Economic and Market Commentary June Quarter 2024

Overview

Large cap global equities performed well again this quarter, but performances elsewhere were quite mixed.

The AI boom thematic continued into the June quarter. International equities again increased, but gains were concentrated in the large cap tech sector. Short-term credit also performed well, but elsewhere returns were negative or more subdued. NZ and Australian equities, global small caps and international property, for example, all fell over the quarter (see Figure 1).

As in our previous update, on the economic front the US economy remains a bright spot, but there are now also increasing signs of activity picking up - or at least stabilising - in other key economies and regions, including China and the EU. Inflation has also continued to trend down globally, to the extent that some central banks have begun to cut interest rates, including the ECB and Bank of Canada. New Zealand – unfortunately - remains a glaring exception. Data releases suggest that we remain in recessionary-like conditions, but despite this, the RBNZ has maintained its relatively hawkish stance.

Market roundup

Gains were strongest in US equities over the past year, reflecting the relative strength of the US economy and the AI boom underway. NZ equities have performed poorly as rates have stayed high and corporate earnings have taken a hit.

Asset class performances were mixed in the quarter. Global equities again rose, by around 3% on an NZD hedged and local currency basis, bringing the annual returns to over 20%. Emerging markets performed in line with global equities. Under the surface equity market performances were much more mixed. Global small cap stocks fell by around 2% in local currency terms, while global value and the Australian equities both fell by around 1%.

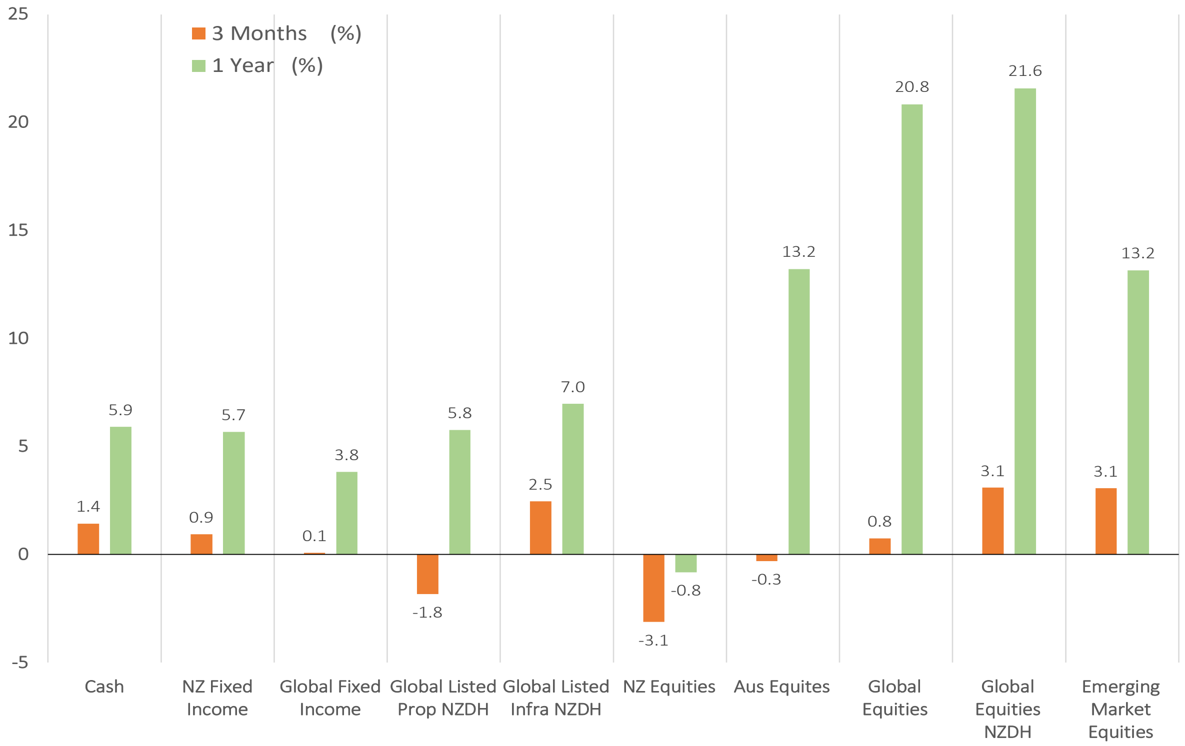
Trailing the pack, NZ equities fell around 3% over the quarter and 1% over the year to June. Most of the largest stocks on our market are utility and infrastructure-type investments sensitive to NZ economic growth and interest rates. While rates remain high and growth very weak our market will likely continue to struggle. Figure 2 suggests that the decline in corporate earnings in our market since the post-Covid peak in early 2022 has been *larger* than falls seen over the GFC period.

