Xtra-Ordinary Opportunities

WEEKLY UPDATE

29th AUGUST 2022

	Price	5 Day % Change	3 Month % Change	1yr % Change
S&P/ASX300	83,552	-0.06%	-0.50%	-1.53%
MSCI World Ex-Aus. (Unhedged)	13,378	-4.40%	-0.58%	-8.39%
MSCI World Ex-Aus. (Hedged)	2,260	-3.41%	-2.41%	-10.56%
Bloomberg AusBond 0+ Composite	9,475	-0.78%	-1.52%	-11.35%
BloombergBarclays Global Agg. (Hedged)	996	-0.59%	-1.80%	-9.94%
S&P/ASX300 Property	59,430	-0.11%	-0.89%	-7.87%
FTSE EPRA Nareit Global Real Estate (Hedged)	2,782	-3.32%	-4.87%	-11.22%
S&P Global Infrastructure (Hedged)	6,187	-0.95%	-1.34%	12.52%
Bloomberg All Hedge Fund Index	1,954	N/A	-0.82%	0.17%
VIX	25.6	24.08%	-0.62%	55.95%
Bloomberg Commodity Index (USD)	124.60	1.86%	-6.93%	29.32%
Iron Ore Index (62% Fe Aus. Off. China, USD)	107.50	4.37%	-17.31%	-29.28%
LME Copper Spot (USD)	8,315.00	3.28%	-11.16%	-10.81%
Coal 1st Future (Newcastle Export, USD)	427.00	2.58%	5.96%	149.71%
Brent Crude 1st Future (USD)	100.99	4.41%	-13.98%	42.10%
LNG 1st Future (Japan/Korea)	68.80	20.66%	205.98%	298.96%
Gold in AUD	2,520	-0.83%	-3.34%	1.75%
AUDUSD	0.6897	0.32%	-2.83%	-4.70%
AUDEUR	0.6916	0.97%	4.34%	10.96%
AUDNZD	1.1229	0.92%	2.44%	7.24%
AUDGBP	0.5872	1.00%	4.10%	10.04%
AUDJPY	94.8850	0.76%	4.92%	16.03%

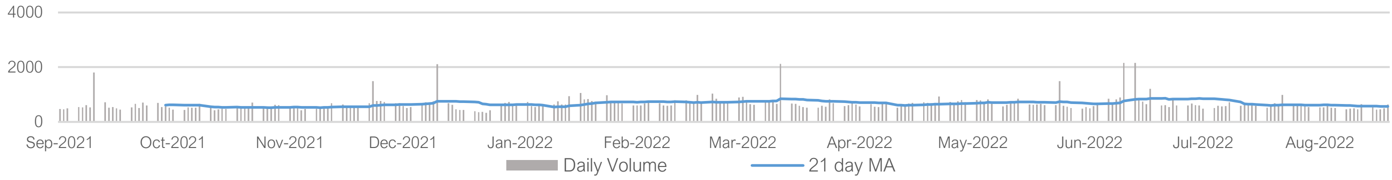
Source: Bloomberg, S&P Dow Jones, MSCI, FTSE Russell, 28th August 2022

A very hawkish speech from the Chairman of the Federal Reserve hit US equities on Friday. He was more explicit that monetary policy would remain restrictive for some time, even at the cost of lower growth and higher unemployment. As a result, the main indices closed down by more than -3% on the day, with Australian shares falling by nearly 2% on the open today. Bonds were relatively little changed, having already adjusted to a higher short-term rate path.

PMI data provided evidence of a broad global slowdown, with Chinese PMIs also expected to weaken later this week. China announced more stimulus but was greeted with scepticism.

Australian earnings are +19% ahead of estimates, with 225 S&P/ASX300 results out so far.

European inflation and US labour market data will be released this week, as well as Australian retail sales and house prices.



