Global economic impacts, China and the failing power sector. What does it all mean?

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Important information

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Global economic impacts

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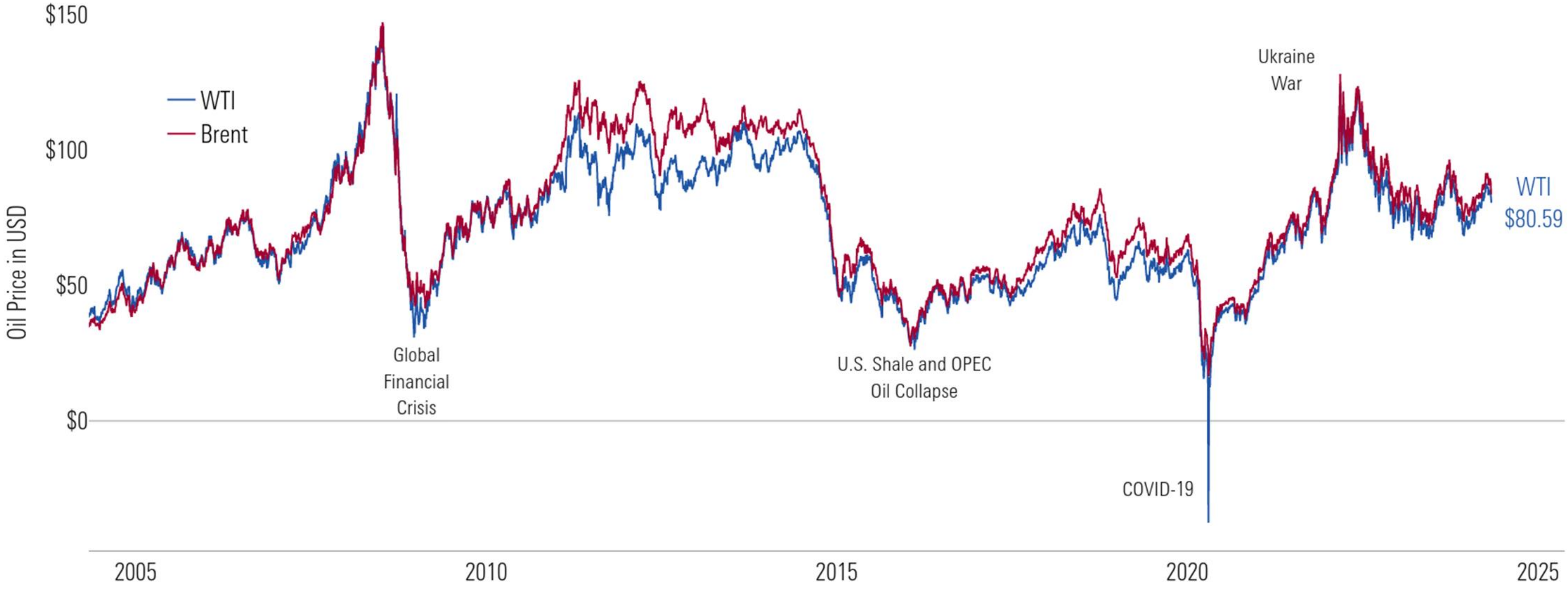
Global Oil Prices

WTI and Brent Crude

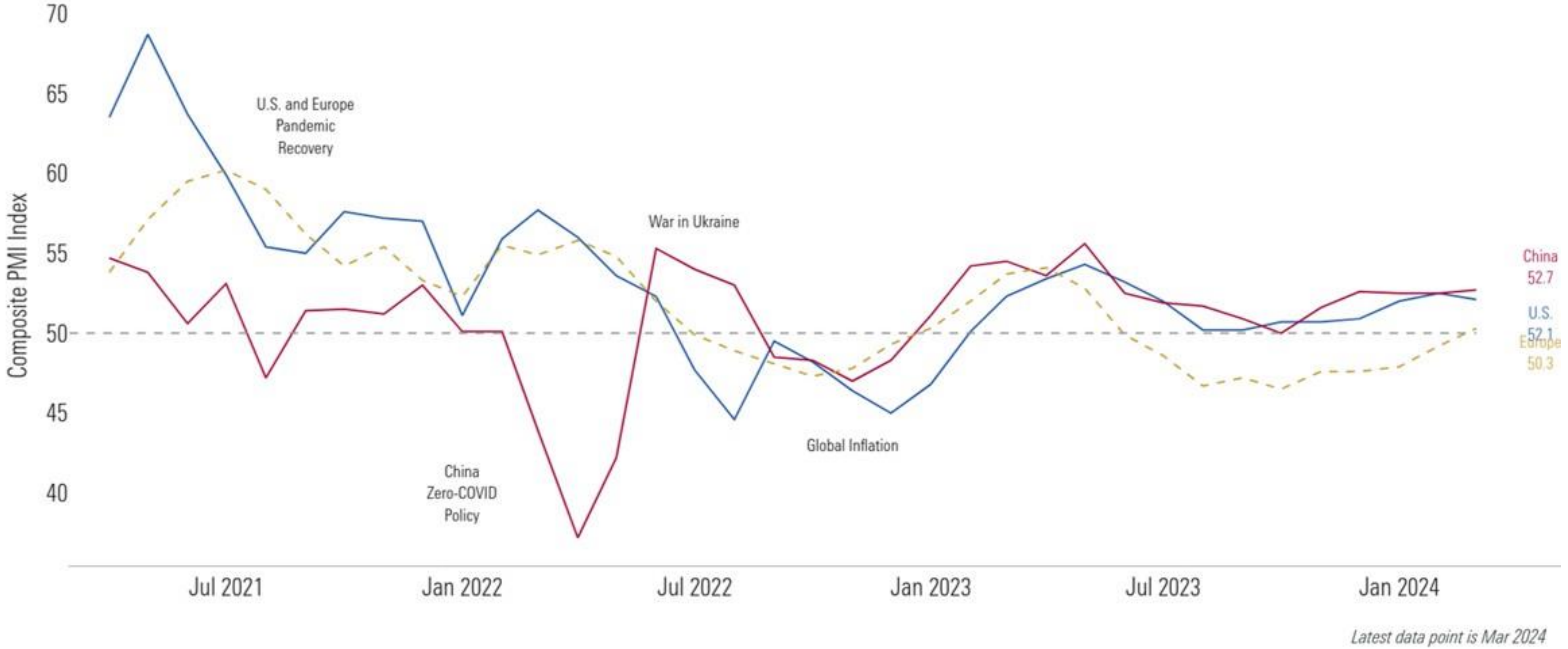


Latest data point is May 3, 2024

Source: Clearnomics, LSEG

Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. References to specific asset classes should not be viewed as a recommendation to buy or sell any specific security in those asset classes.

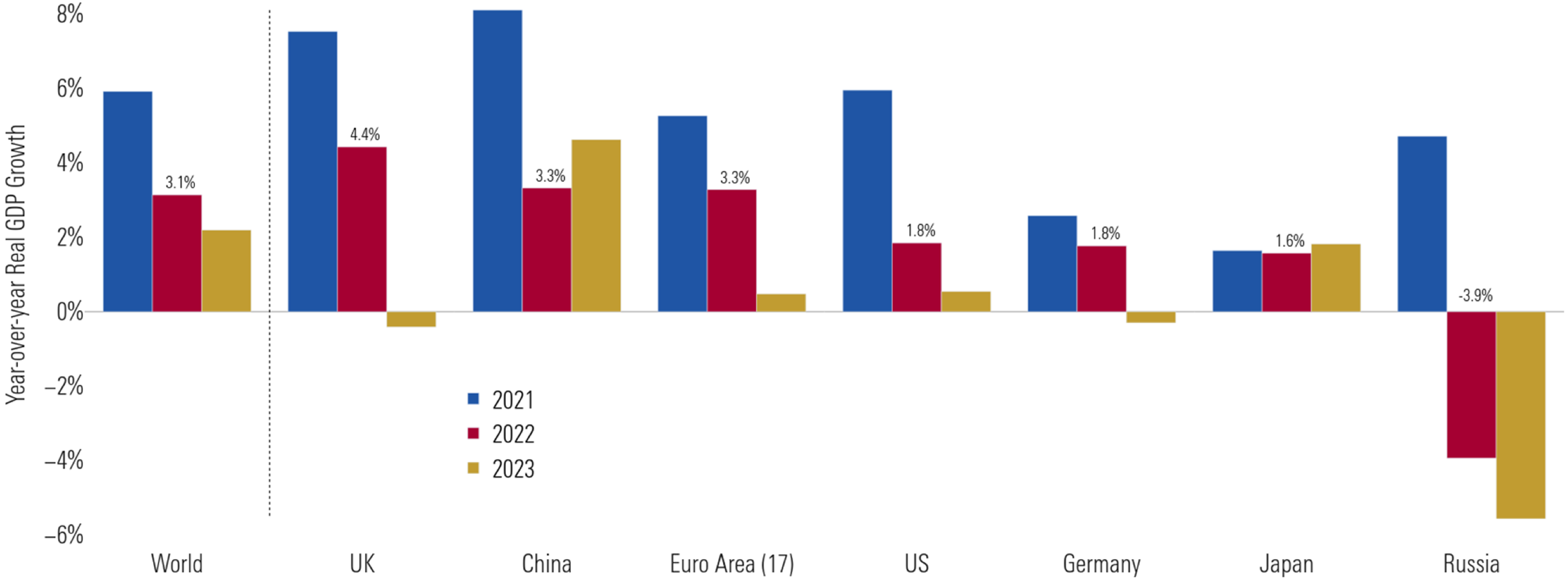
U.S., China, and Europe Composite PMIs. Numbers above 50 represent expansion.



