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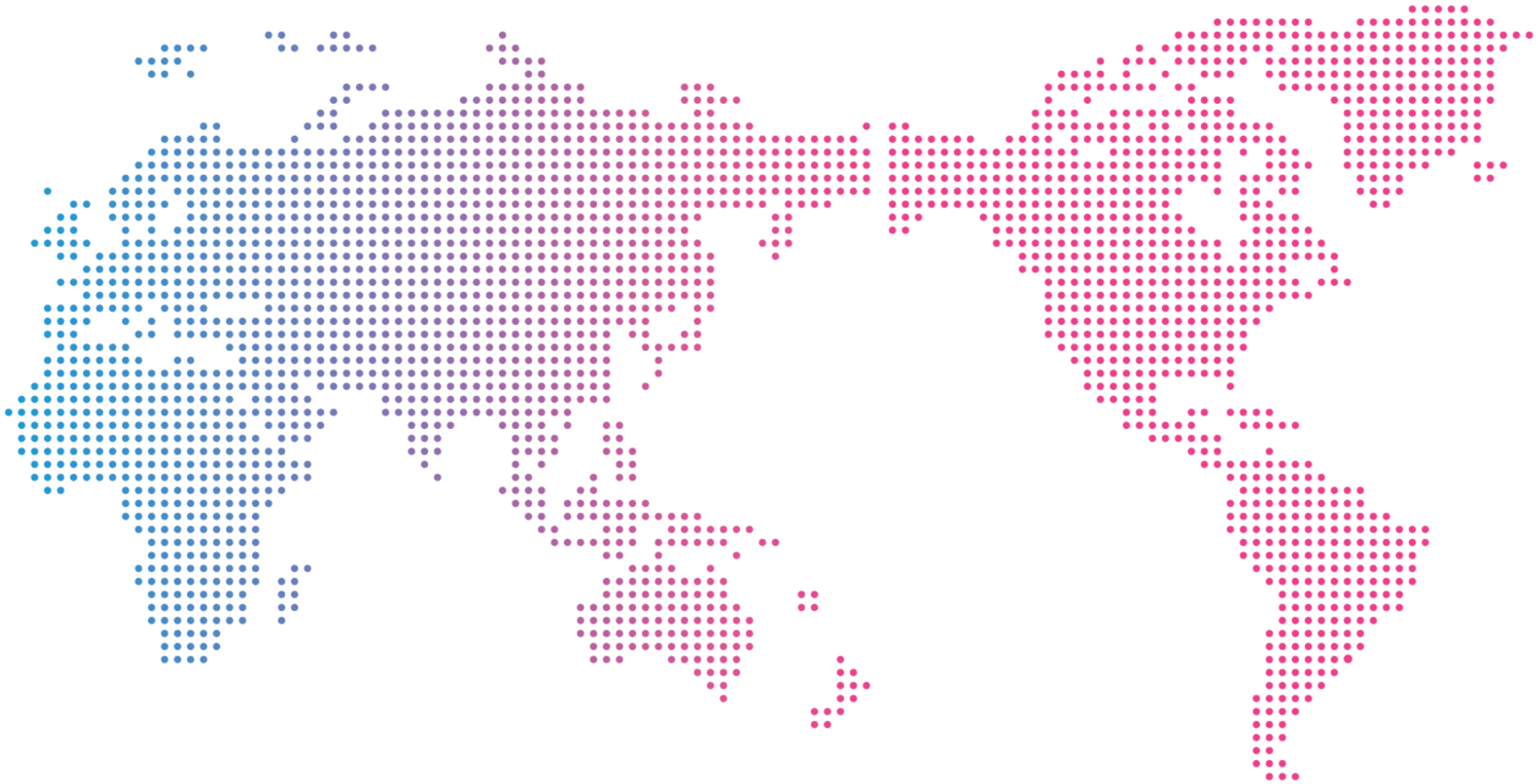
Market Review Quarterly



Q4 2024

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Key takeaways

- Many Central Banks around the world cut interest rates in December and are likely to continue at a more gradual pace, except in Japan where rates are expected to rise as it emerges from a period of deflation.
- The Reserve Bank of Australia (RBA) kept interest rates unchanged at 4.35% for the ninth consecutive meeting.
- The Australia labour market remained strong as unemployment fell to 3.9% over the quarter, beating market expectations for a rise to 4.2%.
- Global share markets saw positive returns in Q4’24 and ended the year with strong gains, international shares (hedged) returning 20.7% and Australian shares up 11.4%.
- We favour global listed property where fundamentals are broadly healthy, and valuations are attractive. We also favour Japanese shares due to the growth rebound and solid earnings growth.
- Domestically, we favour Australian sovereign bonds over cash with interest rates likely to have peaked this cycle.