Source: Bloomberg, S&P Dow Jones, 28th August 2022

Jerome Powell sent equity markets into a tailspin on Friday, delivering a short and clear speech at the Kansas City Federal Reserve's annual symposium in Jackson Hole, ending any hope of a "Fed pivot" to support growth:

"[Compared to previous speeches] *my remarks will be shorter, my focus narrower, and my message more direct.* […] *The Federal Open Market Committee's (FOMC) overarching focus right now is to bring inflation back down to our 2% goal. Price stability is the responsibility of the Federal Reserve and serves as the bedrock of our economy. Without price stability, the economy does not work for anyone. In particular, without price stability, we will not achieve a sustained period of strong labour market conditions that benefit all. The burdens of high inflation fall heaviest on those who are least able to bear them.*

Restoring price stability will take some time and requires using our tools forcefully to bring demand and supply into better balance. Reducing inflation is likely to require a sustained period of below-trend growth. Moreover, there will very likely be some softening of labour market conditions. While higher interest rates, slower growth, and softer labour market conditions will bring down inflation, they will also bring some pain to households and businesses. These are the unfortunate costs of reducing inflation. But a failure to restore price stability would mean far greater pain. […] *Restoring price stability will likely require maintaining a restrictive policy stance for some time. The historical record cautions strongly against prematurely loosening policy.*" (view the video below using the link)

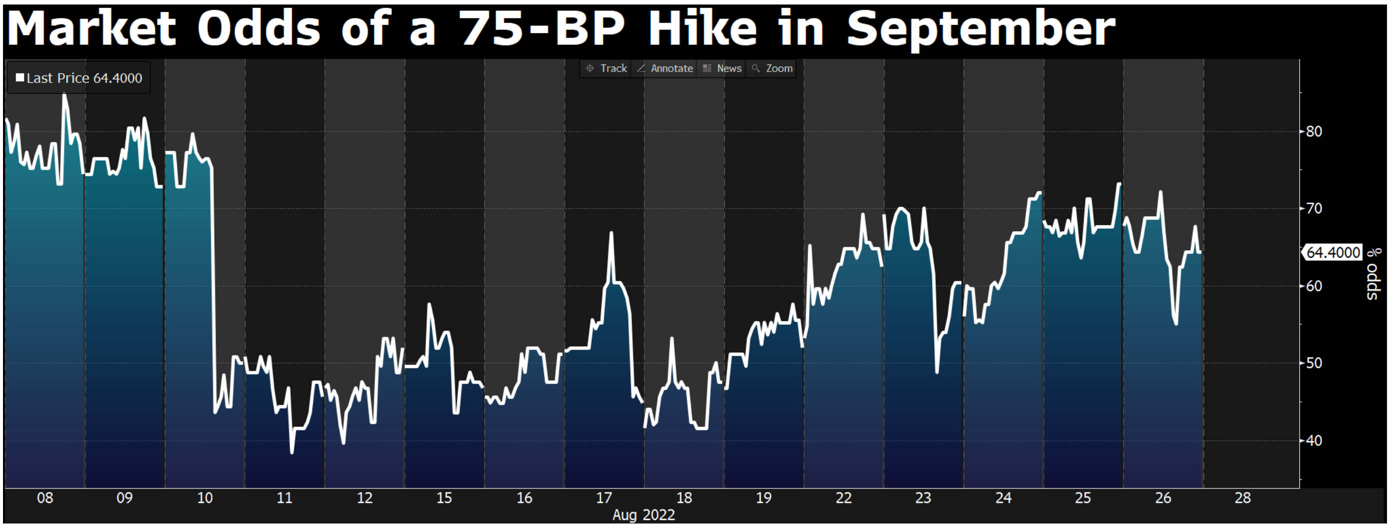
https://www.bloomberg.com/news/videos/2022-08-25/jackson-hole-a-huge-challenge-for-powell-el-erian-video

He gave the most explicit direction so far that the Federal Reserve will push past neutral and hold interest rates in restrictive territory for what appears to be at least several months until they are sure that inflation is returning to target. On Friday night, the Fed's preferred PCE core inflation figure fell by -0.2% but remained well above target at +4.6% over the last year. Economists also expressed concerns last week that President Biden's plans to forgive student debt for about 20 million borrowers could also add to inflationary pressure. The program is estimated to cost between $5 billion and $10 billion per month, favouring borrowers below certain salary thresholds. On Friday this week, the US unemployment rate is expected to remain at 3.5%, with the risks building that the jobless rate will soon rise.

The S&P500 index failed to hold support at the important 4,200 level, which marked both support and resistance over the last several months. Together with the recent failure to rise above the 200-day moving average and the break below the 21-day average, the technical picture now looks very bearish for the US share market. Futures prices indicate that the Australian market will likely open -1.5% lower later today.

