ECONOMIC AND MARKET COMMENTARY
JUNE QUARTER 2021

Australia:

Key points:

- **The strong rebound for the Australian economy is still underway, despite COVID-19 infections rapidly increasing in New South Wales**
- **At its July meeting, the Reserve Bank of Australia (RBA) announced a shift to a flexible form of quantitative easing and changed the weekly pace of purchases**
- **Australia reported a slight fall in the unemployment rate despite the Job Keeper scheme finishing at the end of the previous quarter**

The economic outlook remained positive, despite travel restrictions around Australia tightening as states escalated their response to the nation-wide COVID-19 outbreak. Millions of Australians experienced varying degrees of lockdown measures towards quarter end, with New South Wales, in particular, implementing strict stay at home orders to control the spread of the Delta variant. The Federal Budget was announced, with most changes being adjustments to existing measures in place and some personal income tax changes. Alongside this, headlines surrounding the AstraZeneca vaccine led to a drop in confidence in the jab, with just 5% of Australians fully vaccinated at the end of June. Despite this, Australian equities moved higher over the quarter, increasing by 8.5%. There was some disparity in performance across sectors over the quarter, with Information Technology, Consumer Discretionary and Telecommunication Services being the highest performing sectors, posting returns of 12.1%, 11.6% and 11.1% respectively, whilst, Energy (-2.2%) and Utilities (-4.5%) were the bottom two performing sectors over the quarter.

Economic data released in the June quarter saw the Australian economy advancing further, with quarter-on-quarter economic growth of 1.8%. This was the third straight quarter of expansion, driven by continued monetary and fiscal stimulus, and resulted in annual growth of 1.1%, the first positive annual growth rate since the first quarter of 2020. However, with the vaccination roll-out still slow relative to other developed countries, and fresh lockdown measures in place towards quarter end, the recovery is set to slow. Household consumption grew further, rising 1.2% in Q1, reflective of increased consumption on goods and services over the quarter. Annual inflation rose to 1.1% for the year to the end of the March quarter, slightly lower than the market consensus of 1.4%. The rise in tobacco excise, resetting the Medicare and Pharmaceutical Benefits, the continuation of home building grants and government schemes were all factors that contributed to the inflation reading being the highest since Q1 2020.

With the Federal Government's Job Keeper program concluding in March, there was great uncertainty whether this would cause a steep rise in the unemployment rate. Economic data for May revealed the unemployment rate actually fell further to 5.1%, marking the seventh consecutive month of a fall in the jobless rate, and the lowest reading since February 2020. Even so, the RBA believes there to be still spare capacity in the labour market. During its June meeting, the RBA left the cash rate unchanged at 0.1% and re-affirmed their decision to not increase the rate until at least 2024, when actual inflation is expected to be within the target range of 2–3%. During its July meeting, the RBA decided to shift to a flexible form of quantitative easing, whereby the overall figure for the volume of its bond purchases is not pre-determined and retained the April 2024 issuance for the 3-year yield target, rather than moving to November 2024. The RBA also announced that it will no longer maintain the current weekly pace of Government bond purchases ($5 billion per week) and revised this down to $4 billion per week with the pace set to remain in place "at least until mid-November".

Bond yields largely decreased for the quarter as the Australian 10-year yield fell 30 bps to 1.51%, influenced by changes to inflationary expectations. The Australian 10-year yield continues to trade slightly above the US equivalent, which fell 28 bps to 1.47% at the end of June. The fall in bond yields resulted in the Bloomberg AusBond Composite Index posting a positive overall return of 1.5% for the quarter.

Other economic conditions were mixed over the June quarter. The manufacturing PMI (measured by the Australian Industry Group Australian Performance of Manufacturing Index) increased to 63.2 in June, from 59.9 in the previous quarter, with five consecutive months of rises leading to a record level for the index (a reading over 50 indicates an expansion in activity). The services PMI (measured by the Australian Industry Group Australian Performance of Services Index) fell to 57.8 in June, from 58.7 in March, representing ongoing expansion, but at a slightly lower rate.