Source: Clearnomics, Bloomberg, Standard & Poor's

Global GDP Growth Forecasts

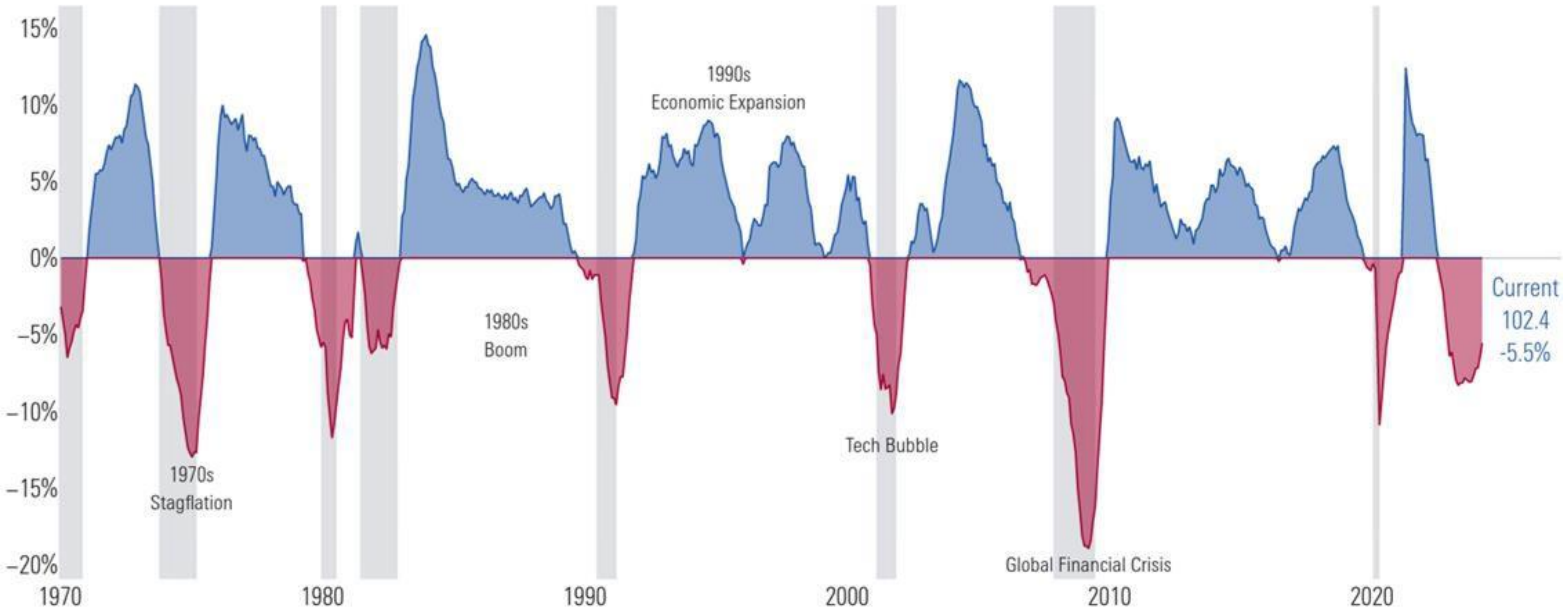
OECD Real GDP Growth, Actuals and Forecasts



Source: Clearnomics, OECD

This is for illustrative purposes only.

Conference Board LEI Year-over-year Percent Change

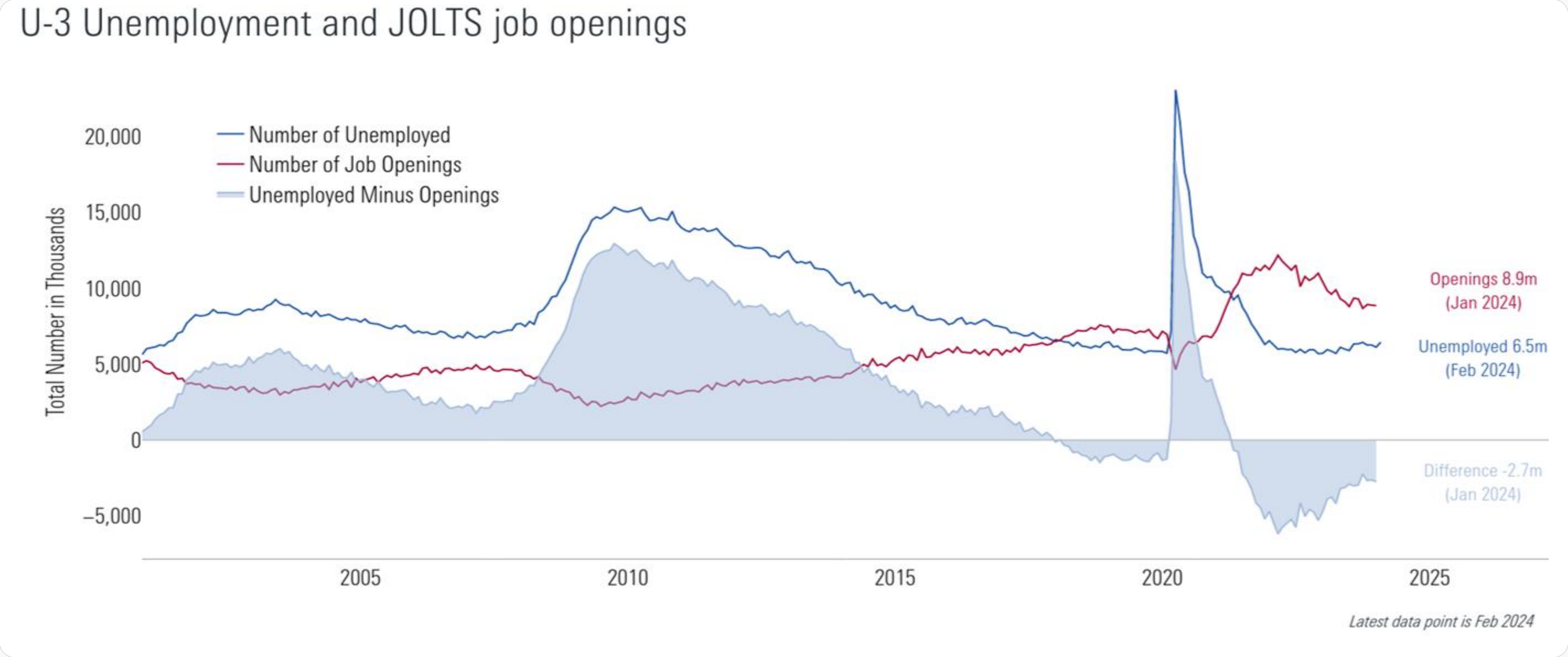


Latest data point is Mar 2024

Source: Clearnomics, Conference Board, NBER, LSEG.

