Xtra-Ordinary Opportunities

WEEKLY UPDATE

7th NOVEMBER 2022

	Price	5 Day % Change	3 Month % Change	1yr % Change
S&P/ASX300	82,086	1.58%	-0.15%	-4.02%
MSCI World Ex-Aus. (Unhedged)	13,469	-2.59%	-1.74%	-9.43%
MSCI World Ex-Aus. (Hedged)	2,121	-2.02%	-7.79%	-19.06%
Bloomberg AusBond 0+ Composite	9,397	-0.51%	-2.83%	-8.83%
BloombergBarclays Global Agg. (Hedged)	947	-0.75%	-6.36%	-13.99%
S&P/ASX300 Property	54,860	0.05%	-9.11%	-18.33%
FTSE EPRA Nareit Global Real Estate (Hedged)	2,454	-0.97%	-13.39%	-23.46%
S&P Global Infrastructure (Hedged)	5,698	0.94%	-6.06%	-0.16%
Bloomberg All Hedge Fund Index	2,044	N/A	5.79%	2.99%
VIX	24.6	-4.66%	16.08%	48.97%
Bloomberg Commodity Index (USD)	117.49	5.13%	-0.30%	14.37%
Iron Ore Index (62% Fe Aus. Off. China, USD)	85.00	2.41%	-23.77%	-12.82%
LME Copper Spot (USD)	7,905.00	3.15%	3.44%	-19.21%
Coal 1st Future (Newcastle Export, USD)	349.50	-9.39%	-9.22%	126.58%
Brent Crude 1st Future (USD)	98.57	2.92%	4.73%	22.39%
LNG 1st Future (Japan/Korea)	28.93	-4.09%	-35.15%	-9.62%
Gold in AUD	2,599	1.32%	1.16%	7.36%
AUDUSD	0.6470	0.92%	-7.19%	-12.58%
AUDEUR	0.6499	0.98%	-4.66%	1.43%
AUDNZD	1.0908	-1.24%	-1.40%	4.50%
AUDGBP	0.5687	2.96%	-0.79%	3.61%
AUDJPY	94.8670	0.31%	2.35%	11.27%

Source: Bloomberg, S&P Dow Jones, MSCI, FTSE Russell, 6th November 2022

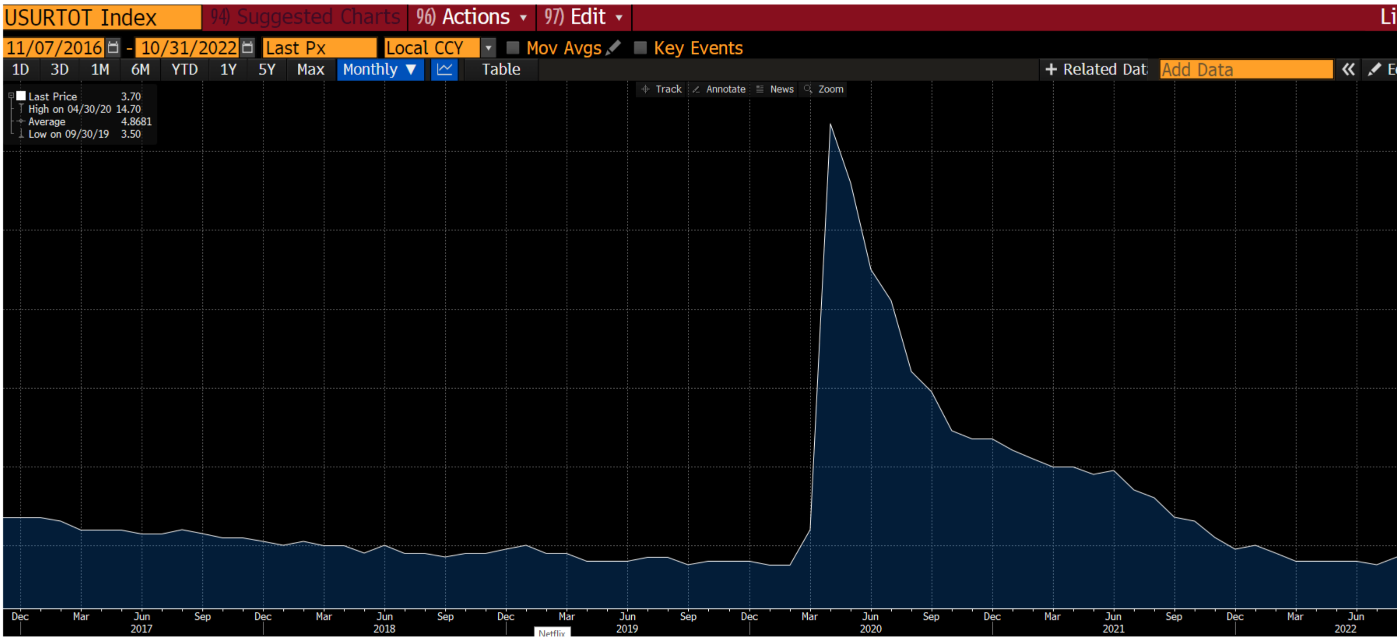
Bond yields continued to rise last week as the RBA, Bank of England and Federal Reserve all raised rates. The Fed's hawkish message prepared investors for interest rates to reach a higher terminal rate and remain higher for longer. Slowing global growth was a significant factor behind lower GDP forecasts in the RBA's Statement on Monetary Policy.

