Economic Insights

Economics | July 1, 2022

Year in Review. Year in Preview

Financial year wrap 2021/22

Financial Markets: 2021/2022 in detail

Aussie Shares	June 30 2021	June 30 2022	% change
ASX 200	7313.0	6568.1	-10.2
All Ordinaries	7585.0	6746.5	-11.1
Returns on Aussie shares	83786.3	77550.9	-7.4

Global Shares	June 30 2021	June 30 2022	% change
US Dow Jones	34502.5	30775.4	-10.8
US S&P 500	4297.5	3785.4	-11.9
World index (MSCI)	3017.2	2574.5	-14.7

Currencies	June 30 2021	June 30 2022	% change
$US per $A, cents	75.18	68.89	-8.4
Yen per $A	83.07	93.95	13.1
Euro per $A, cents	63.20	65.89	4.3
$NZ per $A	1.0745	1.1088	3.2
Trade weighted index	62.7	61.8	-1.4

Interest Rates	June 30 2021	June 30 2022	% change
Cash rate, %	0.10	0.85	nc
90 day bank bills, %	0.03	1.81	nc
3-year bond yields, %	0.42	3.23	nc
10-year bond yields, %	1.50	3.66	nc

Commodities	June 30 2021	June 30 2022	% change
Iron ore, $US per tonne	218.40	130.00	-40.5
Thermal coal, $A per tonne	134.70	385.95	186.5
Oil, $US per barrel	73.47	105.76	43.9
Gold, $US per ounce	1771.60	1807.30	2.0
Wool, Eastern market indicator	1423.00	1430.00	0.5
Beef, US cents per kg	591.94	600.76	1.5
Wheat, $US cents per bushel	671.50	873.25	30.0
CommSec commodity index	181.4	232.08	28.0

Aussie Assets	June 30 2021	June 30 2022	% change
Return on government bonds	10512.5	9408.1	-10.5
Return on residential property*	246.9	282.5	14.4
Price earnings Aussie shares*	21.11	13.38	nc
Dividend yield Aussie shares*	2.65	4.02	nc
Market size $bn, Aussie shares	2691.0	2459.4	-8.6

Global Perspectives	June 30 2021	June 30 2022	% change
US dollar index	92.4	104.7	13.4
US 10-year bond yield, %	1.48	3.01	nc

* As at May 2022
Source: Reuters, IRESS, CommSec, Bloomberg, CoreLogic

Year in Review 2021/22. Year in Preview 2022/23.

- Now that the 2021/22 financial year is over, it is an opportune time to reflect on the past year and look ahead to 2022/2023.
- Every year has its challenges but the past 12 months has been especially taxing. And a war analogy is especially apt. Across the globe we continued to fight Covid with its various strains such as Delta and Omicron. Then there is the war in Ukraine that commenced in late February. And emanating from both these areas has been the new war against inflation.
- As more people succumbed to Covid (and more lately, influenza) they were forced to stay at home. Production was – and continues to be – impeded, causing supply of goods to fall short of demand and serving to push prices higher – the so-called 'supply-chain' problems. The war in Ukraine also pushed up prices of a raft of goods, especially fuel and energy commodities.
- In recent months, central banks and governments have had to scamper to remove the extraordinarily stimulatory settings that had been put in place at the height of the Covid emergency.
- Earlier in 2022, central banks were uncertain whether the supply-chain problems would prove to be temporary or transitory. But over the past few months, central banks have realised that more concerted, co-ordinated and aggressive rate hikes are now required to address soaring rates of inflation – annual inflation readings that were last seen 40 or 50 years ago.
- As always, there is no certainty that central banks will get it right – that is, get inflation under control and back in designated target bands while avoiding pushing economies into recession.
- Investors will clearly need to be alert in these volatile terms and pivot when necessary.

