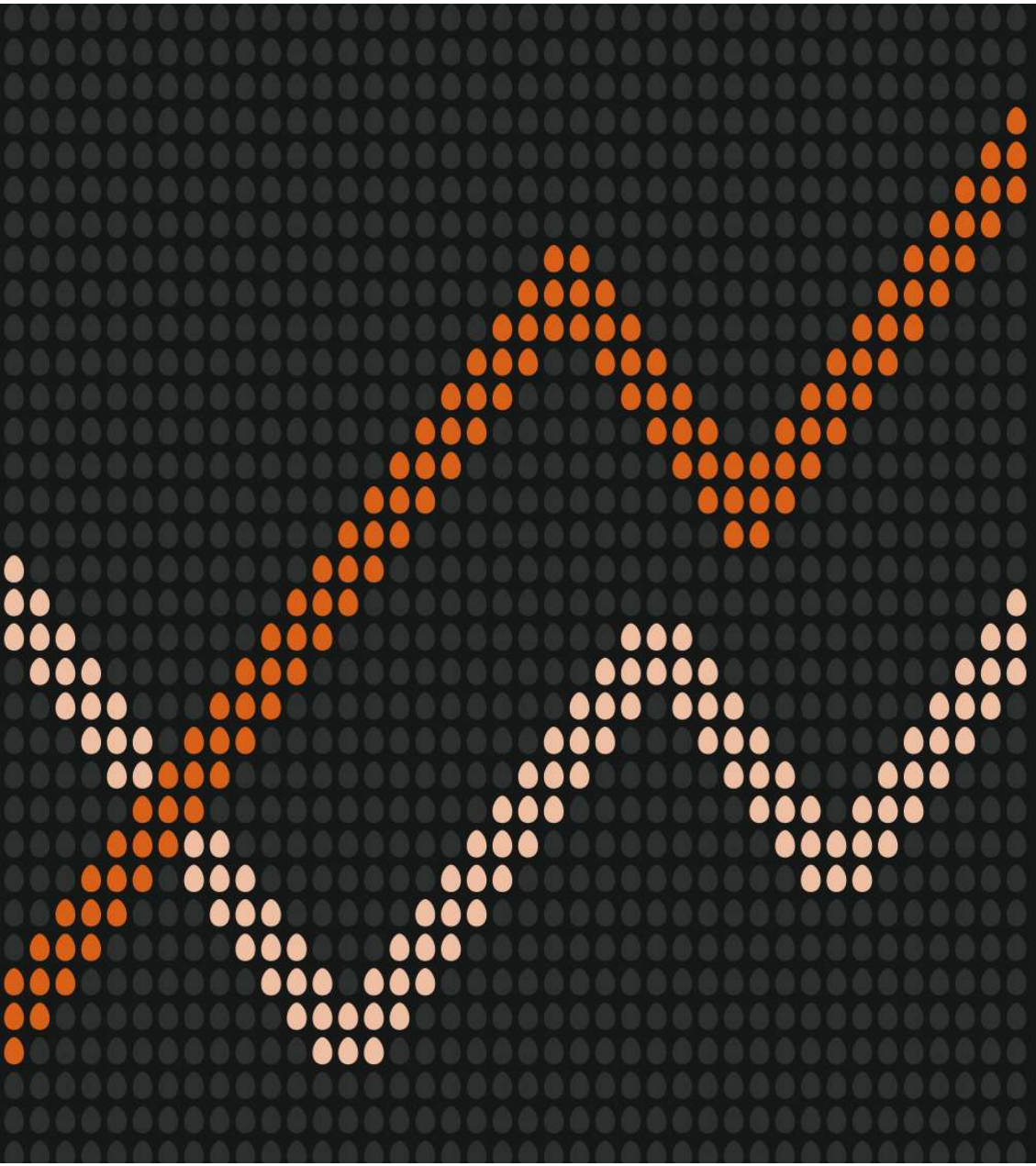


MLC ASSET MANAGEMENT

Global influences on Australian Shares …….

Signposts to assess whether a recession looms or resilience prevails

March 2023

Bob Cunneen

Senior Economist

Beware of Economists bearing forecasts ……..

MLC ASSET MANAGEMENT

" ***The inevitable never happens. It is the unexpected always.***"

John Maynard Keynes

" ***Any observed statistical regularity will tend to collapse once pressure is placed upon it for control purposes.***"

Charles Goodhart

Global share prices have been a rollercoaster ride over the past three years

MLC ASSET MANAGEMENT

A sequence of "Black Swans" has impacted Global Share prices since 2020…..

PANDEMIC (March 2020 -)

CHINESE Government crackdown on property developers & technology companies

Russia – Ukraine conflict

Inflation & Interest Rate shock (2021 -)

What's Next ???