Despite the hawkish tone, equity markets managed to finish the week on a firmer footing as earnings, activity data, and slowing hiring intentions lifted sentiment. Australian equities outperformed international indices, and the Australian dollar strengthened following a higher trade surplus.

Over the weekend, China renewed its commitment to the COVID zero policy. This week will also see Americans vote in the mid-term elections just before US CPI is published, and the Australian banks will publish their business and consumer surveys.

Infrastructure and commodities rebounded last week, while Australian equities and property outpaced the international equivalents. After a buoyant US session on Friday, futures indicate that Australian shares could open higher by as much as +1.3% later today.

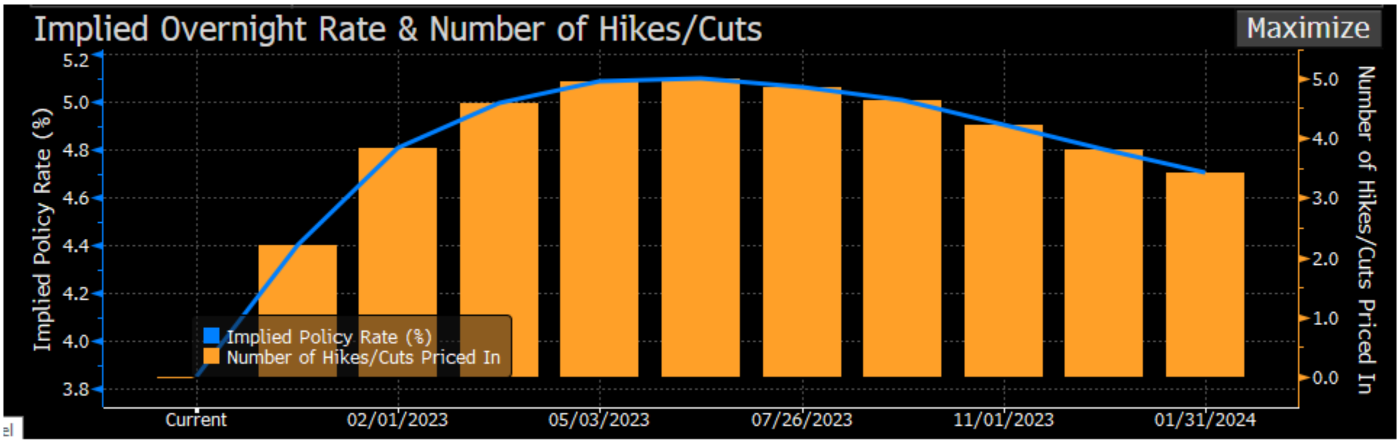
US unemployment rose more than expected, from 3.5% in September to 3.7% in October. (Refer chart below). However, the headline change is difficult to reconcile with data that showed an otherwise tight labour market. The economy added +261k new non-farm payrolls, and September's figure was revised higher from +263k to +315k. Average hourly earnings were slightly stronger in the monthly print but remained up +4.7% over the year. Labour force participation suggested some tightening in labour supply, while job advertisements had unexpectedly risen when released earlier on Tuesday. However, the market took comfort from the fact that the data was still within an overall downward trend, and survey data indicated softer business hiring intentions.



