Monthly economic report

The global economy

Inflation globally has decelerated faster than expected over the past few months. Despite this, central bank officials continue to communicate that they need more evidence that inflation is sustainably returning to target before lowering interest rates. This cautious and patient approach reflects ongoing concerns that inflation could remain too high, particularly components of services inflation. With labour markets around the world still tight, wages growth remains elevated and needs to slow for central banks' to sustainably achieve their inflation targets.

Although central banks are cautious, the US Federal Reserve (Fed) and the European Central Bank have clearly shifted their focus to the question of how long to keep rates restrictive before cutting. In contrast, the Reserve Bank of Australia (RBA) has not ruled out the possibility of further rate rises. The tightening bias in the RBA's communication is likely aimed at discouraging financial markets from pricing in aggressive interest rate cuts and creating an unhelpful loosening in financial conditions.

As central banks have maintained the coordinated message that rate cuts are not imminent, investors have pushed back the expected timing of rate cuts further. Most central banks are now expected to start cutting rates in the third quarter of this year. Investors also expect central banks to cut rates in 2024 by much less than they did a month ago, with market expectations now more aligned with central banks' own projections. For example, investors now expect the Fed to deliver around 3 rate cuts this year, compared to the almost 6 rate cuts expected at the start of February.

Although messaging from central banks in major developed economies is consistent and investors expect a similar amount of rate cuts this year (excluding Australia), economic conditions vary considerably across regions. The US economy is the outlier, with strong economic growth and resilient consumer spending. Most first-tier US economic data was on the stronger side again in February.

In contrast, other developed economies are experiencing recession-like conditions, including in Europe, UK, Japan and Canada. This divergence raises the possibility that – despite similar market expectations and unified central bank rhetoric – interest rates are not lowered in a synchronised fashion once easing cycles commence.

China's economy is also weak, with soft consumer spending, a severe property sector downturn and ongoing deflation. In response, the People's Bank of China cut one of its key interest rates by a larger-than-expected 25bps in February. It is likely that more stimulus measures will be announced in March, following the annual National People's Congress, though it remains to be seen how significant or effective these might be.

The Australian economy

The RBA Board held interest rates steady at its February meeting and noted that a further increase in interest rates could not be ruled out. Like central banks in other developed economies, the RBA needs to be convinced that inflation is sustainably returning to target before it cuts rates. Economic data over the past few months has weakened the case for further rate hikes, with the Australian economy weaker and inflation lower than the RBA expected a few months ago.

Inflation in January surprised to the downside again and consumer spending remains very weak, as many households face ongoing cost of living pressures. The labour market is still tight but has continued to gradually loosen, with total hours worked trending lower, employment growth slowing and the unemployment rate climbing higher. Wages growth is expected to have reached its peak and leading indicators suggest that it will start to decelerate.

Investors have also pushed back the expected timing of the first RBA rate cut, from June to September. The RBA is expected to lower rates once or twice this year, compared to the 2-3 rate cuts that were priced in at the start of February. With the Australian economy weaker than the US economy and inflation expected to return to target at a similar time, it is not obvious why the RBA should wait longer than the Fed to cut rates or cut by less this year.

Financial market commentary

Bond yields rose further in February as investors continued to pare back their expectations for interest rate cuts this year. Despite the higher bond yields, most equity markets rose in the month.

Equity markets (performance in local currency, excluding dividends)

The MSCI World (ex-Australia) index rose by 3.8% in February and the MSCI Emerging Markets index rose by 4.4%. The drivers of equity markets varied across regions. The US S&P500 gained 5.1%, boosted by a strong corporate earnings reporting season, especially better-than-expected earnings from Nvidia. Although gains in the month were broad-based across sectors, higher bond yields in the month weighed on the more interest-sensitive sectors (e.g. utilities and real estate).

Japan's equity market also rose strongly, by 7.9%, boosted by the Japanese yen depreciating a further 1.5% against the US dollar. Equity markets in Japan, the US and Europe all reached historically high levels in February. In contrast, a lacklustre corporate earnings season saw Australian equities underperform, with the ASX200 edging 0.2% higher. Ongoing concerns around weakness in China's economy and future demand for commodities also weighed on mining stocks.