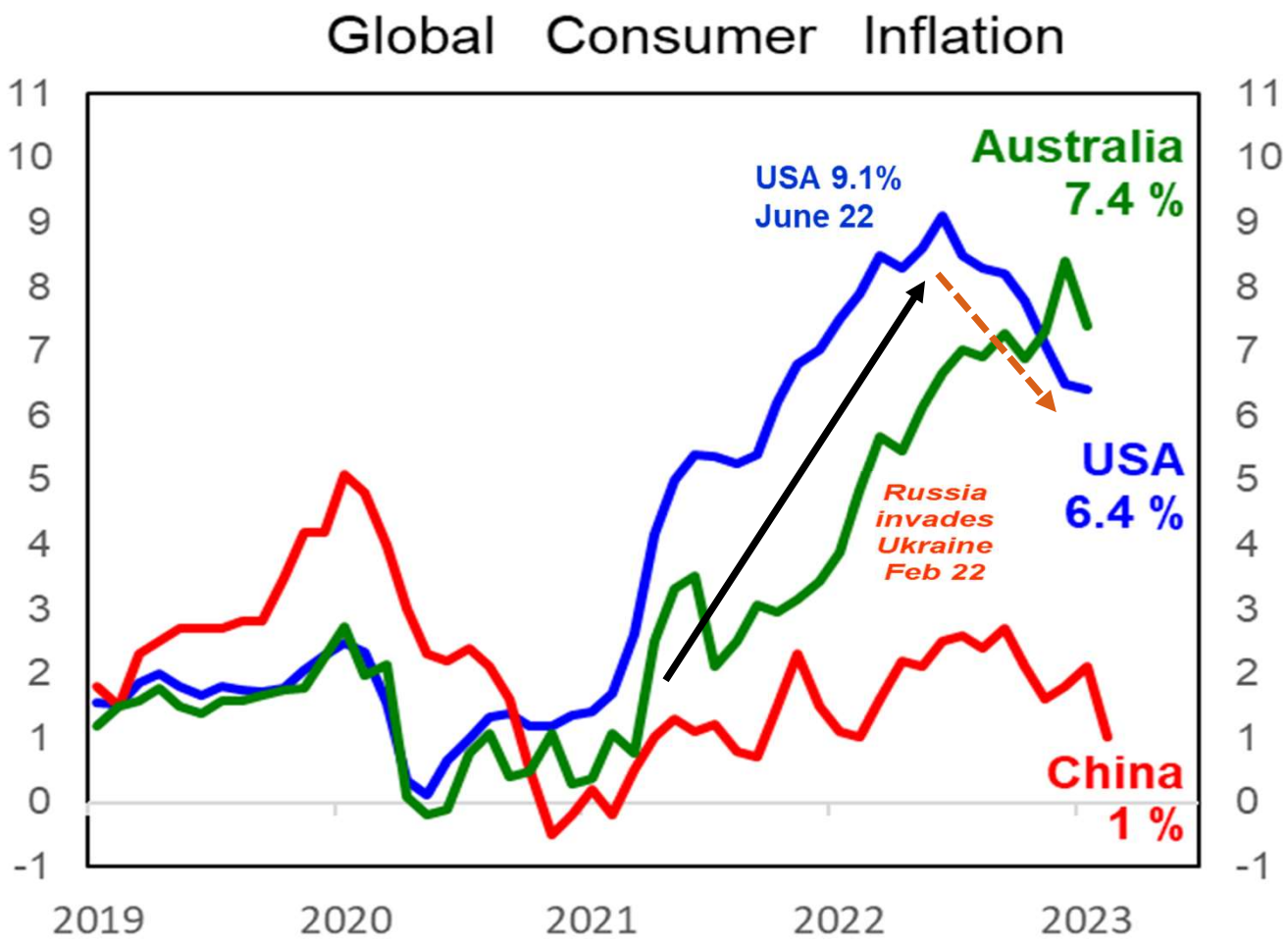
Global consumer inflation has surged to multi-decade highs in 2022

MLC ASSET MANAGEMENT

Australia's annual inflation reached 8.4% in December 2022. The surge in consumer prices was lead by "*food, automotive fuel and new dwelling construction*" according to the ABS. The new monthly CPI measure has since moderated to **7.4% in January.**

US inflation peaked at 9.1% in June 2022 (highest since 1981). There are more constructive signs of a "peak" with a moderation in annual inflation to 6.4% in January 2023.

Notably China has not had a major inflation problem in recent years given that China's economy has struggled with the government's "Zero Covid" strategy and weak property market.



Source: Australian, China and US Bureau of Statistics.

