FINANCIAL MARKET CONDITIONS
October 2023

Local Government Finance Authority

Global equities continued to weaken over October as heightened geopolitical uncertainty related to the Israel-Hamas conflict weighed on market sentiment and investor appetite. Stocks also fell on the prospect that Central Banks will keep rates 'higher for longer' driven by resilient economic data. Equities fell by around 3%, bringing the annual return to 9%, eroding the 15% gains that were witnessed in the first half of the year.

Whilst major data releases in the United States (US) illustrate a resilient economy with consumers still spending, there has been a rebound in immigration which is tempering the pace of hiring, and the unemployment rate increased to 3.9%, signalling a potential softening of the labour market. Inflation data was higher than expected in September, and the annual rate is unchanged at 3.7%, with services inflation remaining uncomfortably high. Consumers are still spending with retail sales strong across the board, increasing by 0.7% vs 0.3% expected for the month. Home sales also surprised with a 12% jump in September, the biggest monthly gain in over a year. US gross domestic product (GDP) for the 4th quarter supported market sentiment on rates remaining 'higher for longer' beating expectations at 4.9% annualised from 2.1% previously. Markets are now expecting that US rates will be on hold until June 2024.

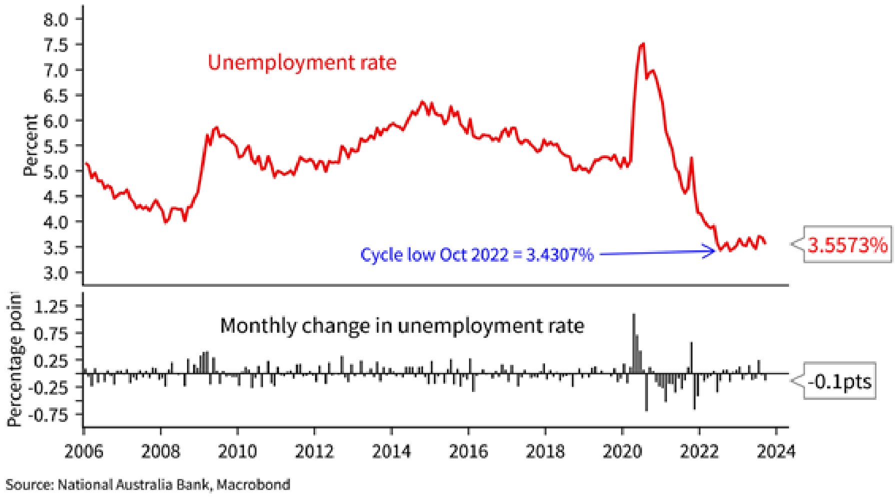
In contrast, data in Europe continues to illustrate challenges in the region. The European Central Bank (ECB) kept rates on hold as widely expected, and the statement reported that interest rates are at levels that, 'if maintained for sufficiently long duration, will bring inflation back to target'. The dampening of demand that the region has witnessed will help to push down on inflation, however the risk of a recession looks likely. European manufacturing remains at very weak levels, reflecting the steepest contraction since November 2020. Europe 3rd quarter GDP weakened by -0.1%, bringing the annual rate to 0.1%, the lowest reading in two years. Eurozone inflation is headed in the right direction, declining to 2.9% annually, below market consensus of 3.1% and reaching its lowest level since July 2021. The aggressive hikes that the ECB has made is impacting the economy rapidly and both the services sector and the broader economy remains weak, however the ECB appear committed to their 2% inflation target rate and maintaining rates at current levels. However, markets are anticipating that there will be a need to cut Eurozone rates by the 2nd quarter of 2024.

In the United Kingdom (UK), inflation remains high at 6.7% despite weaker retail sales, and other economic data illustrating a sluggish economy. Manufacturing data remains weak, and the labour market remains tight with unemployment falling to 4.2%. The Bank of England (BOE) left rates unchanged at 5.25% for a second meeting, as the BoE evaluate recent signs of an economic slowdown in the UK, while simultaneously grappling with the ongoing challenge of stubbornly high inflation. The BoE emphasised that monetary policy is likely to remain restrictive for an extended period in order to steer inflation back towards the 2% target.