Upcoming

1. RBA interest Rate announcement (18th Feb) with the market currently predicting a 68% chance of an interest rate cut.

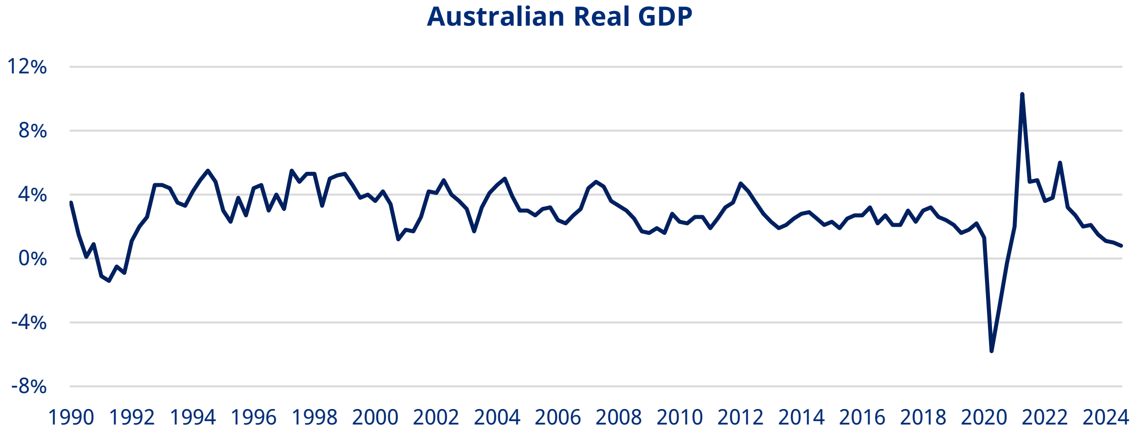
2. Australian Q4 CPI announcement (29th Jan) – Inflation easing is likely to give the RBA freedom to begin interest rate cuts.

3. US Q4’24 earnings season – Earnings growth is forecast to be 11.9% in 2024 and 14.8% in 2025, investors are optimistic.

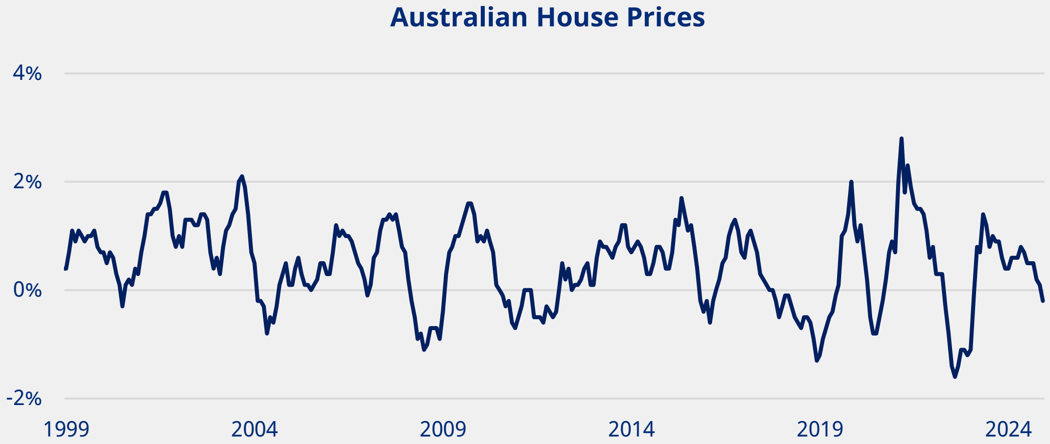
Economic review

Australia: Increased probability of an interest rate cut in February

- The RBA held rates steady at 4.35% over the quarter. However, the softening economic environment has increased the chance of a February interest rate cut.
- Australian Q3'24 GDP was weaker than the market expected slowing to 0.8%, versus expectations of 1.1%. Growth was driven predominantly by government spending while household spending remained flat.
- That said, domestic labour markets remained strong in November as unemployment fell to 3.9% from 4.1% in Q3'24, helped by the fall in participation rate. An additional, 36,700 jobs were added and business surveys reported weaker business confidence in November.
- Australian house prices began softening late in the quarter, falling -0.1% QoQ. Sydney and Melbourne continued to fall, with Sydney down -1.4% and Melbourne down -1.8% The other capital cities remained positive, with Adelaide and Perth experiencing low vacancy rates.