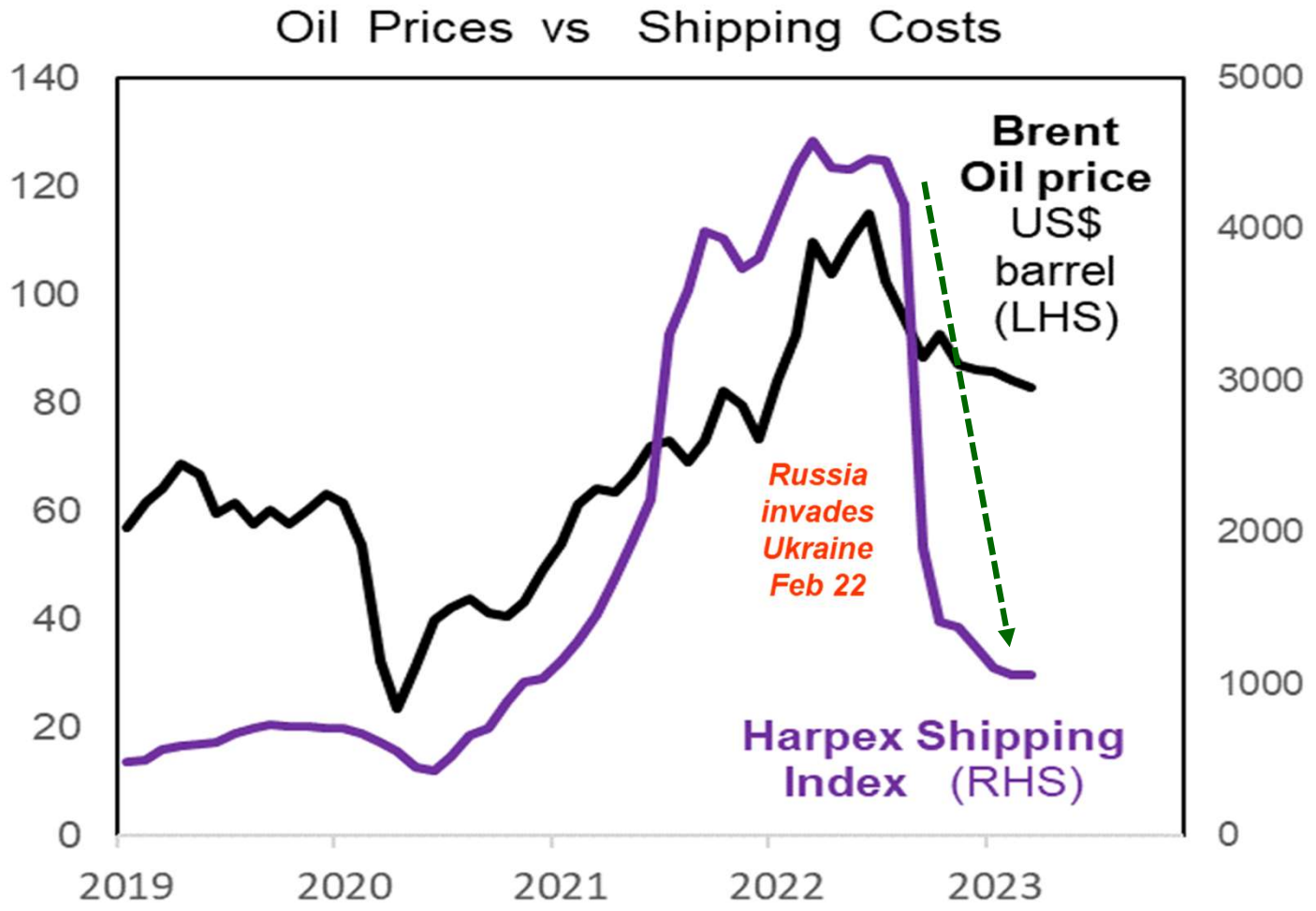
Commodity price pressures and supply chain disruptions seem to be fading judging by the recent falls in oil prices and shipping costs

MLC ASSET MANAGEMENT

A strong global recovery after the initial 2020 Pandemic phase generated rising commodity prices and shipping costs.

However these inflation risks intensified in 2022 through a mix of the Russia-Ukraine conflict and China's "Zero Covid" strategy which delayed production and shipping.

There are some encouraging signs that both oil prices and shipping costs have peaked



