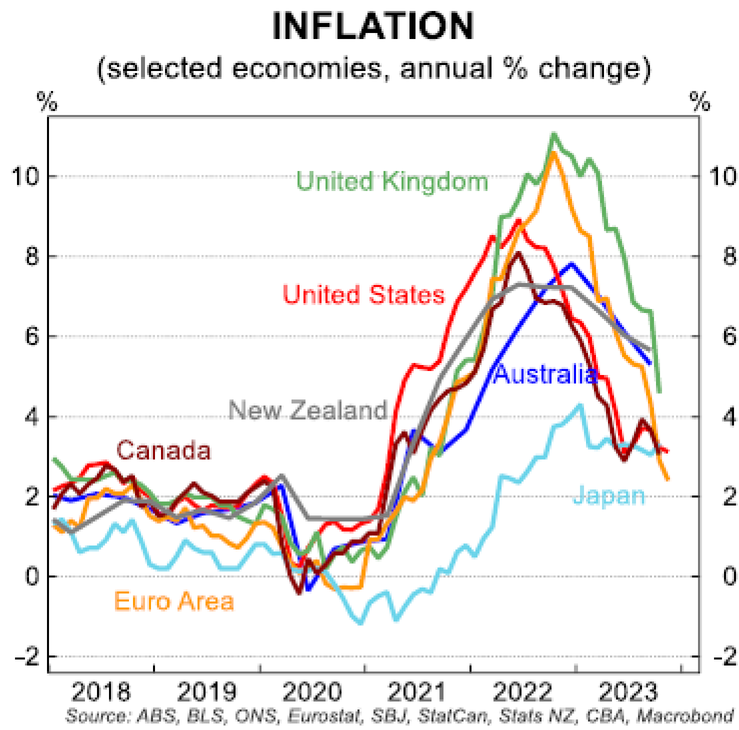
FINANCIAL MARKET CONDITIONS
December 2023

Local Government Finance Authority

Improved risk appetite continued over December and global equities witnessed its longest winning streak since 2017. Equities gained more than 4% over the month, and US equities closed the year 26% higher. Other markets across the globe also witnessed growth of 12-15%, however, China dragged emerging markets growth to be lower at 10%. With the new year in sight, markets are increasingly confident that central banks have done the job of returning inflation to target ranges, with 2024 expected to see major central banks consider easing monetary policy.

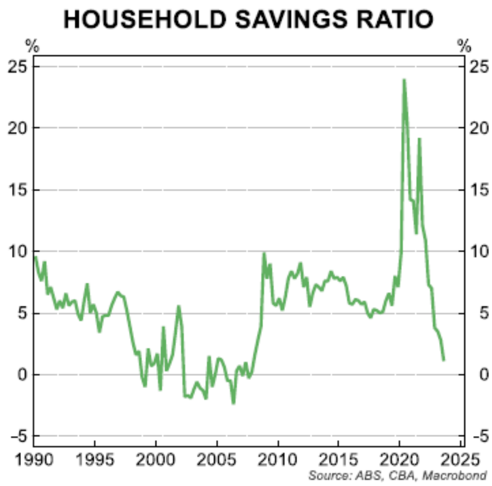
In the United States (US), economic data throughout December broadly witnessed further cooling in economic conditions, with manufacturing data continuing to deteriorate. Output and new orders declined, reflecting weakness in demand conditions, with firms adjusting down their input buying and hiring activity accordingly. However, the services remained resilient, publishing its strongest growth in five months. Retail sales increased modestly, and consumer confidence surged, driven by recovering stock markets and lower gasoline prices. Inflation trends continue to show signs of easing, with the Consumer Price Index (CPI) falling to 3.1%, a significant drop from the 2022 peak of 9.1%, largely aided by falling energy prices for nine consecutive months. While the US Federal Reserve (FOMC) downplayed the idea that a rate cut is imminent, markets are pricing in an 87% chance the FOMC will cut interest rates by 0.25% at its March meeting.