Equity markets in China and Hong Kong rebounded in February, after sharp falls in January. The strength was partly in response to authorities announcing measures to support the equity market, which has trended lower the past 3 years.

Interest rates

Global bond yields rose sharply in February as investors adjusted to the idea of central banks keeping interest rates higher for longer. US 10-year bond yields rose 33bps and German 10-year yields increased 25bps, with larger increases at the short-end. Australian bond yields rose 12-13bps across the curve – smaller increases than in the US or Europe – as rate cut expectations were pared back in Australia.

TCorp bond yields moved broadly in line with those on Commonwealth Government bonds in February.

Currency and commodity markets

Iron ore prices fell further in February, to be 8.4% lower since the start of this year. This reflects concerns about the outlook for China's economy, particularly steel-intensive property construction.

Concerns about China's economy also weighed on the Australian dollar, which depreciated by 1.1% against the US dollar in February. The larger rise in short-end US bond yields relative to Australia also weighed on the Australian dollar, as investors pared back rate cut expectations by more for the Fed than for the RBA.

Financial market performance

Currency markets February 2024	Previous month close	Month high	Month low	Month close	Month change
AUD/USD	0.657	0.657	0.645	**0.650**	-1.1% ▼
AUD/EUR	0.607	0.607	0.599	**0.601**	-1.0% ▼
AUD/JPY	96.50	98.76	96.23	**97.43**	1.0% ▲
AUD/GBP	0.518	0.519	0.512	**0.515**	-0.5% ▼
AUD/BRL	3.255	3.277	3.197	**3.231**	-0.7% ▼
AUD/INR	54.54	54.53	53.57	**53.89**	-1.2% ▼
AUD/CNY	4.709	4.722	4.642	**4.672**	-0.8% ▼

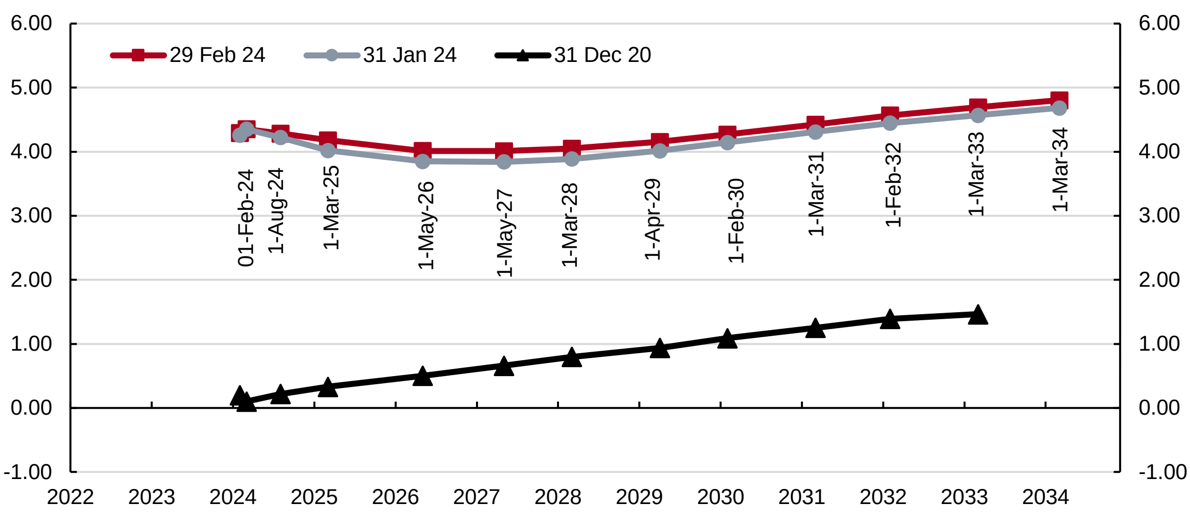
Equity markets* February 2024	Previous month close	Month high	Month low	Month close	Month change
MSCI World ex Australia	3286	3421	3310	**3410**	3.8% ▲
MSCI Emerging Markets	976	1029	982	**1019**	4.4% ▲
S&P/ASX200	7681	7699	7548	**7699**	0.2% ▲
S&P/ASX Small Ordinaries	2956	2999	2916	**2999**	1.5% ▲
S&P500 (US)	4846	5093	4906	**5093**	5.1% ▲
FTSE 100 (UK)	7631	7729	7512	**7630**	0.0% ▼
Stoxx600 (Europe)	486	497	483	**495**	1.8% ▲
DAX (Germany)	16904	17678	16859	**17678**	4.6% ▲
CAC 40 (France)	7657	7967	7589	**7927**	3.5% ▲
Nikkei 225 (Japan)	36287	39240	36011	**39166**	7.9% ▲
Hang Seng (HK)	15485	16791	15510	**16511**	6.6% ▲
Shanghai Composite (China)	2789	3015	2702	**3015**	8.1% ▲
Bovespa (Brazil)	127752	131689	127018	**129054**	1.0% ▲
IPC (Mexico)	57373	58712	55351	**55419**	-3.4% ▼
S&P/BSE Sensex (India)	71752	73158	71072	**72500**	1.0% ▲

