

Monthly economic report

The global economy

Headlines about the Iran war continued to drive financial markets in May. Negative sentiment in the first half of the month weighed on risk assets, with investors focussing on the inflationary impact of higher oil prices. Sentiment then turned positive in the second half of May, as news headlines suggested that the US and Iran were close to reaching a deal to end the war. The deal would see the Strait of Hormuz reopen, toll free, and set out a path for talks about Iran's nuclear program and its frozen offshore assets.

It is becoming increasingly urgent that a deal to re-open the Strait of Hormuz is finalised soon as global inventories of oil and oil products are falling sharply as demand is expected to rise during the Northern Hemisphere summer. CEOs of large global energy companies have warned that inventories have been significantly depleted and will hit all-time lows in coming weeks. If the Strait of Hormuz remains closed, this will put upward pressure on prices, with CEOs and commodity analysts indicating that oil prices could eventually spike to US\$140-\$160 per barrel.

Even if a deal is reached soon, it will take a significant amount of time for global supply chains to normalise. It will take at least a few months to restore trade flows to 80% of pre-war levels and around one year to get to 100%. At the same time, demand for oil and oil products is likely to remain elevated as countries seek to rebuild their inventory buffers. This combination means that oil prices are not expected to return to pre-war levels for at least another few years.

The prospect of higher oil prices for longer has seen central bankers around the world become more worried about lingering high inflation. Minutes from the US Federal Reserve's May meeting were interpreted as hawkish and investors are now expecting a rate hike in late 2026 or early 2027. Some members of the European Central Bank have said that rates need to rise as central banks can no longer 'look through' this shock. Similarly, the New Zealand central bank said it is likely to raise rates soon. Investors expect rate rises in Europe and New Zealand in June and July, respectively.

The Australian economy

The Reserve Bank of Australia (RBA) raised interest rates by 25bps, to 4.35%, as was widely expected. The decision was an 8-1 split, compared to the 5-4 vote in March. The RBA is concerned about upside risks to inflation and inflation expectations, both due to domestically driven price pressures and those caused by the Iran war.

The RBA Governor suggested that the Board may now pause its hiking cycle to see how the conflict develops and wait for other key data. Investors expect the RBA to hold rates steady at its June meeting but think one more rate hike is likely towards the end of this year.

Since the RBA's decision, economic data has been on the weaker side. Labour market data for April was weaker than expected, with the unemployment rate rising to 4.5%, from 4.3%, and employment falling. Looking through monthly volatility, the trend unemployment rate was steady, and trend employment rose. This suggests that there could be some noise in the data, though the fact that consumer and business confidence remains weak suggests that there are downside risks to the labour market.

The housing market has also weakened noticeably over the past few months as confidence in the outlook has been dented by the Iran war, higher inflation, and rising interest rates. House prices have declined in Sydney and Melbourne in recent months, and auction clearance rates have fallen sharply. The housing tax changes announced in the 2026/27 Federal Budget have heightened uncertainty around the outlook for the housing market.

Strong investment in data centres has supported business investment and construction activity, particularly in NSW and Victoria. Renewable energy projects have also supported activity. However, outside of these sectors, business investment has remained weak.

Financial market commentary

Shifting sentiment about the outlook for the Iran war drove volatility in markets, but it was a positive month overall for equity investors in most markets.

Equity markets (performance in local currency, excluding dividends)

Most equity markets rose in May on hopes that the Iran war could soon end and continued strength in AI-related sectors. The MSCI All Countries excluding Australia rose by 4.4% and the MSCI Emerging Markets index gained 9.5%, with the latter supported by strong gains in Taiwan and South Korea's stock markets because of AI related demand. The US S&P500 rose 5.1% in May, with the tech sector outperforming and the Nasdaq index rising over 8%.

Japan's equity market also rose strongly in May (+12%), supported by strength in AI demand, a weaker yen and lower oil prices (as Japan is a major energy importer). This has seen Japan's equity market rise by over 30% since the start of this year, with an additional boost from the expected fiscal easing.

The ASX200 rose 0.8% in May, supported by continued strong gains in resources companies. Banking stocks weighed on the market, however, with concerns that the Federal Government's proposed changes to capital gains tax and negative gearing will weigh on an already-softening housing market (as around two-thirds of lending by Australia's 4 major banks is for housing).

