



Market Insights

Quarterly Perspectives

Politics. Policies. Portfolios.

Australia | 4Q 2024

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Overview

- The U.S. economy is cooling, moving from “hot” to “warm,” and the Federal Reserve (Fed) is shifting its policy priority from taming inflation to safeguarding the labour market. As such, a gradual rate-cutting cycle is likely in the quarters ahead. The U.S. presidential election in November will focus market attention on policy options, especially on taxes and trade.
- Lower policy rates and an economic soft landing in the U.S. have historically facilitated a stock-bond portfolio outperforming cash.¹ International diversification continues to be a critical way to manage risks while tapping into opportunities.
- Investors should look to broaden their sector allocation in U.S. equities into quality companies and those that are less correlated with the economic cycle. Even though government bond pricing already reflects some of the anticipated rate cuts, we believe they can provide income above inflation and a hedge against a worse-than-expected economic downturn.

¹Cash is proxied by U.S. short-term Treasuries.



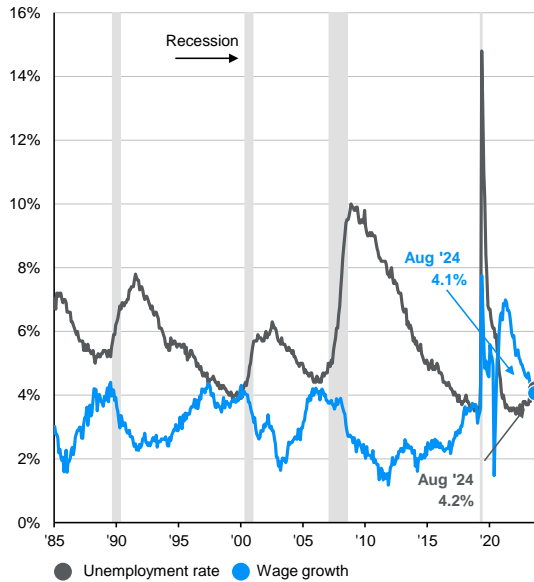
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U.S.: Labour market

GTM AUS 22

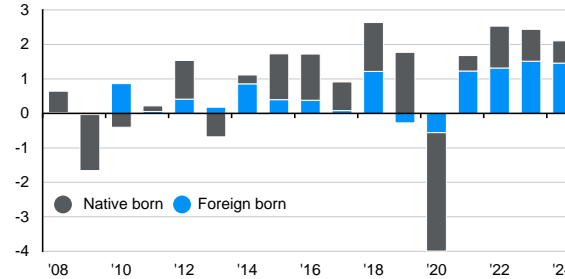
Unemployment rate and wage growth
Wages of production and non-supervisory workers, seasonally adjusted



Source: BLS, FactSet, J.P. Morgan Asset Management;
Guide to the Markets – Australia. Data as of 30 September 2024.

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Labour force growth, native and immigrant contribution
Year-over-year, aged 16+, millions



JOLTS job openings
Total job openings, millions, seasonally adjusted



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U.S. economic growth: From “hot” to “warm”

- The U.S. economy is cooling, shifting from “hot” to “warm.” High interest rates and a lack of fresh fiscal stimulus amid the election season are gently applying the brakes on growth. Consumers, especially those in the lower-income groups, are becoming more price-sensitive as their household balance sheets swing from excess savings during the pandemic era to debt accumulation.
- The labour market is showing signs of slowing, albeit from a high level, as reflected by recent job openings data. The rise in the unemployment rate is partly due to rising labour participation.
- Meanwhile, inflation is also showing more convincing signs of slowing, especially in shelter costs, which constitute one-third of the overall consumer price index. However, medical care and transportation services remain relatively persistent in propping up services inflation. Core goods prices have been falling since the start of 2024, and it is worth watching whether the recent U.S. dollar (USD) depreciation could prompt a modest rebound in imported inflation.