Labour Market

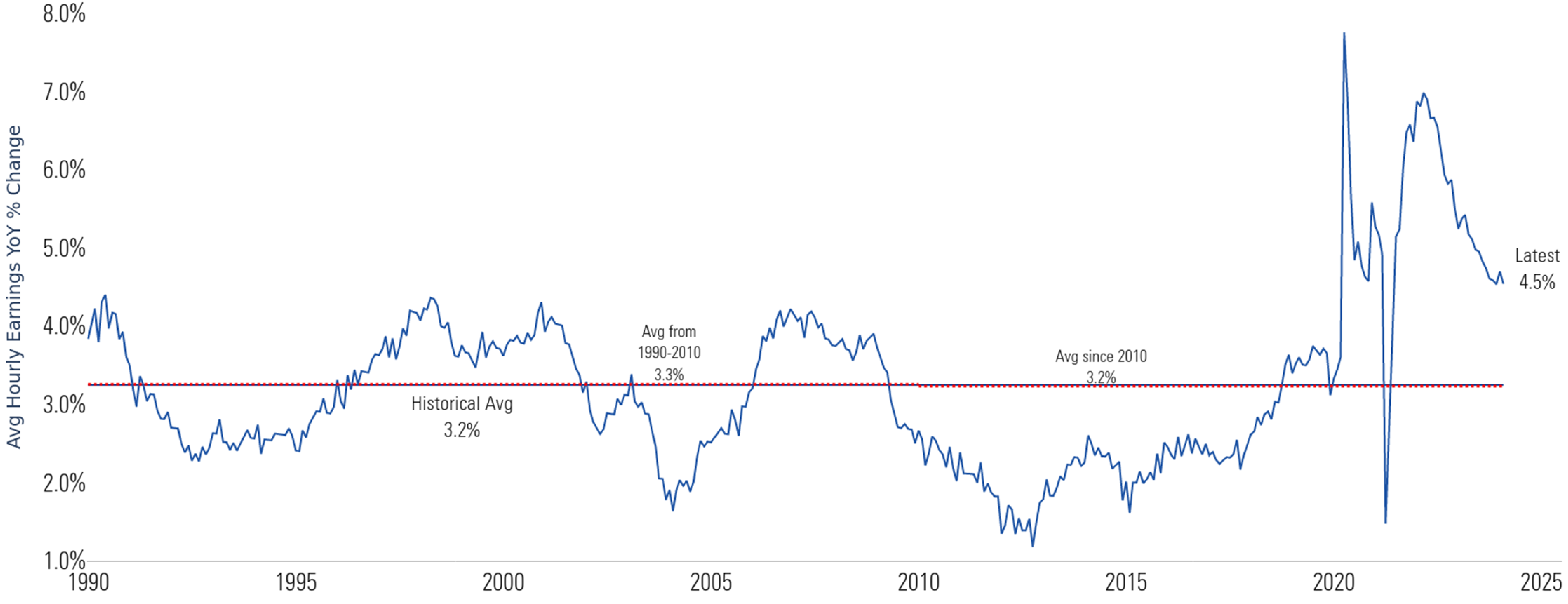
Falling job openings signals potential weakening.



Source: Clearnomics, Bureau of Labor Statistics.

Wage Growth

Year-over-year Change, Production and Non-Supervisory Employees



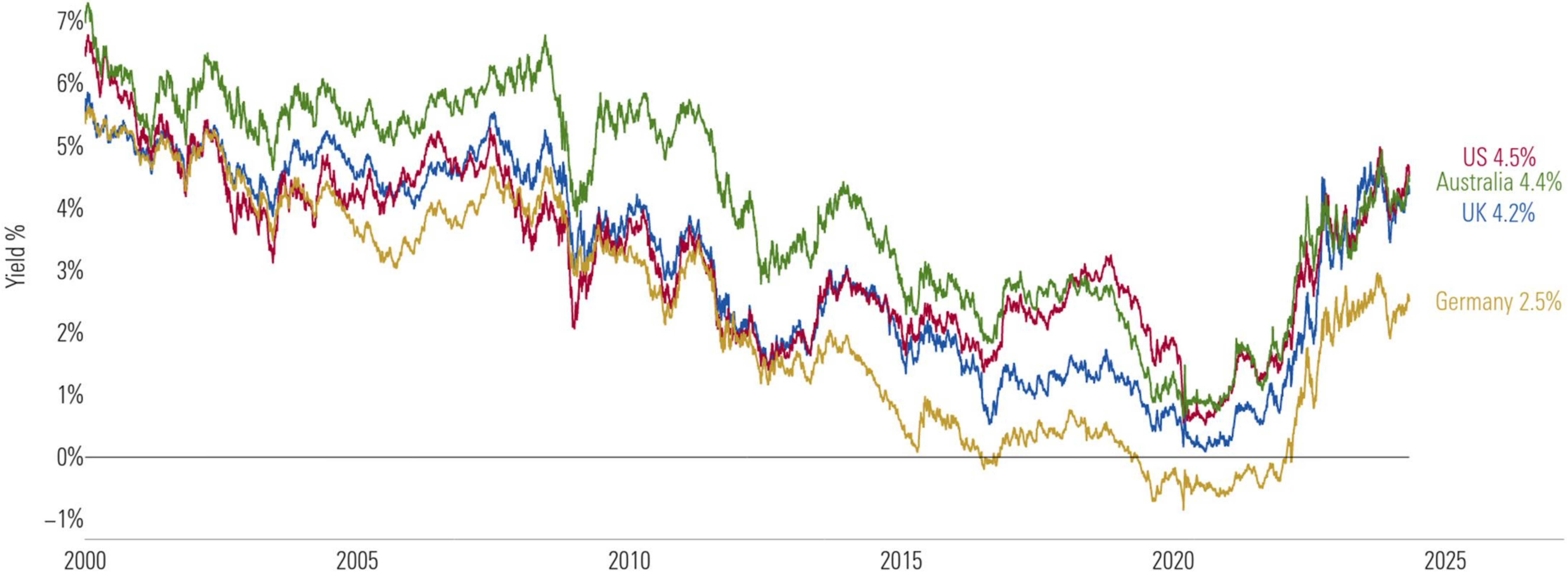
Latest data point is Feb 2024

Source: Clearnomics, Bureau of Labor Statistics

This is for illustrative purposes only.

Interest Rates vs. Major Countries

10-Year Government Bond Yields



Latest data point is May 3, 2024

Source: Clearnomics, Bloomberg

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What is happening in Australia?

Inflation and interest rates in Australia

Persistent but gradually falling inflation

- Annual CPI inflation 3.6% in March 24 quarter (down from 4.1% in Dec 23)
- Money markets pricing in almost 50% chance of late-2024 interest rate rise and possibly no interest rate cuts before May 25 election
- Latest May 24 RBA forecast inflation to return to target 2-3% p.a. in the second half of 2025
- Persistence of services inflation is a key uncertainty, reflecting stronger labour market conditions and gradual increase in unemployment
- Inflationary state and federal budgets

www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release
www.rba.gov.au/media-releases/2024/mr-24-08

