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Monthly View as at 30 June 2023

Overview

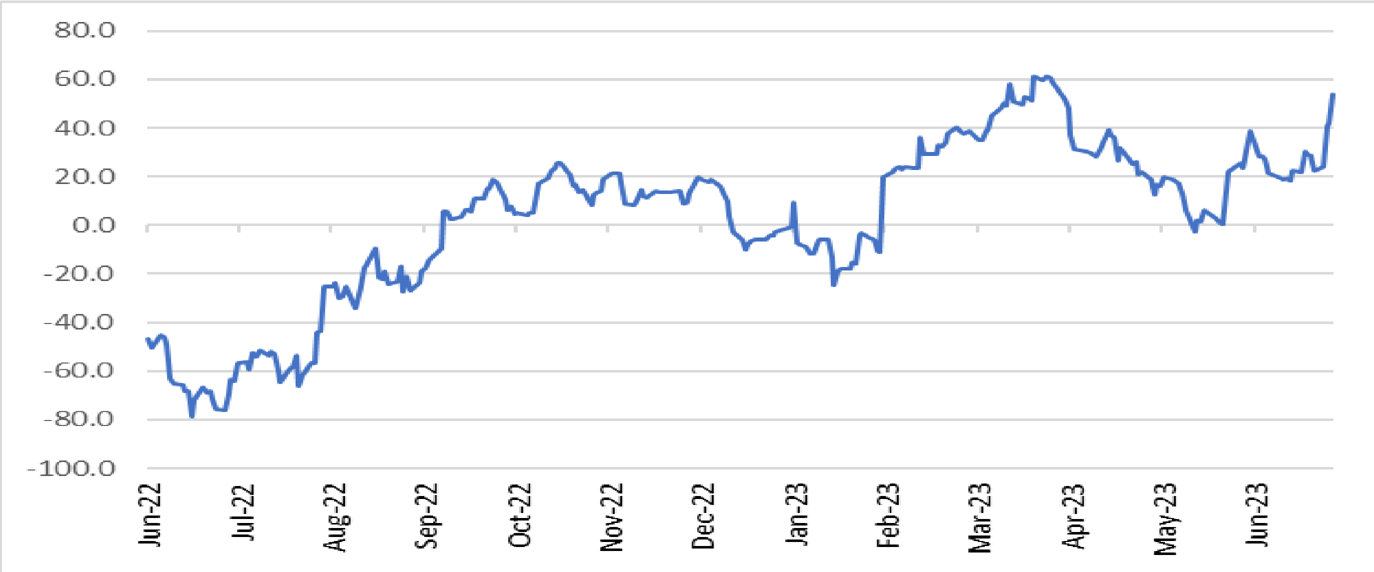
Global equities performed strongly in June, supported by better-than-expected US economic data, further easing of US inflation pressures, and the US Federal Reserve (Fed) pausing interest rate increase.

Although the Fed held rates steady, it surprised investors by forecasting further increases in interest rates by the end of this year. This announcement supports the view that US interest rates will remain higher for longer. Any reduction is unlikely until inflation has come down significantly or the US economy slows.

Encouragingly, measures of US inflation are falling. Annual inflation rose 4.0% for the twelve months ending May, down from the peak of 9.1% last June, and down from April's 4.9% annual increase. May's result was the smallest annual increase in over two years. However, US Core inflation, which excludes the more volatile food and fuel price impacts, remains sticky. Higher housing-rent prices continue to show up in the core inflation figures. Measures of these price pressures are forecast to moderate in the months ahead.

The global inflation backdrop is mixed. European and UK core inflation rose in May, while inflation surprised to the downside in Australia and Canada.

The key reason global equities moved higher in June was better than expected US economic data. This is highlighted by the Citi US Surprise Index in the graph below. A reading of above zero indicates economic data is generally beating expectations. As can be seen, US economic data surprised strongly to the upside in June.



By way of example, US economic activity over the first quarter of 2023 was revised up to 2.0%, much higher than the initial estimate of 1.3% which was good news for share markets. US retail sales rose 0.3% in May, this came after a stronger than forecast increase in April and relative to forecasts of a decline. US consumer confidence also rose more than anticipated in June.