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World equity market returns

GTM AUS 34

Equities

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	3Q '24	10-years '14 - '23	
AUD	24.3% U.S.	25.6% Japan	13.2% Small Cap	31.5% Asia ex JP	6.2% U.S.	31.7% U.S.	14.2% Asia ex JP	36.6% U.S.	-1.1% Australia	25.5% U.S.	20.1% U.S.	7.8% Australia	15.1% U.S.	Small Cap 17.2%
Local	13.7%	12.1%	13.2%	35.9%	-4.4%	31.5%	22.7%	28.7%	-1.1%	26.3%	22.1%	7.8%	12.0%	
	14.9% Asia ex JP 7.7%	14.0% U.S. 1.4%	12.5% U.S. 12.0%	27.5% EM 31.0%	-2.3% Portfolio -7.3%	24.8% Europe 24.6%	9.2% Small Cap 9.2%	24.1% Europe 23.3%	-8.4% Europe -8.0%	19.9% Europe 15.0%	19.5% Asia ex JP 22.0%	6.5% Small Cap 6.5%	9.1% Portfolio 8.3%	U.S. 15.2%
	8.7% Portfolio 6.8%	10.2% Small Cap 10.2%	12.1% EM 10.1%	20.0% Small Cap 20.0%	-2.8% Australia -2.8%	24.0% Portfolio 23.7%	8.1% EM 19.5%	19.0% Portfolio 17.2%	-8.7% Japan -2.5%	19.3% Japan 28.3%	15.3% EM 18.7%	6.4% Asia ex JP 8.1%	8.3% Japan 8.6%	Japan 14.7%
	7.3% EM 5.6%	9.8% Europe 5.4%	11.8% Australia 11.8%	17.2% Japan 22.2%	-4.2% Japan -16.0%	23.4% Australia 23.4%	7.9% U.S. 18.4%	17.2% Australia 17.2%	-8.8% Portfolio -9.5%	15.8% Portfolio 16.2%	14.0% Portfolio 15.2%	4.9% Portfolio 5.0%	7.9% Australia 7.9%	Asia ex JP 14.6%
	5.7% Japan 10.3%	8.4% Portfolio 3.3%	9.4% Portfolio 9.8%	16.9% Europe 13.7%	-4.6% Asia ex JP -12.0%	21.4% Small Cap 21.4%	4.2% Portfolio 8.6%	16.9% Small Cap 16.9%	-12.2% U.S. -18.1%	12.4% Australia 12.4%	12.3% Australia 12.3%	4.8% EM 6.8%	7.6% Europe 7.0%	Portfolio 14.5%
	5.6% Australia 5.6%	2.6% Australia 2.6%	6.3% Asia ex JP 6.4%	16.7% Portfolio 19.1%	-4.7% EM -9.7%	19.4% Japan 18.1%	3.0% Japan 7.4%	7.3% Japan 12.7%	-13.5% Asia ex JP -15.1%	9.6% EM 10.3%	11.5% Europe 11.6%	3.0% Japan -4.9%	7.0% Asia ex JP 5.2%	Australia 14.1%
	3.1% Europe 5.2%	2.5% Asia ex JP -5.3%	4.0% Japan 0.3%	12.8% U.S. 21.8%	-4.8% Europe -10.0%	19.1% EM 18.5%	1.4% Australia 1.4%	3.8% EM 0.1%	-13.9% EM -15.2%	7.8% Small Cap 7.8%	10.8% Japan 14.2%	2.6% Europe 1.6%	6.0% Small Cap 6.0%	EM 13.5%
	-3.8% Small Cap -3.8%	-3.9% EM -5.4%	0.7% Europe 7.9%	11.8% Australia 11.8%	-8.7% Small Cap -8.7%	18.7% Asia ex JP 18.2%	-3.5% Europe -1.7%	1.4% Asia ex JP -2.8%	-18.4% Small Cap -18.4%	5.7% Asia ex JP 6.8%	9.5% Small Cap 9.5%	1.9% U.S. 5.9%	5.9% EM 5.6%	Europe 13.2%