Earnings announcements also supported American stocks. Berkshire Hathaway, the sixth largest stock by market cap in the S&P500, reported a +20% increase in operating earnings compared to last year and has spent more than US$5 bn on stock buybacks in 2022. The US reporting season is seeing profits up approximately +3% against estimates of +0%. This compares favourably to the 775 / 1,073 companies in the S&P Global 1200 index that reported this quarter, where earnings are down by more than -15%. However, profit forecasts are drifting down faster in the US market, and companies are tightening their belts. The most valuable company, Apple, is reported to have paused hiring for all but R&D roles, while Elon Musk's Twitter takeover may lead to as much as half of the 8,000-strong workforce losing their jobs.

A consortium comprised of Australian fund manager Regal Partners and overseas private equity interests launched a surprise bid for trust, wealth, and investment manager Perpetual. The Perpetual share price had fallen as stock markets weakened this year and following the proposed takeover of rival Pendal Group. The Regal bid is reported to be conditional on the Pendal takeover being abandoned and has so far been rejected by the Perpetual board. A higher offer seems likely to be made.

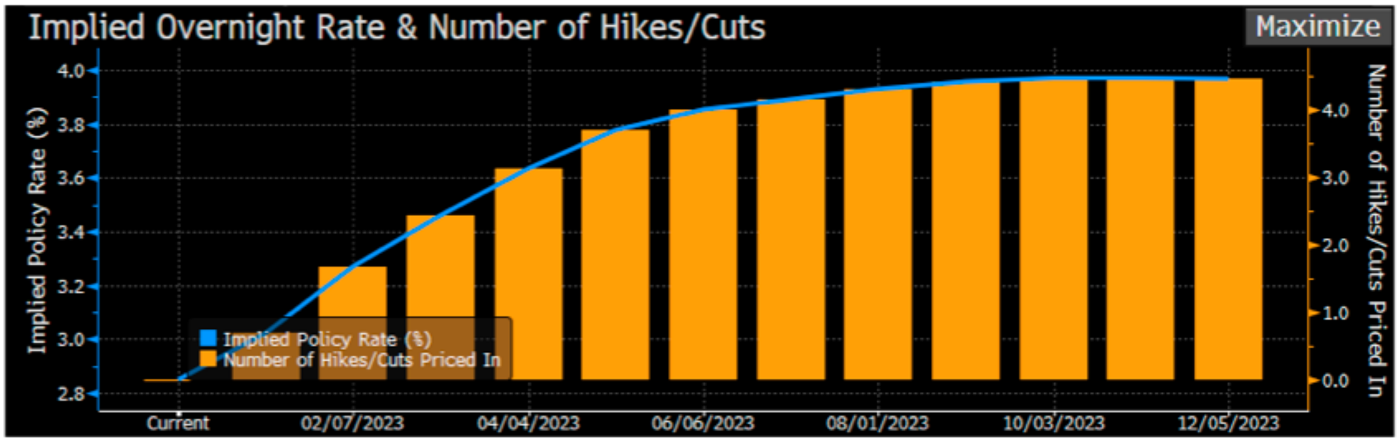
Bond yields continued to rise following the Federal Reserve meeting, where rates were raised as expected by +0.75% to the 3.75% - 4.0% range. The chart below highlights the implied yield curve expectations in the US whereby the market is now pricing in rates to level out at a bit over 5% before beginning to lower towards the end of 2023. This expectation has been pushed out from a mid year 2023 pivot.



The market had hoped that the Fed would follow the RBA and Bank of Canada in preparing to slow the pace of rate rises from December. However, Chair Jerome Powell remained resolutely hawkish as he diverted attention from the pace of rate rises to a higher terminal rate in the cycle than previously anticipated and the likelihood that rates would stay higher for longer than priced into the rates market. As a result, the Federal Funds policy rate is now expected to exceed 5% next year, even as American CPI inflation is expected to show signs of peaking when released this Thursday. Headline CPI is expected to moderate to +7.9% yoy while core inflation is expected to slow only very slightly from +6.6% to +6.5% compared to a year ago. In any event, Jerome Powell's speech undermined the importance of a peak. But a stronger core CPI print would likely push yields higher.