Source: Bloomberg, Mercer



Source: Bloomberg, Mercer

International: Central Banks delivering on interest rate cuts

- In line with market expectations, Central Banks continued to cut interest rates over the quarter. The European and US (FED) Central Banks cutting rates by 50bps and Canada cut 100bps. The FED noted that future interest rate cuts were likely to be gradual and dependent on inflation.
- The Bank of Japan left interest rates unchanged in the quarter at 0.25%, noting that Japan's economy had recovered moderately.
- US CPI data for was mostly unchanged in Q4'24 with annual core inflation remaining at 3.3%. Rent and utility costs, a significant expense for households, has begun to ease, giving the FED enough comfort to cut interest rates at their meeting.
- US employment rate increased slightly to 4.2% from 4.1% in Q3'24. The US National Federation of Independent Business survey surged in Q4'24, suggesting increased optimism following the US election for small businesses.

Market review

Share markets had mixed performance in the quarter

- International shares (Unhedged) moved higher in the quarter assisted by a fall in the Australian dollar (AUD).
- Australian shares ended Q4’24 slightly lower as weaker Australian economic data weighed on the local share market.

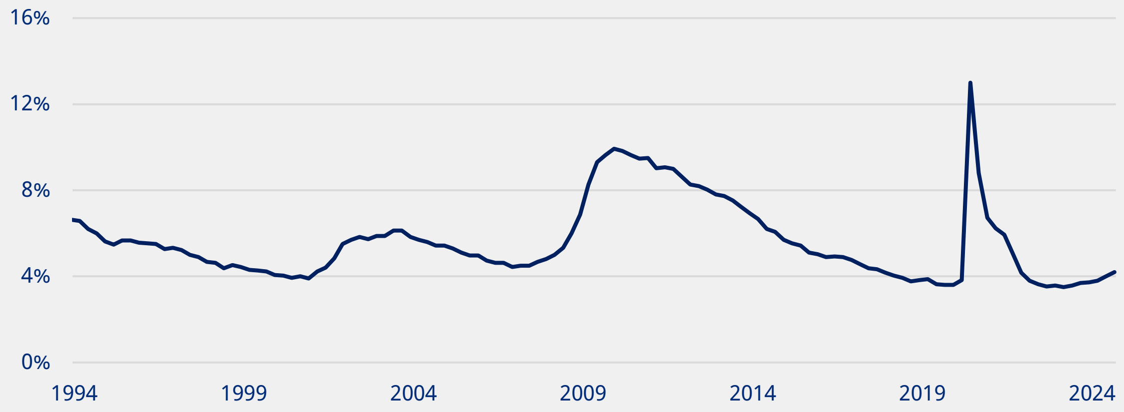
Fixed income markets performance was negative

- International Government Bonds produced negative returns over the quarter. Yields climbed after the FED noted further interest rate cuts will be made cautiously and be dependent on inflation.
- Australian Government Bonds also produced negative returns over the quarter as Australian bond yields rose. Yields rose sharply in October, then retracted after the latest GDP data announcement before ending the quarter higher following an unexpected fall in unemployment.

