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Market **Wrap**

April 2023

Economic and market overview

- Investment markets were relatively calm in April, following a period of heightened volatility in March when banking failures in the US and Europe had shaken confidence.
- Most major share markets closed the month around 2% higher, extending gains in the calendar year to date.
- Overall there was increasing optimism that major economies might be able to avoid recessions this year, despite persistently high inflation and rising borrowing costs. This augurs well for company profitability and provided a tailwind for equity markets.
- Bond markets were relatively quiet too, with yields little changed in most regions. Central banks in Australia, the US, Europe and the UK all left official interest rates on hold during the month.

- **US**: Investors increasingly focused on a looming liquidity crisis, following warnings of a potential problem earlier in the year.
- The US currently has a debt limit, or 'ceiling', of around US$31 trillion. This results in a considerable repayment burden, as regular interest payments on this debt need to be made.
- Janet Yellen, Secretary of the Treasury, has warned that the US government could essentially run out of cash in as little as a month if current borrowing limits are not raised. Increasing borrowing limits is a political hot potato, however, and we can probably expect the Republicans and Democrats to clash on the issue in Congress in the weeks ahead.
- That said, the issue is likely to be resolved one way or another, as the consequences of the US defaulting on its debt – i.e. being unable to afford to pay interest that is due, or repay debt on its maturity date – could be catastrophic for the global financial system. The permitted debt ceiling will therefore probably be increased, as it has been several times previously.

- **Australia**: All eyes were on the release of quarterly inflation data for the first three months of 2023. Headline inflation slowed to an annual rate of 7.0% during the period; well below the 7.8% year-on-year rate in the December quarter of last year.
- The 'trimmed mean' – the preferred measure among Reserve Bank of Australia policymakers – moderated too, to an annual pace of 6.6% from 6.9% previously.
- Against this background, most economists expected the Reserve Bank to leave official interest rates unchanged at 3.60% at its scheduled meeting in early May. *In fact, interest rates were raised by a further 0.25% at this time.*
- There is a growing sense that 3.85% might be the peak in official borrowing costs in this cycle. With inflation slowing as anticipated, officials seem unlikely to continue tightening policy settings in case doing so strangles growth and sends the economy into recession.
- In other news, the latest data showed that more than 50,000 jobs were created in March; a stronger result than the +20,000 consensus forecast. For now, Australian firms appear to remain confident enough to keep hiring staff, despite ongoing cost pressures and an uncertain economic outlook.

- **New Zealand**: Inflation moderated more than anticipated in the first quarter of 2023, suggesting CPI might have peaked. The annual rate of inflation slowed to 6.7%; still a high number, but meaningfully lower than the 7.2% year-on-year rate seen in the final quarter of 2022.
- The Reserve Bank of New Zealand raised official interest rates by half a percentage point early in the month, to 5.25%, but the softer-than-expected inflation print prompted suggestions that the interest rate hiking cycle may now be close to ending.
- Consensus forecasts indicate the central bank will raise interest rates one more time – most likely by 0.25% – before pausing to assess the impact of significant policy tightening over the past 18 months or so.

- **Europe**: GDP growth in the Eurozone appears to have stagnated, but at least remains positive. The Euro-bloc economy expanded by just 0.1% in the March quarter; slightly below the +0.2% consensus forecast.
- Activity levels picked up in France and Italy over the quarter, but GDP growth remained subdued in the region as a whole.
- On the inflation front, price rises are still accelerating in some areas – France and Spain, for example – and food price inflation has risen above 20% year-on-year in Germany.
- These releases must be a concern for European Central Bank policymakers, who have already increased official interest rates by 3.5% in the past year to combat escalating pricing pressures.
- There were some more encouraging indicators in the UK, where previously most observers had anticipated a recession in the months ahead. The Institute of Directors' economic confidence index rose for a fifth consecutive month, returning to levels last seen prior to Russia's invasion of Ukraine more than a year ago.
- Households in the UK appear to be feeling more optimistic too; consumer confidence improved for a third consecutive month.
- Encouragingly, unemployment remains extremely low in the UK – at just 3.5% – and industrial action is helping to secure meaningful wage increases for public sector workers.
- The Bank of England now believes the world's sixth largest economy will grow modestly this year, despite ongoing cost pressures and rising borrowing costs.

- **Asia/EM**: The Chinese economy saw the fastest growth in a year in the March quarter, buoyed by resilient consumer spending. The relaxation in Covid-related restrictions early in the new year appears to have benefited the economy, as officials anticipated at the time.
- Industrial output in China appears to be tailing off, however, which could be a concern for other export-oriented economies. Factory activity in China has historically been quite closely correlated with global demand levels.
- The latest data showed that industrial production is weakening in Taiwan too. Industrial output in March was down 14.5% compared to a year ago.
- In other news, India has overtaken China as the world's most populous country; the first time it has topped the list since data started being collected in 1950.

Australian dollar

- The Australian dollar did not move significantly in April, trading in a channel between 66 and 68 US cents throughout the month.
- The currency finished the month down 1.1%, at 66.2 US cents.
- The AUD depreciated by 0.8% against a trade-weighted basket of international currencies, but did gain ground again selected majors. The 'Aussie' appreciated by 1.6% against the Japanese yen, for example.