The Bank of England also raised rates by +0.75%. The policy rate of 3% is the highest since 2008, with more raises likely to follow. However, in contrast to the Federal Reserve, the governor of the Bank of England pushed back against the market estimates for future rate rises, stating that they were too high and providing forecasts that suggested market rates would push the economy into a two-year recession. In an alternative scenario where rates remain at 3%, the economy would be expected to contract for five quarters, with the most likely outcome falling somewhere between the two models.

The RBA raised rates for the seventh consecutive meeting on Tuesday to 2.85%, guiding again that further increases would likely be required. The Australian dollar rallied after the rise and after a considerable upside surprise of more than +$4 bn in September's trade surplus of $12.4 bn. Unlike in the US, the interest rate expectation in Australia is for rates to peak close to 4% but remain at this level throughout 2023.



Friday's Statement on Monetary Policy saw GDP growth forecasts revised down, while inflation is expected to be more persistent than shown in the August forecasts (see table below). The Statement cited a more pronounced deterioration in the global outlook as the main reason for the change in estimates:

"*Growth in the global economy is expected to slow significantly in the year ahead, to rates well below those seen prior to the pandemic. The post-pandemic recovery in services consumption has largely run its course in most advanced economies, and central banks are increasing policy interest rates rapidly in order to combat high inflation. High energy prices are also likely to continue to weigh on growth, especially in Europe. Growth in China is expected to remain modest, given a range of significant headwinds including a weak property sector and the authorities' approach to managing COVID-19 outbreaks.*

In Australia, inflation is likewise very high and broadly based, and the labour market is tight. Growth in activity appears to have remained solid in the September quarter. Inflation is expected to peak around the end of the year and then decline over the forecast period towards the 2 to 3 per cent target range as upstream cost pressures ease and higher interest rates slow demand in the economy. Similarly, over the forecast period, GDP growth is expected to slow and the unemployment rate to increase a little."

Speaking after Tuesday's Board meeting, the governor said:

"*A couple of weeks ago, I was in Washington DC with the Australian Treasurer at the G20 and IMF meetings. It was a sobering experience. We heard that: inflation globally is way too high; the rising cost of living is hurting many households; the world is falling behind on the agreed carbon reduction targets; war is once again tragically occurring in Europe; and the global economy is becoming more fragmented. As you can imagine, there was not much cheer around, even for somebody like myself who sees the glass as half full.*"

After recalling that Australia was still relatively well-placed compared to global peers, he continued:

"*I understand that the higher interest rates that are needed to bring inflation under control are unwelcome by many people, especially those who have borrowed large amounts over recent times. At our meeting, we discussed how the higher interest rates are putting pressure on family budgets, just at the time that high petrol prices and grocery bills are also squeezing budgets. We are conscious of this and are certainly taking it into account.*

This morning, we also discussed the consequences of not raising interest rates, and allowing high inflation to persist and become entrenched in expectations. If this were to happen, the evil of inflation would be with us for longer and the eventual increase in interest rates needed to bring it down would be greater. This would increase the risk of a severe recession and a sharp rise in unemployment. It would be much better to avoid such a costly outcome and so we have acted strongly to avoid it.

I want to acknowledge, though, that we are travelling along a narrow path here. The Board is seeking to return inflation to the 2 to 3 per cent range while at the same time keeping the economy on an even keel. It is still possible to do this, but there is a lot of uncertainty and we could be knocked off that narrow path, not least because of developments elsewhere in the world."

Over the weekend, China reiterated its commitment to the zero-COVID policy. Bloomberg reported that China would "*unswervingly*" adhere to its current Covid controls as it faces increasingly serious outbreaks, citing health officials and damping hopes that Beijing will ease its stringent policies. If correct, this would increase the likelihood of more lockdowns over the winter and would be a disappointing development for global supply chains, inflation, and earnings.

This week, Americans will vote in the mid-term elections. Polls suggest that Republican chances have improved in recent weeks and that they may secure a slim majority in both the House and the Senate. Such an outcome would do little to affect the domestic economic agenda since President Biden front-loaded almost all of his legislative agenda. However, Republicans may curtail support for Ukraine and US gas exports, both of which would affect the global economy and be adverse developments for Europe in particular.