The Australian Economy

- Overall the Australian economy is well placed to deal with the challenges that lie ahead. In calendar year 2021 the economy grew by 4.8 per cent – the fastest growth in 23 years. And more recently over the year to March 2022 the economy expanded by 3.3 per cent, still well above the 'normal' rate of growth closer to 2.3 per cent.
- Commonwealth Bank (CBA) Group economists expect the economy to grow by 3.7 per cent in the current 2021/22 financial year. Over the next year, economic growth will slow to more sustainable levels as interest rates rise.
- The jobless rate currently stands at 3.9 per cent – the lowest level in almost 50 years. The economy can broadly be described to be at 'full employment'. Wages are starting to rise, especially for those filling new positions or changing jobs. Annual wage growth stands at 2.4 per cent but is tipped to lift to 3.25 per cent in early 2023.
- The annual underlying inflation rate (trimmed mean) is at a 13-year high of 3.7 per cent; and the headline rate of inflation stands a 21-year high of 5.1 per cent. The Reserve Bank Governor expects the headline rate to exceed 7 per cent by the end of calendar year 2022 before starting to ease in the first quarter of 2023.

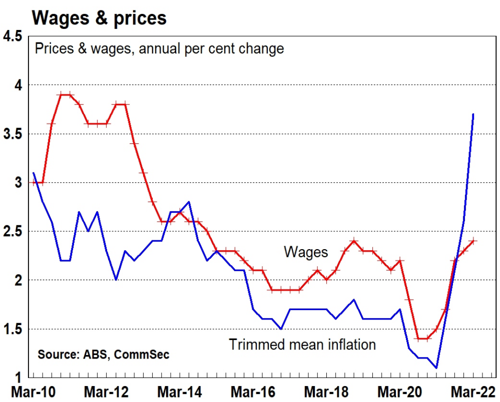
Financial year wrap 2021/22

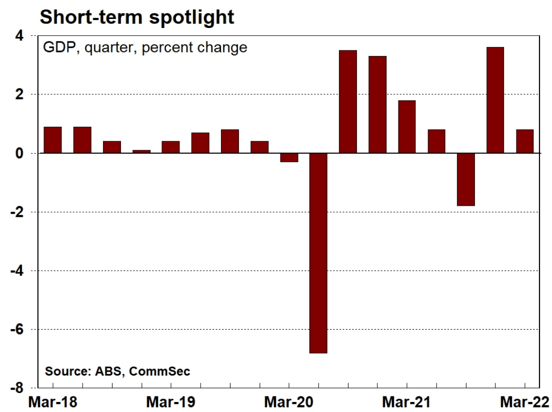
CBA Group Economic Forecasts

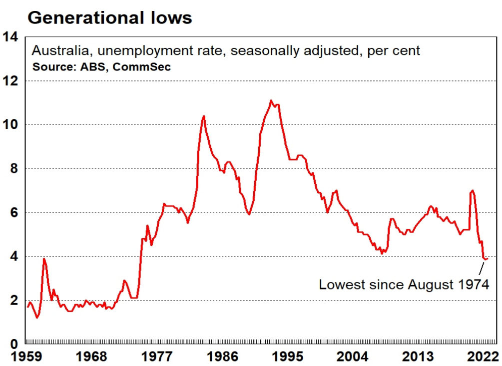
	Financial years			Calendar years		
	2021(a)	*2022*	*2023*	*2021(a)*	*2022*	*2023*
Economic Growth (GDP, %)	**1.6**	**3.7**	**2.9**	**4.8**	**3.5**	**2.1**
Underlying inflation* (annual %)	1.3	3.3	4.0	1.9	4.4	3.0
Unemployment rate % (avg.)	6.2	4.3	3.8	5.1	3.8	4.1