Commodity markets produce mixed results

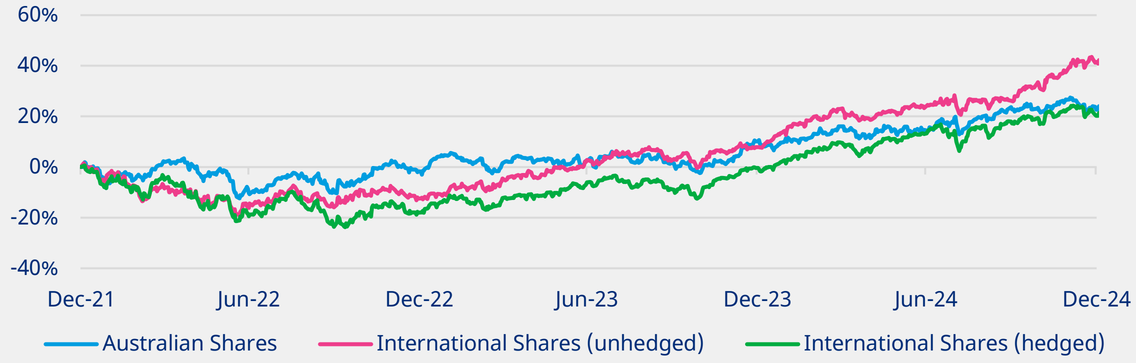
- Iron ore ended the quarter slightly lower reflecting the possible impact of tariffs on China. Copper prices were also lower over the quarter.
- Oil was positive in the quarter with news in December of disruptions to oil flow in the Middle East.
- Gold was marginally lower in the quarter following strong gains over the year and likely reflecting the quieter trading period heading into the holidays.

US Unemployment Rate %



Source: Bloomberg, Mercer

Cumulative asset class returns



Source: LSEG DataStream; MSCI. Data provided 'as is’. Details on chart constituents can be found on last page.

Market Insights

Australia: Probability of the RBA cutting the cash rate in February has increased.

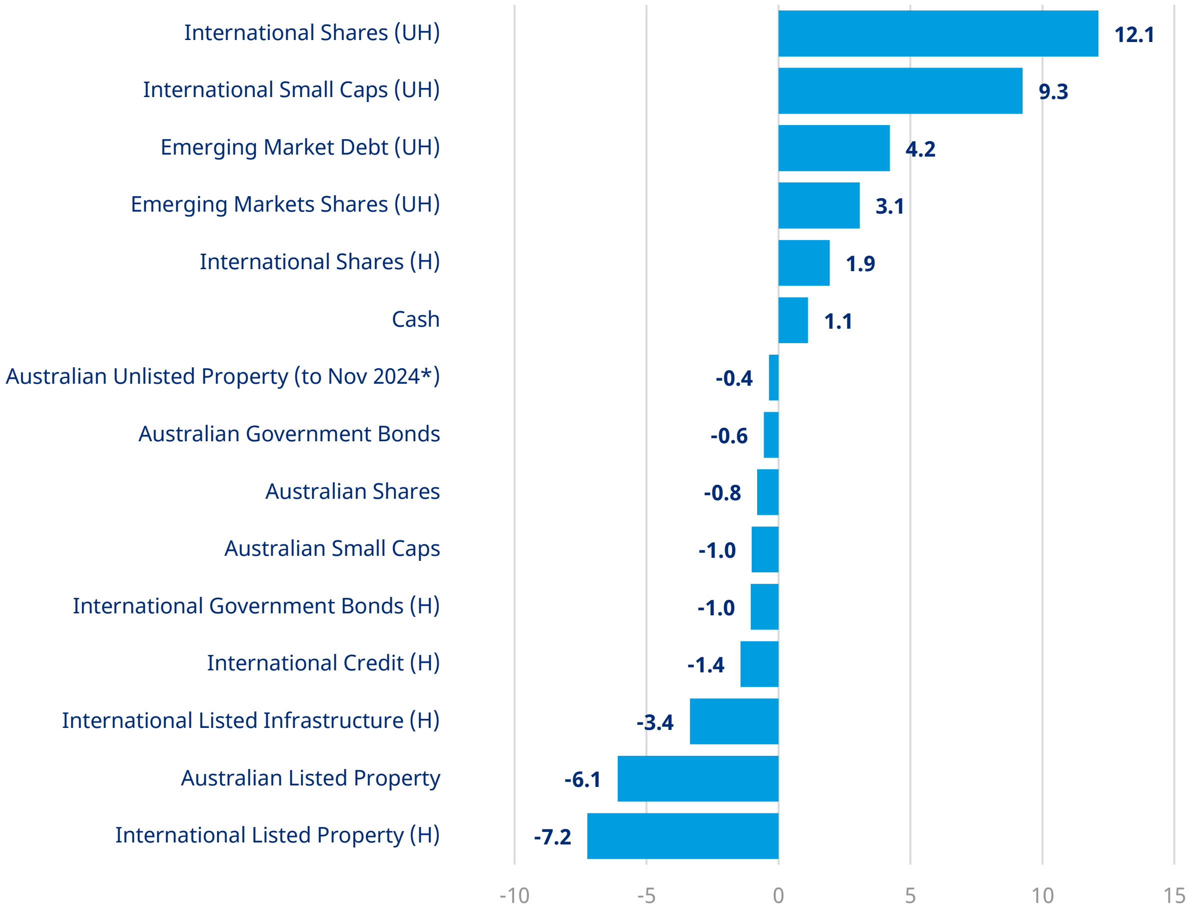
- The RBA continued to hold rates steady in the quarter even though the case for cutting rates is gaining traction. Weak GDP data and softening house prices has increased the possibility of an interest rate cut in February.
- While unemployment remains low, wage growth and job vacancies have been falling suggesting the labour market may weaken and unemployment could start to rise in 2025.
- We continue to expect growth to remain weak as higher interest rates and cost-of-living pressures are likely to keep consumption suppressed.
- Domestically, we favour Australian sovereign bonds over cash with interest rates likely to have peaked this cycle.