Source: Refinitiv Datastream

There are signs of persistent inflation pressures in residential rents

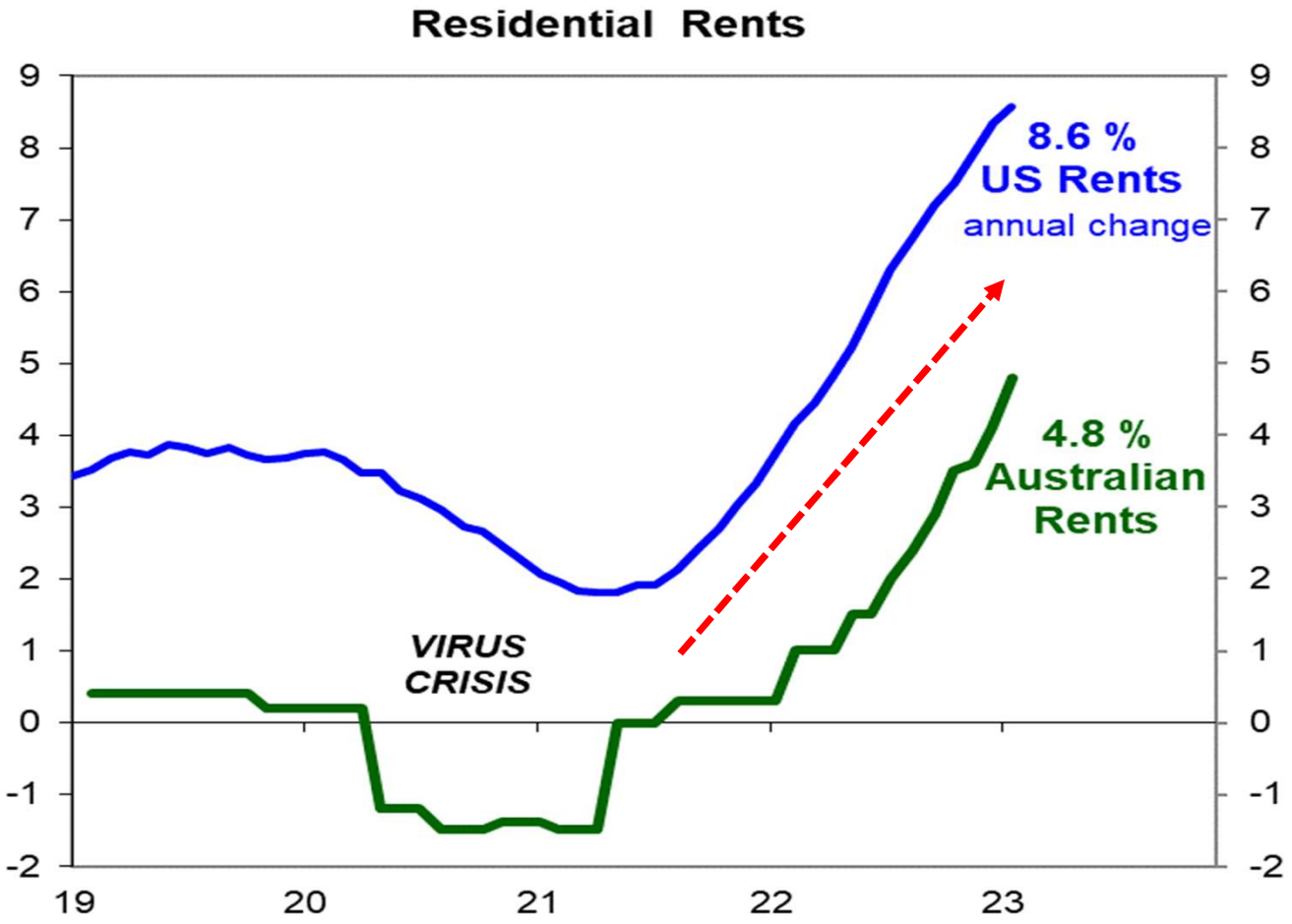
MLC ASSET MANAGEMENT

Federal Reserve Chair Jerome Powell concerns that rent inflation is "too high" but is optimistic of pressures abating :

" …. *while* ***housing services inflation remains too high****, the flattening out in rents evident in recently signed leases points to a deceleration in this component of inflation over the year ahead. "*

RBA Governor Philip Lowe is more cautious on rents with the March 8th comments :

" ***Rents are also rising rapidly****, with rental vacancy rates at very low levels in many parts of the country."*



Source : Australian Bureau of Statistics and US Bureau of Labour Statistics

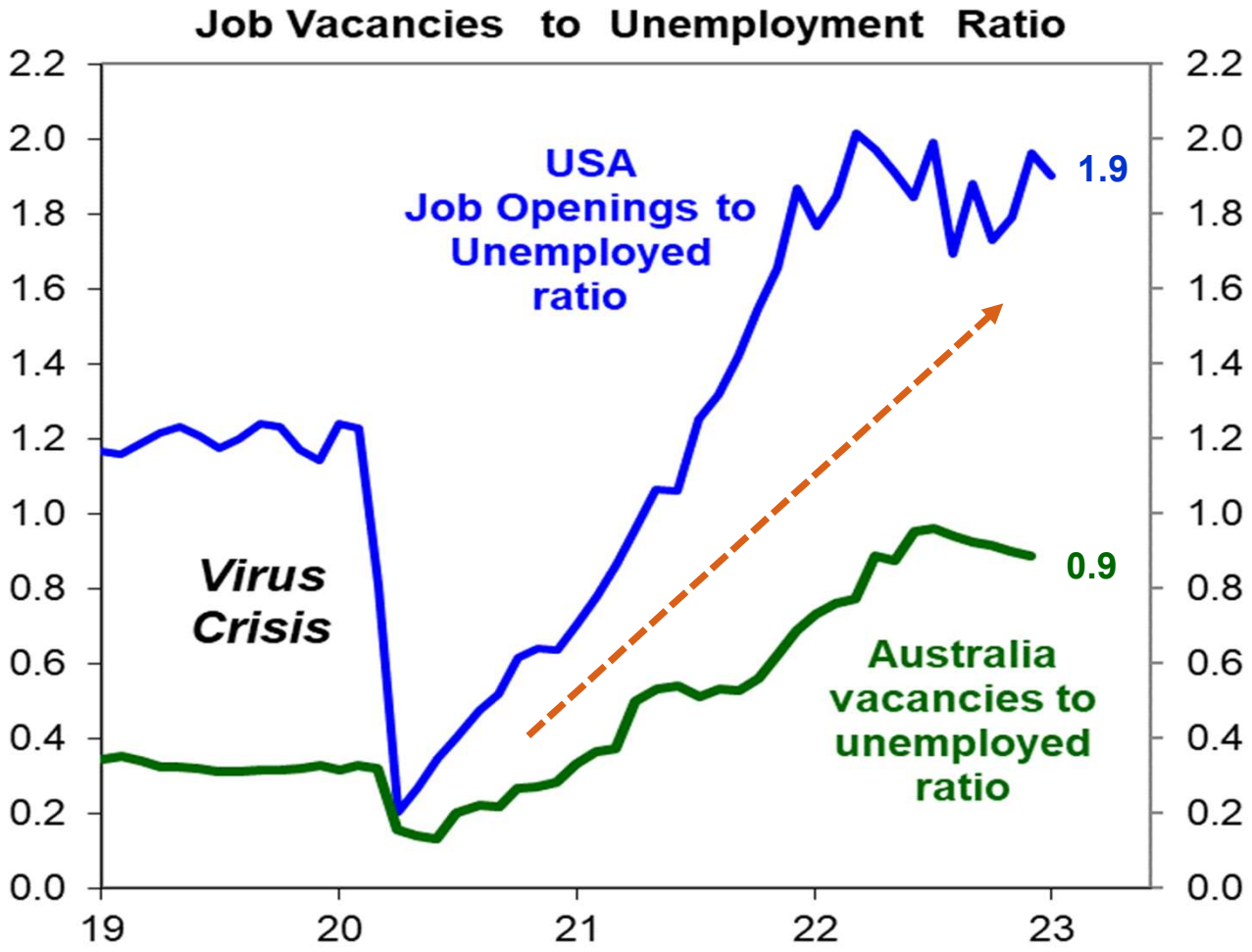
Labour markets are *" tight "* which suggests inflation pressures from wages

