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2021 December Market Wrap Monday 3 January 2022

Happy New Year, wishing you a peaceful, safe and prosperous 2022, I hope you get the to recharge for the new year ahead.

In December, Australia ended the year in a good position with GDP of 3.9% for the Sep Qtr. Consumer Prices at 3.0% for the Sep Qtr, Unemployment rate at 4.6%, Net Foreign Debt $1,191,067m, The RBA cash rate at 0.1%.

There were 2,100,800 public sector employees at the end of June 2021 comprising:

- 247,600 employees in Commonwealth government
- 1,662,400 is state government: and
- 190,800 in local government

Total public sector cash wages and salaries in 2021 was $182,940.4 million.

The Reserve Bank's balance sheet has almost tripled in size since the onset of COVID-19 as a result of the policy measures adopted by the Bank to support the Australian economy. Over the 2020/21 financial year, the balance sheet increased by $279 billion to $540 billion. Growth in assets reflected an increase in the Bank's government bond holdings, purchased in support of the three-year yield target and under the bond purchase program, and an increase in the TFF

Investment markets ended the year on a positive note with a good December, seeing Calendar year being positive in the range of 4% to 26% for major markets with the one exception being Hong Kong down 14%, showing the effects of the China crack down.

Looking forward, 2022 will be all about inflation and the unwinding of ultra-loose monetary and fiscal policy. Central banks in UK, US EU and Australia are all behind the curve. The key now is to deal with inflationary pressures, the tapering process and the raising of interest rates.

The problem has been staring central banks in the face, but they were distracted by the outbreak of Delta. Associated restrictions and lockdowns sent further shock waves through economies and accommodative policy settings remained in place. Government “helicopter money” fuelled consumer demand for goods, while supply chain issues were unresolved. The lag effect saw consumer and producer prices surge in October and November.

Initially, all four appeared to be in the transitory camp regarding inflation. They decided inflation was a visiting bird. Rising prices caused by global supply chain disruptions were designated as passing and short-term. But as prices surged past 30 and 40-year records, convictions wavered, and some banks broke ranks.

A special report from the well-respected Rosenberg Research titled “Why the funds rate cannot go above 1% this cycle”, concludes statistically, the Fed has four increases, at most, before increases generate “either a growth recession or an outright contraction.” A rate above 1% would “tip the economy over and cause a material correction or bear market in any asset class with a cyclical label attached.” The reason for the caution is debt, given how susceptible the “ultra-credit-sensitive economy is to even modest shifts in Fed policy. As market expectations realise this situation, the US 10-year bond yield could fall to 1.30% or below.” That would suggest economic growth has stalled.

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A cumulative rate increase of 1% from the near zero fed funds rate would have implications on the debt-servicing costs of households and companies with flow-on effects on consumption and investment. The negative impact on equities and residential property values would likely erode the wealth effect, cutting into spending and potentially lowering overall GDP growth. Both the global economy and financial markets have been totally reliant on fiscal and monetary policy stimulus. The loss of fiscal support is one step, which will impact household income. The withdrawal of the punchbowl brimming with asset purchase proceeds is another step. Interest rate rises, in the face of soaring inflation, could be a step too far for heavily indebted public and private sectors. Financial markets are seemingly unaware of how vulnerable governments and households are to a cyclical tightening. Remember, we have not experienced a normal economic cycle for over a decade.

The RBA does not see a problem here with inflation and is laying the blame at the feet of fiscal policy, while not taking any blame for the massive increase in liquidity which propelled risk asset prices. The attraction to and unprecedented support to generate the 'wealth effect' will necessitate an unwelcome and possible prickly response.

Federal and state government debt levels are massive as deficits explode. Surpluses are not in any government forecast, probably this side of 2035. Federal government annual interest payments are already at $25bn before rates start to climb.

The pressure on the RBA will continue to build in the early months of 2022.

Both monetary and fiscal policy need to be adjusted, the slower the process the more fragile the Countries position becomes. We need have growth to increase take receipts to repair the Government balance sheet. We need markets to set interest rates without Reserve Bank intervention, so we get the true price of money. Giving the true benchmark price of the risk free rate un turn leading to more accurate price if risky assets.

If you have any questions do not hesitate to contact me.

Summary of Major share indices

Index	1 Month	52 Weeks	YTD
DJIA	+5.08%	+18.73%	+18.73%
Nasdaq	+3.71%	+21.39%	+21.39%
S&P 500	+5.02%	+26.89%	+26.89%
Russel 2000	+3.98%	+13.69%	+13.69%
Europe 600 Index	+5.41%	+22.25%	+22.25%
UK FTSE 100 Index	+3.68%	+14.30%	+14.30%
Hong Kong Hang Seng	-1.55%	-14.08%	-14.08%
Japan Nikkei 225	+3.74%	+4.91%	+4.91%
China Shanghai Composite	+0.90%	+4.80%	+4.80%
India S&P BSE Sensex	+0.97%	+21.99%	+21.99%
ASX 200 (Australia)	+2.75%	+13.02%	+17.23%

Australian Dollar

	Close	52 week Range

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AUD	0.72263%	0.6992-0.8008%

Government Bonds

	Close	52 week Range
US 3 Month Bill	0.050%	0.003-0.101%
US 10 Years Note	1.514%	0.903 – 1.778%
US 30 Years Bond	1.906%	1.638 – 2.515%
Australia 10 years	1.681%	0.943-2.118%

Source: Wall Street Journal.