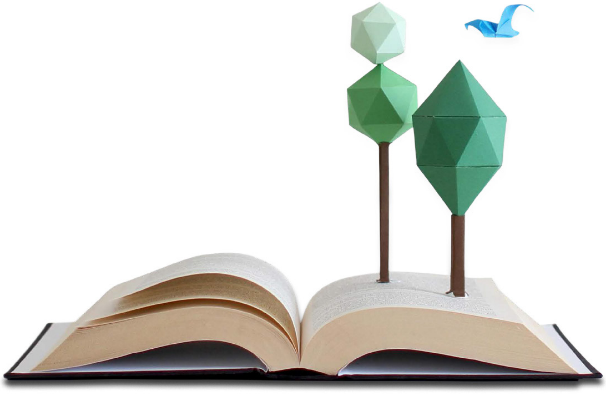
welcome to brighter

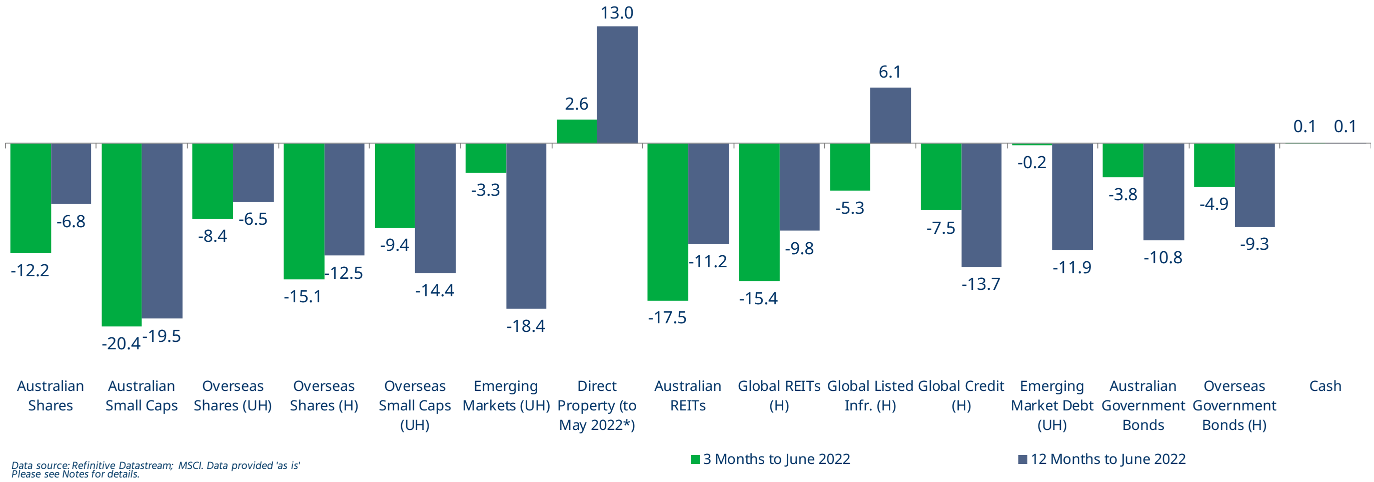
Q2 2022

Market and economic conditions



Selected market indicators commentary

Asset class returns as at June quarter 2022



Markets sold off broadly over the second quarter of 2022. Asset prices were challenged by central bank tightening, economic growth momentum fading and the earnings outlook becoming more challenged. Inflation in the US came in above expectation this quarter and other regions have continued to experience persistent, elevated inflation. Economic data hinted at a slowdown and led to increased recession fears.

Hedged Developed Market Overseas Shares returned -15.1% for the quarter with poor economic and inflation data in the US driving the losses. Australian shares fell 12.2% with recession fears leading the commodity heavy index lower. Emerging market equities outperformed their global counterparts over the quarter, posting a -3.3% decline.

Chinese equities contributed positively to the index over the quarter on the back of a further reopening of the economy and accommodative monetary policy. Conversely, commodity heavy Latin American countries detracted from the EM index over the quarter.

Hedged Overseas Government Bonds returned -4.9% over the quarter as rates continued to rise. The US 10-year yield ended the month at 3.0%. Australian 10-year government bond yields moved in the same direction, with Australian government bonds returning -3.8%. Credit spreads also widened in this risk-off environment, which led to poor performance for credit and growth fixed income assets.

Whilst Australian shares outperformed overseas shares over the quarter, the ASX300 still posted a sharp 12.2% decline. Further declines were felt in small caps, with the ASX Small Ordinaries declining 20.4%. The strongest performing sectors over the quarter were Energy (1.2%) and Utilities (1.7%), whilst the worst performing sectors were IT (-26.3%) and Real Estate (-17.6%). Westpac and ANZ were the largest negative contributors to the ASX300 over the quarter.