MLC ASSET MANAGEMENT

Central Banks are worried that inflation can remain high given strong wages growth.

Labour markets are considered *" tight "* in both Australia and the USA as there are high job vacancies with low unemployment levels.

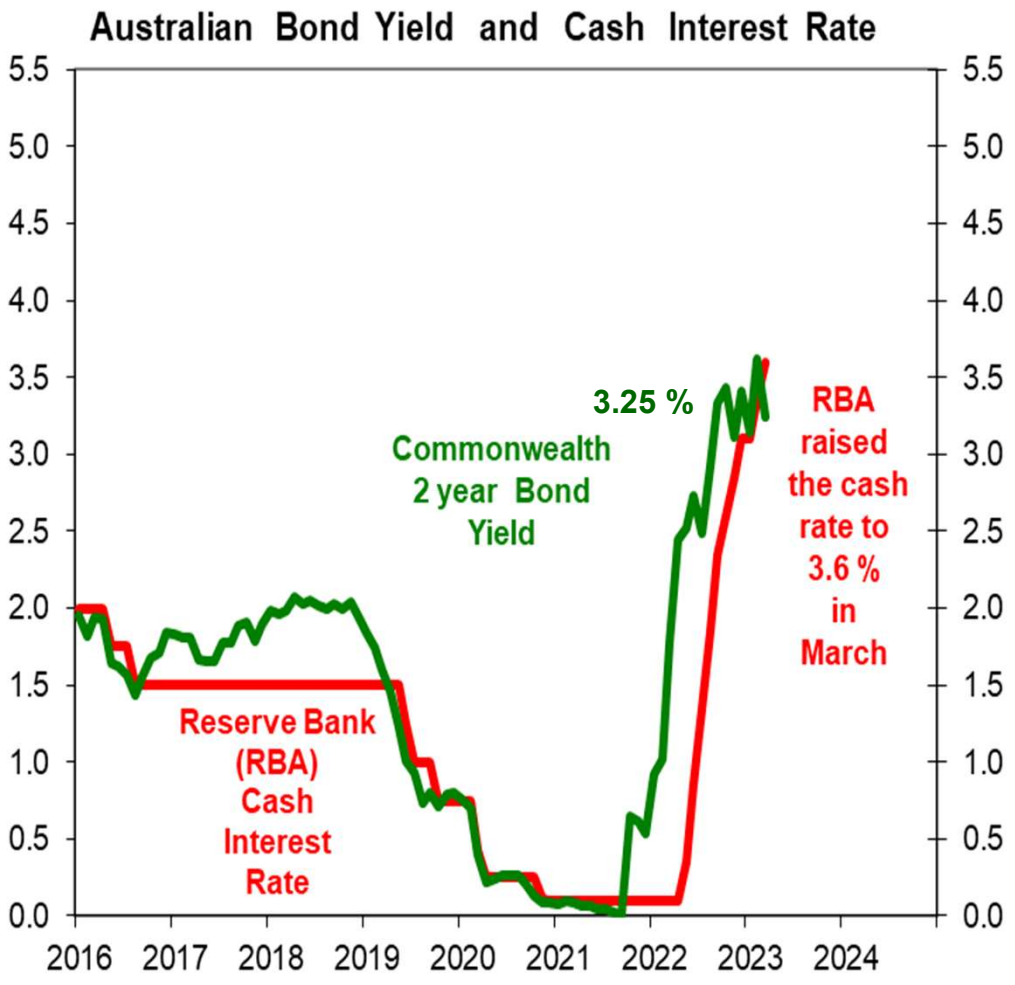
Workers now have more bargaining power to push for higher wages to compensate for the recent inflation surge. **This has lead to fears of a "Prices - Wages spiral" similar to the 1970s.** This risk is more acute in the USA whereas in Australia this is considered a "low" risk according to the RBA Governor on March 8