Equities and property now reflect an outlook that the bond market had already begun to price. At the beginning of August, futures indicated a March 2023 peak of 3.3% for the Federal Funds rate (equivalent to the overnight cash rate), declining to 2.7% in December 2023. The market now expects the March peak to be as high as 3.8%, with the rate remaining above 3.5% for the rest of the year.

Following Powell's comments, the probability of a 0.75% rate hike for the September meeting increased.



Source: Bloomberg

The ECB July minutes also came out with more hawkish comments last week, lamenting the inflationary effects of a falling Euro. The key policy rate was raised by +0.5% to 0% at the meeting. Eurozone CPI is expected to rise to +9.0% yoy when published on Wednesday, with the core CPI figure expected at +4.1%.

There was little for investors to celebrate on the growth side last week. Flash PMI surveys continued to show a broad decline, as expected. US services are now indicating rapid contraction. Australian, German, and Japanese services also dipped below 50, indicating a reduction in activity, while British manufacturing saw a very sharp fall.

Chinese PMIs are expected to bring more disappointment this week as the recovery continues to falter. The State Council last week announced 19 new measures designed to support economic growth (see table below). The PBOC also cut prime lending rates to 3.65% and 4.30% for 1yr and 5yr terms, respectively. The package comes on top of 33 policies the government introduced just three months ago involving trillions of yuan worth of relief. Bond yields were little changed, and major sell-side firms downplayed the impact of the measures.

A top Russian diplomat dismissed hopes of a negotiated peace in Ukraine. Meanwhile, President Putin ordered an expansion of the army to support the war effort.

Despite the international gloom, Australian market news remains relatively upbeat. In data compiled by Bloomberg, the 225 S&P/ASX300 companies that have published half-year results have produced earnings that are +19% ahead of analyst forecasts.

Australian fund manager Perpetual announced that it would acquire competitor Pendal Group at the second attempt this year. Each firm operates as a collection of boutiques, which is expected to continue under one umbrella holding company. As of the end of June, the two groups combined managed over A$ 200 billion. Changes to the organisation are unlikely to occur before the proposal is accepted by the courts, regulators and Pendal shareholders later this year. If the deal is approved, Pendal shareholders will receive A$1.976 in cash for every share and one Perpetual share for every 7.5 Pendal shares held.

Besides the US labour report and European CPI data, Australia will also see updated retail sales figures and house prices this week. Ahead of the unemployment and wage data, American job openings are expected to fall, and the ISM manufacturing survey is likely to echo the deterioration in the S&P Global PMI surveys.

Additional Chinese Stimulus Measures

Fiscal Stimulus

The government will provide more than 300 billion yuan in additional funding for a program that gave state policy banks the tools to finance infrastructure projects, doubling the scale of a plan announced at the end of June.

Local governments are urged to use up more than 500 billion yuan in existing special bond ceiling limits by the end of October.

A batch of infrastructure projects will be approved to start construction. The projects must make a profit, their quality must be ensured, and the funds should be prevented from being used for other purposes.

Energy Supply

Central government-run power generation companies will be supported to sell 200 billion yuan in special debt to ensure energy supply.

Property Support

Local governments will be permitted to use city-specific credit policies in a flexible way and reasonably support the demand for first homes and better housing.

Business Aid

Measures to help private company development and investment will be introduced, and the healthy and sustainable growth of the platform economy will be promoted.

The government will make it more convenient for businesspeople to travel in and out of the country.

Companies will be allowed to delay the payment of their administrative fees by one quarter.

Local governments will be encouraged to set up risk compensation funds for loans to micro, small and medium-sized companies, and individual business owners.

Officials will continue to take measures to ensure smooth logistics.

Agricultural Funding

Some 10 billion yuan in agricultural material subsidies will be granted in addition to the 30 billion yuan already given this year.

