FINANCIAL MARKET CONDITIONS
June 2023

Local Government Finance Authority

Risk sentiment recovered in June, and equity markets across the globe witnessed a bounce back in developed markets of up to 5% over the course of the month and a 15% increase over the first half of the 2023 calendar year. Despite a similar bounce in June, Asian equity markets did not experience the same increases as developed markets over the first half of 2023 which analysts have attributed to the lack of an economic recovery in China.

Economic data continues to be varied as economies across the globe deal with stubborn inflation, keeping central banks with a tightening bias. Overall, global inflation has continued to trend lower, and increasingly the growth outlook weakens, however data is wide ranging with increasing evidence of weakening manufacturing sectors and a resilience in the service sectors.

In the US, the Federal Reserve (FOMC) held its policy rate unchanged in June, however wording suggests that further tightening across the rest of the year is expected. Inflation in May declined to 4%, the lowest since March 2021. Whilst inflation is slowing, the current rate remains a multiple over the FOMC target and a string of positive economic data illustrated strong consumer spending and well above forecast GDP growth of 2% vindicates the notion that the FOMC still has work to do.

In Europe, the European Central Bank (ECB) raised rates by another 0.25% in June, the highest level since 2008. With wage growth now beginning to impact inflation, and labour markets in the region remaining tight, it is clear that the peak in rates has not yet been reached. ECB's president Christine Lagarde commented that 'Inflation in the Euro area is too high and is set to remain so for too long', and there is an expectation for a further rise in July. Despite high inflation, the Eurozone economy shrank in the first quarter of 2023 -0.1%, and Eurozone manufacturing data continues to slide, illustrating the region is witnessing some weakness as a result of recent rate rises.

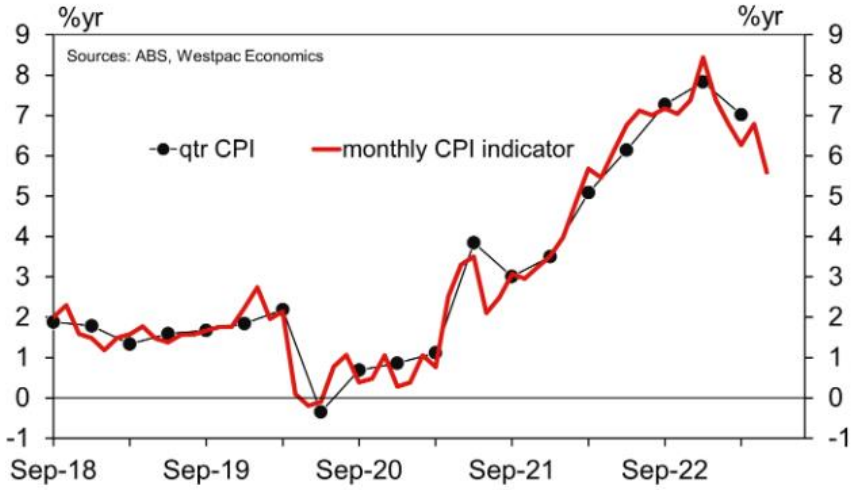
The Bank of England (BOE) similarly raised its policy interest rate in June by 0.50%, marking its 13th consecutive hike. The decision surprised financial markets which had priced in a smaller 0.25% hike, however clear messaging has committed to deliver further rate hikes if ongoing inflationary pressures persist. To support the hike, inflation data unexpectedly held steady at 8.7% in the year to May, remaining significantly above the central bank's target of 2%. However, data continues to be highly varied with manufacturing data witnessing a significant slowdown, with input prices and activity falling by the most since 2009.

Data out of China has not improved over the month, and this has put pressure on Chinese equity markets, the Australian dollar and other industries reliant on Chinese demand. Credit growth continued to slow, and even with cuts to rates, it has not improved demand. Prices fell the most since January 2016, due to lower costs for raw materials in addition to increased market competition and efforts to boost sales. Consumer sentiment also weakened to an 8-month low, amid worries over sluggish market conditions.