The US consumer has been buoyant despite higher interest rates because of elevated levels of employment, the spending of accumulated savings, and long-term mortgages (30-years) that were financed at lower rates.

Conversely, European economic data has been softer than forecast. This includes a recent survey of the European manufacturing sector (see graph below), which points to a contraction in manufacturing activity across Europe. The latest measures of activity within the European services sector have also disappointed.

Despite the weaker than expected economic data, the European Central Bank (ECB) continues to raise interest rates. It has signalled further rate increases are likely. The Bank of England also surprised with a larger than expected interest rate hike, reflecting much stronger than anticipated inflation and labour market data.

New Zealand Share Market

New Zealand's economy has contracted for two consecutive quarters. Activity declined -0.1% over the first quarter of this year after falling a revised -0.7% over the final three months of 2022. Annual growth fell to 2.2%, 0.4% below market expectations. Measures of New Zealand consumer and business confidence remain depressed.

Reflecting the challenging economic backdrop, the New Zealand share market continued to underperform global peers, rising +0.9% in June, and returning +4.3% since the beginning of the year.

There was a very wide range of company performance over the month. Better performers included Fletcher Building (+8.0%), after it provided earnings guidance in line with market expectations, and Fisher & Paykel Healthcare (+6.8%), reflecting it had been given the go ahead to purchase land in Karaka, south of Auckland, on which to develop research and development and manufacturing facilities over the next 30 to 40 years. EBOS Group fell -12.7% after losing a major contract worth around $1.9 billion and Pacific Edge fell -79.5% following the announcement that its cx-bladder tests will not be covered by US national health insurance provider Medicare.

Australian Share Market

The Australian share market rose 1.8% in June and has returned 14.8% over the twelve months. Although the Australian market benefited from the positive global investment sentiment, it underperformed relative to peers due to rising recession risks.

The resumption of interest rate increases by the Reserve Bank of Australia has raised recession concerns. Further interest rate increases would place additional pressure on already stretched household budgets. It is also occurring at a time when the economy appears to be softening in terms of falling retail sales, declining building approvals, slowing plans for growth in business investment, and early indications of a slowing jobs market. Against this backdrop, resource companies outperformed (e.g., RIO and BHP) given a rise in commodity prices over the month. In June the Iron Ore price rose +12.5%, oil +3.7%, and copper +2.9%.

Global Share Markets

Global share markets performed strongly in June (+5.4%) primarily on better-than-expected US economic data and the continued strong performance of large US technology companies.

The US markets outperformed in June. The S&P500 Index and the technology orientated Nasdaq Index returned 6.6% and 6.5% over the month respectively. By contrast, the European markets returned 4.3% as measured Euro Stoxx 50 Index.

The continued strength in US large technology companies was highlighted by Apple becoming the world's first corporate to finish at the end of a day's trading with a market value of more than US$3 trillion. It took 42 years for Apple to become a US$1 trillion company and another two years to reach $2 trillion. Getting to $3 trillion took nearly three more years.

Despite the continued dominance of the large US technology companies, the performance of the US market did broaden in June. The Russell 2000 Index, an index measuring the performance of smaller US companies, was up 8.0% in June.

Summary

Positive sentiment driven by better-than-expected economic data, most recently in the US, has driven global share markets higher so far this year after poor performance in 2022.

The outlook for inflation remains the key for the direction of both fixed income and share markets over the second half of this year. Although inflation remains elevated, and sticky in places, it is expected to moderate in the months ahead. This will provide central banks the opportunity to either pause, or in the case of the Fed cease raising interest rates further. Such an outcome would be positive for global bond markets and provide support for share markets in an environment of likely softer economic activity.

Indices for Key Markets

As at 30 June 2023	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.
S&P/NZX 50 Index	0.9%	0.4%	4.3%	10.6%	2.1%
S&P/ASX 200 Accumulation Index (AUD)	1.8%	1.0%	4.5%	14.8%	11.1%
MSCI ACWI Index (Local Currency)	5.4%	6.6%	14.0%	16.5%	11.8%
MSCI ACWI Index (NZD)	3.3%	8.4%	17.9%	18.7%	12.8%
S&P/NZX 90 Day bank bill Total Return	0.5%	1.3%	2.4%	4.1%	1.7%

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