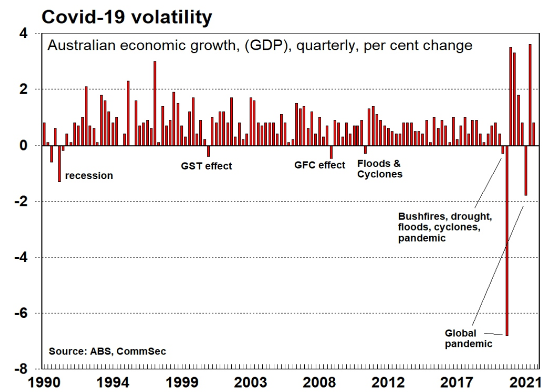
(a) Actual
* Trimmed mean

Source: CBA, CommSec



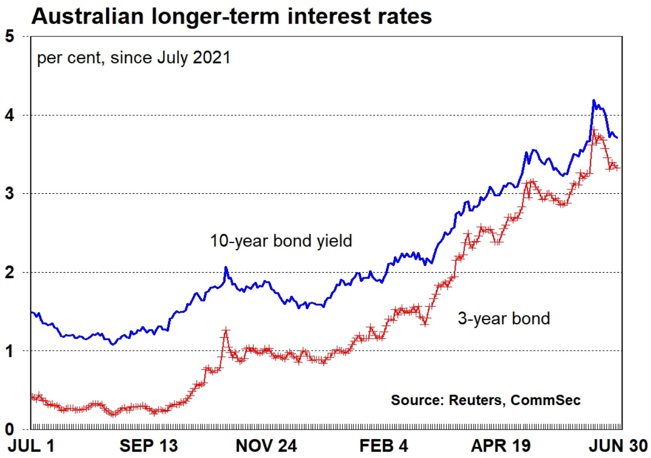


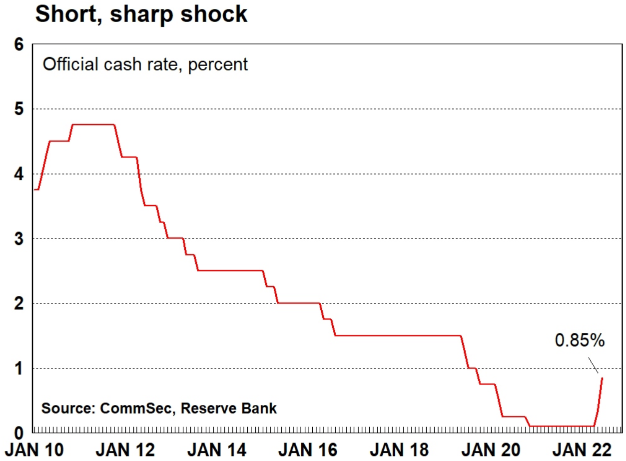


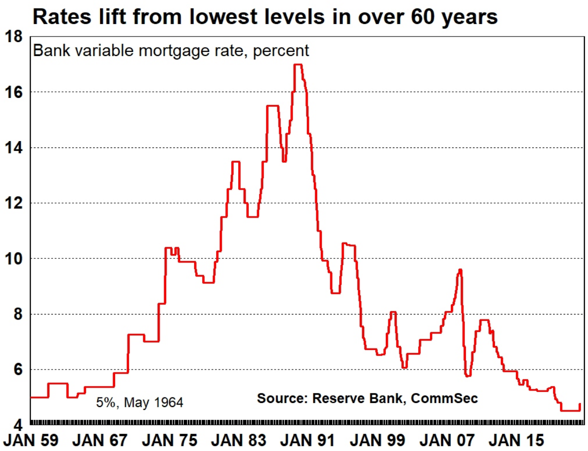


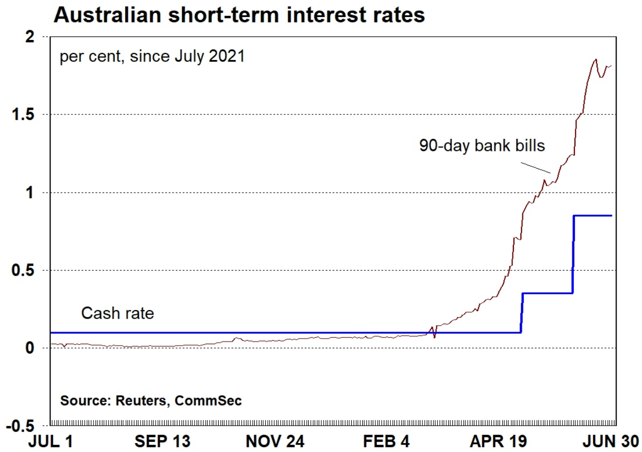
Interest rates

- The era of super-low interest rates is ending. The Reserve Bank (RBA) lifted the cash rate from 0.10 per cent to 0.35 per cent on May 3 – the first increase in 11½ years.
- At the same time RBA Board said that it *"does not plan to reinvest the proceeds of maturing government bonds and expects the Bank's balance sheet to decline significantly over the next couple of years as the Term Funding Facility comes to an end. The Board is not currently planning to sell the government bonds that the Bank purchased during the pandemic."*
- The RBA followed up the May 3 rate hike with an increase of 0.5 per cent on June 7, taking the cash rate to 0.85 per cent. It was the biggest rate hike in 22 years and the first back-to-back rate hikes since May 2010.
- CBA Group economists expect the cash rate to rise to 2.10 per cent over calendar 2022, and perhaps as high as 2.35 per cent. The RBA Governor believes the cash rate could rise as high as 2.50 per cent.
- Ninety-day bank bill yields hit lows of 0.1 per cent on August 6, 2021 and ended June 2022 at 1.81 per cent.
- Ten-year government bond yields lifted from lows of 1.08 per cent on August 23, 2021 to an 8-year high of 4.19 per cent on June 15, 2022 and ended June 2022 at 3.66 per cent.
- The lift in bond yields reflects global and domestic economic recoveries and higher global and domestic inflation. Australia's inflation expectations hit a 14-year high of 6.7 per cent in June. Inflation, the job market and the path of the global economy will determine the direction for longer-term interest rates over the coming year.