Source: FactSet, MSCI, Standard & Poor's, TOPIX, J.P. Morgan Asset Management. Annualised return (Ann.) and volatility (Vol.) covers the period 2014 to 2023. Volatility is based on local currency returns. Small Cap: S&P ASX Small Ordinaries; Asia ex JP: MSCI AC Asia ex Japan; EM: MSCI EM Index; Europe: MSCI Europe Index; Japan: TOPIX first section; Australia: ASX 200 Index; U.S.: S&P 500 Index. Hypothetical portfolio (for illustrative purposes only and should not be taken as a recommendation): 20% U.S.; 30% Australia; 15% EM; 15% Europe; 10% Japan; 10% small cap. All indices are total returns. Past performance is not a reliable indicator of current and future results.
Guide to the Markets – Australia. Data as of 30 September 2024.

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U.S. elections: Different pledges, similar outcomes

- The U.S. presidential election is likely to be a close race between Vice President Kamala Harris and former President Donald Trump. This could raise the possibility of a divided government where the two major political parties, the Democratic Party alongside the Republican Party, split control of the presidency and Congress. In this scenario, it may be more difficult to pass legislation on taxes, spending and regulations.
- Despite their different campaign pledges, there are similarities between the two presidential candidates. The federal government's sizeable fiscal deficit is likely to remain in place, with rising debt over the medium term. U.S. trade policy is expected to remain focused on bolstering domestic manufacturing, especially against imports from China. This would continue to pressure companies, including those from China, to diversify their supply chains to manage the risks of higher tariffs and other trade barriers.
- Historically, market volatility declines following an election. We believe economic and corporate fundamentals will be the dominant drivers of market returns.



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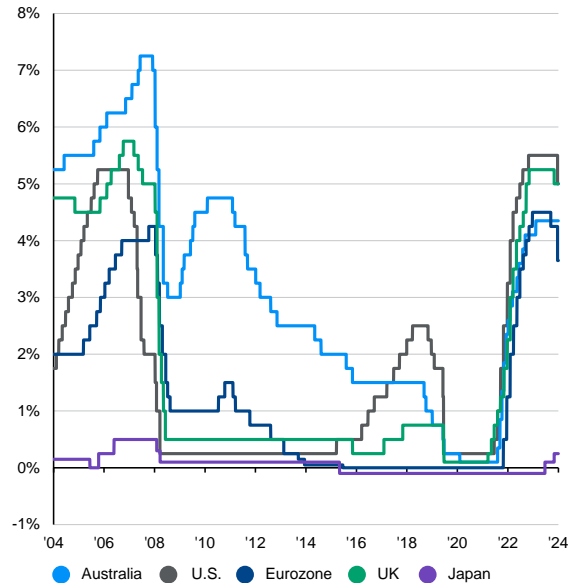


Central bank policy rates

GTM AUS 56

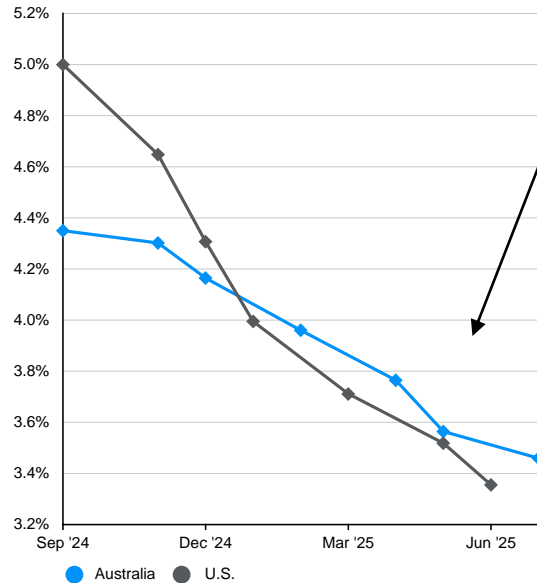
Central bank key policy rates

Target rates



Market implied policy rates

Expected policy rate at coming central bank meetings



Source: Bank of Japan, European Central Bank, FactSet, Reserve Bank of Australia, U.S. Federal Reserve, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results.
Guide to the Markets – Australia. Data as of 30 September 2024.

