Economic commentary

The global economy

Data over the past month raised concerns that high inflation could be more persistent than originally thought, showing better-than-expected global activity that raised hopes of a soft landing in major advanced economies, particularly the US. Together with continued hawkish commentary from central bank officials, these developments prompted investors to expect interest rates to reach higher levels and remain elevated for longer – an outlook now more in line with central banks' forecasts.

The US Federal Reserve raised its policy interest rate by 25bps as expected and Chair Powell indicated that US interest rates were close to their peak levels. However, investors now expect that the Fed will raise rates more aggressively to tame inflation after a stronger-than-expected inflation print in the Fed's preferred inflation gauge, the Personal Consumption Expenditure (PCE) deflator.

Stronger-than-expected data on US economic activity supported this reassessment. Non-farm payrolls increased sharply in January, the unemployment rate declined, and retail sales rose strongly. Services sector PMI and ISM data also improved noticeably. In contrast, there are signs that the housing market is softening, with weaker-than-expected housing starts and existing home sales in January.

The European Central Bank (ECB) raised its policy rate in February by an expected 50bps and commentary by ECB officials has remained hawkish. Recent data has also intensified concerns that eurozone inflation may take longer to bring down, particularly core inflation. Combined with resilient services sector activity, investors now also expect the ECB's policy rate to reach a higher level and stay high for longer.

The Bank of England and Sweden's Riksbank also raised their policy rates by 50bps. Both central banks remain concerned about high inflation being more persistent than expected, particularly in Sweden where core CPI inflation was much stronger than expected in January.

The Australian economy

At the February meeting, the Reserve Bank of Australia (RBA) raised its policy rate by 25bps. The meeting minutes and subsequent comments by the RBA Governor indicated a more hawkish stance, with the bank also revising up its wage growth and inflation forecasts this month. In turn, investors increased their expectations for the peak policy rate and now believe the RBA will raise rates by a further 100bps over the next 6 months.

The heightened concerns around more persistent inflationary pressures have emerged despite a key measure of wages growth, the Wage Price Index, increasing by less than expected in the December quarter. While the labour market remains tight, employment fell unexpectedly for the second consecutive month and the unemployment rate rose from 3.5% to 3.7%.

Retail sales volumes (that is, after adjusting for inflation) fell slightly in the December quarter and consumer confidence is weak. Nominal retail sales rose in January, partly reversing December's large fall but, on average, there has been no growth in this metric since September 2022. Building approvals also continued to trend lower in December.

Financial market commentary

Financial markets were generally weaker in February after a very strong January. Global bond yields rose, and most equity markets fell on the expectation that interest rates will reach higher levels and remain higher for longer.

Equity markets (performance in local currency, excluding dividends)

Movements in global equity markets were mixed in February. The US S&P500 fell by 2.6% with many sectors exposed to consumer retail spending dragging down the index. The ASX200 declined by 2.9%, with resource stocks underperforming as the initial optimism surrounding the reopening of China's economy faded.

Banking stocks were also weak in February triggered by Australia's largest lender revealing that it is preparing for a rise in bad debts as the economy slows. Reduced optimism about the impact of China's reopening also weighed on Hong Kong's equity market, which fell by 9.4% and retraced most of the rise in January.

In contrast, European stocks rose by 1.7% in February and have outperformed in 2023 to date. Mild winter weather and sufficient gas reserves have supported activity and sentiment and reported corporate earnings for the December quarter have been relatively stronger than in the US. Equity markets in the UK and Japan also rose, by 1.3% and 0.4%, respectively.

Interest rates

Expectations that central banks will have to raise interest rates by more and keep them higher for longer pushed global bond yields higher. Short end yields rose most noticeably, with 3-year Australian government bond yields and 2-year US government bond yields increasing by 42bps and 62bps, respectively,

Australian 10-year government bond yields rose by 30bps to 3.85% and German bond yields rose by 37bps to 2.65%. US 10-year bond yields rose most sharply, by 42bps to 3.93%, more than retracing the fall in January.

The rise in global bond yields also pushed TCorp bond yields higher, though by less than the increases in Australian government bond yields.

