Can markets avoid recession? The September 2023 Quarterly Market Update

By Perpetual Wealth Management

18 October 2023

In the September 2023 Perpetual Private Quarterly Market Update we take a look at how the market is adjusting as monetary policy continues to take hold. You can download our full report – or read our concise review below.

Please note: except where otherwise noted or quoted, the views in this article are those of Perpetual Private's investment team.

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September Quarter 2023: What happened?

- Having enjoyed an environment of increasing optimism, Australian shares had a challenging quarter. Although momentum carried markets higher in July, they softened through August and September, returning -0.7% over the three months.
- International shares followed an almost identical path to that of their Australian equivalents in the three months to September. An upbeat July, followed by a complete

retracement over the following two months, saw international equities lose 0.4% over the quarter.

- As enthusiasm for large tech companies began to wane, the NASDAQ dropped -3.9%. The less technology-focused S&P 500 proved to be mildly more resilient (-3.4%).
- The domestic bond market returned -0.72% during the September 2023 quarter, while international fixed income returned -0.46%. Credit outperformed the general market, especially high yield debt, which returned 3.3% for the period.

(Indices referenced: MSCI AC World, S&P/ASX 300, Bloomberg Global Aggregate index, Bloomberg AusBond Composite (0+Y) index. All performance numbers to end September 2023 quarter unless otherwise stated).

"Spring is the time of year when it is summer in the sun and winter in the shade" Charles Dickens

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It has been an eventful eighteen months. After the negativity of 2022, the September 2023 quarter was typified by further swings in sentiment and valuations, as markets and economies continue to adjust to the new monetary landscape. The period started with positive momentum as investors marvelled at the power and potential of artificial intelligence. However, as economies and, more importantly inflation, continue to be resilient, appreciation that interest rates would truly be 'higher for longer', led to a lurch downwards across asset markets.

Perpetual Private Investment Director, Andrew Garrett, says the current volatility is not unusual.

"We expect this to continue for some time, as markets come to terms with the new economic reality. However, we do expect as we enter the new year to progressively get greater clarity of the true path ahead for investment markets," he says.

We suggested in our June quarter market update that the supply side of the inflation shock may be behind us, but the escalating circumstances in the Middle East may lead to a much larger regional conflict that affects energy prices and pushes inflation higher for longer.

Inflation calms, but the pressure on consumers increases

The September quarter marks the first extended pause in interest rate increases since the Reserve Bank of Australia (RBA) began tightening in May 2022. Current expectations for inflation returning to the 2-3% target range, according to the bank's own forecasts, currently sit in the closing months of 2025.

This suggests the heavy lifting by the central banks has largely been completed. Even so, Australian average household disposable income is contracting at the fastest rate for 30 years. However, both labour markets and consumer behaviour remain at odds with the pressure on disposable income.

Broad trends begin to engulf global investment market

The current trend of deglobalisation appears likely to be a feature of international markets going forward, affecting supply chains, reducing the benefits of specialisation and scale, and effectively placing a rising floor under inflation.

China faces significant internal challenges. Anaemic consumer confidence, a rapidly decreasing population, and the significant structural and oversupply problems faced by the local real estate industry could act as a challenging headwind for the Chinese economy in the years ahead. It remains to be seen what effect this will have on global growth outlook.

Can the US engineer a soft landing?

The US economy could still avoid a recession, but it's hard to be confident about it. The possibility of a recession was strong at the start of the year and, historically, soft landings are difficult to achieve given the variable lag that comes with the implementation of any monetary policy.

The expected negativity of the 2024 presidential election is also very likely to feed into the drivers of volatility and will not help against heightened levels of economic uncertainty.

Petrol prices continue to fuel interest rates

The geopolitical conflict in the Middle East will inevitably lead to a tightening of energy markets.

We are already experiencing price spikes at the petrol pumps. Oil prices gained 22.3%[1] between June and October, and buoyant consumer behaviour has tightened the market for energy prices.

Rising oil prices are historically associated with recessions over the last 50 years due to their tendency to inflate costs within and across the supply chain, as well as more indirect

inflationary effects. If the current price spike holds, central banks will focus on bringing inflation down and will have less ability to reduce interest rates anytime soon.

[1]Measured by Brent Crude (continuous)

Opportunities from volatility

The current market is a stock-picker's market, presenting bottom-up fundamental managers with opportunities to deploy capital to quality and possibly oversold companies at more attractive valuations as markets gyrate.

"From our point of view, it really is the kind of environment in which you need to do extra work, because that extra work you do today will set you up for the next few years," says Andrew Garrett.

"For us, it's an environment rich with opportunity."

Perpetual Private's Quarterly Investment Update for September 2023 covers the changing nature of investment dynamics and looks at the outlook for shares, fixed income, real estate, currency and alternatives.

Download the report

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