Significant Developments

- During its July 2022 meeting, the Reserve Bank of Australia (RBA) decided to increase the current target cash rate by 50 basis points to 1.35% per annum and the interest rate on exchange settlement balances from 0.75% to 1.25%. Global inflation is being boosted by COVID-related disruptions to supply chains, the war in Ukraine and strong demand which is putting pressure on productive capacity. Inflation in Australia is also high due to global factors mentioned, and also domestic factors, such as strong demand, a tight labour market and capacity constraints in some sectors. Inflation is forecasted to peak later this year and then decline back towards the 2–3% range next year. Higher interest rates will also help establish a more sustainable balance between the supply and demand for goods and services. The Australian economy remains resilient as the unemployment rate was steady at 3.9% in May, and is expected to decline further. There has been a lift in wages growth as firms compete for staff in the tight labour market. One source of ongoing uncertainty about the economic outlook is the behaviour of household spending, where household budgets are under pressure from higher prices and higher interest rates. Housing prices have also declined in some markets over recent months. The Board will be paying close attention to these various influences on household spending as it assesses the appropriate setting of monetary policy. The Board will also be paying close attention to the global outlook, which remains clouded by the war in Ukraine and its effect on the prices for energy and agricultural commodities. There are also ongoing uncertainties related to COVID, especially in China. The resilience of the economy and the higher inflation means that the support supplied during the pandemic is no longer needed. The board expects to take further steps in the months ahead. The size and timing of future interest rate increases will be guided by the incoming data and the Board's assessment of the outlook for inflation and the labour market.
- Australian seasonally adjusted employment increased by 60,600 in May, above expectations for an increase of 25,000 and above the prior month's increase of 4,000. The unemployment was the same for May at 3.9%, above expectations of 3.8%. The participation increased by 66.7%, above expectations of 66.4%. Part time jobs decreased by 8,700 and full time jobs increased by 69,400.
- The CoreLogic House price index indicated Australian residential house prices declined by -0.8% in the first quarter of 2022. Australian building approvals increased by 9.9% month-on-month to May, compared to the decrease of 3.9% (revised) for April.
- The Institute for Supply Management (ISM) Manufacturing Index recorded 53 in June, below consensus for 54.5 and below the 56.1 recorded in May. Of the 15 manufacturing industries, Apparel, Leather & Allied Products and Textile Mills were the two industries that reported the highest growth. The only industries that reported a contraction over June was Paper Products, Wood Products, and Furniture & Related Products. The ISM Services Index recorded 55.3 in June, above consensus for 54 and below the 55.9 recorded in May. Of the 18 services industries, the top performers were Mining and Management of Companies & Support Services. No industry reported a decrease in the month of June.
- US Non-Farm Payrolls increased by 372,000 in June, below the 384,000 increase (revised) recorded for May. The unemployment rate stayed the same at 3.6% over June, in line with expectations.
- US GDP third estimate for Q1 2022 is -1.6% quarter on quarter (QoQ) annualised, which was below expectations of -1.5%
- US headline consumer price index (CPI) increased to 1.3% MoM and increased to 9.1% YoY in May.
- The Caixin Manufacturing PMI in China recorded 51.7 in June, above expectations of 50.2, as manufacturing output rebounds whilst pandemic restrictions recede.
- Chinese GDP increased 4.8% YoY for Q1 2022, above expectations for 4.2%. Seasonally adjusted GDP increased 1.3% QoQ for Q1 2022, above expectations for 0.7%.
- The preliminary estimate of the European Core CPI recorded 3.7% over the year to June, below expectations of 3.9%. The unemployment increased over the month to 7.1% in June 2022.
- The Eurozone composite PMI decreased to 52 in June, above expectations for 51.9.
- The final estimate recorded for Q1 2022 Eurozone seasonally adjusted GDP is 0.6% QoQ and 5.4% YoY.

Australian Equities

Australian shares were negative over Q2 2022 as the S&P/ASX 300 Index returned -12.2% for the period. The S&P/ASX 50 Accumulation Index was the strongest performer for the quarter returning -10.6%, while the S&P/ASX Small Ordinaries was the weakest performer, returning -20.4%.

The best performing sectors were Energy (1.2%) and Utilities (1.7%), while the weakest performing sectors were IT (-26.3%) and Real Estate (-17.6%). The largest positive contributors to the return of the index were CSL, BHP and Transurban with absolute returns of 0.6%, -8.1% and 6.8% respectively. On the other hand, the most significant detractors from performance were Westpac, ANZ and Macquarie with absolute returns of -18.6%, -19.0% and -18.4% respectively.