Returns for period ending 30 June 2021	Month	1 Year
Australian Equities[1]	8.5%	28.5%
Consumer Discretionary	11.6%	48.6%
Consumer Staples	5.4%	7.6%
Energy	-2.2%	10.2%
Financials, ex Property Trusts	8.8%	41.1%
Health Care	8.7%	6.2%
Industrials	6.2%	10.8%
Information Technology	12.1%	39.6%
Materials	9.5%	35.7%
Telecommunications Services	11.1%	33.1%
Utilities	-4.5%	-18.6%

[1] S&P/ASX 300. Below are sub-sectors.

Business sentiment (measured by the NAB Business Confidence survey) decreased to 11 in June, falling from 20 in the previous month, signalling weakening confidence levels in all industries except mining and manufacturing. Consumer confidence (measured by the Westpac Bank Consumer Sentiment Index) fell from 111.8 in March to 107.2 in June, with concerns over lockdown measures contributing to the index reporting a five month low.

The Aussie Dollar (AUD) depreciated against a basket of major currencies over the quarter, with the Trade-Weighted Index measuring 62.7 at the end of June, declining from 64.2 at the end of March. The AUD also depreciated against the USD falling from 75.96 US cents at the end of March, to 74.98 US cents at the end of June.

International:

Key points:

- **Vaccine rollouts are gaining momentum globally, with vaccination rates over 60% in the UK and close to 50% in the US and European Union**
- **The successful vaccination roll-outs temporarily eased concerns towards the spreading of the virus, instead inflation and the response of central banks became greater focuses over the June quarter**
- **President Biden's administration secured a deal on a $1.2 trillion infrastructure package in late June, which will upgrade roads, bridges, and broadband networks over the next eight years**

Against a backdrop of broadly generous policy support, vaccination rollouts gained significant momentum, with 2.2 billion COVID shots administered globally by the end of the second quarter. Investor sentiment picked up with the prospect of faster re-opening of economies, despite new, more contagious COVID-19 variants spreading. Global equities continued to rally, with the MSCI World ex Australia Index (hedged to AUD) posting a 7.6% return over the quarter. Inflation and the response of central banks came increasingly into focus during the quarter, while tensions between the US and China continued to linger in the background, with increased regulation on Chinese technology companies and, in particular, their foray into financial services.

US equities continued to perform strongly, gaining 8.5% over the quarter, as measured by the S&P 500 Composite Index in local currency terms, with news of President Biden securing a deal on a $1.2 trillion infrastructure package created to upgrade roads, bridges and broadband networks over the next 8 years. The US Federal Reserve met in mid-June and announced no change to its policy, leaving the target range for its federal funds at 0–0.25% and re-affirming there will be no rate hike until at least 2023, whilst policymakers signalled they expect two increases by the end of 2023. The Fed recognised that inflation has increased notably over the quarter, reflecting a combination of supercharged demand, disrupted supply, low base effects and increases in oil prices to consumer energy prices, whilst attributing this mainly to "transitory factors" that will abate.

US economic data released in Q2 was broadly encouraging, with the economy expanding by an annualised 6.4% in the first quarter of the year. The Markit US Manufacturing PMI increased to 62.1 in June, up from 59.1 in March, supporting a continued strong recovery in operating conditions (any number above 50 signals an expansion in manufacturing activity). The National Association of Home Builders/Wells Fargo Housing Market Index (HMI) dropped marginally to 81 in June, from 82 in March (although remaining well above 50, which indicates more builders view sales conditions positively). The US unemployment rate fell to 5.9% in June, lower than what was reported in March (6.0%), continuing the job market recovery, albeit unemployment remains above pre-pandemic levels. Consumer sentiment rose slightly to 85.5 in June, from 84.9 in March, as measured by the University of Michigan Consumer Sentiment Index, and the US annual core inflation was reported at 4.5% in June, a substantial rise from 1.6% in the March quarter.