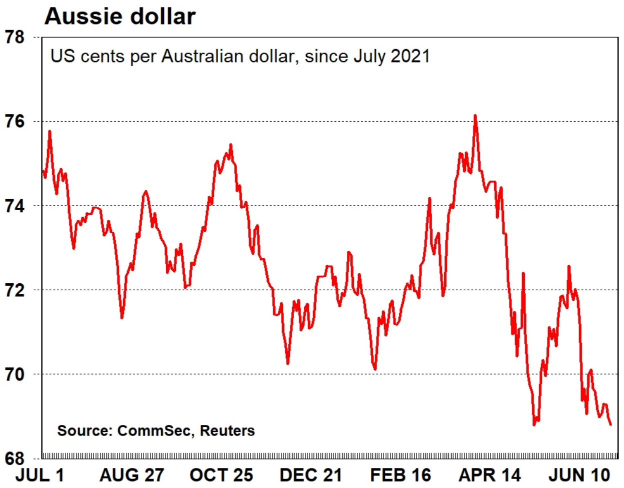


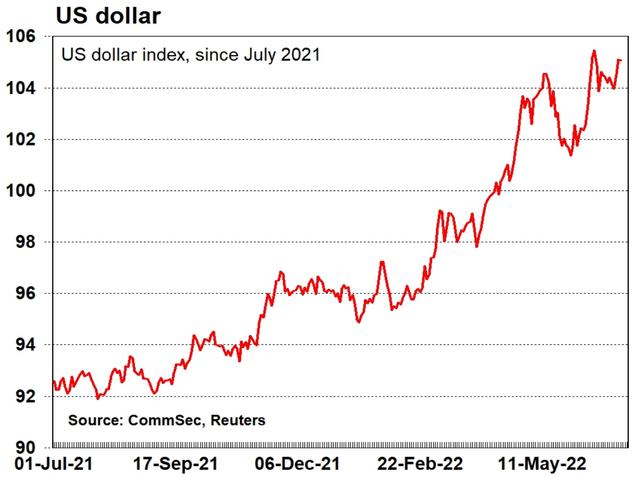


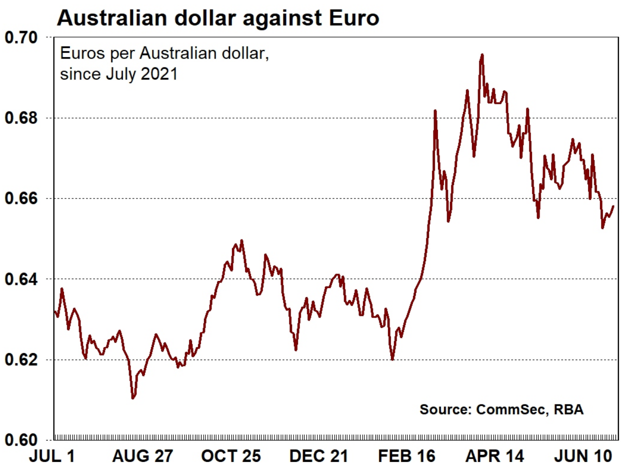


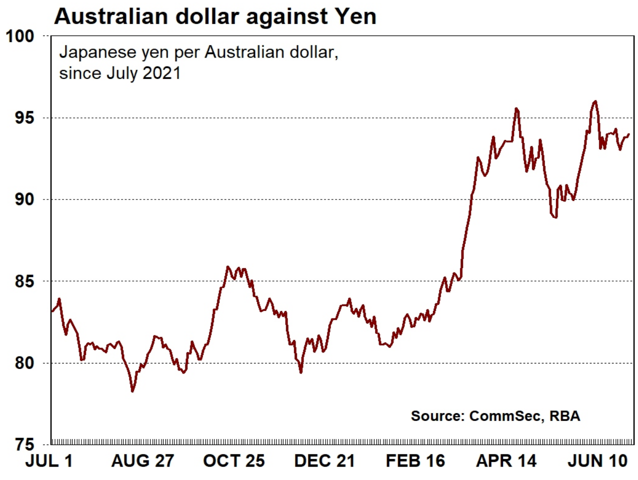
Exchange rates

- The Aussie dollar began the 2021/2022 financial year around US75 cents and ended the year below US69 cents. But it has been a largely directionless year for the Aussie, reflecting fluctuations in factors such as sentiment for the global economy, sentiment on the US dollar, changes in commodity prices, central bank policy settings and the war in Ukraine.
- The high for the year was US76.61 cents on April 5, 2022 and the low occurred just over a month later at US68.27 cents on May 12. On June 30, the Aussie was trading near US68.90 cents.
- While the Aussie lost 8.4 per cent against the US dollar over the year, this reflected a stronger greenback rather than a weaker Aussie. In fact the US dollar index is just off 20-year highs, rising by 13.4 per cent over 2021/22. The Aussie dollar was actually been mixed against other major currencies over the period.
- Over 2021/22 the Aussie dollar rose by 13 per cent against the Japanese yen; lifted 4 per cent against the UK pound and Euro; and rose 3 per cent against the NZ dollar. But the Aussie fell by 5 per cent against the Chinese yuan and the Canadian dollar.
- The weaker Aussie against the greenback occurred despite strong Australian-side fundamentals – solid economy, higher commodity prices, consistent trade surpluses and a record current account surplus. The lower Aussie dollar is providing valuable support for Aussie businesses, especially exporters.