Global Equities

The broad MSCI World ex Australia Accumulation Index decreased -8.4% in unhedged terms and decreased -15.1% in hedged terms over the quarter, as the AUD weakened against most major currencies over the period. The strongest performing sectors were Energy (3.6%) and Consumer Staples (2.3%), while Consumer Discretionary (-16.8%) and IT (-14.6%) were the worst performers. Other global shares were negative as the MSCI Small Caps Total Return Index returned -9.4% and the MSCI Emerging Markets Accumulation Index returned -3.3% over the quarter, all in AUD terms.

Over the June quarter, the NASDAQ (-22.4%), the S&P 500 Composite Index (-16.1%) and the Dow Jones Industrial Average decreased (-10.8%), all in USD terms. European markets experienced negative returns, as the FTSE 100 (United Kingdom) (-3.7%), the CAC 40 (France) (-8.9%) and the DAX 30 (Germany) (-11.3%) decreased, all in local currency terms. Equity returns were mixed across Asia as the SSE Composite (China) (4.5%) and Hang Seng (Hong Kong) (0.9%) increased while the S&P BSE 500 (India) (-10.0%) and the TOPIX (Japan) (-3.7%) decreased, all in local currency terms.

Real Assets

Domestic listed property experienced poor performance over the quarter and returned -17.5%. Global REIT's returned -15.4% (in AUD hedged terms) over the June quarter. The Australian unlisted property sector (NAV) increased 2.6% over the quarter on a one month lagged basis and the FTSE Global Core Infrastructure 50/50 Index decreased -5.3% for the quarter in hedged AUD terms.

Fixed Interest

Global sovereign bonds produced broadly negative returns over the June quarter as ten-year bond yields increased in the US (65bps to 2.97%), Germany (86bps to 1.37%), UK (62bps to 2.21%) and Japan (2bps to 0.23%). Two-year bond yields increased in the US (68bps to 2.94%), Germany (72bps to 0.54%) and the UK (52bps to 1.88), whilst decreasing in Japan (-2bps to -0.06%). In terms of Global Bond indices, the Barclays Capital Global Aggregate Bond Index returned -4.7% and the FTSE World Government Bond (ex-Australia) Index decreased by 4.9% over the June quarter, both on a fully hedged basis.

Domestically, the Australian 10-year bond yield (82bps to 3.66%), five-year bond yield (76bps to 3.36%) and two-year bond yield (119bps to 2.99%) all increased. The Bloomberg Ausbond indices returned broadly negative results over the quarter, with the Bloomberg Ausbond Bank producing the highest quarterly return, returning 0.1%, and the weakest being the Bloomberg Ausbond Inflation, returning -5.9%.

Currency Markets

The Australian Dollar (AUD) depreciated against major developed market currencies over the June quarter, finishing at US$0.69. The AUD depreciated against the USD (-8.4%), the Pound Sterling (-0.7%) and the Euro (-2.5%), while appreciating against the Japanese Yen (2.5%). On a trade-weighted basis, the local currency depreciated by 2.8% over the quarter.

Commodities

The S&P GSCI Commodity Total Return Index increased by 11.4% over the quarter. Gold prices finished the quarter at US$1,806.87 per ounce, decreasing by 6.9%. Meanwhile, Iron Ore prices decreased by 19.9% to US$122.5 per metric tonne over the period and Oil increased by 7.0% to US$114.93 per barrel.

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Chart Constituents

Notes

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

Asset class	Benchmark	Data type
Australian Shares	S&P/ASX 300	Total Return
Australian Small Caps	S&P/ASX Small Ordinaries	Total Return
Overseas Shares (UH)	MSCI World ex Australia	Net Index
Overseas Shares (H)	MSCI World ex Australia 100% Hedged	Net Index
Overseas Small Caps (UH)	MSCI World Small Cap	Total Return
Emerging Markets (UH)	MSCI Emerging Markets	Net Index
Direct Property (one month lag)	MSCI/Mercer Australia Core Wholesale Monthly PFI	NAV Post Fee
Australian REITs	S&P/ASX 300: Industry Group: A-REIT	Total Return
Global REITs (H)	FTSE EPRA/NAREIT Developed Hedged	Total Return
Global Listed Infrastructure (H)	FTSE Global Core Infrastructure 50/50 Hedged	Total Return
Global 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
Overseas Government Bonds (H)	FTSE WGBI Non Australia	Hedged Return
Cash	Bloomberg AusBond Bank Bill	Total Return

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- The value of Gilts, bonds, and other fixed income investments including unit trusts can go down as well as up and you may not get back the amount you have invested.
- Investments denominated in a foreign currency will fluctuate with the value of the currency.
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- For higher volatility investments, losses on realisation may be high because their value may fall suddenly and substantially.
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