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Fed policy: Changing course

- The Fed's policy focus has shifted to safeguarding the labour market as it sees inflation on track towards its 2% target. This is reflected by the 50 basis points (bps) rate cut at the Federal Open Market Committee (FOMC) meeting in September. More importantly, in its updated Summary of Economic Projections, the median of forecasts shows FOMC members expect the policy rate to be cut by 100 bps in 2025.
- Considering the current economic performance, which is consistent with a soft landing of the U.S. economy, the Fed can afford to be more patient in bringing the policy rate back to neutral. Of course, the pace and timing of rate cuts could change based on incoming inflation and job numbers. One potential challenge is how the Fed will react to a rebound in inflation brought about by supply-side shocks. This could include disruptions in the global supply chain or potentially higher import costs based on any change in trade policy.



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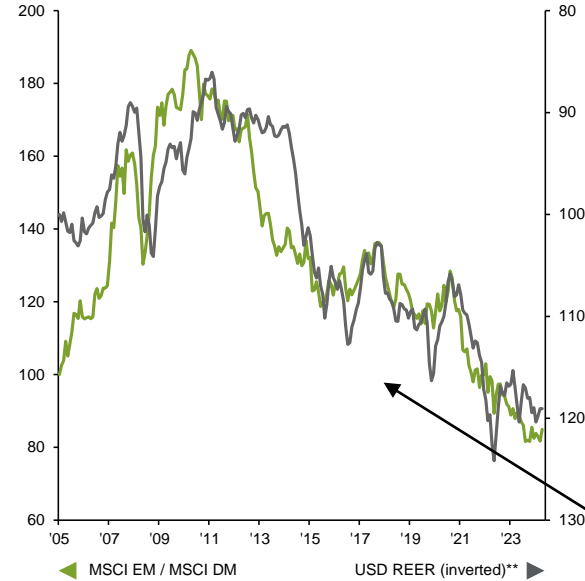
Emerging market equity performance drivers

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Growth in nominal exports and earnings per share
MSCI Asia Pacific ex-Japan, USD, year-over-year



EM equity relative performance to USD
Indexed 2005=100



Source: FactSet, MSCI, J.P. Morgan Asset Management; (Left) CEIC, national statistics agencies; (Right) U.S. Federal Reserve. *EM Asia ex-China includes Hong Kong, Korea, Malaysia, Singapore, Taiwan, Thailand and Vietnam. Overall exports aggregate is gross domestic product (GDP)-weighted. **REER is the real effective exchange rate. Past performance is not a reliable indicator of current and future results.
Guide to the Markets – Australia. Data as of 30 September 2024.

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Asian economies: Robust exports

- Despite concerns over the pace of corporate investment relating to generative artificial intelligence (AI), Asia's technology and semiconductor export momentum remains largely intact. The next supporting shift for the region may be an increase in demand for consumer electronics with AI processing capabilities, or Edge AI.
- Economic activity in China remains unbalanced, with challenges in the housing market weighing on consumption and corporate investment. More aggressive fiscal and monetary policies may be required to facilitate a sustainable recovery. While exports have experienced a stronger recovery in 2024, export growth may be hindered by an uncertain trade outlook and the recent tariffs on electric vehicles imposed by the U.S., EU and Canada.
- The window for Asian central banks to cut rates is widening. Lower policy rates in the U.S. have helped to weaken the USD. Alongside lower inflation in the region, Asian central banks may start to cut rates in late 2024. That said, the pace and timing of rate cuts would be determined by domestic circumstances.