Bond yields

Bond yields fell in Europe, the UK and Australia alongside the decline in oil prices. Australian 3-year and 10-year bond yields fell by 29bps and 23bps, respectively, with weaker domestic economic data causing investors to pare back expectations for further RBA rate hikes.

In contrast, US 10-year bond yields rose by 6bps, as US economic data continues to point to a resilient economy and elevated inflation.

The spread between 10-year TCorp bonds and Australian Commonwealth Government bonds was little changed in May, at 59bps.

Currency and commodity markets

Optimism about an imminent deal between the US and Iran saw the Brent crude oil price fall by 19% in May, to US\$92 per barrel – its lowest level since mid-April. The spread between prices of refined fuels and oil (e.g. diesel, jet fuel) narrowed in May, though remains elevated.

Moves in currency markets were small in May. The Australian dollar depreciated by 0.2% against the US dollar and has traded in a narrow range over the past month. The Japanese Yen rose by 1.7% against the US dollar, with Japanese authorities suspected to have intervened in the market to support the Yen during the month.

Financial market performance

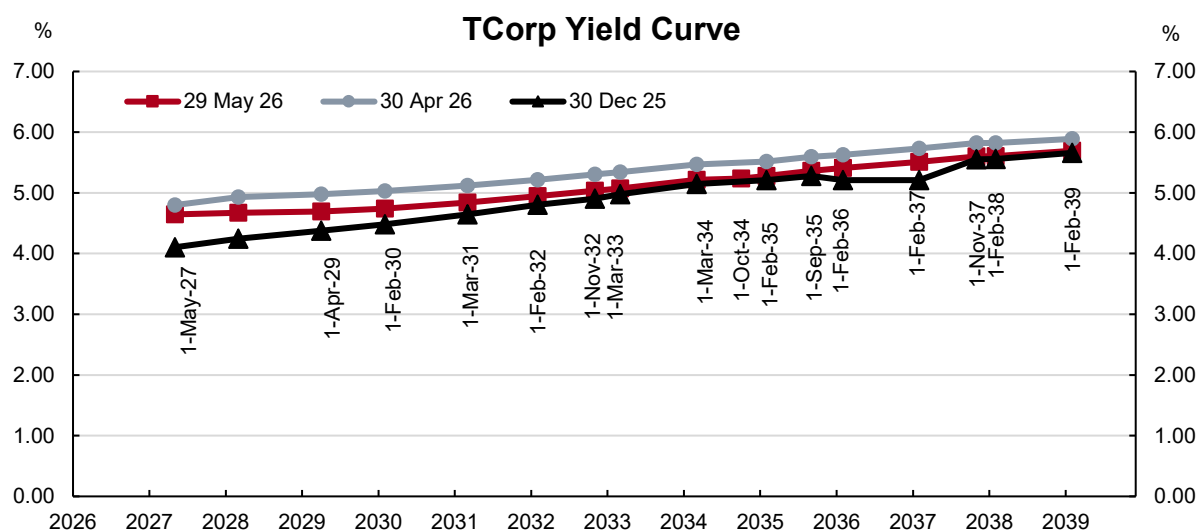
Currency markets May 2026	Previous month close	Month high	Month low	Month close	Month change
AUD/USD	0.720	0.726	0.711	0.719	-0.2% ▼
AUD/EUR	0.614	0.620	0.612	0.616	0.4% ▲
AUD/JPY	112.76	114.57	112.69	114.44	1.5% ▲
AUD/GBP	0.529	0.539	0.530	0.534	0.9% ▲
AUD/BRL	3.568	3.638	3.527	3.618	1.4% ▲
AUD/INR	68.35	69.47	67.94	68.26	-0.1% ▼
AUD/CNY	4.917	4.930	4.841	4.862	-1.1% ▼