The data calendar is a little lighter this week. Besides the US CPI figures, the banks will publish the latest Australian business and consumer survey data tomorrow.

Forecast Table – November 2022[(a)]

Percentage change over year to quarter shown[(b)]

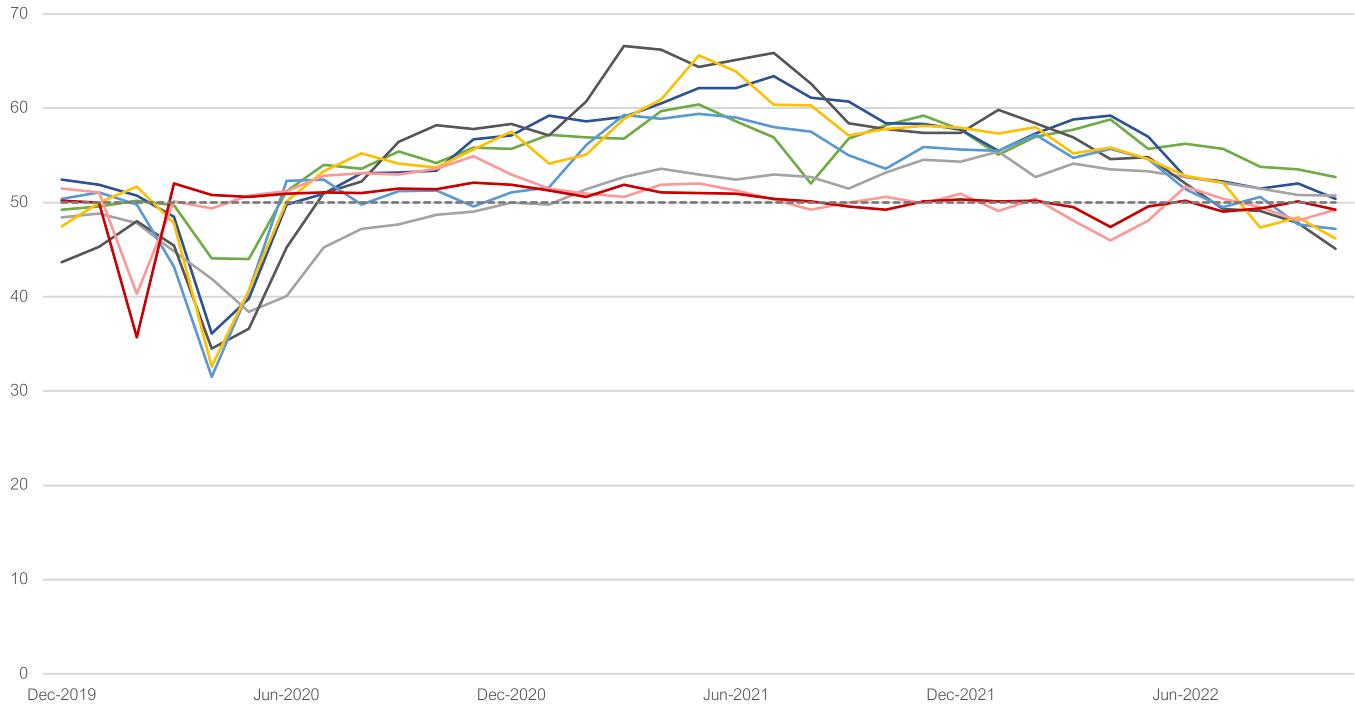
	Jun 2022	Dec 2022	Jun 2023	Dec 2023	Jun 2024	Dec 2024
Gross domestic product	3.6	2.9	2.0	1.4	1.4	1.6
Household consumption	6.0	6.6	2.8	1.3	1.4	1.7
Dwelling investment	−4.6	0.8	3.6	−2.8	−4.7	−5.6
Business investment	1.4	3.4	4.8	6.1	5.0	3.3
Public demand	5.7	3.7	0.2	−0.6	1.0	1.4
Gross national expenditure	4.4	4.3	1.5	0.7	1.4	1.5
Imports	10.0	16.6	6.4	3.9	2.8	2.0
Exports	4.9	7.8	8.4	7.0	2.8	2.6
Real household disposable income	2.1	−2.6	−2.6	−1.2	0.3	2.3
Terms of trade	7.5	1.4	−13.7	−7.4	−6.0	−4.3
Major trading partner (export-weighted) GDP	2.7	3.0	4.3	3.4	3.6	3.5
Unemployment rate (quarterly, %)	3.8	3.4	3.5	3.7	4.0	4.3
Employment	3.3	3.8	1.4	1.2	1.0	0.9
Wage price index	2.6	3.1	3.7	3.9	3.9	3.9
Nominal (non-farm) average earnings per hour	5.0	4.2	4.6	5.3	5.1	4.7
Trimmed mean inflation	4.9	6.5	5.4	3.8	3.4	3.2
Consumer price index	6.1	8.0	6.3	4.7	4.2	3.2