International: Regional divergence expected to continue

- We expect international economic growth to remain resilient but regionally divergent with the US experiencing a period of softer economic activity compared with other parts of the world. President elect Trump brings both upside and downside uncertainty to growth and inflation.
- Central Banks around the world are likely to continue to cut rates as inflation moderates but at a slower pace. The exception is Japan where we expect interest rates to rise as it emerges from a multi-decade deflation period.
- Japan is likely to continue to do well economically, driven by income growth and continued investment in capital expenditure. We continue to favour Japanese shares relative to other developed country share markets.
- We favour global listed property as fundamentals are broadly healthy, and valuations are attractive. We also favour Japanese shares due to the potential growth rebound and solid earnings growth.

Performance

Market performance 3 Months to December 2024



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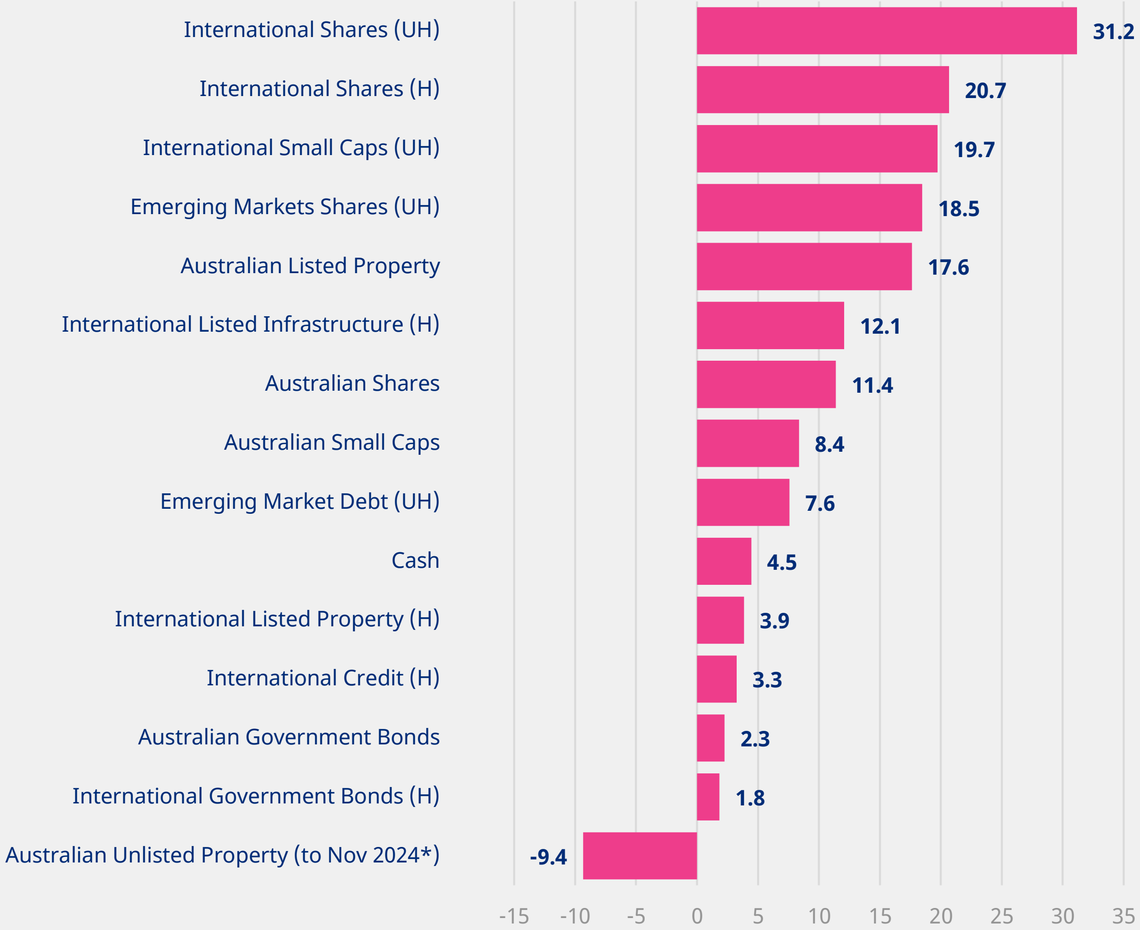
Market performance 12 Months to December 2024



