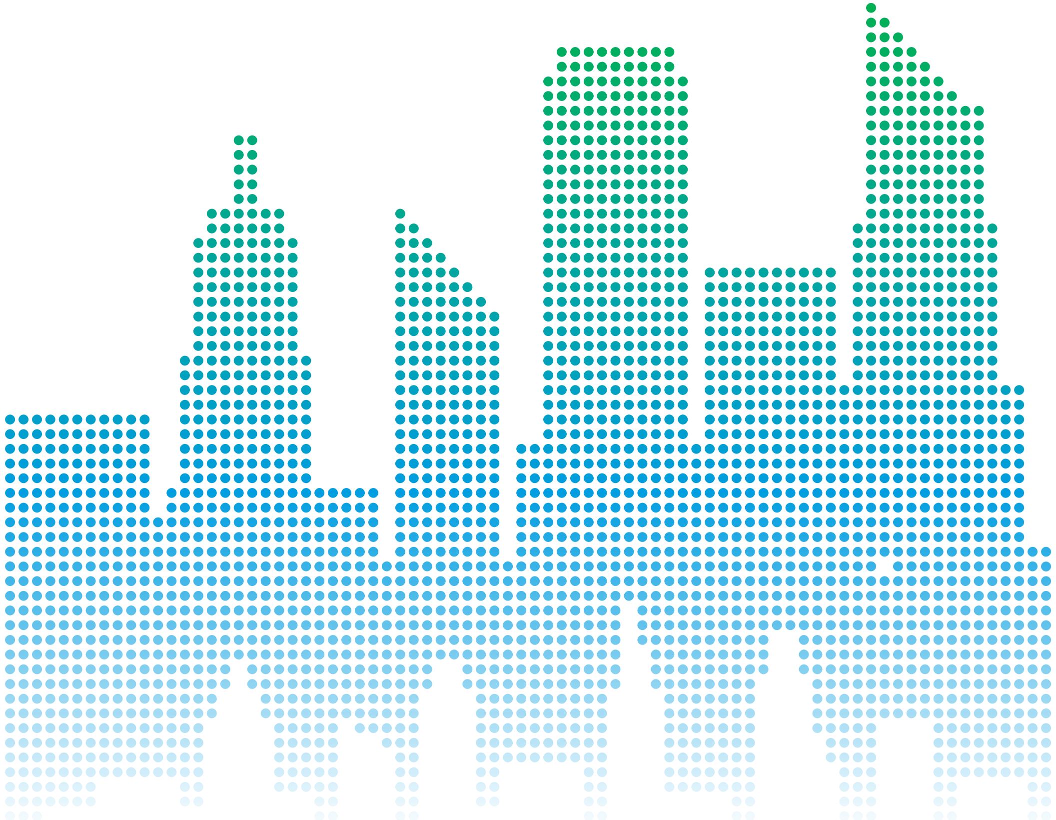
Mercer

welcome to brighter

Market Review Monthly

December 2024



A business of Marsh McLennan

Key takeaways

- 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 Australian labour market remained strong in November as unemployment fell to 3.9% beating market expectations for a rise to 4.2%.
- Equity markets were weaker in December but had strong gains over the year with 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 Japan 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.

