (down in yield) as the Central Bank hold on the cash rates in the developed countries and hints of future interest rate falls was well received by investors. In Australia, the short-dated 2-year Government bonds trading at **3.89%** on the 15th of December 2023 and longer dated 10-year bonds trading at **4.14%.**

Global Bonds ended up (+2.96%) and Australian Bonds ended up (+2.97%) for the month of November 2023 and up (+0.17%) and down (-0.48%) respectively for the previous three months.

The RBA left the **target cash rate at 4.35%** following the 5th of December 2023 board meeting and stated that:

*“Whether further tightening of monetary policy is required to ensure that inflation returns to target in a reasonable timeframe* ***will depend upon the data*** *and the evolving assessment of risks. In making its decisions, 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, 5th December 2023.*

The US Federal Reserve Bank (the Fed) paused their monetary policy tightening measures by holding the target range for **federal funds to 5.25% to 5.50%** on the 13/14 December 2023 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 (4.33%) for the month down in yield (-0.596%) from the previous month close of (4.926%).

The Australian Government 10-year bonds finished lower in yield in November 2023 at (4.362%) down in yield (-0.556) from (4.918%) price in October 2023.



Source data: Lonsec as of 30th November 2023

## Currency

The $A closed lower at AUD/USD 0.6648 at the end of November 2023 which cost investors who held offshore assets unhedged (-4.76%) over the month and (+0.75%) over the last three months.

**Currency example for unhedged USD investors:**



**Note**

* The AUD/USD has weakened -3.76% over the 12-month period.
* The S&P500 price index in USD has strengthened +7.75% over the same period.
* The AUD valuation (gain) reflects a benefit of +11.96% showing the currency impact (+4.21%).

In this example, holding unhedged international assets such as USD in a client’s portfolio results in currency gains of (+4.21%). The hedged or unhedged decision has ramifications on the performance of the offshore assets depending upon the direction of the AUD against all currencies not just the USD in this example.

When the AUD/USD exchange rate falls, this benefits investors who hold offshore assets in USD or other currencies. Holding any offshore assets in the local currency will be subject to the strength or weakness of the AUD as investors sell AUD to purchase the other currency so valuations will be subject to the fluctuations of the AUD against that currency.



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 firmed to 3.9% in December 2023 from 3.7%. The **core Inflation rate fell to 5.2%** in the third quarter of 2023 which is above the Reserve Bank’s targeted 2% to 3% target range. The **inflation rate eased to 5.4%** in the third quarter of 2023 down from 6.0% in the second quarter 2023.

##

## Current Market View

### Domestic View

The Australian share market rebounded strongly as Global interest rates rallied hard following the lead given by Central Banks that **interest rates have peaked** and may ease in the months ahead.

Pressure was building for further interest rate rises as inflation remains elevated with the catch cry, **higher for longer** is repeatedly voiced by analysts however, after the latest inflation numbers indicated lower inflation in several countries, **markets responded with renewed optimism**.

Investors are gaining a better understanding of what industries and which countries are navigating the geopolitical events, inflation, and volatility in the share and bond markets. The disruption to the supply of goods and services is abating however, this may be more demand driven as consumers tighten their belts.

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 “risk-on, **buy on dips**” and **optimistic** **over the long run** as interest rates ease back searching for equilibrium.

### Global View

Global markets recovered well over November 2023 in AUD terms despite the headwinds of a strengthening AUD/USD exchange rate which cost (-4.76%) on the performance results. Inflation, interest rates and the political uncertainty remain the key focus. For China, the world encouraged by the direction of their policy towards the re-opening of their economy and is looking for growth to emerge.

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 rest of 2023 to reflect the pull bank in interest rates and support for company valuations. **From November to January markets have historically performed** well. November was a good start and December is also running in the right direction. Fingers crossed history repeats itself.

**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 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.

Immigration along with agriculture and the resource sector is providing a support mechanism for Australia which has sheltered, to a degree, our economy, and our share market.

The latest rhetoric from Central Banks now **confirms the change to monetary policy thinking**. 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 and there is economic evidence pointing to a potential mild global recession in the US and Europe down the track however, it is worth noting that **markets are forward looking**, so it is likely they will **find a bottom and consolidate** before starting to recover again. We have just seen the start of that recovery process.

Fingers crossed that this latest monetary policy moves in the US and in other 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 15/12/2023. 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.