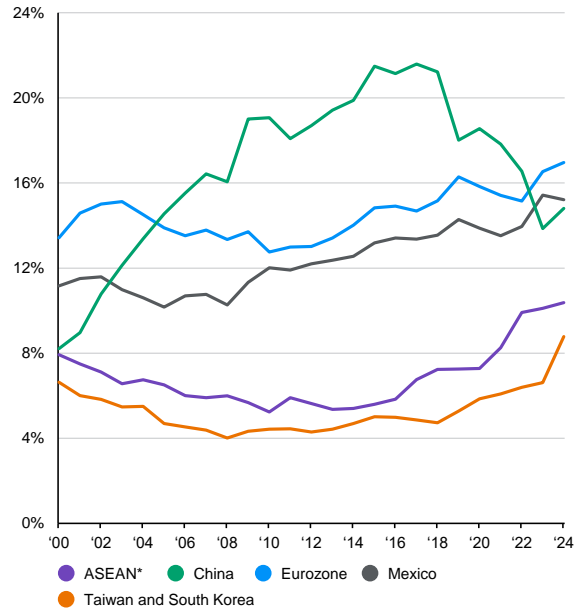
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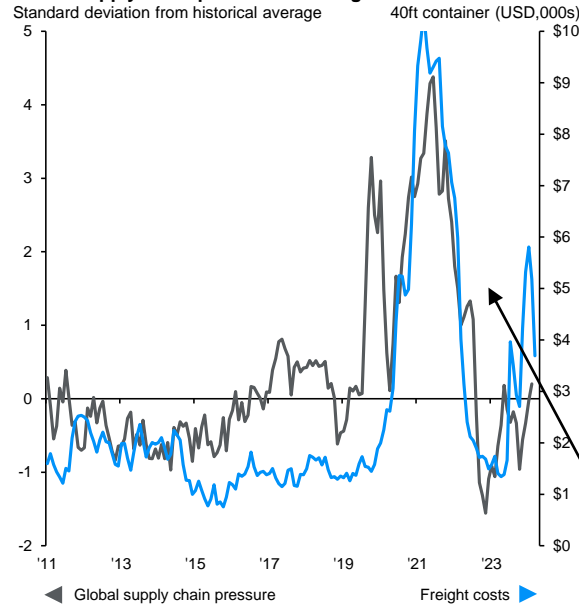
Supply chains

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U.S. goods imports by country
% of total U.S. goods imports



Global supply chain pressure and freight costs



Source: FactSet, J.P. Morgan Asset Management; (Left) U.S. Census Bureau; (Right) Bloomberg, Drewry, U.S. Federal Reserve. *ASEAN countries include Brunei Darussalam, Myanmar/Burma, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam. Guide to the Markets – Australia. Data as of 30 September 2024.

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Risks: Conflicts and supply chain disruptions

- Unexpected turns in growth (recessions) or inflation (price rebound) are probably the most relevant to investors in recent times. On inflation rebounding, it is important to define the trigger given the different policy implications of demand-side or supply-side shocks. The former, which we believe is less likely, could necessitate a return to higher rates.
- Geopolitical tension in the Middle East limited freight traffic through the Red Sea and Suez Canal earlier in the year. This could continue with rising tension between Israel and Iran, as well as heightened concerns over energy transportation that goes through the Strait of Hormuz. Ukraine's military action inside Russian territory also raises the risk of escalation of the conflict in Europe.
- Additionally, the global manufacturing supply chain remains vulnerable to disruptions. China's export limits of critical minerals used in semiconductors and other technological equipment can also lead to shortages in electronic components. Natural disasters related to climate change are always within sight, even if a solution is difficult to plan for.



