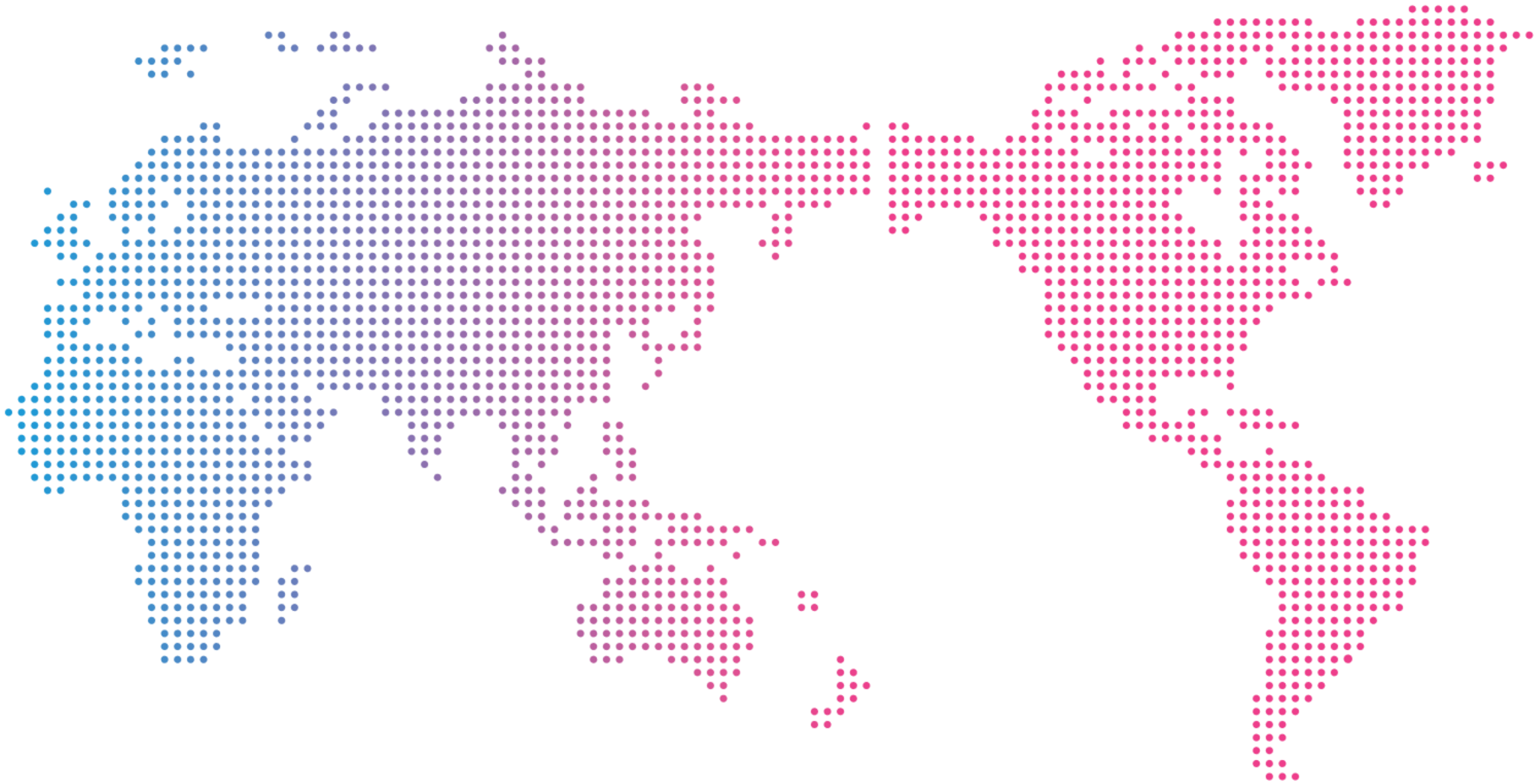
Mercer

welcome to brighter

Market Review Quarterly

Q3 2024



A business of Marsh McLennan

Key takeaways

- The US Federal Reserve (Fed) cut interest rates by 0.5% to 4.75 - 5.00% p.a. as confidence grew around the inflation outlook. Several European regions, Canada and New Zealand also cut rates during the quarter.
- The Reserve Bank of Australia (RBA) kept interest rates unchanged at 4.35% p.a. noting that inflation concerns have eased according to the latest quarterly core readings.
- China’s policymakers pledged necessary fiscal expenditures to meet this year's economic growth targets and address the decline in the property market.
- Looking ahead, we do not expect the US to enter a recession as consumer and corporate balance sheets remain strong, and growth across emerging economies are expected to be supported by government policy measures.
- We favour **emerging markets over developed markets** due to their more appealing valuations and promising economic prospects.
- In Australia, we expect growth to remain weak and **favour Australian government bonds,** as cash rates have likely peaked this cycle.