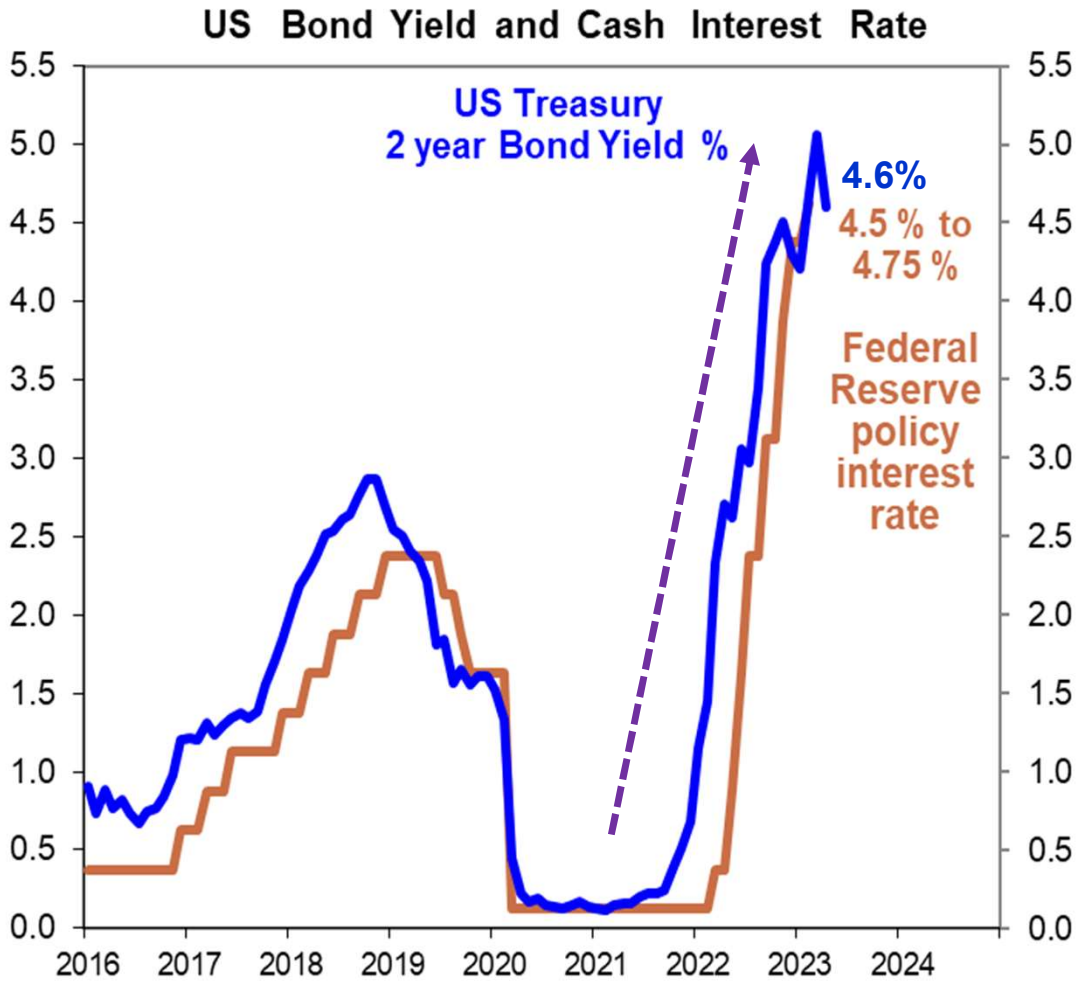


Source: Australian and US Bureau of Statistics.

Investors need to focus on the 2 year Government Bond yields rather than central banks to judge the direction of interest rates

MLC ASSET MANAGEMENT





Source: Refinitiv Datastream

Global recession fears given high inflation and rising interest rates.

Consumer sentiment is the ‘canary in the coal mine’