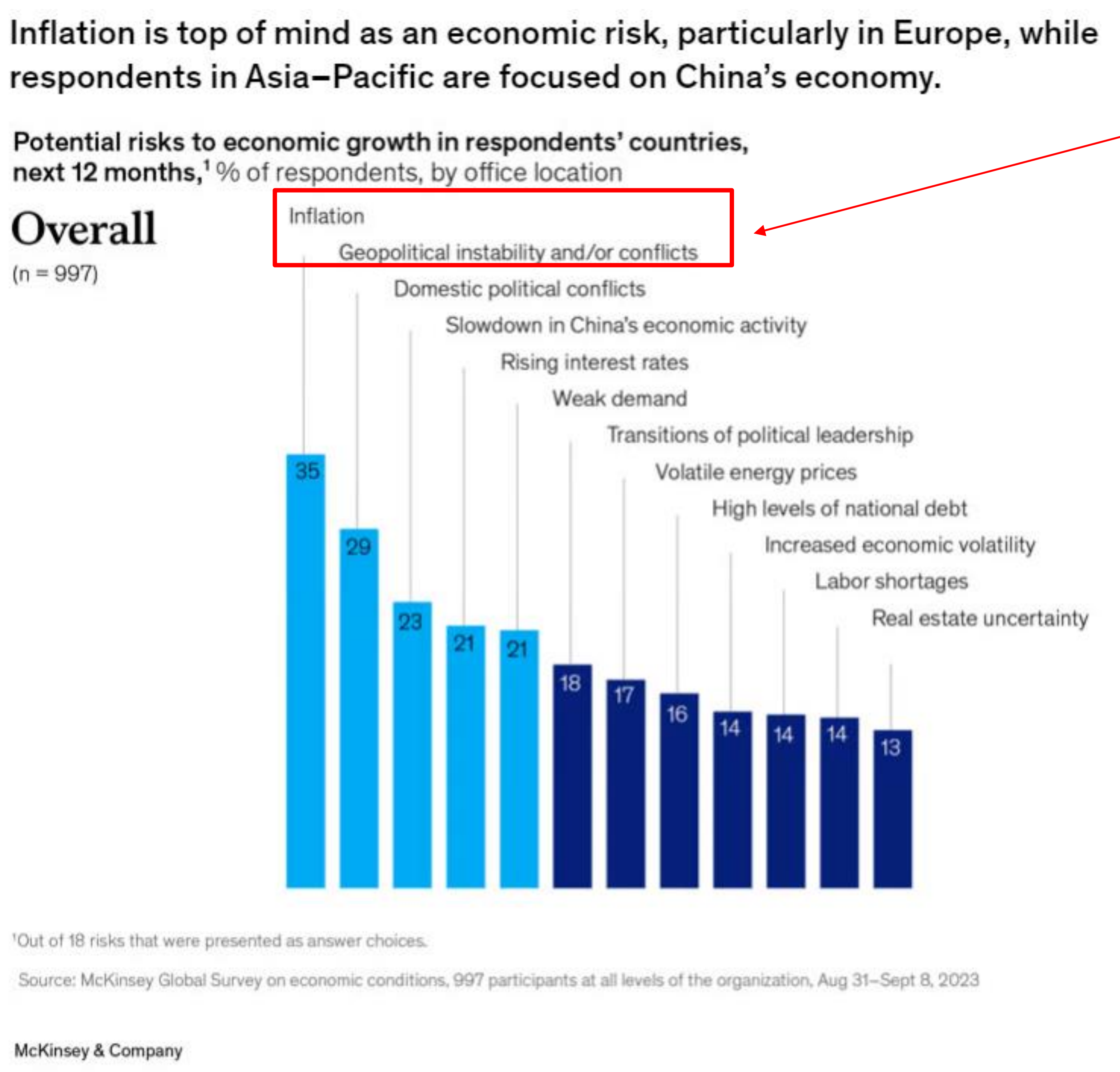
Some observations on the Federal budget

- $7.8 BN cash splash will be inflationary and make the RBAs job much harder
- A return to bigger spending, higher taxing government with large future deficits
- Designed to win votes – perhaps an early election?
- Usual nonsense around efficiency and quality of spending
- Questionable ‘Future made in Australia’ policy has been allocated over $27 Bn of taxpayers money spent on ‘winners’ picked by the Government – solar panels and Hydrogen??
- Decent investment of $6.2 Bn in housing supply supported by increased training for tradies and higher levels of trade skilled immigration

www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release
www.rba.gov.au/media-releases/2024/mr-24-08

What about China?

Globally, inflation is viewed as the major risk to economic growth



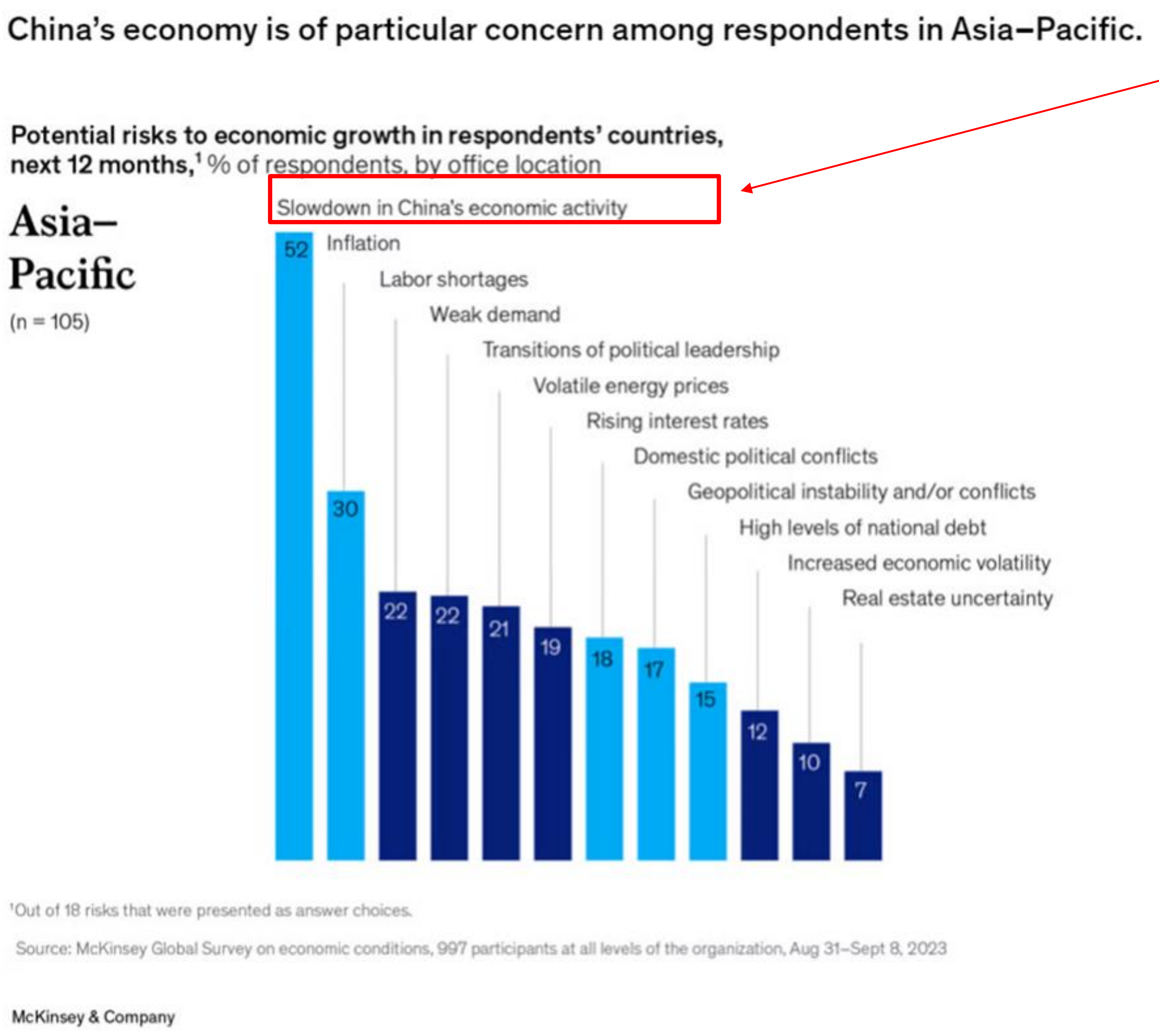
McKinsey

Top 2 risks to economic growth globally:

- Inflation
- Geopolitical – Taiwan, Ukraine, Middle East

Inflation is top of mind as an economic risk particularly in Europe

Within Asia-Pacific, China's Economy is viewed as the major risk to economic growth

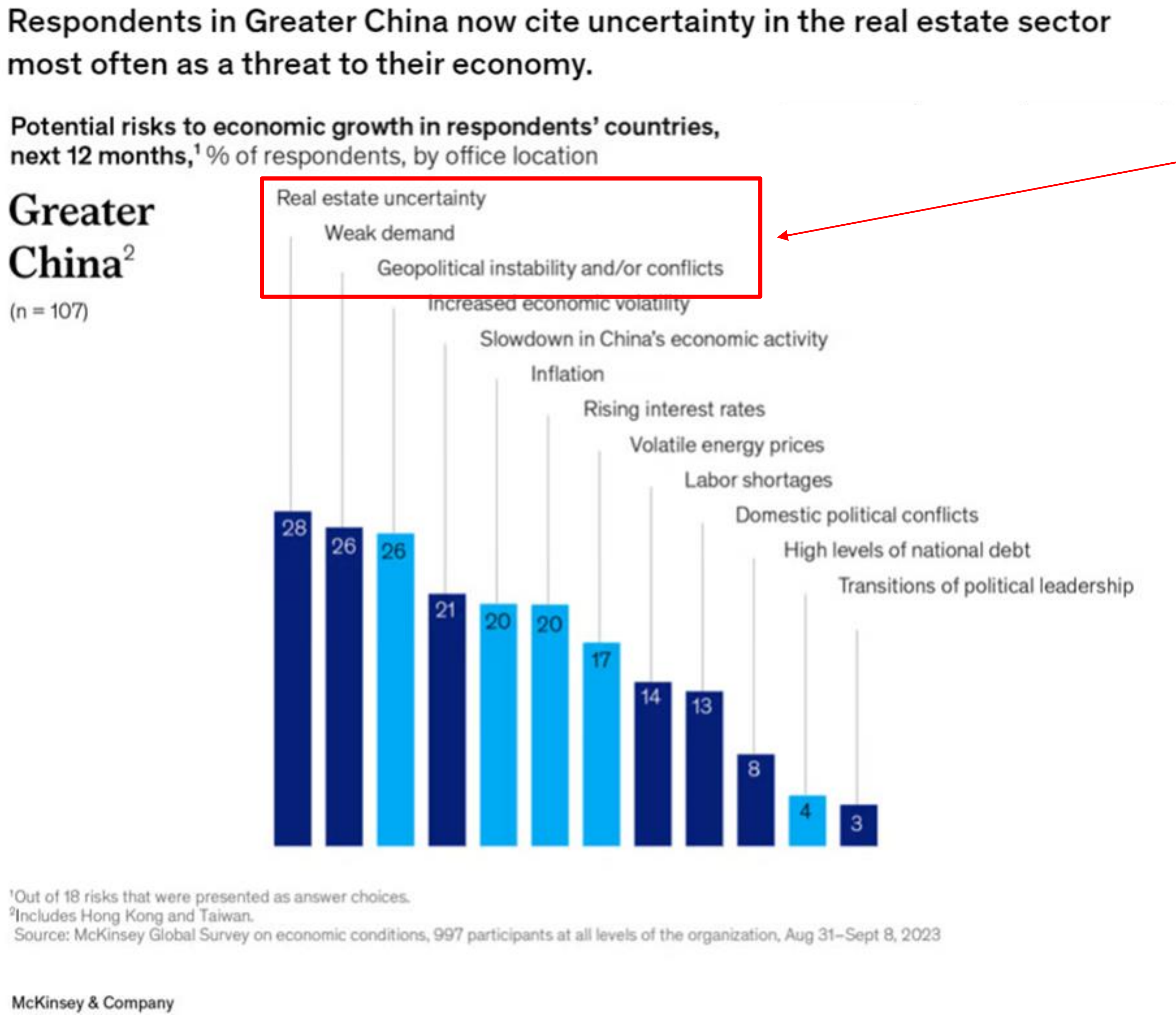


The view amongst Asia-Pacific countries:

- China's economy is the main potential risk to economic growth
- This is perceived as a far greater risk than even global inflation and geopolitical risk

McKinsey

Within China, uncertainty in the real estate sector is viewed as the greatest threat to their economy



Zooming in on China, the top three threats to their economic growth are:

- Real estate uncertainty
- Weak consumer demand
- Geopolitical instability (largely of their own making)

McKinsey

China's new home prices declined at fastest pace since 2015

Despite support policy measures to mitigate impact of a prolonged property downturn, prices are still falling

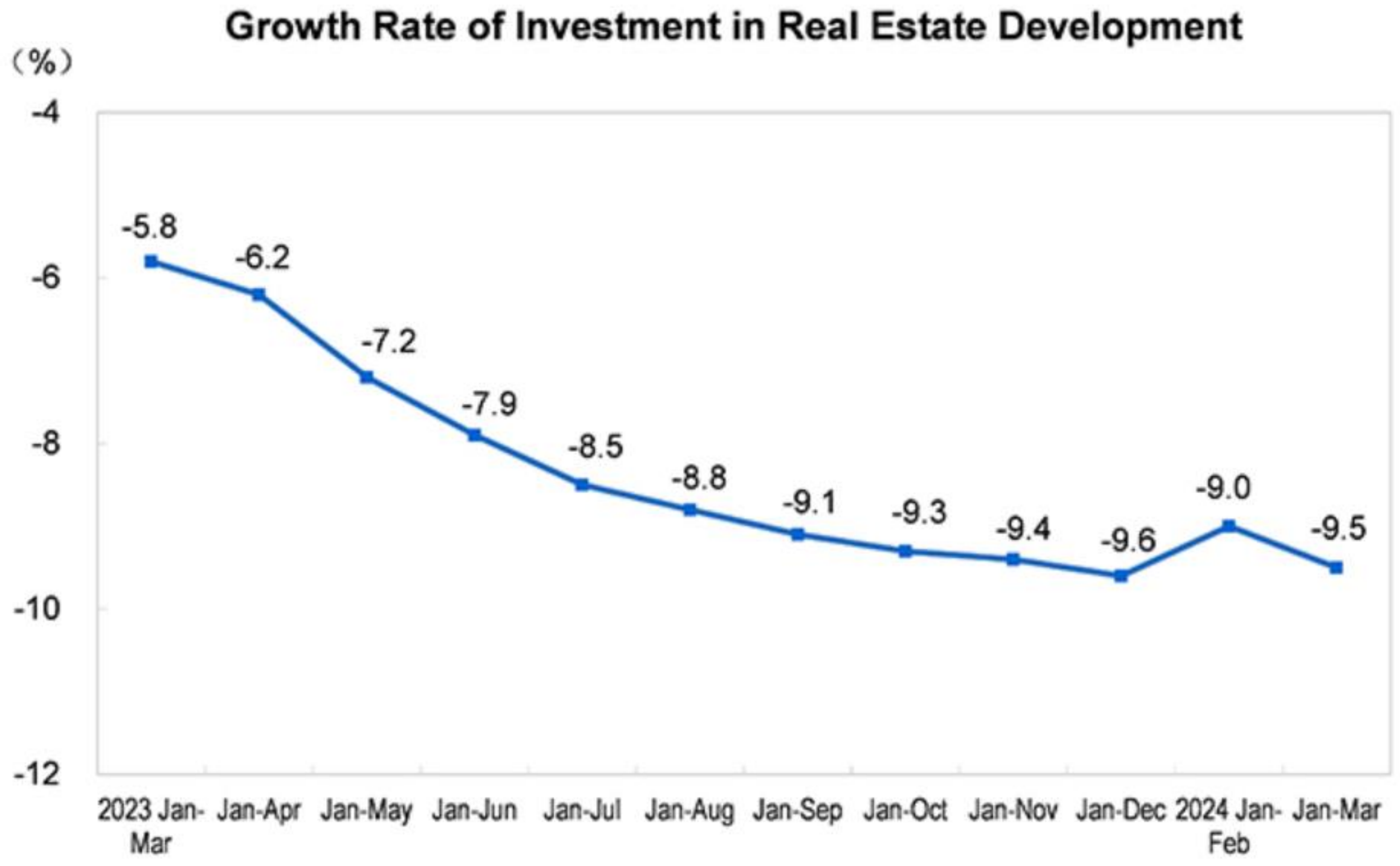
March 2024:

- **-2.2%** annual decline
- The 9th straight month of decline
- Steepest pace of decline since August 2015

www.tradingeconomics.com/china/housing-index

www.reuters.com/world/china/chinas-new-home-prices-decline-fastest-pace-since-2015-2024-04-16/ (Apr 24)

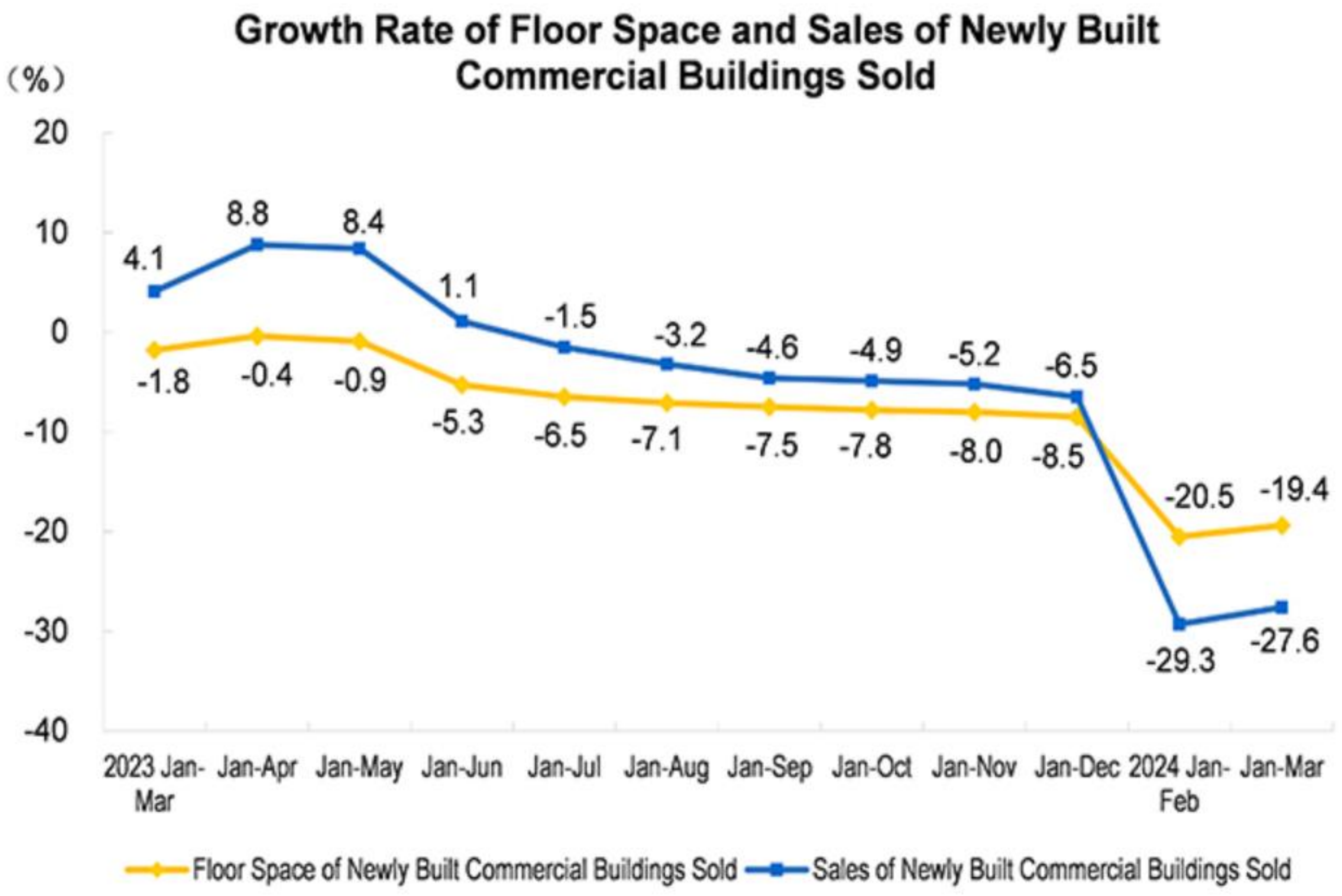
Investment in real estate development in China continues to fall