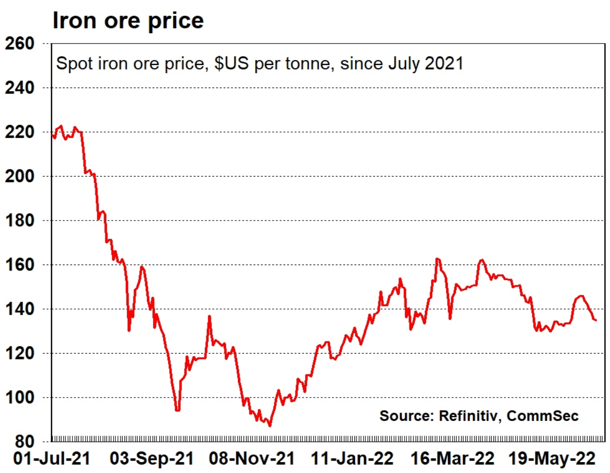


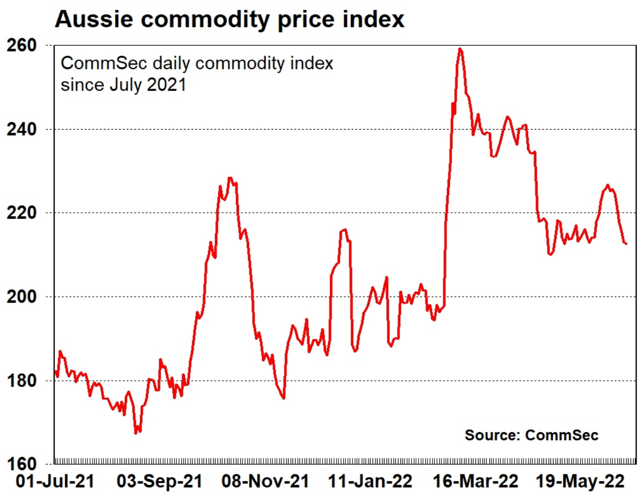


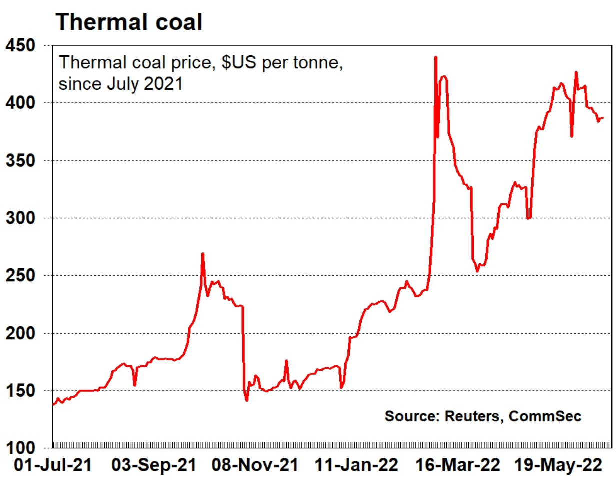


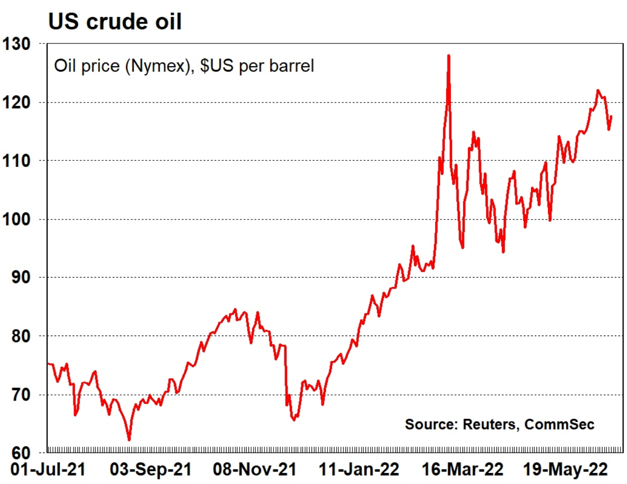
Commodities

- Quite remarkably, the Aussie dollar fell by 8.4 per cent against a stronger greenback over 2021/2022 but at a time of higher commodity prices. While events such as the war in Ukraine have supported the US dollar on its 'safe-haven status, remarkably the higher commodity prices didn't provide a bigger boost to the Aussie dollar.
- The Commodity Research Bureau (CRB) futures index lifted by 36 per cent over 2021/2022. The CommSec daily commodity index rose by 28 per cent over 2021/2022 with broad-based price gains across energy, metals and agricultural commodities.
- Over the year to May the Reserve Bank commodity index increased by 30.4 per cent in SDR terms, led by higher LNG, coking coal and thermal coal prices. The index increased by 33.7 per cent in Australian dollar terms.
- The rise in commodity prices reflects the re-opening of developed economies, boosting demand for raw materials. And the war in Ukraine with supply disruptions lifting prices for a number of commodities such as oil, gas, wheat and vegetable oils. The supply-demand imbalance has increased energy and food prices globally, stoking inflation.
- The slowdown in top consumer China, as a result of a 'zero-Covid' policy, has served to cap commodity prices. But China is expected to maintain stimulatory policies over the coming year to boost economic recovery and this should serve to support industrial-dependent commodity demand and prices.
- While the price of iron ore has continued to recede from the record high of US$233.10 a tonne recorded in mid-May 2021, the current price near US$130 a tonne is still well above long-term average and the US$15-20 a tonne cost of production.
- Over the past year the thermal coal price lifted 186 per cent; natural gas price (Asian buyers) lifted 196 per cent; cotton rose by 40 per cent; crude oil was up 44 per cent and wheat was up by 30 per cent.
- But iron ore has fallen 40 per cent; while base metals like aluminium, copper and lead have fallen by up to 16 per cent.