Research

[Managing the total Portfolio]

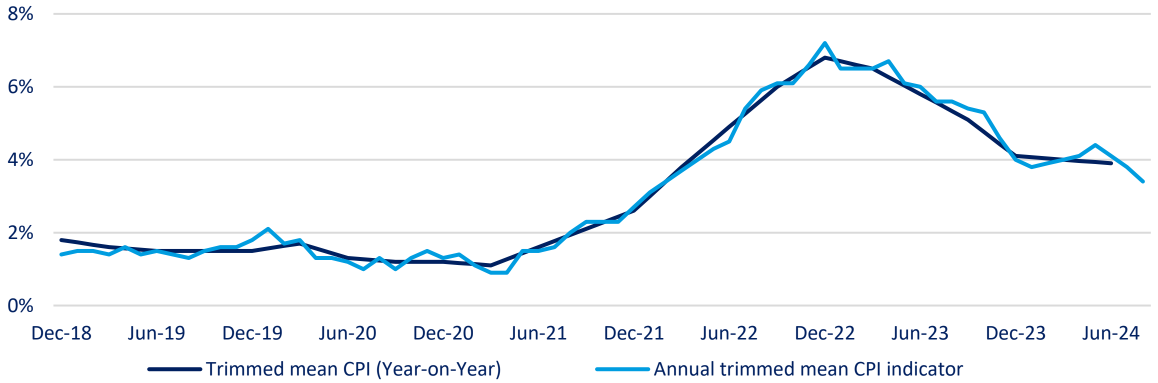
[Statement by the Reserve Bank Board: Monetary Policy Decision]

Economic review

Australia: RBA remains vigilant to upside risks to inflation despite weak growth

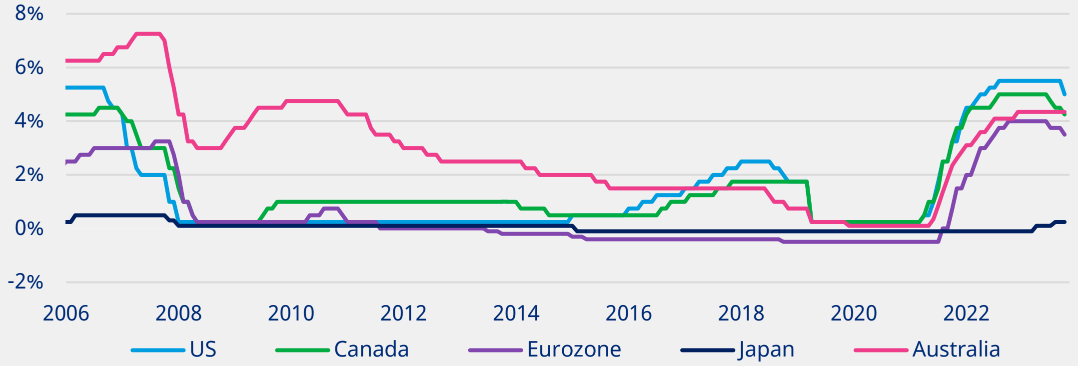
- Economic activity remained weak over the quarter. Q2’24 GDP was 0.2% Quarter-on-Quarter (QoQ), bringing the Year-on-Year (YoY) rate to 1.0%, driven by weak household consumption. Business survey responses indicated slowing conditions, with retail facing the most challenges.
- The trimmed mean CPI (the RBA’s preferred measure of inflation) rose by 0.8% QoQ in Q2’24, down from 1.0% QoQ in Q1’24, easing concerns about accelerating underlying inflation in Australia. More recent inflation indicators have also eased, driven by the government's energy rebate for households.
- The RBA kept interest rates unchanged at 4.35% p.a. over the quarter noting it "remains vigilant to the upside risks to inflation" effectively pushing back against expectations for an interest rate cut in the coming months.