- From January to March 2024, total investment in real estate was down -9.5% year-on-year comparable basis
- Investment in residential buildings was down by 10.5%

www.stats.gov.cn/english/PressRelease/202404/t20240424_1955015.html

Sales of newly built buildings in China continues to decline



- From January to March 2024, the floor space sold and total sales of commercial buildings decreased by 19.4% and 27.6% on a year-on-year basis

- Residential building sales decreased at a greater rate of 30.7%

Implication: There are a lot of vacant buildings!

www.stats.gov.cn/english/PressRelease/202404/t20240424_1955015.html

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Unsold apartments in China

Ghost towns

- Moderate estimates of 65-80m vacant homes
- He Keng, former deputy head of China's statistics bureau, estimates more vacant homes than can be filled by China's 1.4 billion population

What happened

- Credit-fuelled building boom created oversupply
- Local governments got dependent on land sales to developers
- All based on assumption that property prices would continue to increase – BUBBLE!

People affected

- Home buyers paid for homes that have not materialised
- Reduced future homebuyer confidence
- Market share continuing to shift to state-owned companies

www.fortune.com/asia/2023/09/25/china-housing-crisis-how-many-vacant-homes-evergrande-country-garden/

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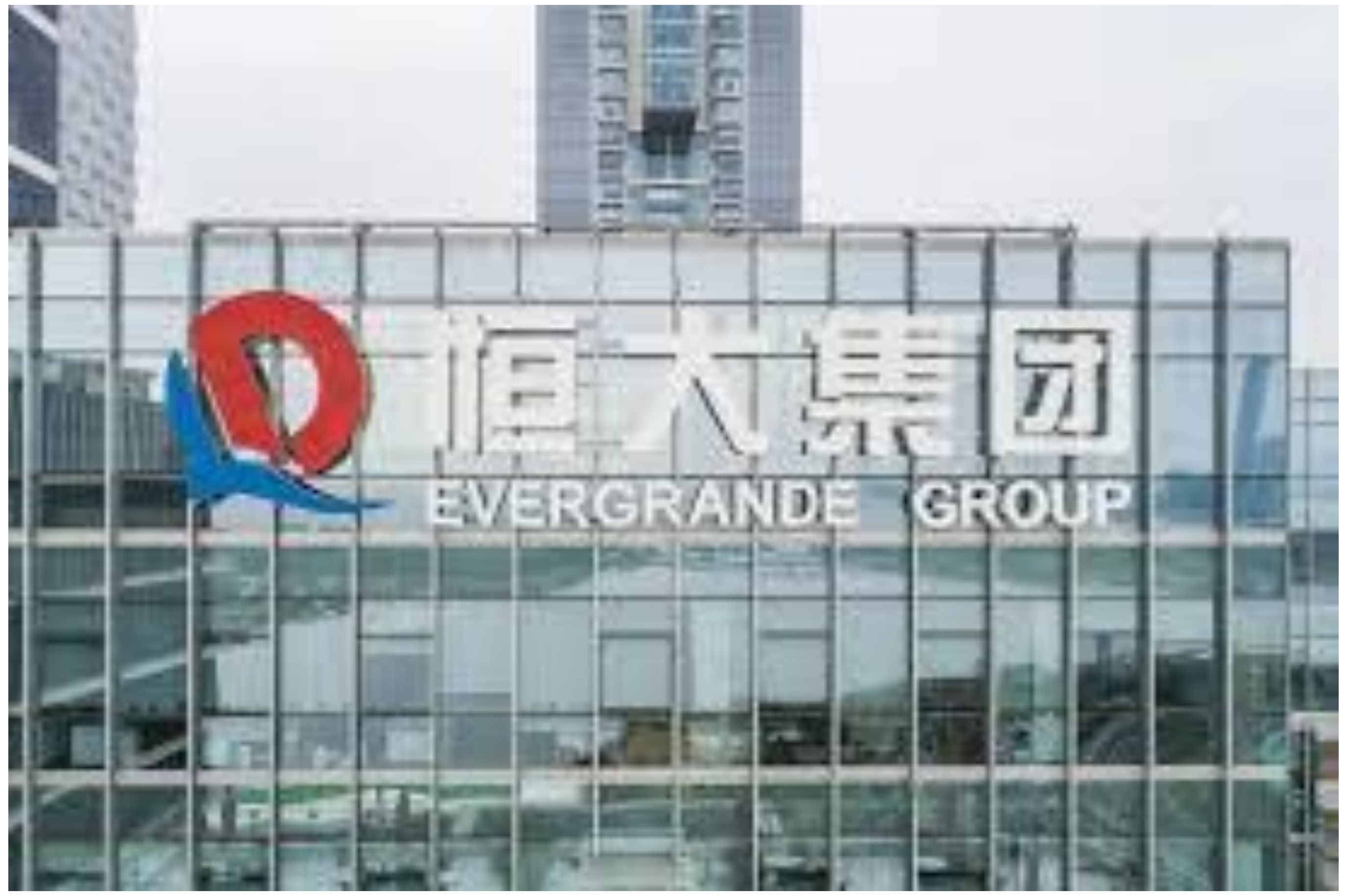
Evergrande – the first domino to fall?

What happened?

- Property Giant Evergrande defaulted on its debts in December 2021
- Hong Kong court ordered to liquidate more than 2 years after default
- Awaiting response from Beijing. To the rescue? Too big to fail?
- $300bn USD debt!



Ripple effects on the economy

- Downturn in housing market affects other developers like Country Garden with $200bn debt
- Stock markets affected
- Creditors, especially foreign, may not get their money back
- Construction and material suppliers
- Credit crunch and reduced lending from banks

www.fortune.com/asia/2023/09/25/china-housing-crisis-how-many-vacant-homes-evergrande-country-garden/
www.bbc.com/news/business-58579833

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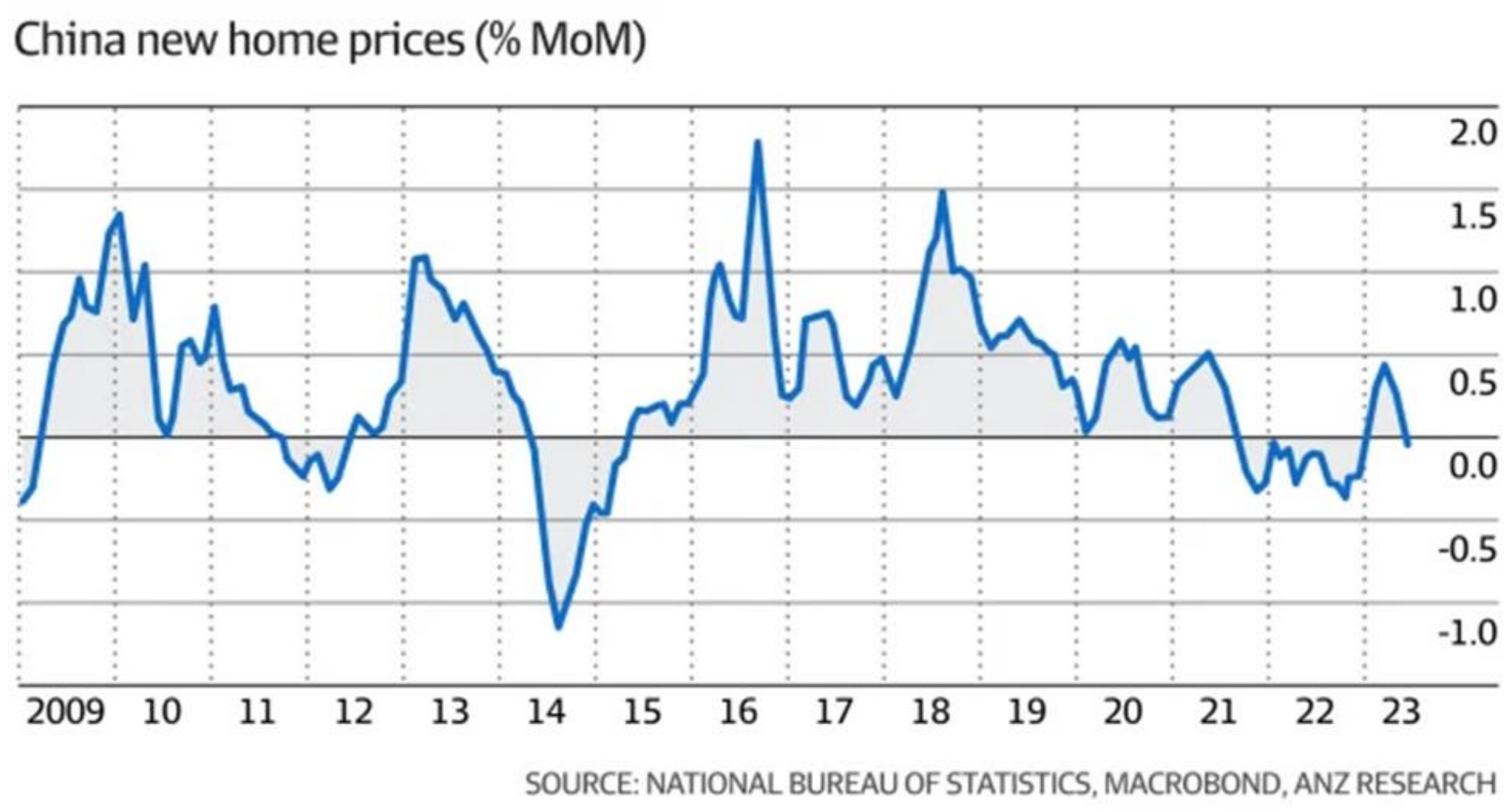
Potential implications for Australia – China is slowing