Listed global property fell around 2% while global infrastructure increased by 2.5% on an NZD hedged basis. Over the year, these asset classes have returns around 6% and 7% respectively. Bond performances were also mixed. New Zealand investment grade bonds increased 0.7% in the quarter and 5.2% over the year, but within this government bonds, which are longer duration, returned around 4.7%, while corporate bonds returned 6.3%. International investment grade bond returns were flat this quarter as they suffered from the marked-to market impact of markets pricing in delays to interest rate cuts, particularly in the US. But short-term credit and high yield performed very well, with funds that allocate to these asset classes returning around 2.5% in the quarter and in some cases over 10% (net of fees) for the year.

Diversification as always remains essential across markets and asset classes.

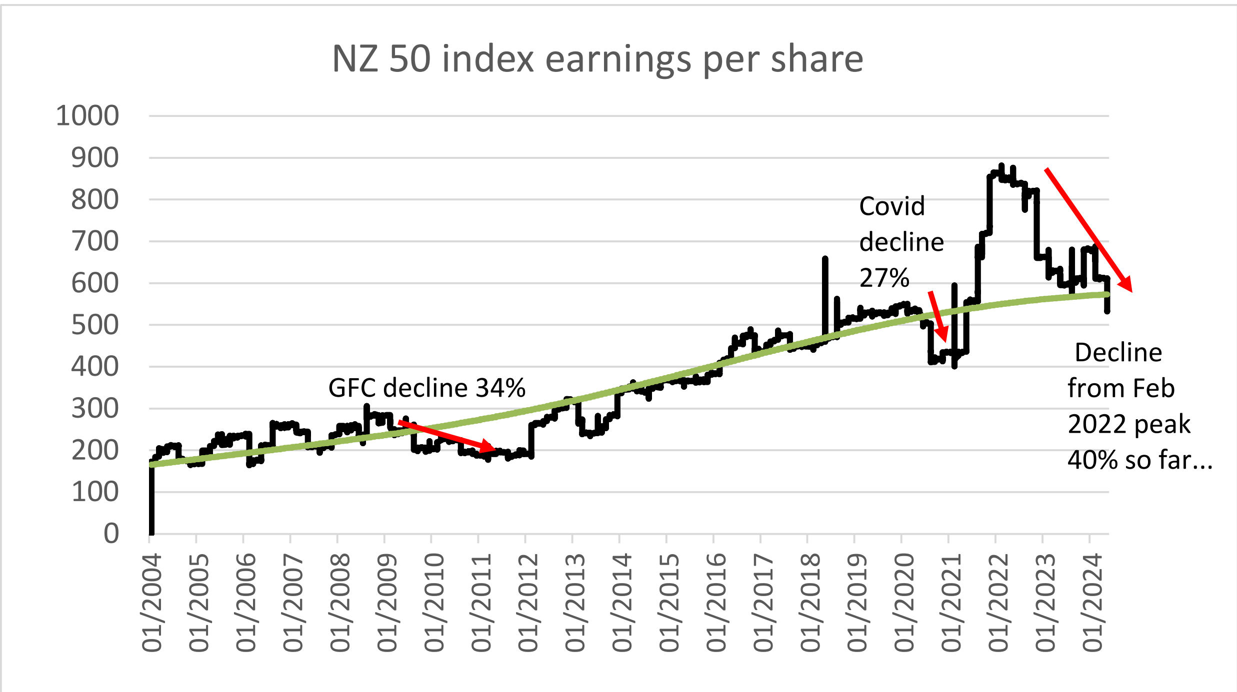
As always, the mixed performances of markets argues for ensuring portfolios remain well diversified. While large cap growth stocks are in vogue now, any shortfall in their earnings could well precipitate a large correction. While NZ stocks are out of favour, they are interest rate sensitive and as such they are primed to rally when the RBNZ joins its international peers in cutting rates.

Figure 1: Mixed performances in the June quarter



Source: Morningstar Direct, MyFiduciary

Figure 2: Large decline in NZ listed corporate earnings



Source: Datastream, MyFiduciary