Currency and commodity markets

The Brent crude oil price rose in the first half of February as Russia cut back production and China's reopening boosted expectations of increased oil demand. However, oil prices more than reversed the gains in the second half of the month to end 0.7% lower in February.

The rise in bond yields over February supported the US dollar. The Australian dollar depreciated in February, falling by 4.7% against its US counterpart to US$0.67. The Australian dollar also fell by 2.1% against the euro and 2.4% against the British pound.

Iron ore prices remained resilient in the month, rising by 1.9%, despite fading optimism around China's reopening.

Financial market performance

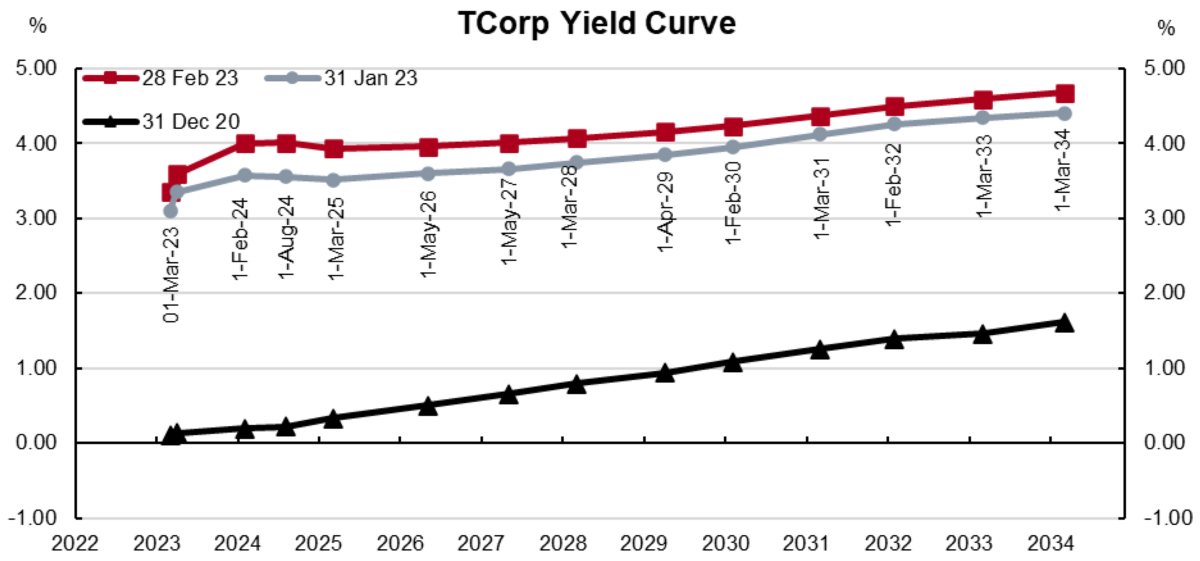
Currency markets **February 2023**	**Previous month close**	**Month high**	**Month low**	**Month close**	**Month change**
AUD/USD	0.706	0.714	0.673	**0.673**	-4.66% ▼
AUD/EUR	0.649	0.651	0.635	**0.636**	-2.09% ▼
AUD/JPY	91.78	93.03	90.82	**91.58**	-0.21% ▼
AUD/GBP	0.573	0.579	0.559	**0.559**	-2.35% ▼
AUD/BRL	3.581	3.659	3.494	**3.522**	-1.64% ▼
AUD/INR	57.80	58.47	55.60	**55.60**	-3.80% ▼
AUD/CNY	4.766	4.812	4.665	**4.665**	-2.12% ▼

