ECONOMIC AND MARKET UPDATE

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MLC ASSET MANAGEMENT

Key events in October 2026

- Global shares fell modestly in October. Concerns over the potential escalation of the Iran War, the US Congressional election result in November, as well as the rapid acceleration in Artificial Intelligence (AI) capital investment and corporate borrowing, have made investors more cautious.
- US share prices achieved historic highs in early October given optimism on AI prospects and encouraging US corporate profit results. US corporates are set to deliver astonishing annual profit gains exceeding +30% in the September quarter according to FactSet. Large technology companies continue to rapidly increase their AI capital investment which is also supporting economic activity. However, corporate credit spreads are widening given the AI capital spending boom. The US central bank is also warning that interest rates may be raised given that "*inflation remains elevated.*"
- Asian share markets delivered a weaker performance. Japanese, Korean and Taiwanese shares fell with more caution on future AI demand for computer chips. Chinese shares slumped with continued subdued results for consumer spending and the housing market.
- Australian shares made mild gains in October. The Utilities, Financial and Health Care sectors made very strong gains with investors becoming more defensive on Australia's prospects. However, there were sharp declines in the Resources sector, weighed down by lower global iron ore and gold prices. The Information Technology sector also declined sharply, continuing its weak performance this year.
- Australia's inflation data was again disappointing which has compelled the Reserve Bank of Australia (RBA) to raise interest rates in November. Australia's headline annual inflation climbed to 4.3% in September which is well above the central bank's 2% to 3% target range. There were also subdued results for both household spending data and the unemployment rate, which climbed to 4.7% in September.

Asset class summary

Asset class returns in Australian dollars – periods to 31 October 2026.

	CYTD %	1 month %	3 months %	1 year %	3 years pa %	5 years pa %	10 years pa %
Australian shares	4.5	1.1	0.3	3.1	13.2	7.7	9.3
Global shares (hedged)	11.7	-1.4	0.2	12.7	21.4	9.9	11.9
Global shares (unhedged)	5.4	-2.7	-0.3	4.5	18.1	11.6	13.3
Emerging markets (unhedged)	7.5	-9.1	-5.6	6.1	18.1	8.3	9.0
Global property securities (hedged)	5.6	2.4	-6.1	6.2	11.2	-0.1	3.1
Global listed infrastructure (hedged)	12.0	7.7	0.5	13.2	15.4	6.7	7.3
Australian bonds	1.9	1.2	0.1	0.4	4.6	1.0	1.8
Global bonds (hedged)	0.5	1.8	0.2	0.4	4.5	-0.1	1.4
Global high yield bonds (hedged)	1.1	0.6	-0.8	2.3	7.4	2.5	4.1
Australian inflation-linked bonds	3.5	1.3	0.6	2.0	4.4	3.0	2.9
Cash	3.5	0.4	1.1	4.1	4.2	3.4	2.3
AUD/USD	5.5	1.1	0.2	7.5	3.6	-1.3	-0.8

Past performance is not a reliable indicator of future performance.
Sources: Australian shares – S&P/ASX 300 Total Return Index; Global shares (hedged) – MSCI All Countries World (A$ hedged, Net); Global shares (unhedged) – MSCI All Countries World in A$ (Net); Emerging markets – MSCI Emerging Markets in A$ (Net); Global property securities – FTSE EPRA/NAREIT Developed (A$ hedged, Net); Global listed infrastructure – FTSE Global Core Infrastructure 50/50 (Hedged $A); Australian bonds – Bloomberg AusBond Composite 0+ Yr Index; Global bonds (A$ hedged) – Barclays Global Aggregate (A$ hedged, Gross); Global high yield bonds (A$ hedged) – Barclays US High Yield Ba/B Cash Pay x Financials ($A Hedged); Australian inflation-linked bonds – Bloomberg AusBond Inflation Government 0+ Yr Index; Cash – Bloomberg AusBond Bank Bill Index; AUD/USD – WM/Reuters Daily (4 pm GMT).

Key events in global markets over the last three months to October 2026

Global shares (hedged) made a flat quarterly return of 0.2%. Optimism on AI has been challenged by rising bond yields and energy prices over recent months. The brief ceasefire between Iran and the US collapsed in July with the resumption of military strikes and another closure of the Strait of Hormuz as a shipping route.

While global shares have shown remarkable resilience to events in the Middle East this year, this strength is now being tested as the Iran War intensifies again. Wall Street has been a key source of strength by making historic highs. Yet this strength is counterbalanced by sharp weakness in Asian and European share markets. Chinese shares have been a disappointment with a very weak -11.8% return for the MSCI index in local currency terms.

Global bonds (hedged) posted a sedate 0.2% quarterly return. Concerns over the inflation risk with rising energy prices and persistent government deficits have generated sharp rises in global bond yields this year. Australian bonds have also struggled with the inflation threat by recording a subdued 0.1% quarterly return.

Key events in Australia over the last three months to October 2026

Australian shares made a mild 0.3% quarterly return, but this was a mixed performance across industry sectors. Some of the sectors that were beaten down earlier this year have made a recovery over recent months. The Health Care sector made a remarkable revival with a 29.6% quarterly return as investors considered that Cochlear and CSL had become cheap. There were also strong gains for the Energy sector given the surge in oil and gas prices with the Middle East conflict.

However, there were large share price declines in a range of sectors exposed to the threat of higher interest rates and a consumer spending slowdown. The Real Estate sector fell sharply by -6.9%.

Australia's economy is confronting significant challenges given persistent high inflation and rising interest rates. Consumer spending is slowing as the 'cost of living' squeeze continues. Housing prices are falling sharply given higher mortgage interest rates as well as the Federal Government's major changes to capital gains tax and negative gearing in May.

Australia's high inflation remains troubling and has motivated the RBA to raise interest rates in both September and November. Persistent price pressures remain prominent in a wide range of goods and services. Housing costs have increased by 5.2% over the past year given rising electricity prices (12.8% annual inflation), new dwelling construction costs (4.7% annual) and rents (3.6%). Healthcare costs have risen by 3.7% and education has increased by 4.7% in the past year.

Global prospects

Financial markets are trying to find a balance between hopes that AI will drive strong economic growth and corporate profitability and the harsh reality that Eastern Europe and the Middle East are in turmoil.

The recent escalation of the Iran War and the Russia-Ukraine War presents a severe challenge for the global economy. Shipping costs have surged while there is limited spare capacity in fuel refineries around the globe to produce sufficient diesel and petrol supplies. If this energy shock escalates further, the pain will spread as both inflation and unemployment could dramatically rise. Central banks would then confront a major challenge in their decision making. Do central banks raise interest rates to restrain inflation pressures or lower interest rates to assist economic activity and mitigate rising unemployment?

Regrettably, major central banks seem set to raise interest rates further to address the immediate inflation threat. The US central bank joined its fellow counterparts in Europe and Japan by raising interest rates in September. Bond markets are now pricing in a sequence of further interest rate rises across the globe to address inflation risks. Global share markets could then prove vulnerable should interest rates rise sharply.

Australia's persistent price pressures in food, health and housing continue to squeeze budgets. This "cost of living" squeeze is likely to weigh heavily on consumer spending over coming months. Lower house prices will also caution some consumers on their spending.

Given these complex risks, investors should maintain a disciplined and diversified strategy.

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