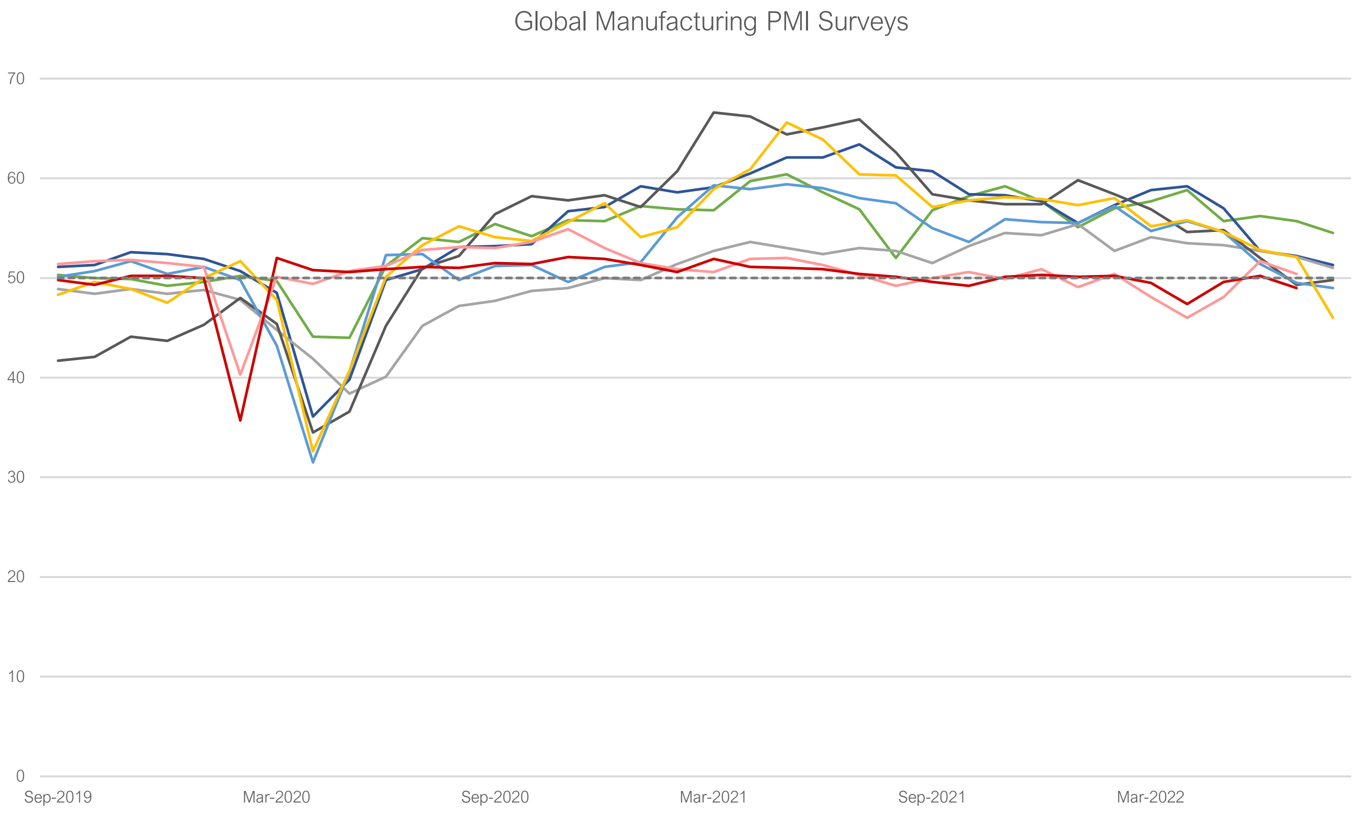
Supervision of Implementation

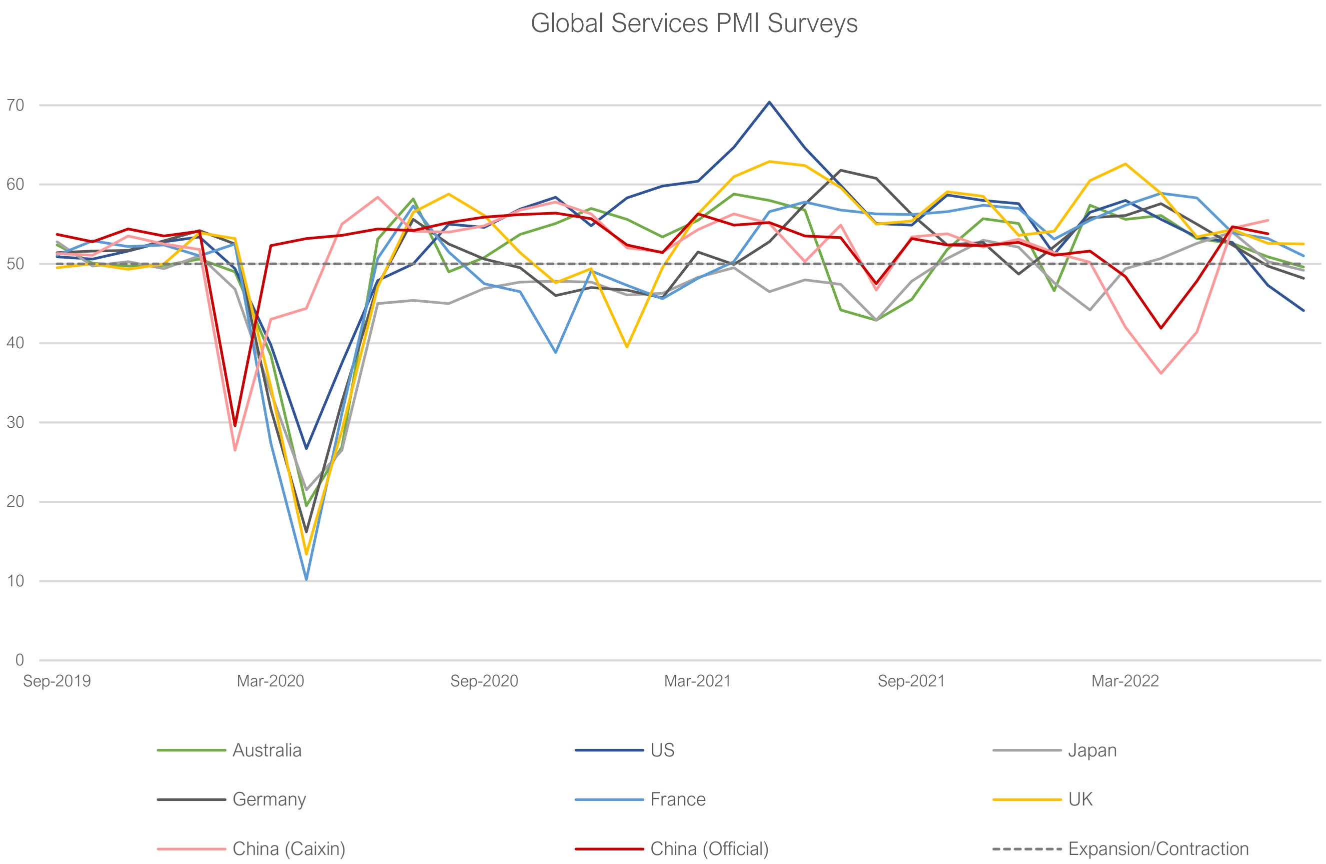
Government agencies are urged to “quickly” release specific details for the implementation of the policies, and local authorities should introduce supporting measures.

The State Council will send supervision and working groups to regions; teams led by heads of central government agencies will be dispatched to economically strong provinces to improve the efficiency of project approvals and accelerate the implementation of the measures.

The work of local officials to stabilize the economy will be supervised by the State Council inspectors, who will also provide necessary aid for the execution of the task.

Source: Bloomberg reporting on announcements by the Chinese State Council, 24th August 2022