Australian trimmed mean Consumer Price Index (CPI) (year-on-year) and annual trimmed mean CPI indicator



Source: Bloomberg, Mercer; Chart is shown on monthly frequency. Trimmed mean CPI is a quarterly release and has been interpolated to a monthly frequency for this chart.

Central Bank Policy Rates



Source: Bloomberg

International: US Federal Reserve cuts by 0.5%

- Fears of a US recession grew, due to weaker conditions in labour markets and the manufacturing sector. However, other data showed strong overall conditions including Q2’24 GDP growth of 3.0% QoQ annualised, driven by household consumption.
- Economic conditions weakened in the Eurozone, led by German manufacturers. Meanwhile, conditions remained lacklustre in China driven by ongoing weakness in its property markets, while economic activity improved in Japan with wage increases boosting consumption.
- With greater confidence in the inflation outlook, the Fed cut interest rates by 0.5% to 4.75-5.00% p.a. Stating that the size of the cut should not be extrapolated and that future decisions will be data dependent and made at each meeting.
- A number of European regions, Canada and New Zealand also cut interest rates by 0.25% in the quarter due to reducing inflationary pressures. Japan was the exception raising rates from 0.1% p.a. to 0.25% p.a.
- China’s policymakers have pledged to stop the decline in the property market with the Peoples’ Bank of China cutting interest rates and reserve ratio requirements.

Market review

Equity markets end higher despite some volatility

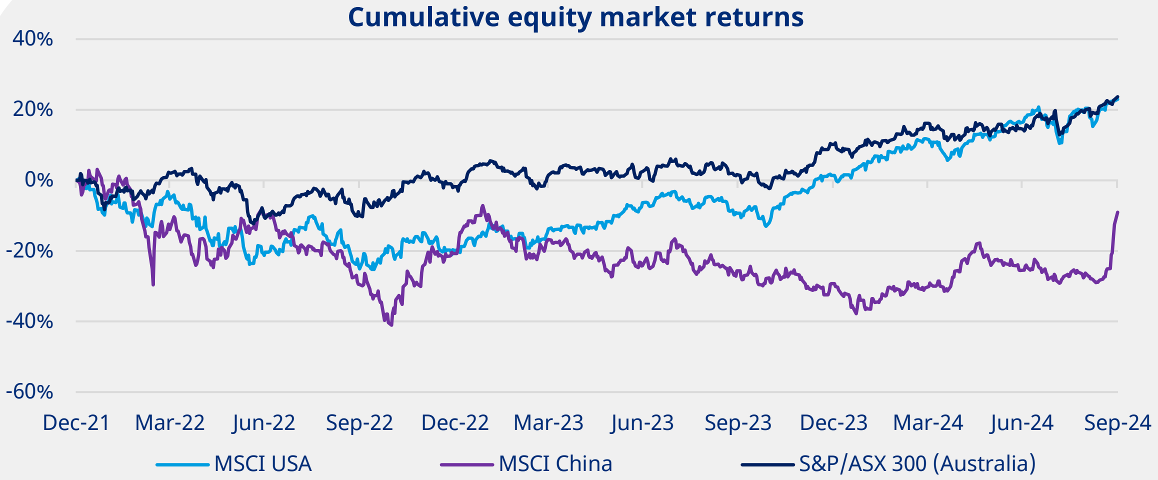
- International Shares overall continued to produce strong returns. The quarter saw some volatility, with markets initially declining due to fears of a US recession before recovering as the Fed began cutting interest rates.
- International Small Caps performed well as investors rotated from International Shares.
- Emerging Market Shares also performed well as investor optimism rose following the pledge from Chinese policymakers to address the decline in their property market.