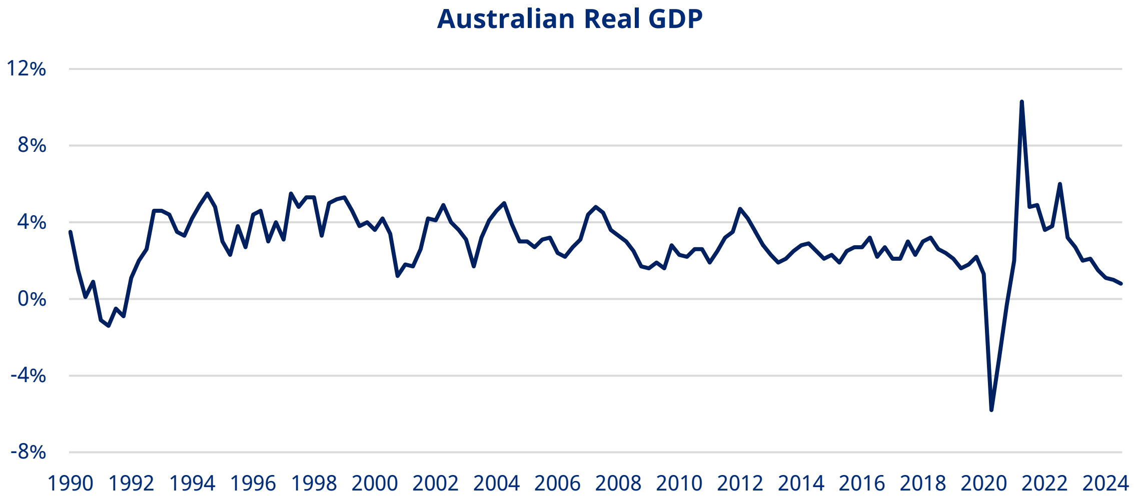
2. Australian Q4 CPI announcement (29th Jan) – Inflation easing will give the RBA freedom to begin interest rate cuts.

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

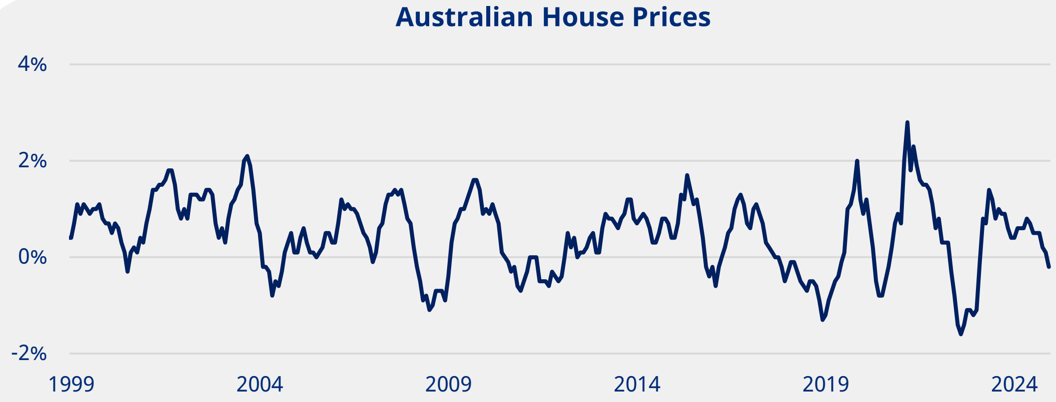
Economic review

Australia: Increased probability of an interest rate cut

- The RBA kept rates steady at 4.35% for their ninth consecutive meeting. However, the softening economic environment has increased the chance of a February interest rate cut.
- Australia's 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, the domestic labour market remained strong as unemployment fell to 3.9% from 4.1% in November, helped by the fall in participation rate. In addition, 36,700 jobs were added and business surveys reported weaker business confidence in November.
- Australian house prices have started to soften -0.1% lower in December. Sydney and Melbourne, continued to fall, with Sydney down -0.2% and Melbourne down -0.4% 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 in December, The European (ECB) and US (FED) Central Banks cutting rates by 25bps and their Canadian (BOC) and Swiss (SNB) counterparts cutting rates by 50bps.
- The Bank of Japan (BoJ) left interest rates unchanged at 0.25%, noting that Japan's economy had recovered moderately.
- US CPI data (Annual core) for November rose 0.3% MoM to 3.3%. Rent and utility costs, a significant expense for households, was lower in November, possibly giving the US Federal Reserve (FED) enough comfort to cut interest rates at their next meeting.
- US employment data was strong with 227,000 jobs added in November and unemployment increasing slightly to 4.2% from 4.1%. The US NIFB small business survey suggested increased optimism following the US election.
- US ISM manufacturing was better than expected, but still in contractionary mode as the new orders component moved into positive territory.

Market review

Equity markets had mixed performance over the month

- International Shares (Hedged) ended December lower and were likely due a pause following strong performance over 2024.
- International Shares (Unhedged) were higher in December assisted by a fall in the Australian Dollar (AUD).
- Australian Shares ended December lower following the direction of hedged international markets as weaker Australian economic data weighed on local equity markets.