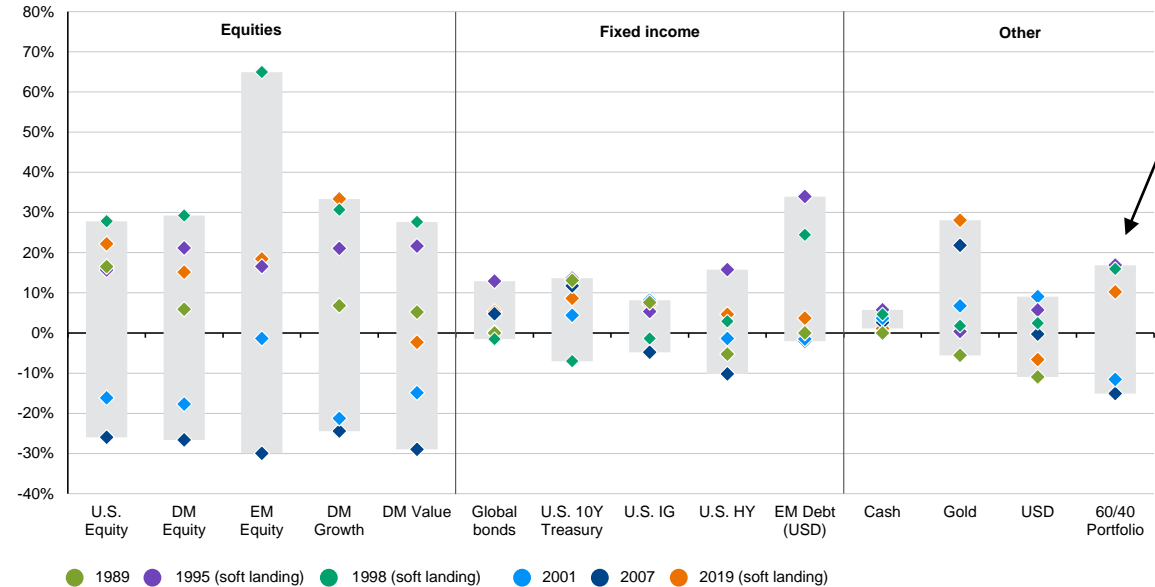
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Rate cuts and asset performance

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Asset class returns following the start of U.S. rate cuts
Average returns 12 months following the first rate cut



Source: Bloomberg L.P., FactSet, MSCI, Standard & Poor's, U.S. Federal Reserve, J.P. Morgan Asset Management.
Total returns in local currency unless otherwise specified. Past performance is not a reliable indicator of current and future results.
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Asset allocation: Rate cuts to boost stocks and bonds

- Our core view of a rate cut amid a U.S. economic soft landing has worked out well so far, with both fixed income and equities outperforming cash² as the Fed's intention to ease monetary policy becomes clearer. We continue to see a balanced stock-bond allocation as optimum in portfolio construction.
- Given the prospects of softer growth in the U.S., investors should also consider a plan B, in case the deceleration in growth is worse than expected. This is where government bonds, investment-grade (IG) corporate debt and defensive equities could help balance the goal of generating returns while managing volatility. Some investors may consider cash-equivalent² assets to be a good hedge against a recession, but they typically underperform government bonds and IG corporate debt as falling yields could provide potential additional returns from higher bond prices.

²Cash is proxied by U.S. short-term treasuries.

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U.S. equities: Mega-cap valuations and earnings

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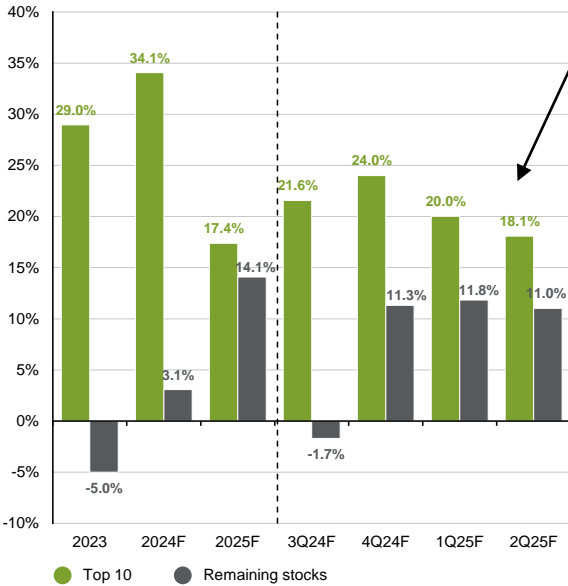
P/E ratio of the top 10 and remaining companies in S&P 500

Next 12 months, 1996 - present



Earnings growth

Pro-forma earnings per share, year-over-year



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.
The top 10 S&P 500 companies are based on the 10 largest index constituents at the beginning of each month. Top 10 companies in the index were MSFT, AAPL, NVDA, AMZN, META, GOOGL, BRK.B, GOOG, LLY, AVGO and TSLA. The remaining companies represent the rest of the 493 companies in the S&P 500.
Guide to the Markets - Australia. Data as of 30 September 2024.