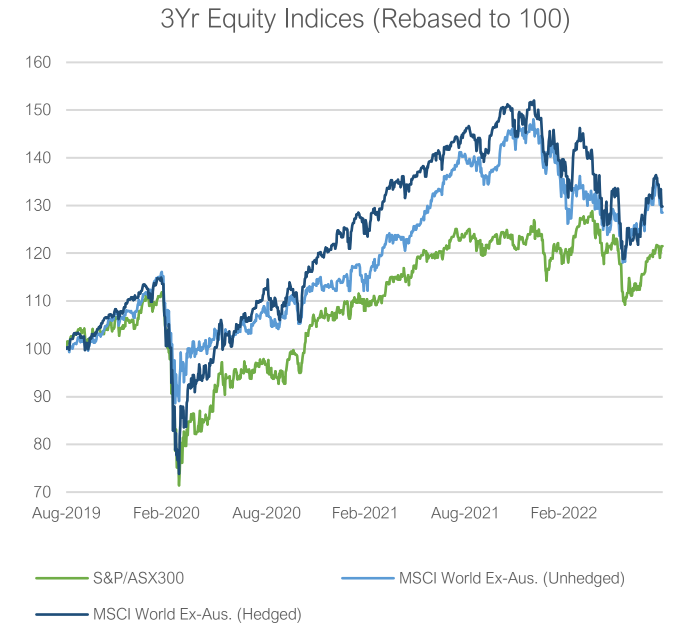


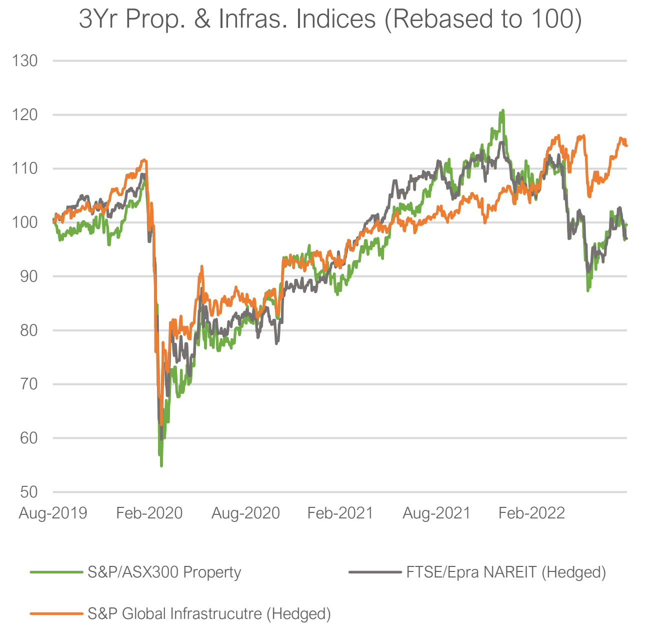


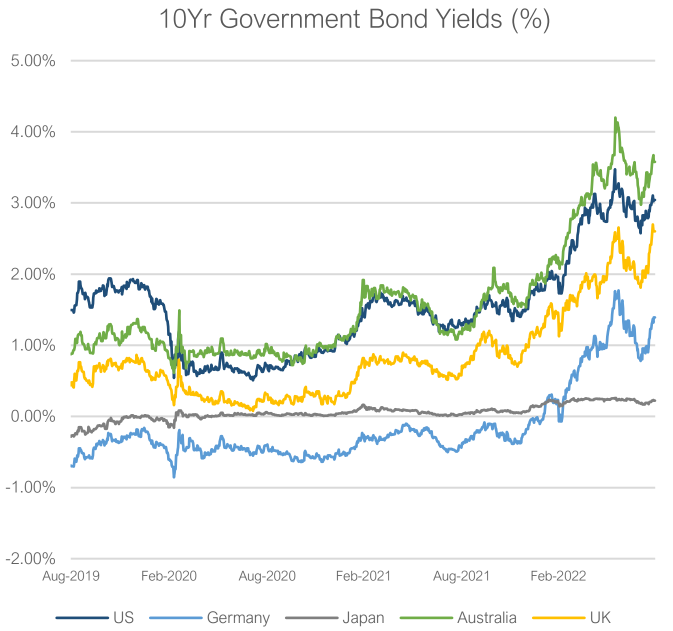
Source: Bloomberg, S&P Global, JPMorgan, Jibun, BME, CIPS, CFLP, 28th August 2022

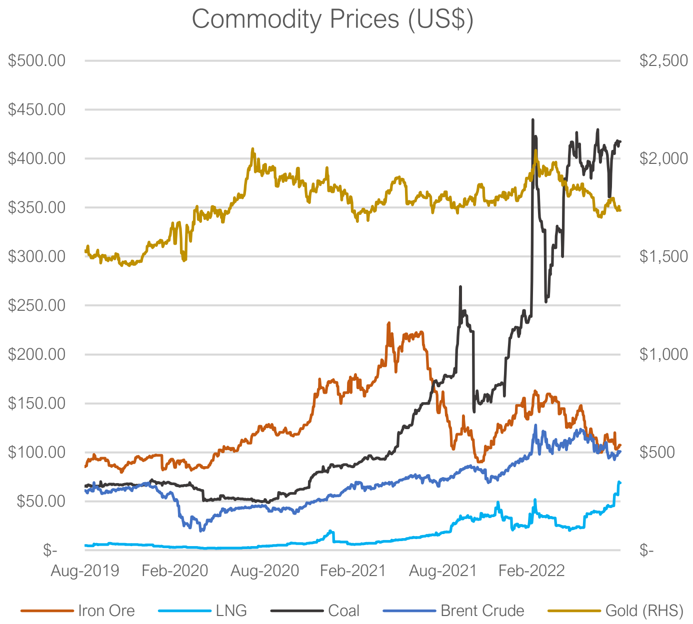
Significant Upcoming Data:

	Monday	Tuesday	Wednesday	Thursday	Friday
Australia	**Retail Sales**	**Building Apps;** Private Sector Houses	**Private Sector Credit;** Construction Work Done	**RBA Commodity Index;** **CoreLogic House Prices;** **Private Capex;** Home Loans; S&P Global Manuf. PMI (F)	
US	**Dallas Fed Manuf. Activity**	**JOLTS Job Openings;** **Conf. Board Cons. Conf.;** S&P CoreLogic House Prices; FHFA House Price Index	**ADP Employment;** **MNI Chicago PMI;** MBA Mortgage Apps.	**ISM Manuf. Survey;** **Unit Labour Costs;** **Challenger Job Cuts;** Construction Spending; S&P Global Manuf. PMI (F); Weekly Jobless Claims [Wards Total Vehicle Sales]	**Labour Report;** **Durable Goods;** **Factory Orders**
Europe	**Swedish Q2 GDP, Trade & Ret. Sales;** Irish Ret. Sales; Unicredit Bank Austria Manuf. PMI	**EZ Ind., Serv. & Econ. Conf.;** **German, Spanish & Belgian CPI;** **UK Money Supply;** **Swiss KOF leading Indicator;** **Swedish Wages & Econ. Tendency Survey;** Italian Ind. Sales Spanish & Finnish Ret. Sales; Austrian PPI; Dutch Prod. Conf.;	**EZ & Irish CPI;** **Italian CPI & PPI;** **German Unemp.;** **Danish Unempl. & Q2 GDP;** **French Cons. Spending CPI & PPI;** Finnish House Prices, Trade & Q2 GDP; Dutch Ret. Sales; Austrian CPI	**EZ, Italian & Belgian Unemp.;** **Swiss CPI;** **German Ret. Sales;** **2nd Tier S&P Global Manuf. PMIs;** UK Nationwide House Prices; Swedish Curr. Acc.; Italian Budget Balance	**EZ PPI;** **German Trade;** **Norwegian & Spanish Unemp.;** **Irish Q2 GDP & Curr. Acc.**
Japan	**Leading/Coinc. Indices**	**Jobless Rate;** **Job-to-Applicant Ratio**	**Industrial Prod.;** **Retail Sales;** **Cons. Conf.;** **Housing Starts**	**Capital Spending;** **Company Profits;** Vehicle Sales	**Monetary Base**
China			**Official PMIs**	**Caixin China Manuf. PMI**	









Source: Bloomberg, S&P Dow Jones, MSCI, FTSE Russell, 28th August 2022

Further commentary from Jackson Hole

We found Mohamed El-Erian's (Univ. of Cambridge Queens' College President) very interesting and closely sums up our own views with many of the points he raises.

El-Erian notes the following:

- Current policy framework is not fit for purpose
- The current policy framework is aimed at a world of deficient aggregate demand and the world we live in today is a world of deficient aggregate supply
- Stickiness of inflation is dynamic – core inflation will prove to be more resistant in coming down – headline inflation may go down, but core inflation will be sticky
- Wages will be a driver of costs, which will eventually lead to higher prices
- Macro stability isn't everything, but without it you have nothing
- The Fed has little choice but to put the inflation genie back in the bottle, but this is at the cost of economic growth
- It will take some time to tame inflation as the Fed has been asleep at the wheel
- The reason the market hasn't heard the Fed is:
  - Because they have been asleep at the wheel
  - Powell not long ago hinted we were at a neutral rate and the market move in a significant fashion. All the talk about pivot became amplified
  - Communication hasn't been consistent
- Previously, like in 2018 when push came to shove the Fed blinked – they have been flipping and flopping. The question is will they do it again?
- What is the neutral rate? - this is hard to say and no one knows