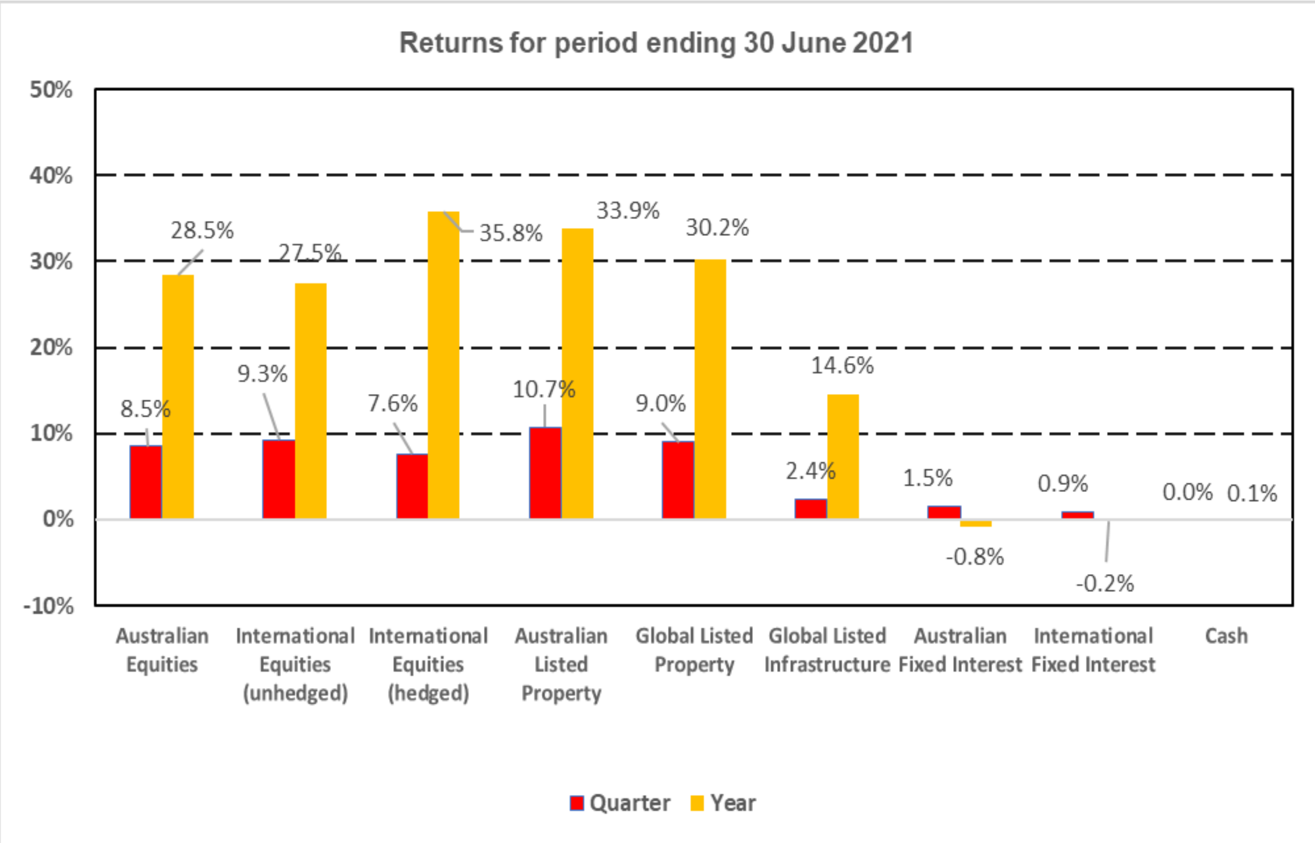
European equities posted another advance, climbing by 4.9%, as measured by the Euro Stoxx 50 Index in local currency terms. Many countries continue to battle rising COVID-19 infections, and new lockdowns have been imposed in several countries, however, with nearly half of the EU's adult population having had at least one dose, and 28% fully vaccinated, this has greatly benefitted the rally and improved investor sentiment. During the June meeting, the European Central Bank left interest rates unchanged and expected net purchases under the Pandemic Emergency Purchase Programme (PEPP) to be conducted at a significantly higher speed than in previous months. Manufacturing activity edged to a new record high following the twelfth consecutive month of expansion, with the Markit Eurozone Manufacturing PMI reaching 63.4 in June, compared to 62.5 in March. Eurozone headline inflation was reported at 1.9% in June, compared to 1.3% in March, as price growth slowed for energy and services, but accelerated for non-energy industrial goods, foods, alcohol, and tobacco. Core inflation came in at 0.9% in June, unchanged from the March quarter. The Eurozone unemployment rate fell to 7.9% in May, the lowest rate since May 2020 and marginally below market expectations of 8.0%.