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U.S. equities: Rising tides lifting more boats

- We continue to see value in U.S. equities both in the short term and the long term. In the short term, a broadening of corporate earnings can help some of the laggards catch up to the mega-cap technology companies. In fact, so far in 3Q 2024, health care, utilities, real estate and consumer staples have outperformed information technology and communication services. This trend reflects the more defensive nature of investor appetite and is broadly consistent with the historical trend of sector performance following the start of the rate-cut cycle.
- In the longer run, technology and growth are still expected to lead. U.S. technology companies have deployed their capital to engage in research and development as well as building capacity to grow. Hence, an economic slowdown could lead to a correction in these growth sectors. Yet, these corrections have historically been an optimal time to build a position in these long-term growth drivers.



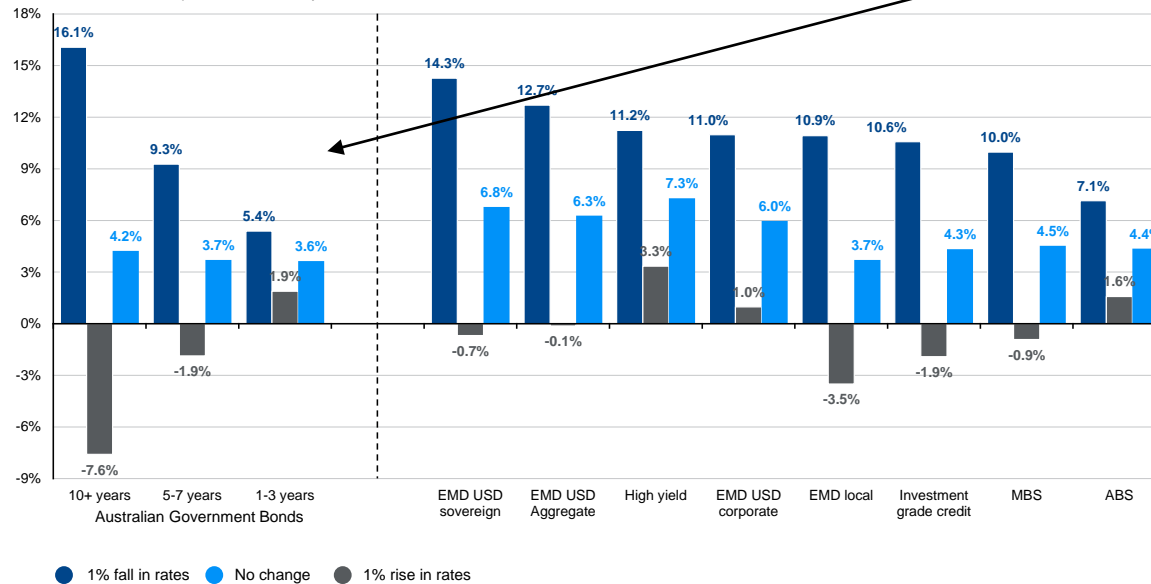
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Fixed income interest rate sensitivity

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Impact of a 1% rise or fall in interest rates
Total return, assumes a parallel shift in the yield curve



Source: Bloomberg L.P., FactSet, J.P. Morgan Asset Management. Past performance is not indicative of current or future results. Guide to the Markets – Australia. Data as of 30 September 2024.

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Fixed income: Time to focus on quality again

- Government bonds play two important roles in portfolio construction. First, we believe they are an important source of income contributing to total return. Government bond yields in most developed and Asian economies are now above inflation, presenting an income above the rate of inflation. Second, rate cuts by central banks should cap the upside for bond yields, and hence limit the downside potential for bond prices. Moreover, even if the government bond markets have already priced in central bank rate cuts in the months ahead, government bonds can still hedge the risk that a soft landing becomes a slide into recession.
- Additionally, a growing number of central banks in both developed economies and emerging markets are embarking on their own easing cycle, thus providing a wide opportunity set for bond investors to choose from.
- High-quality fixed income, such as IG corporate debt, can play a similar role while potentially providing higher yields than government bonds. For high-yield, non-IG corporate bonds, their price stability is dependent on the economy not falling into a sharp recession, which could accelerate corporate defaults and widen spreads.