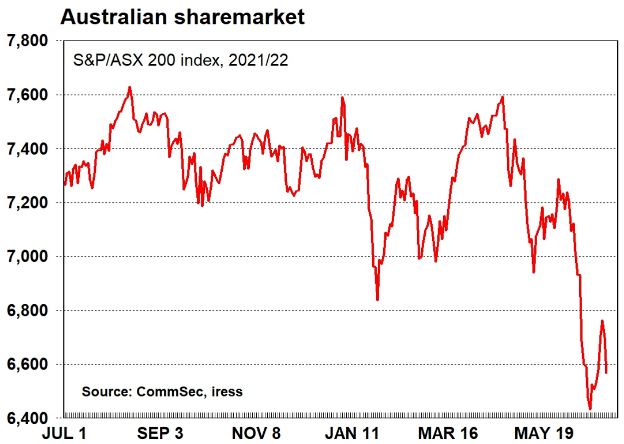


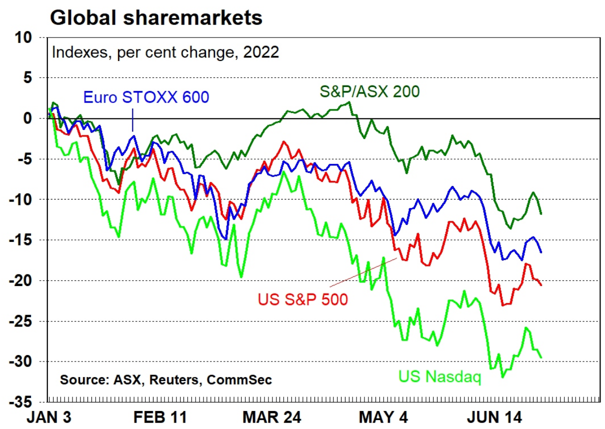


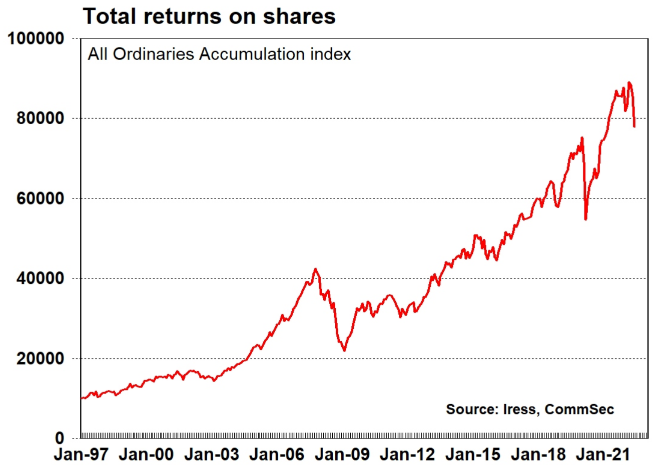


Sharemarkets

- After rising by around 25 per cent in the 2020/2021 financial year, the Australian All Ordinaries index lost 11.1 per cent in 2021/22 while the S&P/ASX 200 fell by 10.2 per cent, just the third financial year loss in the past decade. The indexes also respectively ended 2021/22 down 14.6 per cent and 13.9 per cent from the all-time highs set on August 13, 2021.
- While losses for Australian shares exceeded those in Japan in 2021/22 (down 8.3 per cent) they were in line with mainland European markets (STOXX 600, down 10.1 per cent), and were generally in line with the benchmark US indexes. The US Dow Jones fell by 10.8 per cent over 2021/2022 with the S&P 500 index down by 11.9 per cent while the Nasdaq fell by 24 per cent. But the commodity-linked UK FTSE actually rose by 1.9 per cent.
- The world index (MSCI) excluding Australia in US dollar terms fell by 14.7 per cent in 2021/2022 after soaring 37 per cent the previous year. The MSCI Australia index in US dollar terms fell by 15.5 per cent in 2021/2022 after rising 35.3 per cent in the prior year.
- Total returns on Australian shares (All Ords Accumulation index) fell by 7.4 per cent over 2021/2022 after rising 30.2 per cent in the prior year. The cash rate ended the 2021/2022 year at 0.85 per cent while bond returns (Bloomberg AusBond Govt 0+ Yr index) fell by 10.5 per cent over the financial year. But residential property (CoreLogic Home Value index) returned 14 per cent in the year to June.
- Australia's Utilities sector out-performed in 2021/22. The Utilities sector lifted by 29.3 per cent over 2021/2022, ahead of Energy (+24.5 per cent) and Industrials (+0.8 per cent). They were the only sectors that rose over the year. At the other end of the scale, the interest rate sensitive Information Technology shares fell by 38.7 per cent while Consumer Discretionary shares lost 22.8 per cent with Real Estate shares 15.9 per cent lower
- Of the ASX index size groupings, the S&P/ASX50 out-performed (down 8.6 per cent), followed by the S&P/ASX20 (down 9.9 per cent); the MidCap50 (down 10.8 per cent); and the Small Ordinaries (down 21.6 per cent).