(a) Forecasts finalised on 2 November. The forecasts are conditioned on a path for the cash rate broadly in line with expectations derived from surveys of professional economists and financial market pricing. Other forecast assumptions: TWI at 62; A$ at US$0.64; Brent crude oil price at US$89bbl. The assumed rate of population growth is broadly in line with the profile set out in the Australian Government Budget 2022–23.

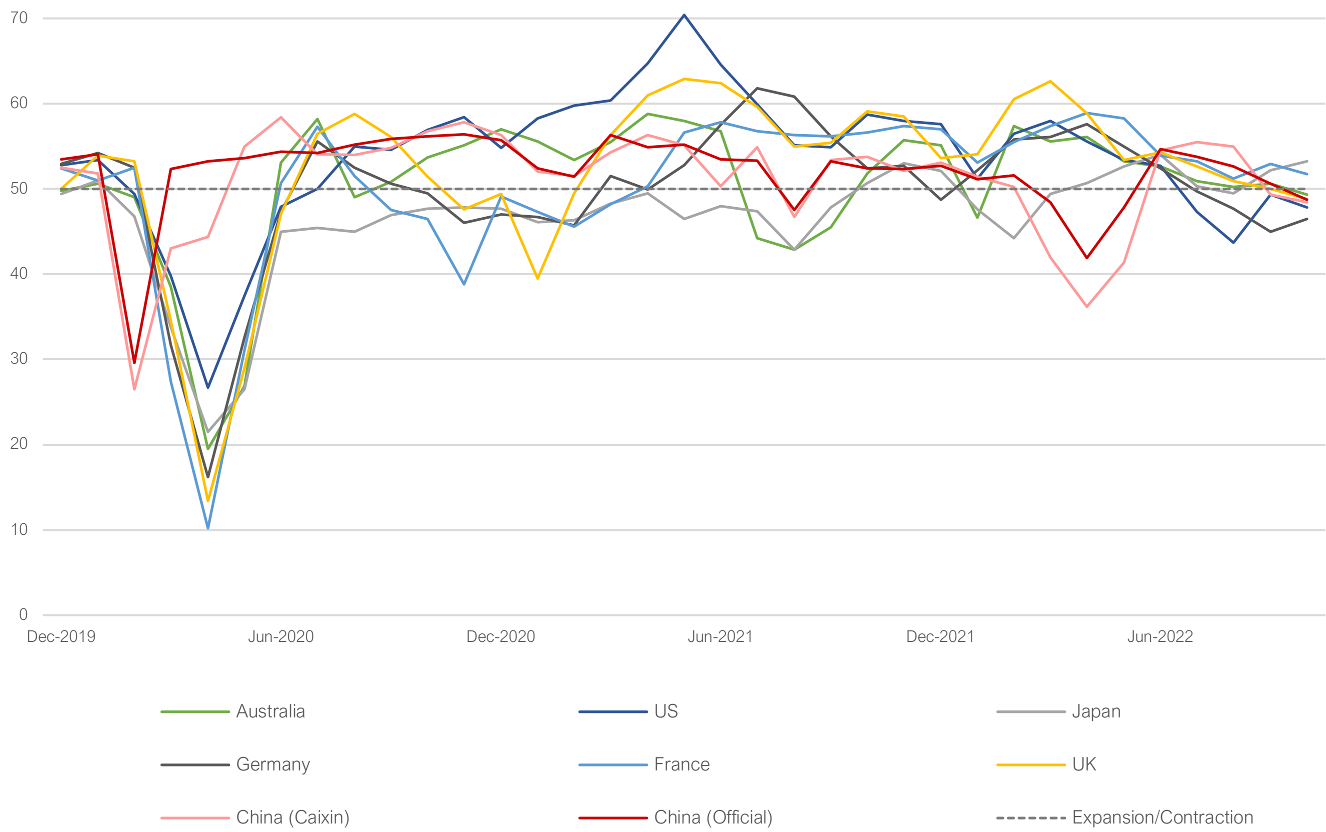
(b) Forecasts are rounded to the first decimal point. Shading indicates historical data.