Fixed income markets rally

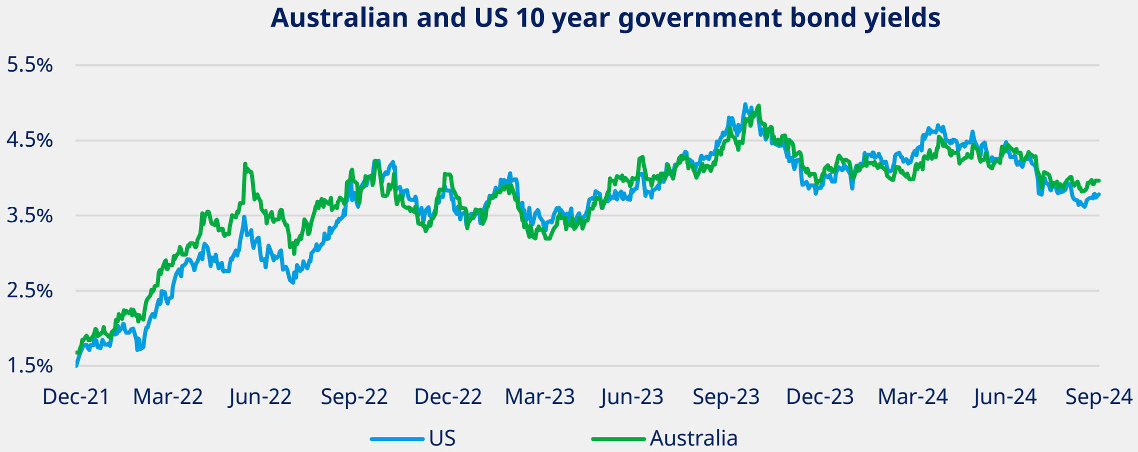
- International Government Bonds rose due to US recession concerns and anticipation of a US interest rate cut.
- Australian Government Bonds also produced positive returns but lagged behind International Government Bonds as the RBA kept interest rates unchanged and noted it did not foresee a near term rate cut.

Commodity markets experience mixed results

- Gold prices hit a record high as central banks cut interest rates internationally.
- Industrial metals like iron ore ended the quarter slightly lower due to weak economic data from China, despite a late recovery after Chinese policymakers pledged to stop the decline in property markets.
- Oil prices ended the quarter lower, despite rising tensions in the Middle East, due to speculation of supply increases by OPEC+.



Source: LSEG Datastream, Mercer; USA and China are net returns, whilst Australia is total return. Returns are shown in local currency terms.