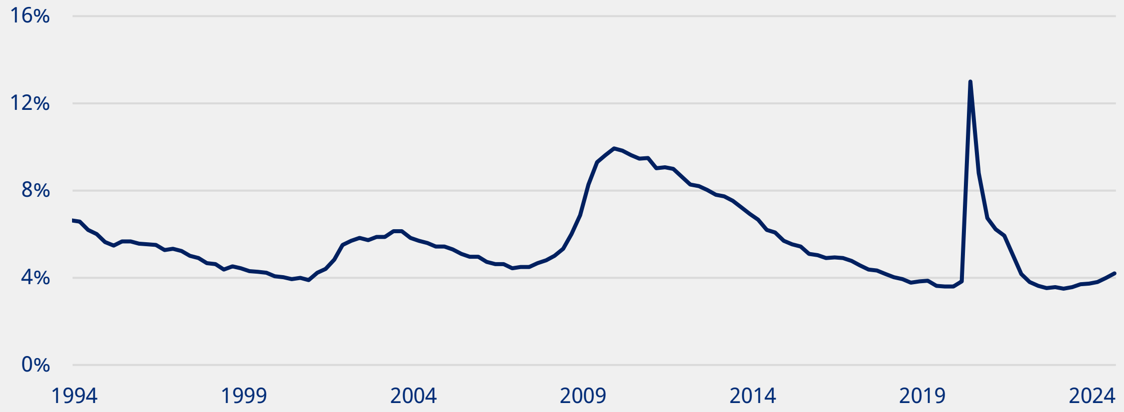
International fixed income markets performance negative

- International Government Bonds saw negative performance in December after the FED noted further rate cuts will be made cautiously and be dependent on inflation.
- Australian Government Bonds had positive performance in December with yields almost unchanged over the month. While Australian 10yr sovereign bond yields initially fell after the latest GDP data announcement, they moved higher after the unexpected fall in unemployment to finish the month up marginally 2bps.
- International Credit also had a small negative return due to the rise in International Bond yields.

Commodity markets produce mixed results

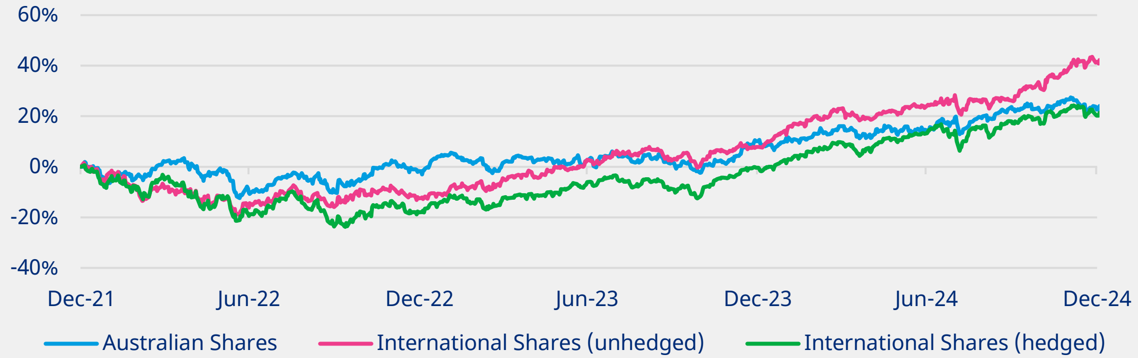
- Iron ore ended the month slightly lower reflecting the possible impact of tariffs on China. Copper prices were also lower in December.
- Oil saw strong gains over the month following disruptions to oil flow in the Middle East.
- Gold was unchanged over December likely reflecting the quieter trading 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 back page.