Sources: ABS; CEIC Data; Consensus Economics; Refinitiv; RBA

Global Manufacturing PMI Surveys



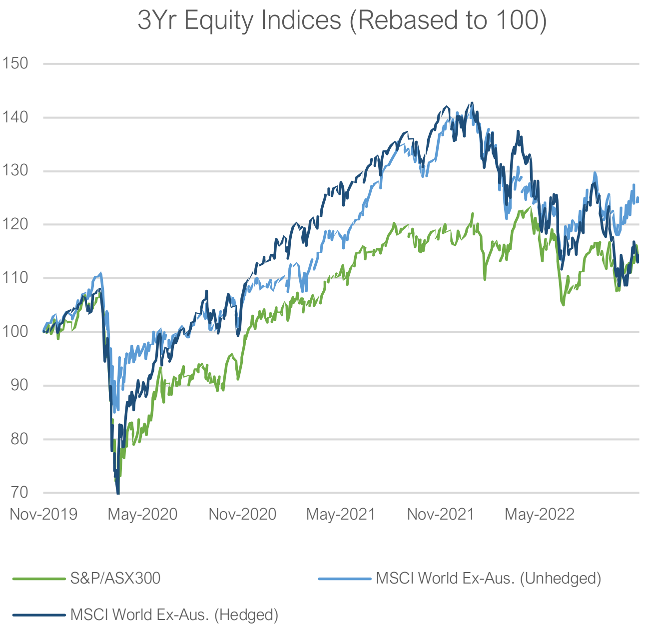
Global Services PMI Surveys

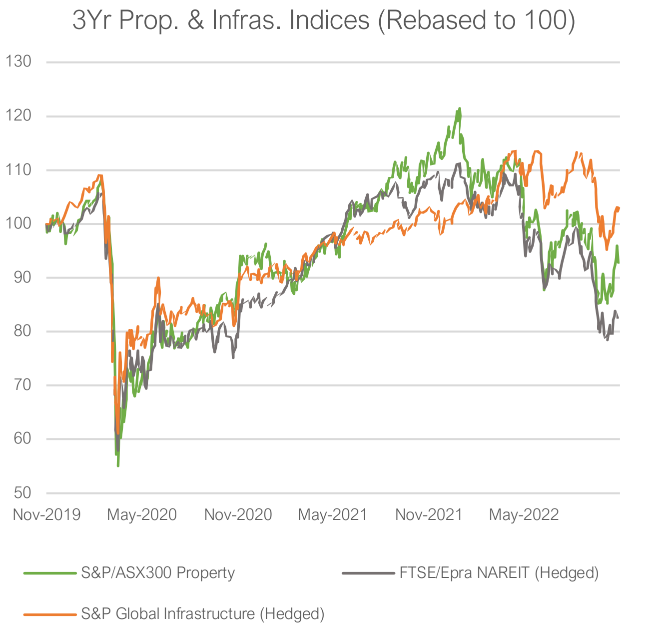


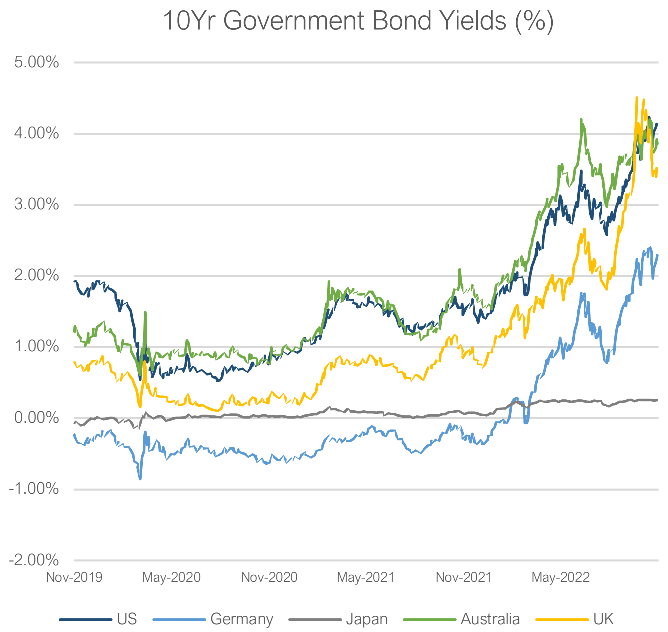
Source: Bloomberg, S&P Global, JPMorgan, Jibun, BME, CIPS, CFLP, 6th November 2022

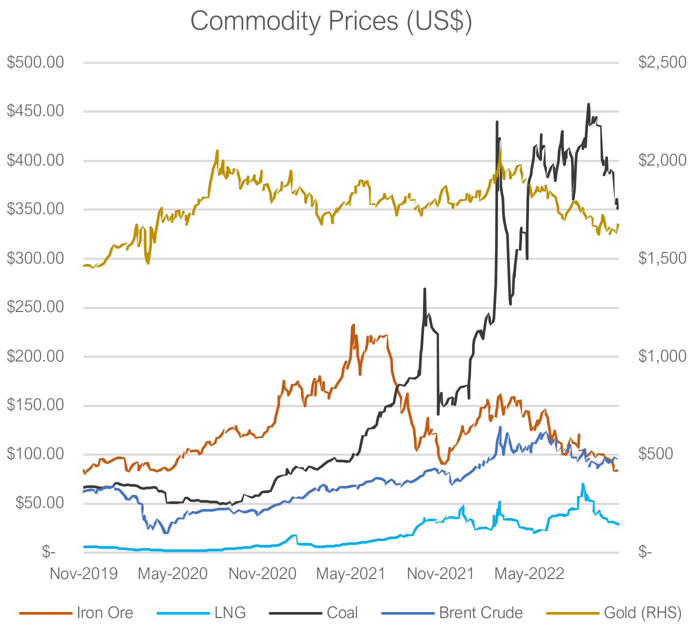
Significant Upcoming Data:

	Monday	Tuesday	Wednesday	Thursday	Friday
Australia		**NAB Business Conditions; CBA Household Spending; Westpac Cons. Conf.;**		**Consumer Inflation Expectations**	
US	**Consumer Credit**	**NFIB Small Business Opt.**	**W.sale Trade & Inventories;** MBA Mortgage Apps	**CPI;** Monthly Budget Statement; Real Ave. Hourly Earnings; Weekly Jobless Claims	**UMich Cons. Sentiment**
Europe	**German, Danish & Norwegian Ind. Prod.; Swiss Unempl.;** S&P German Constr. PMI; Finnish Trade SEB Swedish House Prices Austrian Wholesale Price Index	**EZ & Italian Ret. Sales; French Trade & Curr. Acc.;** Dutch CPI;	**Swedish Ind. Orders & Household Cons.; Danish Curr. Acc.;** Irish Ind. Prod. & New Vehicle Licences; Polish Trade & Unempl.	**Italian, Austrian & Finnish Ind. Prod.; ECB Economic Bulletin; Norwegian PPI;** UK RICS House Prices; Dutch Ind. Sales & Manuf. Prod.; Danish, Norwegian, Irish & Greek CPI; Belgian Budget Balance; UK RICS House Prices;	**UK Q3 GDP, Ind. Prod., Trade & Constr. Output; EU Commission Economic Forecasts; German & Polish CPI; German & Finnish Curr. Acc.;**
Japan		**Leading & Coinc. Index;** Real & Labour Cash Earnings; Household Spending	**BoP Trade & Curr. Acc.;** Bank Lending	**M2 & M3 Money Stock;** Machine Tool Orders; Tokyo Ave. Office Vacancies	**PPI**
China	**Trade**		**CPI & PPI [M0 / M1 /M2 Money Supply]**		**[FDI; 1yr Med. Term Lending Facility]**









Source: Bloomberg, S&P Dow Jones, MSCI, FTSE Russell, 6th November 2022

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