- We are now seeing widespread oversupply and price decreases
- Properties are taking on average 14 months to sell
- Developer defaults now spreading to the finance sector

- This will negatively impact demand for iron ore and coal – Imports are already down 12.4%
- This will drive down the Australian dollar and making flighting inflation harder
- Flight of capital – more Chinese capital flowing into the Australian property market driving prices here

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The energy 'transition' in Australia

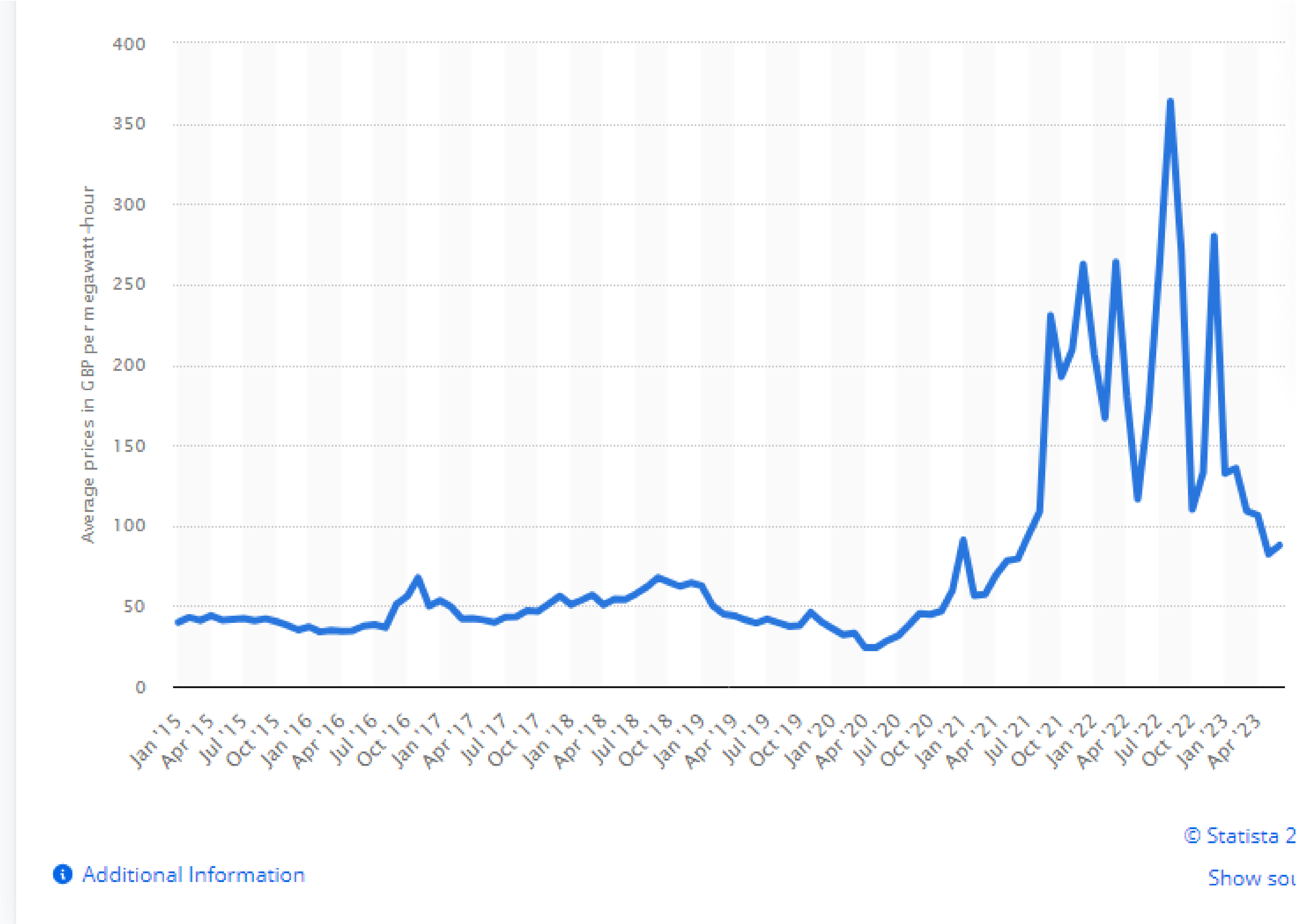
The UK energy transition plan – renewables as baseload power

- Climate change targets driving very aggressive renewables approach
- Aggressively close down legacy coal fired baseload generation
- Large scale wind and solar generating capacity
- Some gas and nuclear back up
- Become a renewable energy ‘superpower’

Does this plan sound familiar ???

How did this plan work out for the UK?

Average UK electricity prices



- Multiple days when there was no generation from the solar network and 5% of capacity from the wind network
- Wide scale industrial blackouts
- 'Load shedding' and power rationing across residential areas
- Soaring power prices

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The Australian plan

- Aggressive transition to a ‘net zero’ energy footprint – even though Australia produces 1.4% of global emissions – China is 30%
- Renewables to represent 82% of energy by 2030
- Some gas fired plants as ‘firming generation capacity’
- Rapidly build wind and solar to replace baseload coal fired plants
- **This means 22,000 500-watt solar panels every day for eight years along with 40 7MW turbines every month – backed by at least 10,000km of additional transmission lines. Land requirement – half the size of Victoria**
- Unlike the UK, Australia does not have the backups of nuclear (16%) and European transfers (16%)