Source: LSEG Datastream, Mercer

Market Insights

Australia: RBA unlikely to commence a series of interest rate hikes

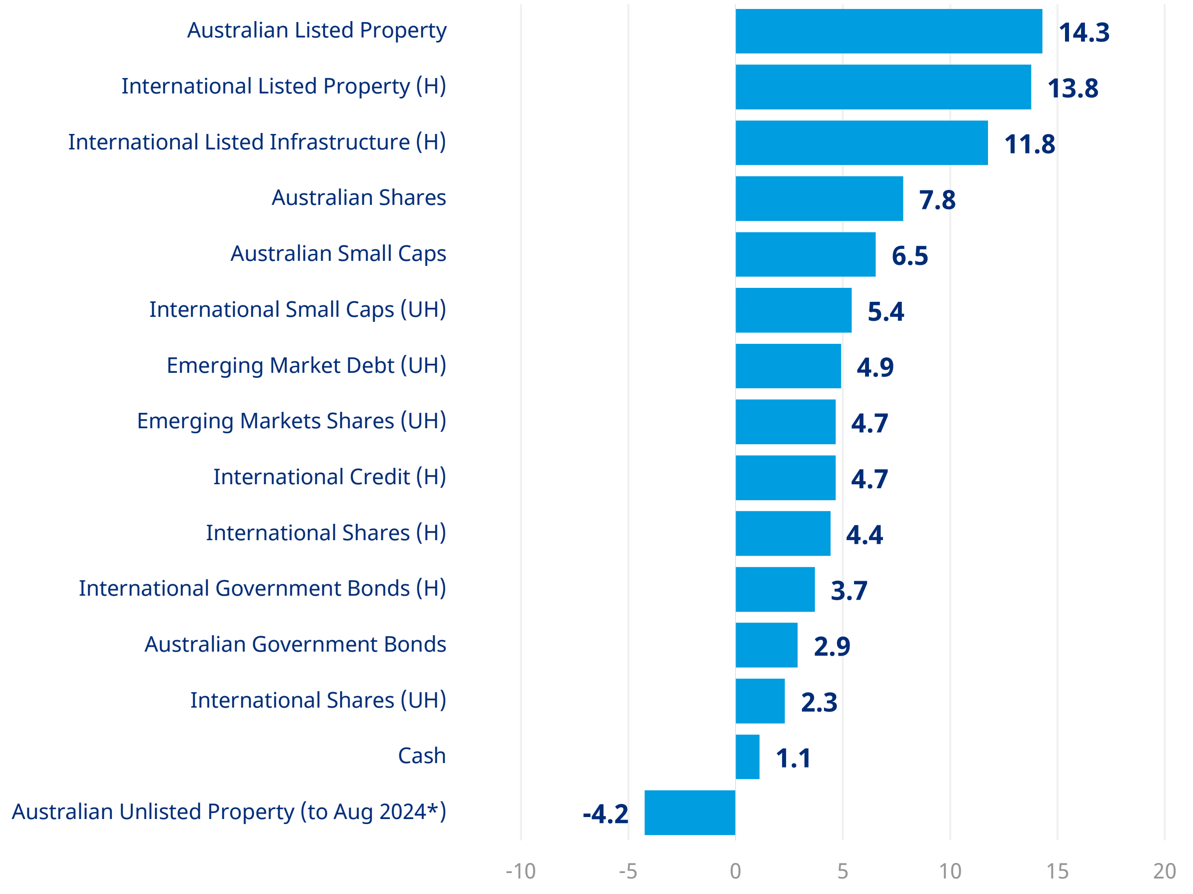
- We expect high interest rates and cost-of-living pressures to keep household consumption and economic growth suppressed.
- Core inflation is expected to decline at a slower pace compared to other developed economies due to pressures in residential rental markets.
- While the RBA has indicated vigilance against inflation risks, we do not believe it will commence a new series of hikes. Rather, we believe that interest rates have likely peaked this cycle.
- We favour Australian government bonds over cash with interest rates likely to have peaked this cycle.

International: Soft landing expected for the US

- We expect international economic growth to remain resilient but regionally divergent.
- We do not expect the US to enter a recession but anticipate slowing yet positive growth, with corporate and consumer balance sheets remaining strong.
- We expect US inflation to slow further, driven by a decline in services inflation, and expect the Fed to continue cutting rates. The market's expectations for US interest rates cuts appears excessive.
- We expect China's growth to improve from its current slow pace, supported by favourable government policies. Other emerging economies will also benefit from these policies and their own central bank policies, aiding their growth.
- We favour emerging markets over developed markets due to their better economic prospects and more attractive valuations.