Market Insights

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

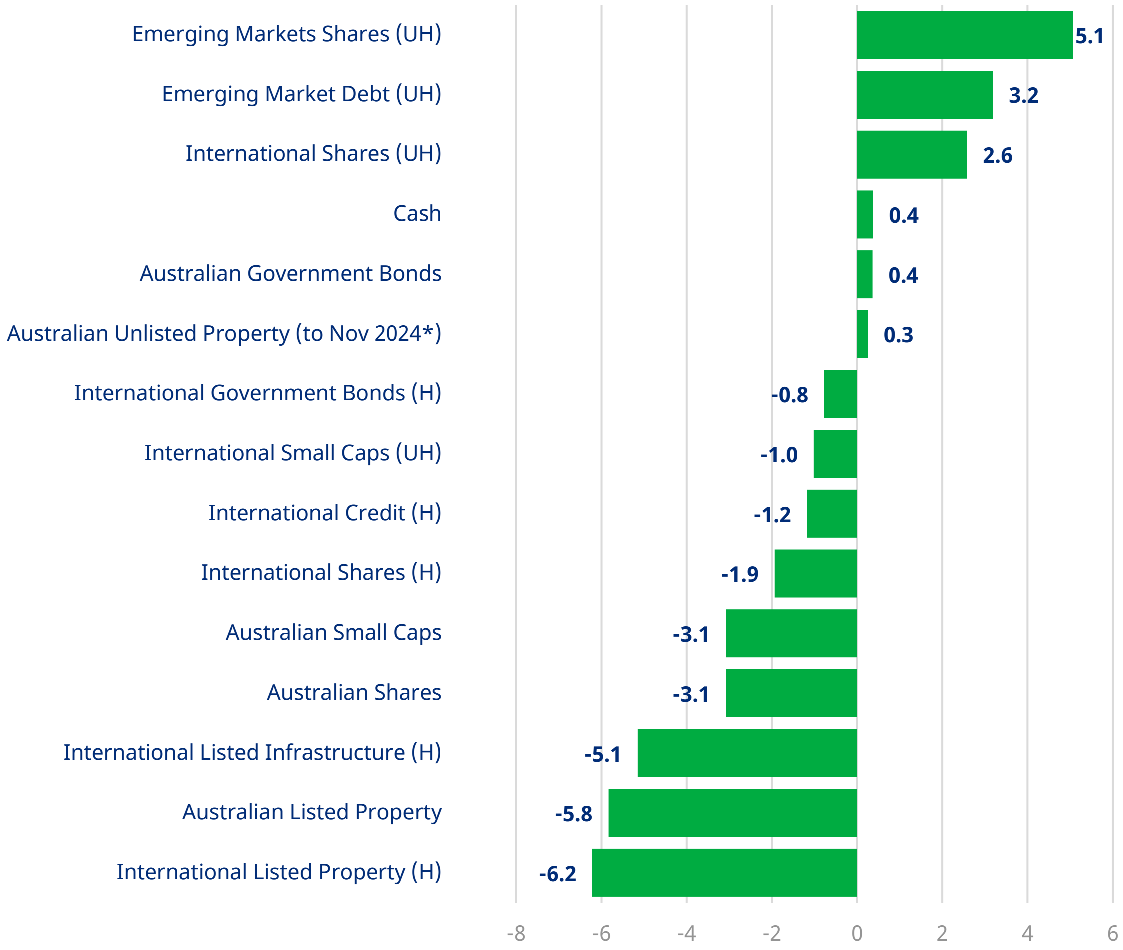
- The RBA decided to hold rates steady in December even though the case for cutting rates is gaining traction. Weak GDP data and softening house prices has significantly increased the possibility of an interest rate cut in February.
- While unemployment remains low, wage growth and job vacancies have 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 going through 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 Japan shares relative to other developed country equity markets.
- We favour global listed property as fundamentals are broadly healthy, and valuations are attractive. We also favour Japan shares due to the potential growth rebound and solid earnings growth.