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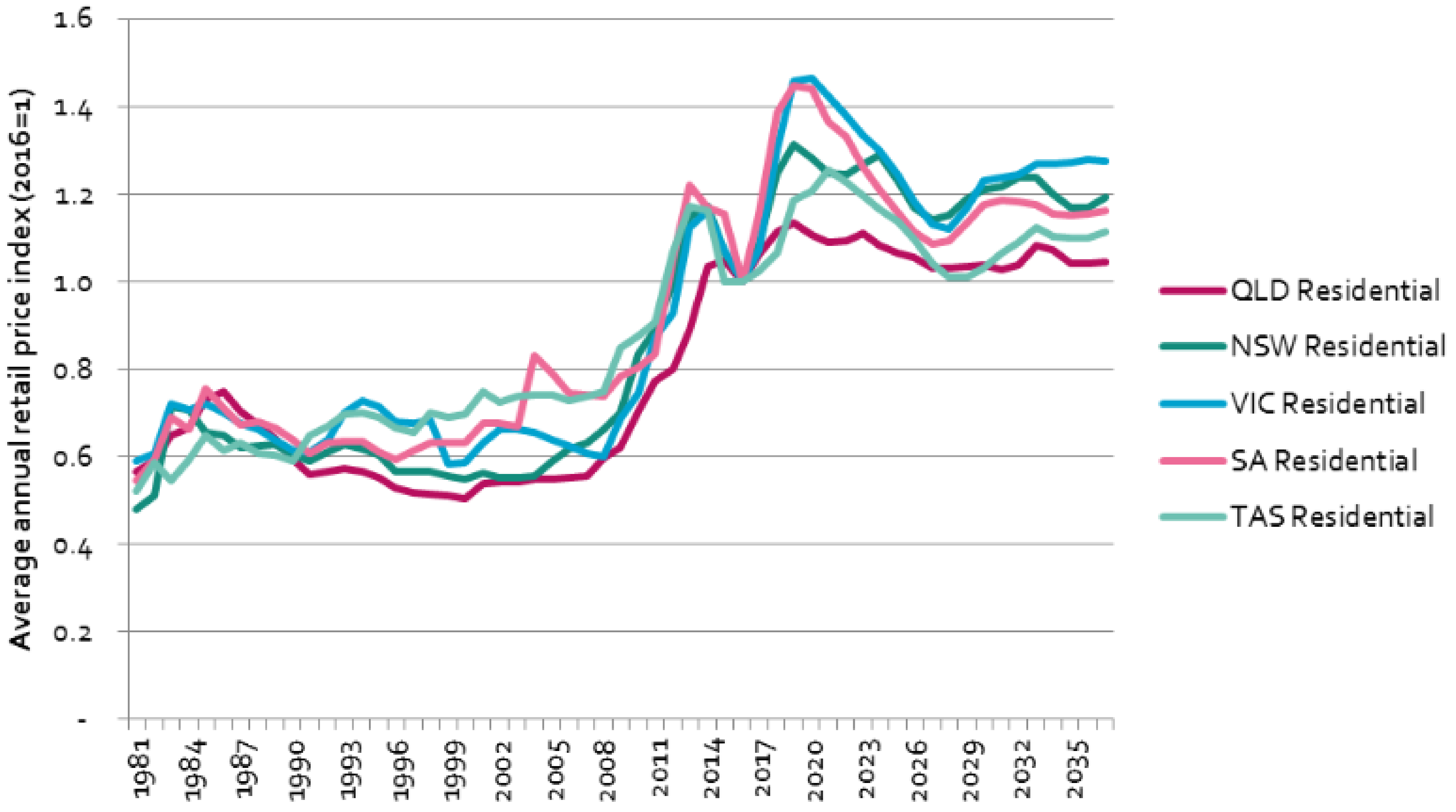
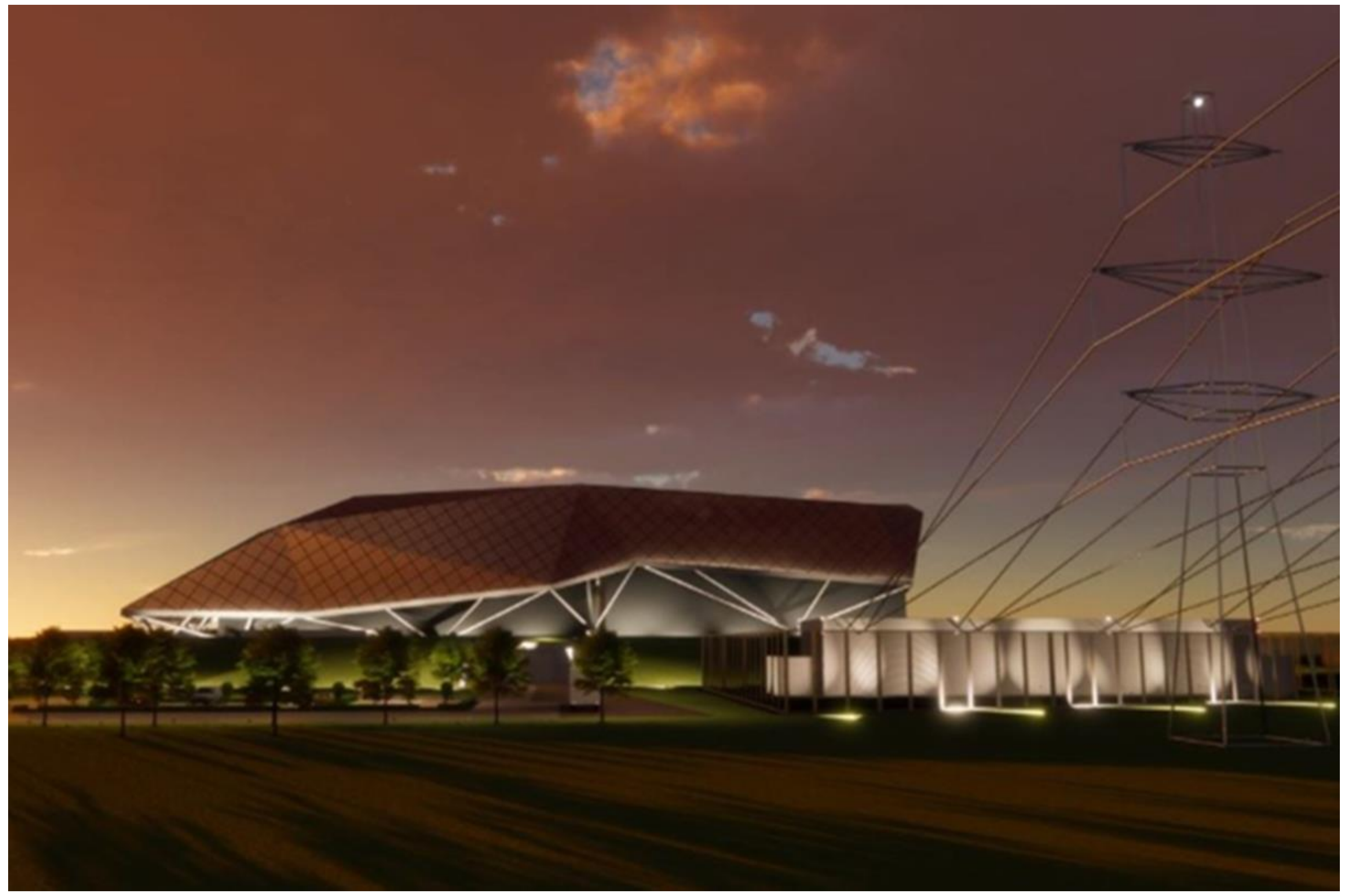
How is it going here?

Australian retail electricity prices



What is the new UK plan?

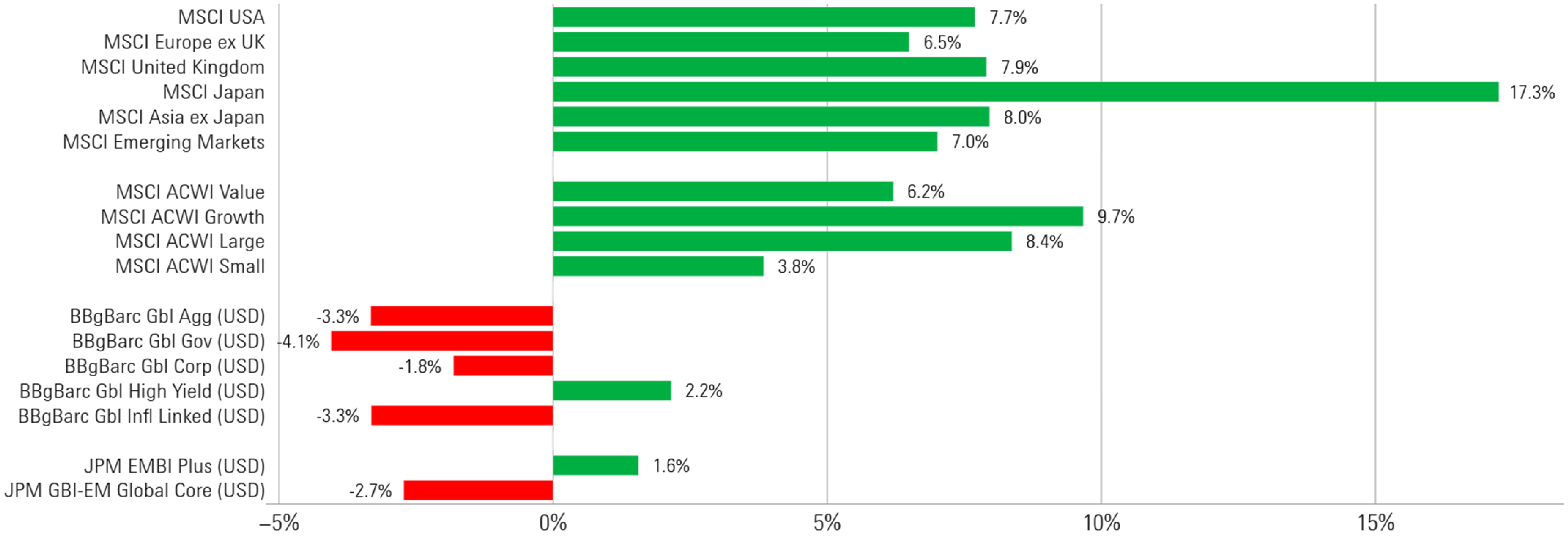


- £20 billion dollar investment into supercharging the country's nuclear industry so it can produce 24% of peak demand as reliable baseload power
- Combination of large scale plants and small modular reactors – Rolls Royce already builds them for nuclear submarines – built on the sites of decommissioned power stations to limit new transmission
- Interesting trivia – Australia has the largest uranium reserves in the world with 30% of global totals compared to Saudi Arabia which has 17% of world oil reserves

Where will we end up in Australia?

What does this mean for your super?– stay diversified!!

Global Asset Class Returns: Year-to-Date



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Source: Clearnomics, Morningstar, MSCI, Bloomberg, JPMorgan

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