Equity markets* May 2026	Previous month close	Month high	Month low	Month close	Month change
MSCI World ex Australia	4795	5007	4780	5007	4.4% ▲
MSCI Emerging Markets	1600	1752	1601	1752	9.5% ▲
S&P/ASX200	8666	8878	8497	8732	0.8% ▲
S&P/ASX Small Ordinaries	3434	3523	3314	3502	2.0% ▲
S&P500 (US)	7209	7580	7201	7580	5.1% ▲
FTSE 100 (UK)	10379	10505	10195	10409	0.3% ▲
Stoxx600 (Europe)	611	632	606	626	2.4% ▲
DAX (Germany)	24292	25389	23951	25105	3.3% ▲
CAC 40 (France)	8115	8299	7953	8183	0.8% ▲
Nikkei 225 (Japan)	59285	66330	59513	66330	11.9% ▲
Hang Seng (HK)	25777	26626	25006	25182	-2.3% ▼
Shanghai Composite (China)	4112	4243	4069	4069	-1.1% ▼
Bovespa (Brazil)	187318	187691	173787	173787	-7.2% ▼
IPC (Mexico)	67858	70246	67284	68588	1.1% ▲
S&P/BSE Sensex (India)	76914	77959	74559	74776	-2.8% ▼

*Returns are in local currency, and exclude dividend payments

Bond markets (%) May 2026	Previous month close	Month high	Month low	Month close	Month change
RBA Official Cash Rate	4.10	4.35	4.10	4.35	0.25 ▲
90 Day Bank Bill	4.37	4.46	4.37	4.46	0.08 ▲
180 Day Bank Bill	4.77	4.82	4.73	4.82	0.04 ▲
New institutional term deposits	4.00	4.20	4.00	4.20	0.20 ▲
3 Year CGS Bond	4.76	4.74	4.48	4.48	-0.29 ▼
10 Year CGS Bond	5.06	5.11	4.83	4.83	-0.23 ▼
10 Year US Bond	4.37	4.67	4.35	4.44	0.06 ▲
10 Year German Bond	3.04	3.19	2.94	2.94	-0.10 ▼
10 Year Japanese Bond	2.53	2.79	2.48	2.67	0.14 ▲

TCorp bonds (%)	Previous month close	Month high	Month low	Month close	Month change
May 2026					
20-May-27	4.80	4.80	4.65	4.65	-0.15 ▼
20-Mar-28	4.93	4.90	4.67	4.67	-0.26 ▼
20-Apr-29	4.98	4.94	4.69	4.69	-0.29 ▼
20-Feb-30	5.03	4.99	4.74	4.74	-0.29 ▼
20-Mar-31	5.12	5.10	4.84	4.84	-0.28 ▼
20-Feb-32	5.22	5.21	4.95	4.95	-0.27 ▼
22-Nov-32	5.30	5.31	5.04	5.04	-0.27 ▼
08-Mar-33	5.34	5.34	5.08	5.08	-0.26 ▼
20-Mar-34	5.47	5.48	5.21	5.21	-0.25 ▼
17-Oct-34	5.48	5.51	5.24	5.24	-0.24 ▼
20-Feb-35	5.52	5.55	5.28	5.28	-0.24 ▼
20-Sep-35	5.60	5.63	5.36	5.36	-0.23 ▼
20-Feb-36	5.63	5.66	5.41	5.41	-0.22 ▼
20-Feb-37	5.73	5.76	5.51	5.51	-0.22 ▼
20-Nov-37	5.82	5.86	5.60	5.60	-0.22 ▼
24-Feb-38	5.82	5.86	5.60	5.60	-0.22 ▼
22-Feb-39	5.89	5.94	5.69	5.69	-0.20 ▼
CIB 2.50% 20 Nov 35	3.04	3.09	2.80	2.82	-0.22 ▼



Source: TCorp

Commodity markets (US\$)	Previous month close	Month high	Month low	Month close	Month change
May 2026					
Brent Oil (per barrel)	114.0	114.4	92.1	92.1	-19.3% ▼
Iron Ore (per tonne)	108.3	111.9	108.3	108.8	0.4% ▲

TCorp forecasts	Jun-26	Dec-26	Jun-27	Dec-27
RBA Official Cash Rate	4.35	4.35	3.85	3.35
90 Day Bank Bill	4.50	4.25	3.75	3.25
10 Year CGS Bond	4.75	4.50	4.00	4.00



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About New South Wales Treasury Corporation (TCorp)

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