Data source: LSEG Datastream; MSCI. Data provided 'as is'. Details on chart constituents can be found on the last page.

Asset class

▼ Australian Shares

- Australian shares ended the Q4’24 slightly lower as weaker Australian economic data weighed on the local share market.
- The Financial sector was the best performing sector in the quarter with Block Inc the best performing stock following price upgrades from investment banks. The Materials sector was the weakest performing sector.

▲ International Shares

- International shares (Hedged) ended the Q4’24 with a small gain, following solid gains over the year. Strong US growth relative to other economies and strong tech stocks gains likely drove investors to continue to favour US stocks which represent over 70% of international shares.
- International shares (Unhedged) moved higher in the quarter assisted by a fall in the AUD.
- Consumer Discretionary was the best performing sector and Materials was the worst performing sector in the MSCI World index over the quarter.

▼ Fixed Interest

- International Government Bonds had a negative return in the quarter as bond yields rose. The FED noted that interest rates are significantly closer to neutral and future cuts would be gradual which caused a significant increase in US sovereign bond yields.
- Australian Government Bonds ended the quarter lower. Australian sovereign bonds yields rose only slightly compared to US yields after the FED announcements and weaker economic data in Australia.
- International Credit had a small negative return due to the rise in International Bond yields.

▼ Real assets

- Interest rate sensitive assets like Australian Listed Property, International Listed Property and International Listed Infrastructure performed poorly as international sovereign bond yields rose in the quarter.

▼ Currency

- The AUD depreciated against the USD in the quarter. Comments by the FED were seen as more hawkish and weaker economic data in Australia were the key reasons.
- Most currencies depreciated against the USD in the quarter.

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Chart Constituents

Asset class	Benchmark	Data type
Australian Shares	S&P/ASX 300	Total Return
Australian Small Caps	S&P/ASX Small Ordinaries	Total Return
International Shares (UH)	MSCI World ex Australia	Net Index
International Shares (H)	MSCI World ex Australia 100% Hedged	Net Index
International Small Caps (UH)	MSCI World Small Cap	Net Return
Emerging Markets Shares (UH)	MSCI Emerging Markets	Net Index
Australian Unlisted Property (one month lag)	MSCI/Mercer Australia Core Wholesale Monthly PFI	NAV Post Fee
Australian Listed Property	S&P/ASX 300 A-REIT	Total Return
International Listed Property (H)	FTSE EPRA/NAREIT Developed Hedged	Net Return
International Listed Infrastructure (H)	FTSE Global Core Infrastructure 50/50 Hedged	Net Return
International Credit (H)	Bloomberg Global Credit	Hedged Return
Emerging Market Debt (UH)	JP Morgan GBI EM Global Diversified Composite	Total Return
Australian Government Bonds	Bloomberg AusBond Treasury 0+ year	Total Return
International Government Bonds (H)	Bloomberg Global Treasury Hedged	Hedged Return
Cash	Bloomberg AusBond Bank Bill	Total Return

Notes

- *Currency: AUD.*
- *UH: Unhedged.*
- *H: Hedged.*
- *Where a lag exists, the performance start and end dates shift accordingly.*
- *Total Return: Total Return Index with Gross Dividends.*
- *Net Index: Total Return (Net Dividends Reinvested).*

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