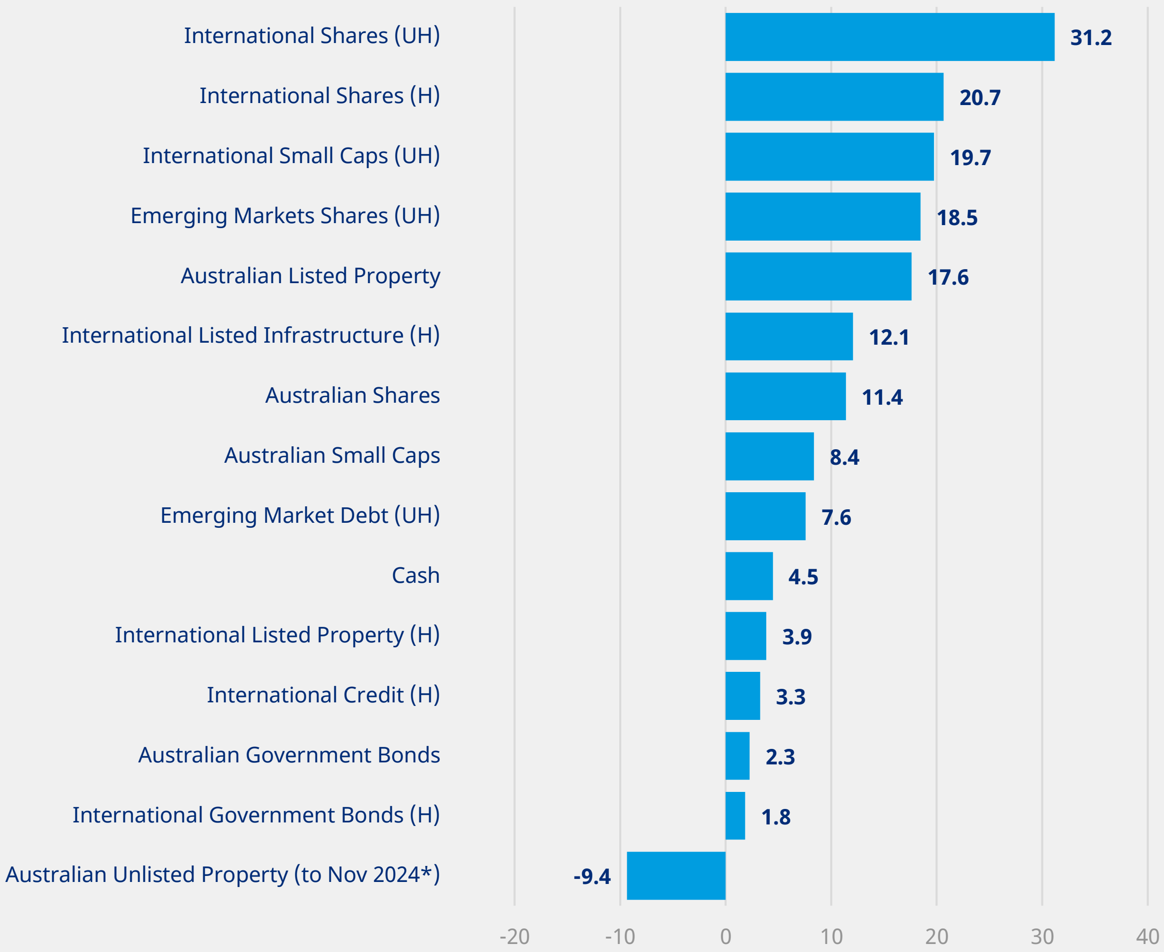
Performance

Market performance December 2024



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

Market performance 12 Months to December 2024



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

Asset class

Australian shares

- Australian Shares ended December lower following the direction of international markets as weaker Australia economic growth data weighed on equity markets.
- The Consumer Staples and Energy sectors were the only sectors ending positive in December with Bega Cheese continuing several months of strong performance, while Beach Energy, performed strongly after analyst upgrades. The property sector was the weakest, as the fall in the property sector reflected the higher bond yields.

International shares

- International Shares (Hedged) ended December lower, following solid gains over the year and were poised for a pause at some point. The optimism that drove markets higher following the US election may have led investors to consider what a 2nd Trump term would entail.
- International Shares (Unhedged) were higher in December assisted by a fall in the AUD.
- Consumer Discretionary was the best performing sector and the Materials sector was the worst performing sector in December.

Fixed interest

- International Government Bonds had a negative return in December 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 were also negative for the month. Australian sovereign bonds yields rose slightly compared to US yields after the FED announcement and weaker economic data in Australia.

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.

Currency

- The AUD depreciated against the USD in December. 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 as it rallied following the FED’s announcement.

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