Equity markets* **February 2023**	**Previous month close**	**Month high**	**Month low**	**Month close**	**Month change**
MSCI World ex Australia	2845	2909	2767	**2783**	-2.1% ▼
MSCI Emerging Markets	1032	1046	967	**967**	-6.2% ▼
S&P/ASX200	7477	7558	7225	**7258**	-2.9% ▼
S&P/ASX Small Ordinaries	2981	3017	2825	**2864**	-3.9% ▼
S&P500 (US)	4077	4180	3970	**3970**	-2.6% ▼
FTSE 100 (UK)	7772	8014	7761	**7876**	1.3% ▲
Stoxx600 (Europe)	453	465	453	**461**	1.7% ▲
DAX (Germany)	15128	15534	15181	**15365**	1.6% ▲
CAC 40 (France)	7082	7366	7077	**7268**	2.6% ▲
Nikkei 225 (Japan)	27327	27696	27104	**27446**	0.4% ▲
Hang Seng (HK)	21842	22072	19786	**19786**	-9.4% ▼
Shanghai Composite (China)	3256	3307	3224	**3280**	0.7% ▲
Bovespa (Brazil)	113431	112074	104932	**104932**	-7.5% ▼
IPC (Mexico)	54564	55019	52482	**52758**	-3.3% ▼
S&P/BSE Sensex (India)	59550	61320	58962	**58962**	-1.0% ▼

*Returns are in local currency, and exclude dividend payments

Bond markets (%) **February 2023**	**Previous month close**	**Month high**	**Month low**	**Month close**	**Month change**
RBA Official Cash Rate	3.10	3.35	3.10	**3.35**	0.25 ▲
90 Day Bank Bill	3.37	3.56	3.34	**3.56**	0.19 ▲
180 Day Bank Bill	3.72	3.93	3.64	**3.93**	0.21 ▲
1 Year Term Deposit Rate	2.85	2.90	2.85	**2.90**	0.05 ▲
3 Year CGS Bond	3.18	3.64	3.01	**3.60**	0.42 ▲
10 Year CGS Bond	3.55	3.88	3.38	**3.85**	0.30 ▲
10 Year US Bond	3.51	3.95	3.39	**3.93**	0.42 ▲
10 Year German Bond	2.29	2.65	2.08	**2.65**	0.37 ▲
10 Year Japanese Bond	0.50	0.51	0.49	**0.51**	0.01 ▲

TCorp bonds (%) February 2023	Previous month close	Month high	Month low	Month close	Month change
20-Apr-23	3.35	3.59	3.33	**3.59**	0.24 ▲
08-Feb-24	3.58	4.02	3.47	**4.00**	0.43 ▲
20-Aug-24	3.56	4.04	3.43	**4.01**	0.45 ▲
20-Mar-25	3.51	3.97	3.33	**3.93**	0.42 ▲
20-May-26	3.60	4.00	3.38	**3.96**	0.36 ▲
20-May-27	3.66	4.05	3.45	**4.01**	0.35 ▲
20-Mar-28	3.74	4.11	3.53	**4.08**	0.33 ▲
20-Apr-29	3.85	4.19	3.65	**4.16**	0.31 ▲
20-Feb-30	3.96	4.27	3.74	**4.24**	0.28 ▲
20-Mar-31	4.12	4.40	3.89	**4.37**	0.25 ▲
20-Feb-32	4.26	4.53	4.02	**4.50**	0.25 ▲
CIB 2.75% 20 Nov 25	0.44	0.70	0.27	**0.59**	0.15 ▲
CIB 2.50% 20 Nov 35	1.84	2.24	1.70	**2.18**	0.35 ▲



Source: TCorp

Commodity markets (US$) February 2023	Previous month close	Month high	Month low	Month close	Month change
Brent Oil (per barrel)	84.5	86.6	79.9	**83.9**	-0.7% ▼
Iron Ore (per tonne)	123.4	127.0	122.3	**125.8**	1.9% ▲

TCorp forecasts	June-23	Dec-23	June-24	Dec-24
RBA Official Cash Rate	3.85	3.85	3.85	3.85
90 Day Bank Bill	4.15	4.15	4.15	4.15
10 Year CGS Bond	3.75	3.75	3.75	3.75

About New South Wales Treasury Corporation (TCorp)

TCorp provides best-in-class investment management, financial management, solutions and advice to the New South Wales (NSW) public sector. With A$107 billion of assets under management, TCorp is a top 10 Australian investment manager and is the central borrowing authority of the state of NSW, with a balance sheet of A$145 billion. It is rated Aaa (Stable) by Moody's, AAA (Stable) by Fitch, and AA+ (Stable) by S&P.

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