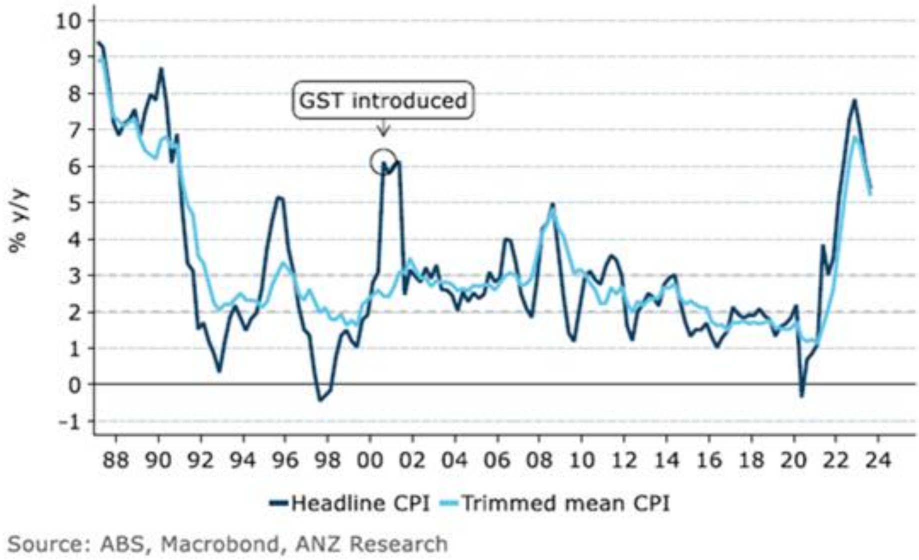
China's economic data has continued to improve over the month, with increasing skepticism on the quality of the data, with GDP for the 3rd quarter growing by 1.3% and the fifth consecutive period of expansion. Growth in the region has been helped by a range of monetary stimulus measures over the past three months, including interest rate cuts and liquidity injections by China's central bank. Retail growth jumped to 5.5%, and imports witnessed its first increase since February. However, the property market remains fragile, and this business confidence fell over the month illustrating that there is still some cautiousness in the region.

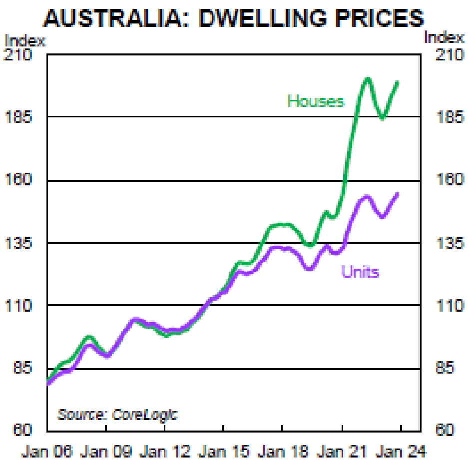
In Australia, despite weak consumer and business sentiment, consumer spending continues to grow. Retail trade rose strongly in September and is up 2% over the year. The September quarter inflation (CPI) surprised to the upside rising by 1.2%, and whilst there was further moderation in the annual pace from 6% to 5.4%, this level of inflation is higher than expected. Whilst the unemployment rate fell from 3.7% to 3.6%, levels are broadly unchanged since mid-2022 and illustrates a tight labour market. This is despite significant population growth in Australia, the strongest in over 50 years, with 2.2% growth over the year. Property prices in Australia rose for a ninth consecutive month by 0.9% and despite borrower capacity reducing by around 30%, property prices are now back to their previous peak reached in April 2022. Population growth and home building not keeping pace has meant that vacancy rates have dropped to record lows in most capital cities, putting upward pressure on home prices and the rental market.

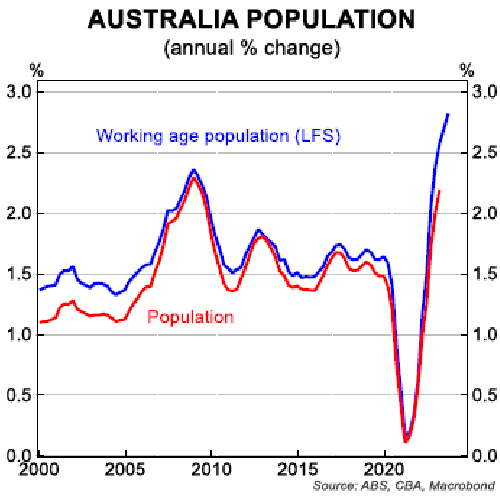
Australian Unemployment Rate



Australian Consumer Price Index







As the data continued to illustrate strength in the local economy, the Reserve Bank of Australia (RBA) increased the cash rate by 0.25% on Melbourne Cup Day to 4.35%. The move was largely anticipated by markets. The RBA signalled that inflation is likely to take longer to return to target than previously expected. Markets anticipate that the RBA are at or near the top of the cycle, with a chance of a further hike in February 2024 depending on 4th quarter CPI, and that the RBA will not start to cut rates until 2025.