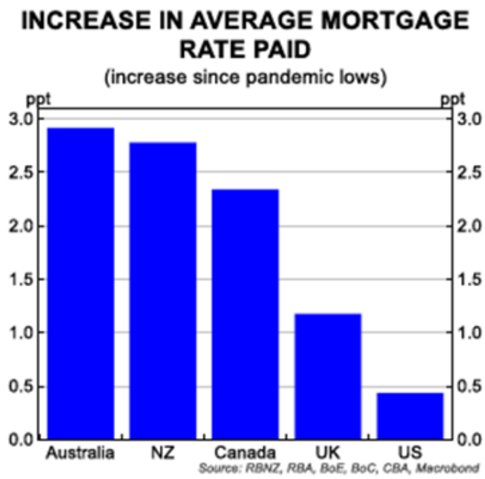
Economic data and conditions, in the United Kingdom (UK) and the Eurozone, were mixed. UK's CPI in November surprised markets printing sharply lower falling to 3.9%, indicating less inflationary pressure than anticipated by the Bank of England. 3rd quarter gross domestic product (GDP) also fell more than expected, suggesting further potential contraction in the 4th quarter. In contrast, manufacturing data rose notably in December showing the fastest growth since June and contrasting with the contraction in manufacturing in the Eurozone. Eurozone manufacturing data remained weak, with output and job losses continuing for the seventh consecutive month. However, consumer confidence improved following the expectation that the European Central Bank (ECB) has reached the peak in interest rates in addition to an expected slowing in inflation. Share markets were also more confident, reaching 22-month highs in December. Despite Eurozone inflation rising slightly from 2.4% to 2.9%, overall, the trend in inflation is downward, and there is the expectation for further weakness in January's inflation data.



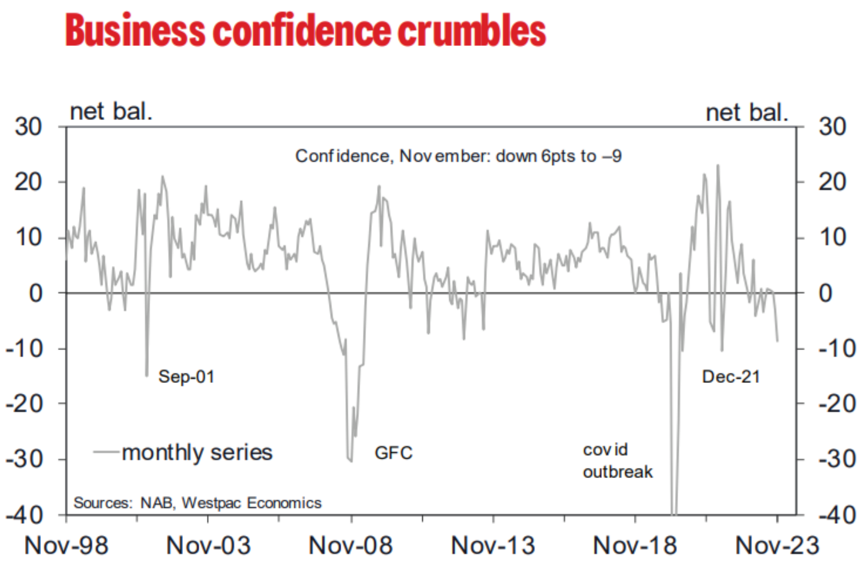
China's economic activity backdrop improved further throughout the month, industrial production rose by 6.6%, and was the fastest pace of growth in industrial production since February 2022. Manufacturing index data also inched up in December, pointing to the highest reading since August. Despite this, business and consumer confidence remained weak due to a faltering recovery in the face of property weakness, deflationary risks, and mounting global headwinds. Deflation persisted in November with the headline rate falling to -0.5%, the fastest decline in the CPI since November 2020. US rating agency downgraded China's A1 rating outlook from stable to negative as China continues to face challenges achieving its target growth rate of 5% in 2024.

Locally, Australia's economic landscape is starting to witness the impact of the Reserve Bank of Australia's (RBA) 13 rate rises over the past 18 months, putting upward pressure on the unemployment rate and downward pressure on inflation and economic growth. With borrowing costs now at their highest level since January 2011, borrowers are starting to feel the pinch. Real household disposable income declined by 1.7% in the September quarter to be 5.6% lower over the year. Interest paid on housing debt is up by 70.6% over the past year and a massive 173.3% from pandemic lows.





Australia saw a weaker than expected 0.2% quarter-on-quarter increase in real GDP for 3rd quarter 2023, a significant slowdown from previous quarters. This deceleration in GDP growth, which stood at 2.1% on a year-on-year basis, reflects the impact of the RBA's aggressive rate hikes intended to curb demand. Concurrently, the business confidence index dropped sharply to -9, among the lowest in its history, reflecting deepening pessimism in the business sector. Consumer sentiment rose slightly in November, however, remains at pessimistic levels and marking its second worst year on record as a surge in the cost of living and sharply higher interest rates weighed heavily. The index has remained in this territory since March 2022, the longest streak since the early 1990s recession.



Inflation is decelerating in Australia, but at a slower pace than some other nations. Inflation is expected to decelerate further to be back at 3% by the end of 2024. Markets continue to anticipate that the RBA are at or near the top of the cycle, with financial markets predicting that the RBA will begin a modest monetary policy easing cycle from late 2024.