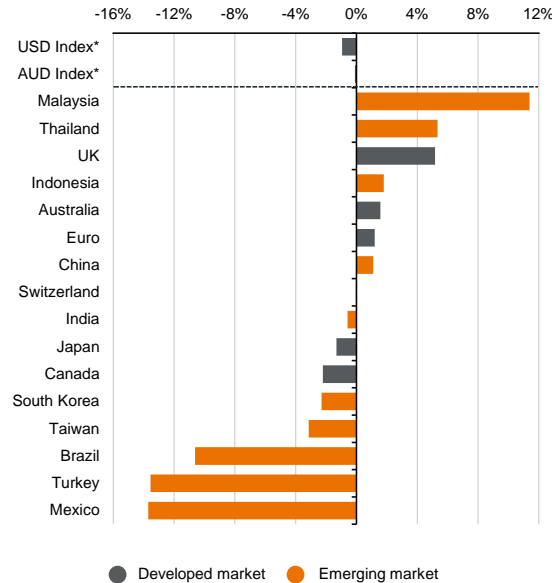
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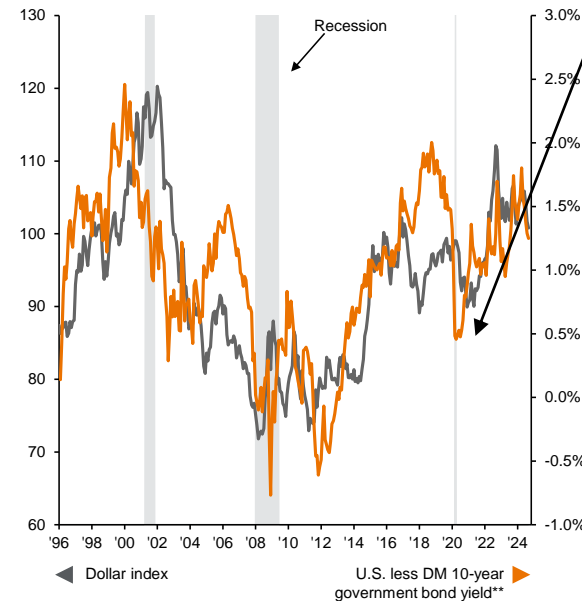
Global currencies

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Currency movements
2024, vs. USD



U.S. dollar index and interest rate differential



Source: FactSet, J.P. Morgan Asset Management; (Left) Reserve Bank of Australia; (Right) OECD.
*USD and AUD Index shows performance vs. a basket of trading partners. **DM is developed markets and the yield is a GDP-weighted average of the 10-year government bond yields of Australia, Canada, France, Germany, Italy, Japan, Switzerland and the UK. Past performance is not a reliable indicator of current and future results.
Guide to the Markets – Australia. Data as of 30 September 2024.

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The USD: Let gravity do the work

- The USD index has dropped by 5.0% since its recent high in late June. This is driven by the prospects of lower interest rates in the U.S., alongside some long-standing structural forces that would mean a lower USD. These include overvaluation of the greenback and persistent and sizeable current account and fiscal deficits of the U.S. economy.
- Still, a shift in growth differentials may be needed to materially further weaken the USD. The global economy would need to avoid a sharp recession or financial stress, otherwise, the USD would act as a safe-haven currency and appreciate once again on the back of demand. A convergence in global growth rates, rather than the U.S. exceptionalism experienced since the end of the pandemic, would drive investors towards opportunities outside of the U.S.
- International assets, including emerging market (EM) and Asian fixed income and equities have historically benefited from a weaker USD. Even though stronger Asian currencies could undermine export competitiveness for the region's exporters, many companies with high technology content, such as semiconductors, are typically less impacted. A weaker USD also allows Asian and EM central banks more flexibility in cutting rates, thus supporting their fixed income markets.



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