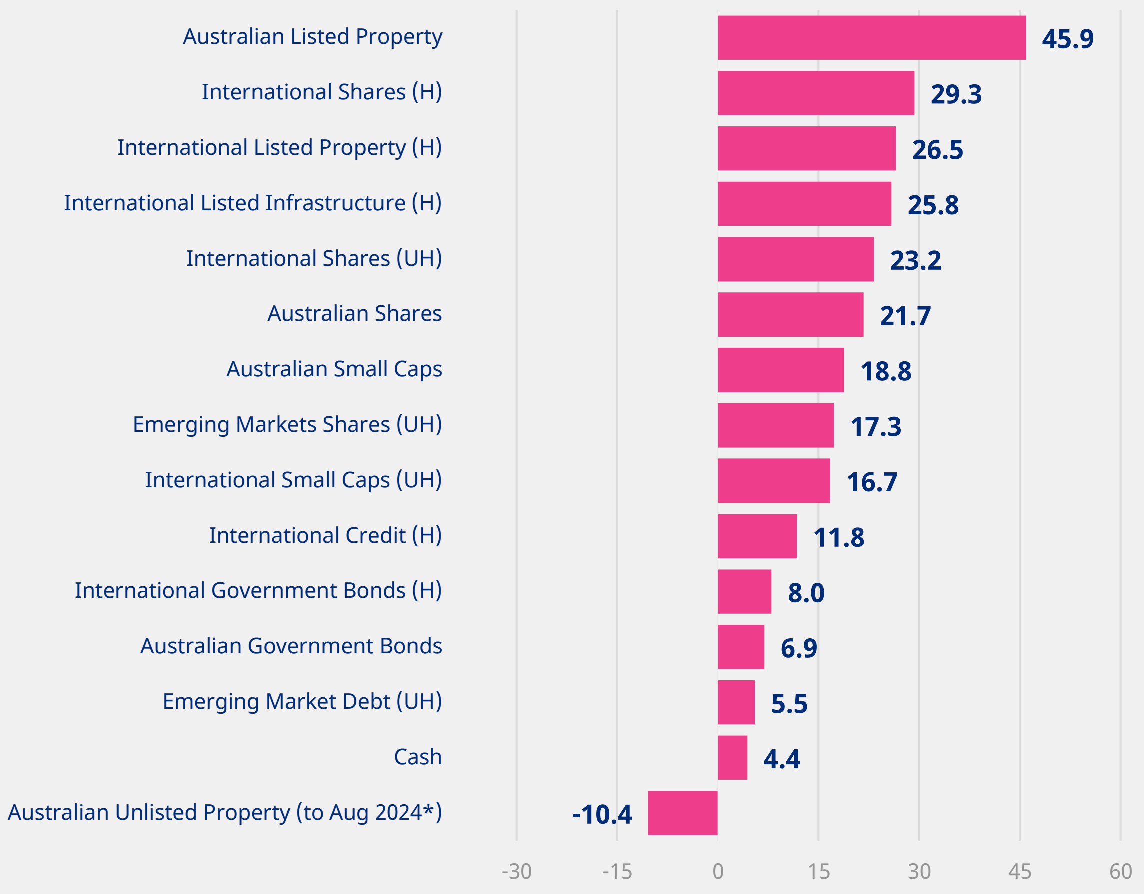
Performance

Market performance 3 Months to September 2024



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

Market performance 12 Months to September 2024



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

Asset class

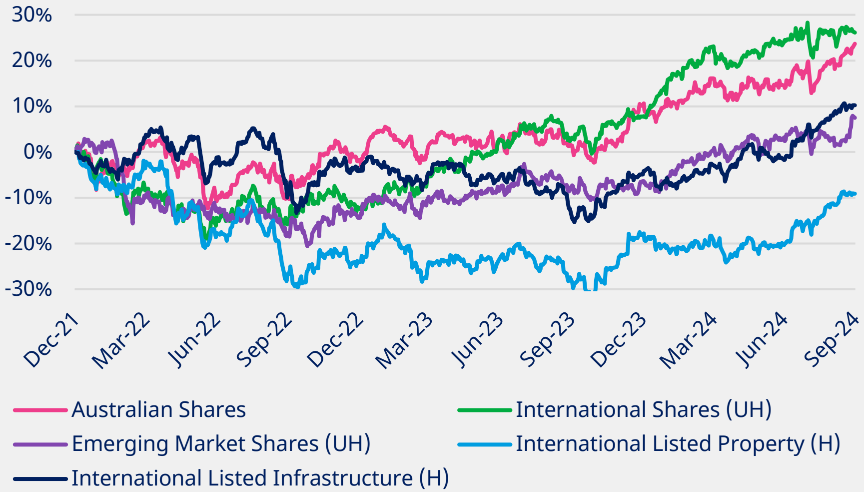
▲ Australian Shares

- Australian Shares rose as investor optimism for international interest rate cuts grew and Chinese authorities announced policy measures to support its property market.
- Against this backdrop, interest rate sensitive sectors such as Real Estate performed well. The Materials sector also did well in the quarter, supported by a late recovery in industrial metals prices.
- Australian Small Caps also performed well driven in part by a strong contribution late in the quarter from the Materials sector which benefited from the rise in precious and industrial metals prices.