*Returns are in local currency, and exclude dividend payments

Bond markets (%) February 2024	Previous month close	Month high	Month low	Month close	Month change
RBA Official Cash Rate	4.35	4.35	4.35	**4.35**	0.00 –
90 Day Bank Bill	4.35	4.35	4.32	**4.34**	-0.01 ▼
180 Day Bank Bill	4.43	4.48	4.38	**4.48**	0.05 ▲
New institutional term deposits	4.70	4.70	4.70	**4.70**	0.00 –
3 Year CGS Bond	3.57	3.86	3.55	**3.70**	0.13 ▲
10 Year CGS Bond	4.01	4.27	3.98	**4.14**	0.12 ▲
10 Year US Bond	3.91	4.32	3.88	**4.24**	0.33 ▲
10 Year German Bond	2.17	2.46	2.15	**2.41**	0.25 ▲
10 Year Japanese Bond	0.73	0.75	0.67	**0.71**	-0.02 ▼

TCorp bonds (%) **February 2024**	**Previous month close**	**Month high**	**Month low**	**Month close**	**Month change**
20-Aug-24	4.22	4.35	4.25	**4.28**	0.06 ▲
20-Mar-25	4.02	4.24	4.02	**4.18**	0.16 ▲
20-May-26	3.85	4.13	3.85	**4.01**	0.16 ▲
20-May-27	3.84	4.14	3.83	**4.01**	0.17 ▲
20-Mar-28	3.89	4.18	3.87	**4.05**	0.16 ▲
20-Apr-29	4.01	4.27	3.99	**4.15**	0.14 ▲
20-Feb-30	4.14	4.39	4.11	**4.27**	0.12 ▲
20-Mar-31	4.31	4.54	4.27	**4.42**	0.12 ▲
20-Feb-32	4.45	4.68	4.41	**4.56**	0.12 ▲
08-Mar-33	4.57	4.80	4.53	**4.69**	0.12 ▲
20-Mar-34	4.68	4.91	4.64	4.80	0.12 ▲
CIB 2.75% 20 Nov 25	1.25	1.45	1.29	**1.34**	0.09 ▲
CIB 2.50% 20 Nov 35	2.17	2.41	2.17	**2.31**	0.14 ▲

TCorp Yield Curve



Source: TCorp

Commodity markets (US$) **February 2024**	**Previous month close**	**Month high**	**Month low**	**Month close**	**Month change**
Brent Oil (per barrel)	81.7	83.7	77.3	**83.6**	2.3% ▲
Iron Ore (per tonne)	135.1	132.4	124.7	**124.9**	-7.6% ▼

TCorp forecasts	**June-24**	**Dec-24**	**Jun-25**	**Dec-25**
RBA Official Cash Rate	4.10	3.85	3.10	2.35
90 Day Bank Bill	4.10	3.10	3.10	2.50
10 Year CGS Bond	3.50	3.25	3.25	3.25

About TCorp

TCorp provides best-in-class investment management, financial management, solutions and advice to the New South Wales (NSW) public sector. With A$111 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$172 billion. It is rated Aaa (Stable) by Moody's, AAA (Stable) by Fitch, and AA+ (Stable) by S&P.

TCorp

Level 7, Deutsche Bank Place,
126 Phillip Street, Sydney, NSW 2000

Tel: +61 2 9325 9325
www.tcorp.nsw.gov.au
www.linkedin.com/company/tcorp-nswtreasurycorporation/

NSW GOVERNMENT | tcorp