Australian equities

- Like elsewhere, it was a relatively quiet month for Australian equities. Market movements were dictated by domestic and international company announcements, continuing bouts of mixed economic data, and persisting hopes that the global interest rate tightening cycle might be nearing its end.
- Overall, the S&P ASX 200 Accumulation Index ended the month 1.9% higher, extending gains in the year-to-date to 5.4%.
- Sentiment towards the Information Technology sector (+4.8%) continued to improve. Megaport (+36.7%) was the strongest performer, rallying off the back of a positive trading update. The company materially increased its earnings guidance for FY23 and FY24, suggesting results will exceed consensus forecasts. WiseTech Global (+5.3%) and Xero (+4.4%) also fared well in this part of the market.
- Financials (+3.3%) also performed well, recouping some of their March losses.
- The iron ore price fell by around 16% in April reflecting an uncertain outlook demand from China – the world's largest buyer – and associated concerns about oversupply in the market. This adversely affected Materials stocks including Mineral Resources (-8.6%), Fortescue Metals Group (-6.9%), Rio Tinto (-6.6%) and BHP (-6.0%). Negative contributions from these stocks resulted in the Materials sector moving -2.6% lower; the only sector to produce a negative return.
- Utilities was another relative underperformer, rising 'only' 1.4%. Origin Energy (+0.6%) announced its Final Investment Decision on the construction of a battery at its Eraring Power Station. This announcement was in line with the firm's stated strategy to accelerate the energy transition.
- Small caps outperformed their larger peers, with the S&P/ASX Small Ordinaries returning 2.8%. Like in the S&P/ASX 200, Materials stocks were among the worst performers in the Index.

Global equities

- Listed companies started releasing their earnings for the first quarter of the year. The reports will gather pace in May, but so far there have been few no major trends in the releases.
- In general, resilient earnings and hopes that major economies might avoid recessions this year benefited equities and enabled most major share markets to gain ground. The MSCI World Index added 3.2% in Australian dollar terms.
- The S&P 500 Index in the US added 1.6%, benefiting from broad-based strength. Oil company Exxon released particularly stellar results, announcing its strongest ever start to a year. Net income more than doubled to US11.4 billion in the three-month period, which was the highest first-quarter profit in the firm's 140-year history.
- Technology stocks typically fared less well, which held back the NASDAQ (+0.0%). Among the major tech firms, Amazon spooked investors by suggesting that sales growth in the cloud segment may be slowing. That said, the e-commerce giant had earlier reported stronger-than-expected revenues and profitability.
- Most of the large European markets – including France, Germany and Switzerland – added between 1% and 3%, which supported positive returns from the Euro Stoxx 50 Index. In the UK, the FTSE 100 closed the month 3.1% higher.
- Performance in Asian markets was more mixed. Share markets in Japan and Singapore made solid progress, but we saw negative returns in China and Hong Kong. This appeared to be due to the release of some less encouraging economic data in China. Although overall GDP growth quickened in the March quarter, the latest industrial production data was worse than expected. This clouded the earnings outlook for Chinese firms operating in various industry sectors.
- The downbeat indicators in China hampered shares in other exporting countries in Asia and prevented the MSCI Emerging Markets Index (+0.2% in Australian dollar terms) from making more meaningful progress.

Listed property

- Global property securities fared reasonably well, with the FTSE EPRA/NAREIT Developed Index adding 2.0% in AUD terms.
- The best performing regions in local currency terms included Germany (+11.5%), the UK (+6.4%) and Japan (+5.7%).
- Generally speaking, European property markets recovered some of their losses from recent months. Sentiment improved towards various property sub-sectors that had been hampered by downgrades in the first quarter of the year. The most notable example was the German residential sector, where valuations have begun to appear more attractive.
- Laggards included Canada (-0.7%), Spain (-0.3%) and Hong Kong (-0.1%).
- Asian property markets such as Hong Kong and Singapore underperformed due to weaker than expected data from China's economic recovery, which eroded confidence in the region.
- Locally, the Reserve Bank of Australia left the cash rate unchanged at 3.60% at its meeting in early April. This helped support long duration sectors of the share market, including A-REITs, which returned 5.3%. Mirvac Group was the top performer in the sector, rising 15.9%, despite announcing a downgrade to earnings guidance. Delays in residential projects seem likely to reduce the number of settlements.

Global and Australian Fixed Income

- Bond yields were less volatile than they have been in recent months, as forward-looking interest rate forecasts stabilised in most major regions.
- Most importantly in the US, there were growing suggestions that the Federal Reserve might be preparing to pause its interest rate hiking cycle. Consensus forecasts indicate the Federal Funds rate might be raised one more time – by a quarter of a percentage point at the central bank's meeting in early May – but that borrowing costs will then be unchanged for a period.
- Treasury yields drifted slightly lower against this background, which supported positive returns from global fixed income. The Bloomberg Global Aggregate Index (AUD hedged) added 0.4% over the month.
- Assuming inflation continues to come off the boil as the economy digests higher borrowing costs, there are even suggestions that the Federal Funds rate could be lowered before the end of this year, or in early 2024. Encouragingly, breakeven rates – which reflect the market's expectations for future inflation – moved lower during April.
- Yields were little changed locally too, as forward-looking interest rate projections did not move much during the month. Australian bonds performed slightly less well than comparable securities in the US, but the Bloomberg AusBond Composite 0+ Year Index nonetheless added 0.2%.

Global credit

- The general improvement in risk appetite supported credit markets. Spreads narrowed slightly in both the investment grade and high yield sub-sectors.
- The start of the Q1 corporate earnings announcement season was generally supportive, with few firms disappointing relative to market expectations. With profitability holding up quite well, most companies appear well placed to service their debt repayment obligations and default rates are not expected to increase significantly. The higher prospective yields available from credit relative to comparable government bonds therefore remain appealing for income-oriented investors.

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