▲ International Shares

- International Shares ended the quarter higher, recovering from an earlier decline as US recession concerns eased and the Fed began cutting interest rates.
- Utilities and Real Estate were the best performing sectors, supported by interest rate cuts and a decline in government bond yields internationally.
- Emerging Market Shares performed well, recovering late in the quarter as Chinese policymakers pledged to address the decline in their property market.

Cumulative asset class returns



Source: LSEG Datastream; MSCI. Data provided 'as is'. Details on chart constituents can be found on back page.

▲ Fixed Interest

- International Government Bonds produced healthy returns as concerns about the US economy rose and expectations for US interest rate cuts increased.
- International Credit and Emerging Market Debt also performed well, supported by the decline in government bond yields internationally and increased investor risk appetite following the US interest rate cut.
- Australian Government Bonds produced positive returns but lagged International Government Bond returns as the RBA kept interest rates unchanged.

▲ ▼ Real assets

- Rising anticipation of US interest rate cuts and declining bond yields boosted listed real asset markets with Australian Listed Property, International Listed Property and International Listed Infrastructure all recording strong returns for the quarter.
- Australian Unlisted Property was down due to downward valuation adjustments, especially in the Office sector.

▲ ▼ Currency

- The Australian dollar (AUD) recorded mixed performance against major currencies over the quarter.
- The AUD appreciated against the US dollar, with the latter depreciating in anticipation of Fed interest rate cuts, while the AUD depreciated against the Japanese Yen as the Bank of Japan raised interest rates and signalled more increases ahead.

Mercer

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).*

Important notices

This document is issued by Mercer Investments (Australia) Limited ABN 66 008 612 397 AFSL 244385 ('MIAL'). MIAL is a wholly owned subsidiary of Mercer (Australia) Pty Ltd ABN 32 005 315 917 ('Mercer Australia'). References to Mercer shall be construed to include Mercer LLC and/or its associated companies. 'MERCER' is a registered trademark of Mercer Australia.

This document contains confidential and proprietary information of Mercer and is intended for the exclusive use of the parties to whom it was provided by Mercer. Its content may not be modified, sold or otherwise provided, in whole or in part, to any other person or entity, without Mercer's prior written permission.

The findings, ratings and/or opinions expressed herein are the intellectual property of Mercer and are subject to change without notice. They are not intended to convey any guarantees as to the future performance to any MIAL Fund, asset classes or capital markets discussed.

Information contained herein has been obtained from a range of third party sources. While the information is believed to be reliable, Mercer has not sought to verify it independently. As such, Mercer makes no representations or warranties as to the accuracy of the information presented and takes no responsibility or liability (including for indirect, consequential or incidental damages), for any error, omission or inaccuracy in the data supplied by any third party.

MIAL is the Responsible Entity and issuer of interests in any MIAL Fund. Investors should be aware that the value of an investment in any MIAL Fund may rise and fall from time to time and that neither MIAL nor Mercer guarantees the investment performance, earnings or return of capital invested in any MIAL Funds. Past performance does not guarantee future results.

If you are investing in or considering an investment in any MIAL Fund, you should note that the information contained in this document is general in nature only, and does not constitute an offer or a solicitation of an offer to buy or sell securities, commodities and/or any other financial instruments or products or constitute a solicitation on behalf of any of the investment managers, their affiliates, products or strategies that Mercer may evaluate or recommend. It does not take into account your personal needs and circumstances.

Before deciding whether to acquire, continue to hold or dispose of an investment, you should refer to the Product Disclosure Statement (PDS) and Target Market Determination (TMD) (available at mercer.com.au/mercerfunds) before making a decision about the product and consider seeking independent advice from a professional financial adviser. The Financial Services Guide (FSG) for MIAL can be obtained via mercer.com.au/mercerfunds. Conditions, fees and charges apply to MIAL Fund/s and may change from time to time.

Where MIAL has appointed third party manager(s) as the investment manager of any MIAL Fund, the relevant investment manager has consented to the statements pertaining to it in this document, in the form and context in which they appear and has not withdrawn its consent as at the date this document was published.

A business of Marsh McLennan