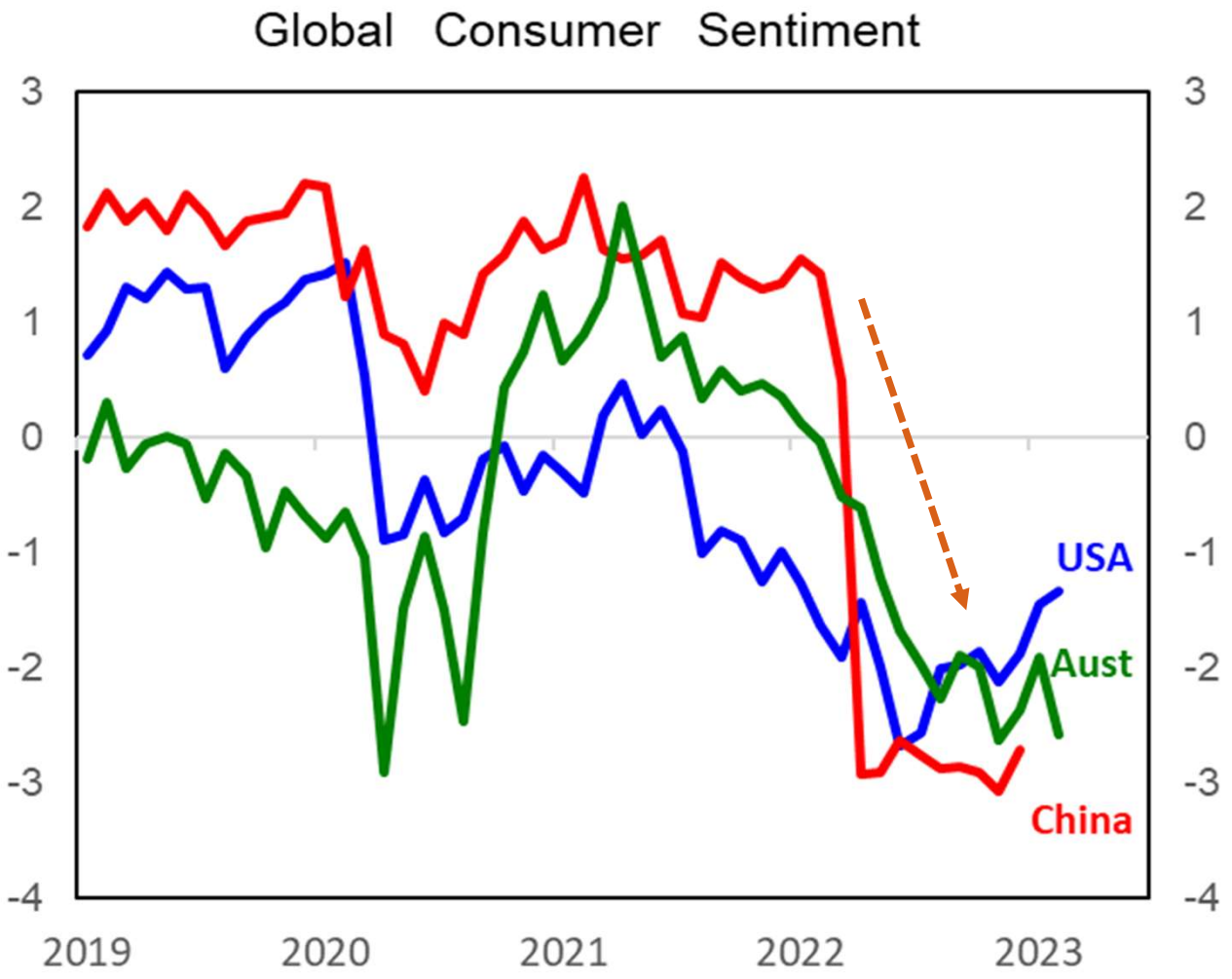
MLC ASSET MANAGEMENT

Consumers are acutely sensitive to the “cost of living crisis “ with incomes being squeezed by higher inflation and interest rates.

The RBA has recognised this concern :

*“**The pressure on household budgets from higher interest rates and inflation have contributed to a sharp decline in consumer sentiment,** which is around the lows observed at the onset of the pandemic and during the global financial crisis ” .*

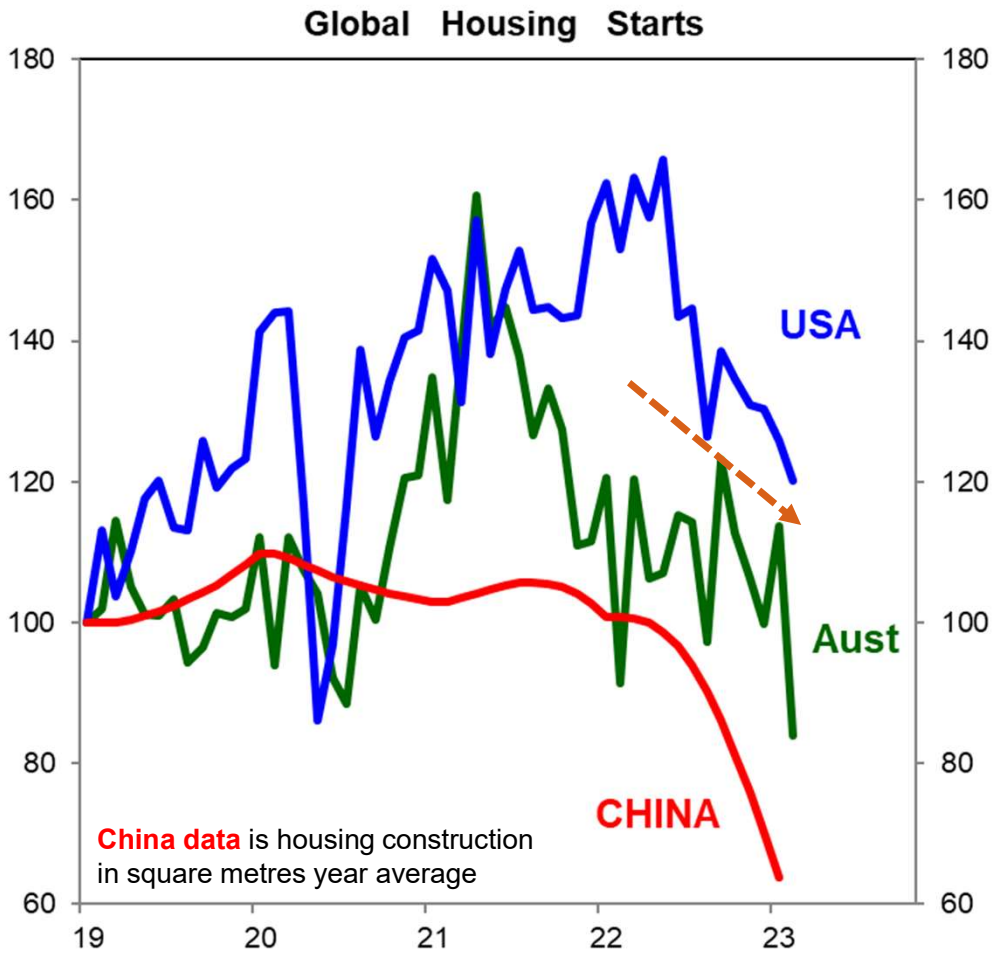
A sharp decline in consumer sentiment is a warning sign that economies are at risk of a recession. The more pessimistic the consumer becomes , the more likely they will cut spending which damages economic activity.