Onshore Chinese equities soared during the June quarter, returning 10.1%, as measured by the MSCI China A Index (unhedged to AUD). Over the quarter, the Government announced new regulations for the technology sector and ongoing US and China tensions persisted. The Caixin Manufacturing PMI increased slightly to 51.3 in June, from 50.6 in March (a reading above 50 indicates an expansion of the manufacturing sector compared to the previous month), and China's GDP increased by 0.6% in the March quarter, signalling the weakest quarterly growth rate since the contraction in the first quarter of 2020.

Japanese equities rose 1.2%, as measured by the MSCI Japan Index (in local currency terms) over the quarter. There were localised outbreaks of COVID-19 over the quarter, which led to renewed lockdowns of metro areas and, although the rate of infections in Japan remains markedly below most other countries, the persistent increase in cases continues to cause concern ahead of the Olympics and has heightened criticism of the government's response. The Markit/Nikkei Final Japan Manufacturing PMI fell over the quarter, coming in at 52.4, the weakest reading since February, but still indicating growth in manufacturing. Year-on-year inflation was -0.1% in May, the highest reading since September 2020, with prices starting to recover from 2020 lows.

Global bonds generally recovered somewhat from the spike in bond yields experienced over the previous quarter. The US 10-year Government bond yield decreased by 28bps to 1.47%, the UK 10-year yield decreased to 0.72% in June from 0.85% in March and Japanese 10-year Government bond fell 4bps to 0.05%. Conversely, the German 10-year yield rose by 9bps to -0.20%, and the Italian 10-year yield increased by 16bps to 0.82%, resulting from changes to inflation forecasts.

Global listed infrastructure and global listed property continued to show steady signs of recovery, posting returns of 2.4% and 9.0% respectively over the June quarter, as measured by the FTSE Developed Core Infrastructure 50/50 Index (AUD hedged) and the FTSE EPRA/NAREIT Developed Rental Net TRI Index (AUD hedged) respectively.



Returns for period ending 30 June 2021	Month %	1 Year %
International Equities (unhedged) [2]	**9.3%**	**27.5%**
North America	*10.4%*	*30.3%*
UK	*7.4%*	*20.9%*
Europe (ex UK)	*9.3%*	*25.3%*
Japan	*1.2%*	*14.5%*
Asia Pacific (ex-Japan)	*5.0%*	*28.5%*
Emerging Markets	*6.6%*	*29.2%*
China A Shares	*10.1%*	*29.1%*
International Equities (hedged) [3]	**7.6%**	**35.8%**
Australian Listed Property [4]	**10.7%**	**33.9%**
Global Listed Property [5]	**9.0%**	**30.2%**
Global Listed Infrastructure [6]	**2.4%**	**14.6%**
Australian Fixed Interest [7]	**1.5%**	**-0.8%**
International Fixed Interest [8]	**0.9%**	**-0.2%**
Cash [9]	**0.0%**	**0.1%**

1. S&P/ASX 300 Accumulation Index
2. MSCI World ex-Australia Index (with net dividends reinvested in A$)
3. MSCI World ex-Australia Index (with net dividends reinvested hedged in A$)
4. S&P/ASX 300 A REIT Accumulation Index
5. FTSE EPRA/NAREIT Developed Net TRI Index (Net Total Return hedged in A$)
6. FTSE Developed Core Infrastructure 50/50 Index (Net Total Return hedged in A$)
7. Bloomberg AusBond Composite Index
8. Barclays Global Aggregate Hedged in AUD Index
9. Bloomberg AusBond Bank Bill Index

All returns are based on accumulation indices. Data sourced from eVestment Alliance, Datastream and Thomson Reuters to their personal objectives, situation and needs, and consult their financial planner. Past performance is no guarantee of future performance.