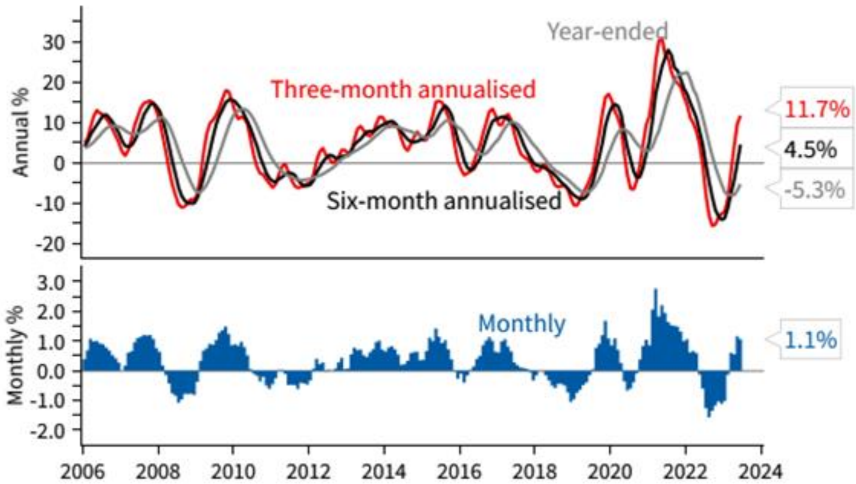
The Reserve Bank of Australia maintained its cash rate at 4.10% during its July meeting after raising it by 0.25% in June, with a total of 4.00% since May 2022. The board said it needed more time to assess the impact of past hikes while leaving the door open to future increases as inflation is still too high and would remain so for some time yet.

Data in Australia was also varied throughout the month. Monthly CPI fell from 6.8% in April to 5.6% in May, the lowest annual pace since April 2022. However, strong retail sales and job vacancies data still illustrate resilience in the Australian economy. The level of vacancies is almost 90% higher than pre-pandemic levels. In addition, strong housing data with home loan commitments rising by 4.8% in May, a 20.6% increase in dwelling approvals and an increase in Australian dwelling prices illustrate that areas of the Australian economy are not yet slowing.

CPI Monthly Indicator vs. qtr CPI



Australian Dwelling Price Growth

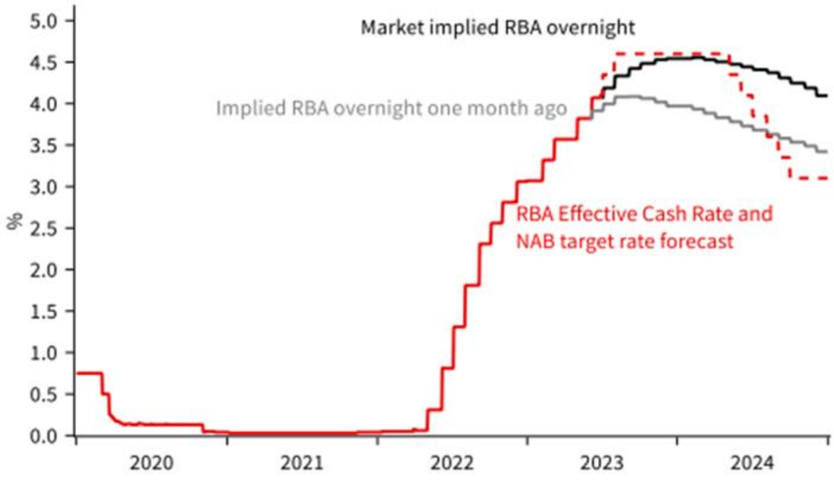


Source: National Australia Bank, CoreLogic

As a result, the RBA continued to reiterate that ‘further tightening may be required’ and major banks still expect the cash rate to rise to 4.60% in coming months.

Chart 1: RBA pricing has increased in the past month

RBA Market Expectations



Source: National Australia Bank, Bloomberg