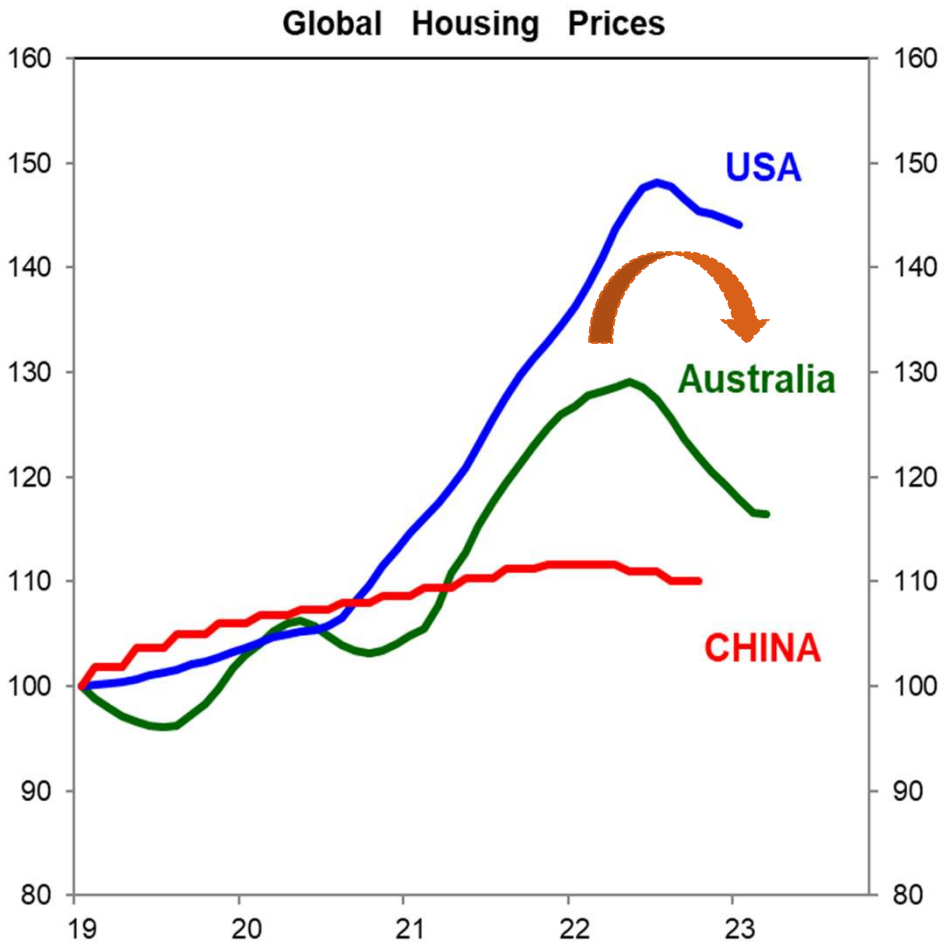


Source: Refinitiv Datastream, WMI, NBS and Michigan Consumer sentiment Z score 2006-14

New Housing Starts and Housing Prices are key barometers for recession risks.

MLC ASSET MANAGEMENT





Source : Australian , China and US national bureau of statistics

Australia's CoreLogic, BIS for China, Case Shiller for US house prices

Key views

MLC ASSET MANAGEMENT

Australian Shares have been hit by weakness in both American and Chinese share markets over the past year.

Global inflation seems to have peaked with commodity prices and supply chain disruptions moderating. ***However rising rents and wages suggest a long tail of price pressures this year.***

Central Banks are still signalling the need to further raise interest rates to contain inflation.

Global recession risks remain prominent given the chance that consumers are compelled to cut spending given the 'painful squeeze' from high inflation, rising interest rates and rents.

Housing starts and house prices are key barometers for judging whether there is a recession or resilience.

MLC
ASSET MANAGEMENT

Thank You