Outlook

- As noted earlier, the Australian economy may have grown by 3.7 per cent in 2021/22. CBA Group economists expect a slower 2.9 per cent expansion over 2022/23 in response to higher interest rates and slower consumer spending. But growth is still expected to exceed the decade average or 'normal' rate of growth.
- The jobless rate is expected to average around 3.8 per cent over the remainder of 2022 but lift to 4.2 per cent in September quarter 2023. Effectively the economy should continue to operate at 'full-employment'. In response to the tight job market, wage growth will lift to around 3.25 per cent by March quarter 2023 from current annual growth near 2.4 per cent.
- The headline inflation rate is tipped to lift to 6.2 per cent in the year to the September quarter 2022 (annual growth stands at 5.1 per cent currently). The underlying rate of inflation is tipped to hit 4.7 per cent over the same period (from 3.7 per cent currently) and is expected to return to the target range in June quarter 2023.
- After lifting 21 per cent over 2021, Australian home prices are tipped to fall by 6 per cent over 2022 and then fall a further 8 per cent in 2023. Sydney and Melbourne are expected to lead the falls in 2022 with Adelaide and Brisbane down the most in 2023.
- At the start of the year we forecast modest 5 cent growth of the Australian sharemarket over 2022 after the stellar gains of the previous year. But even these relatively downbeat views have proved too optimistic. Faced with soaring inflation, central banks have adopted more aggressive policies to wind back the Covid period stimulus.
- The Aussie sharemarket is tipped to fall by 7-9 per cent in 2022; lift 7-9 per cent over 2022/2023; and rise 5-8 per cent over calendar 2023. Australian companies are well cashed up with profits at record highs. Companies are choosing to pass on higher costs to consumers but they will find it harder to do so as interest rates rise further and spending growth slows. With margins pressured, earnings expectations are likely to adjust lower as growth slows. But cheaper valuations, attractive dividend yields and Australia's likely relative economic outperformance is supportive of local shares.
- After lifting 6.4 per cent in 2021, CBA Group economists expect the global economy to slow to 3.1 per cent in 2022 and to 2.2 per cent in 2023 ("average" world growth is near 3.7 per cent). CBA Group economists "*expect Western central banks to tighten monetary policy well into 'restrictive territory'. As a result, we expect the global economy will slow significantly in 2023, particularly in the west".*
- CBA Group currency strategists expect the Aussie dollar to hold broadly between US60 cents and US70 cents over the coming year. The Aussie is tipped to ease to lows near US62 cents in the first half of 2023 before recovering to US66 cents by December quarter 2023.

Financial year wrap 2021/22

Sectors performance

Percent change

Utilities	29.3
Energy	24.5
Industrials	0.8
Consumer Staples	-2.2
Materials	-8.6
S&P/ASX50	**-8.6**
S&P/ASX100	**-8.9**
Telecom	-9.2
S&P/ASX20	**-9.9**
S&P/ASX200	**-10.2**
Health Care	-10.6
MidCap50	**-10.8**
All Ordinaries	**-11.1**
Financials ex Prop Trusts	-11.3
Financials	-11.3
Property	-15.4
Small Ordinaries	**-21.6**
Consumer Discretionary	-22.8
Info Technology	-38.7

Source: IRESS, CommSec

CommSec

Financial year wrap 2021/22

CBA Group Global Forecasts	*2020*	*2021*	*2022*	*2023*
World	**-4.9**	**6.1**	**3.1**	**2.2**
US (Dec qtr vs Dec qtr)	-2.6	5.2	1.3	0.4
Eurozone	-7.3	5.4	3.1	0.5
Japan (fiscal year)	-5.9	2.5	1.0	0.3
China	2.3	7.9	3.8	4.6

Source: CBA, CommSec

CommSec

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