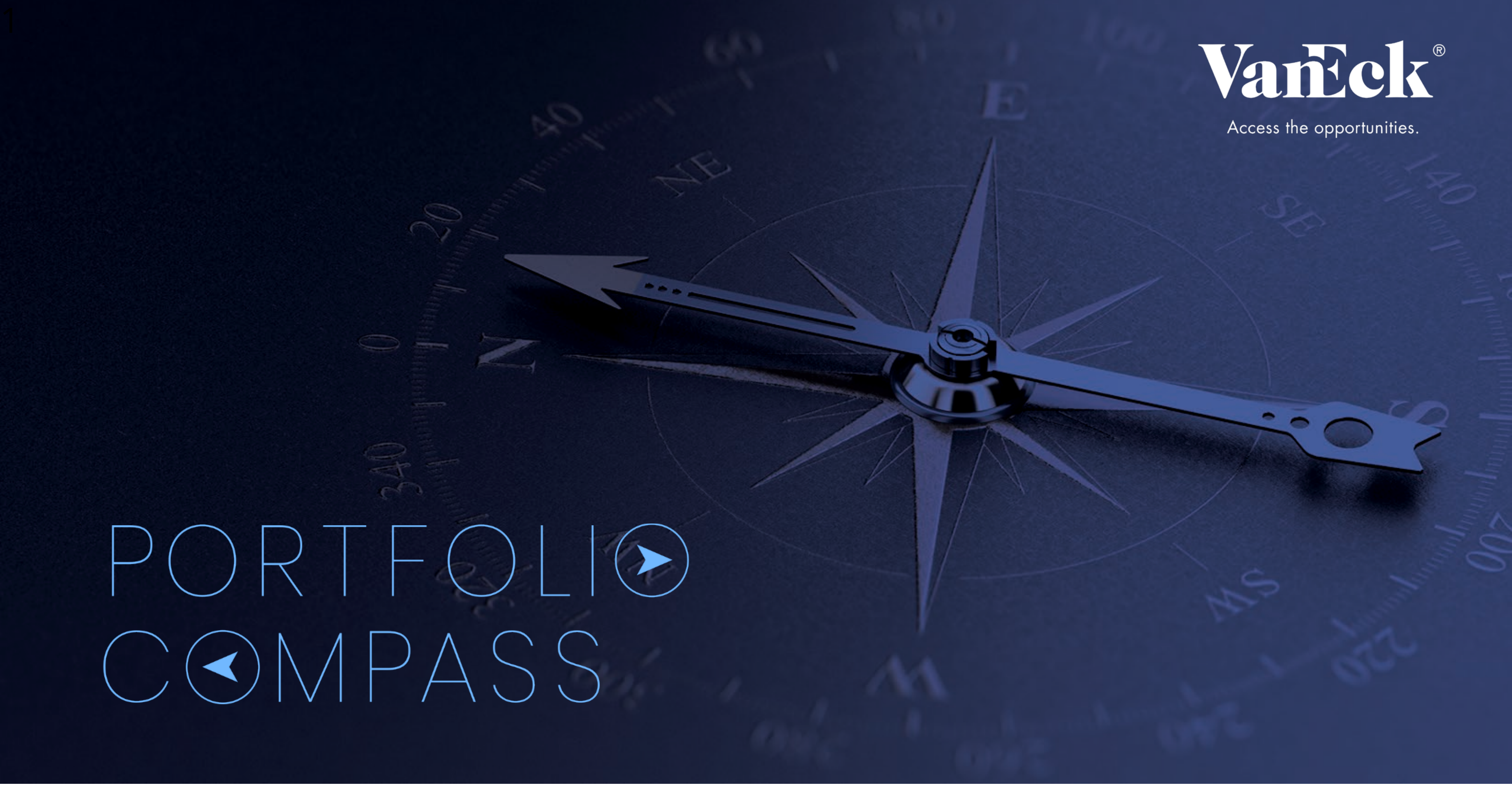


Australian Equities Outlook

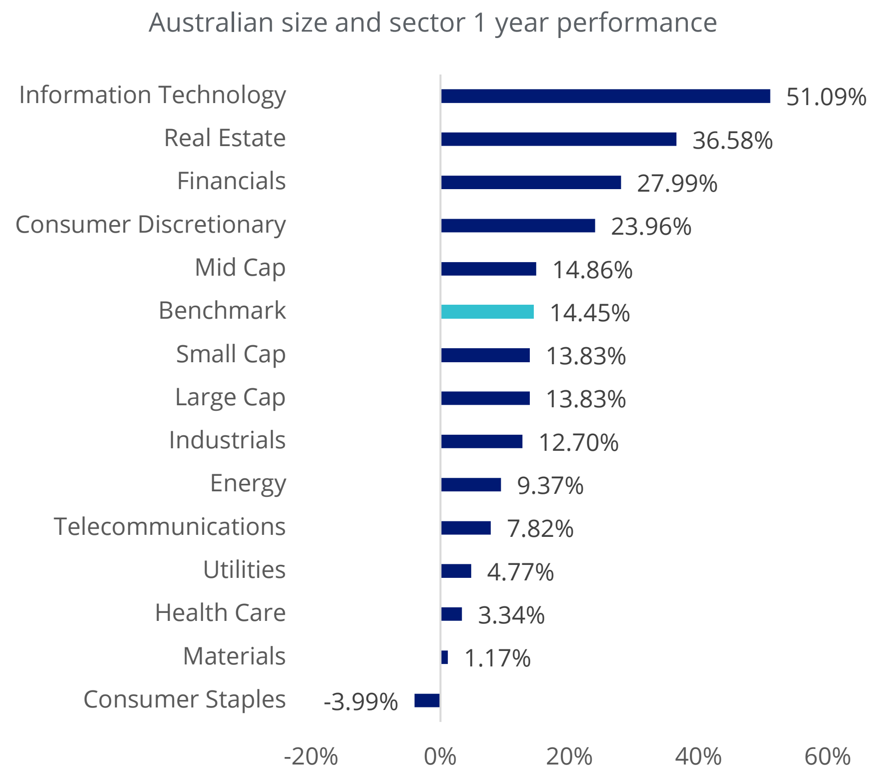
April 2024

Executive summary

If the past 12 months has taught investors anything, it's that being selective and diversified is key to riding the economic cycle. Had investors avoided risk assets on the back of many economists calling the "most anticipated recession" that never happened, they would have missed the double-digit return recorded by Australia's equity benchmark S&P/ASX 200. Market shifts in expectations for a soft landing and increasing likelihood of policy rate cuts in 2024 contributed to notably Australia's big 5 bank share prices surging to all-time highs. Unprofitable technology names also had their time in the sun again following a broad loosening in financial conditions.

VanEck's Australian Equities Outlook dissects our views on inflation, policy rates, economic growth, exogenous risks and market implications as the lagged effect of the one of the sharpest rate hike cycles may hit hard this year. On balance, Australia should avoid a recession with the RBA holding the cash rate at 4.35% until at least 2025. Inflation may prove to be stickier than the market anticipates, which reaffirms our higher-for-longer bias.

Australian mid-caps could be set to shine. Valuations are attractive and smaller companies typically outperform in a recovery. Sector wise, A-REITs, industrials and consumer discretionary are our picks.



Source: Bloomberg, 31 March 2023 to 31 March 2024, returns in Australian dollars. Utilities is S&P/ASX 200 Utilities Index, Industrials is S&P/ASX 200 Industrials Index, Materials is S&P/ASX 200 Materials Index, Consumer Staples is S&P/ASX 200 Consumer Staples Index, Consumer Discretionary is S&P/ASX 200 Consumer Discretionary Index, Financials is S&P/ ASX 200 Financials Index, Energy is S&P/ASX 200 Energy Index, Healthcare is S&P/ ASX200 Heath care Index, Telecommunications is S&P/ASX 200 Telecommunications Index, Information Technology is S&P/ASX 200 Information Technology Index, Real Estate is S&P/ASX 200 AREIT Index, Large Cap is S&P/ASX 20 Index, Mid Cap as S&P/ASX Mid Cap 50 Index, Small Cap as S&P/ASX Small Ordinaries, Benchmark is S&P/ASX 200 Index. Past performance is not a reliable indicator of future performance. You cannot invest directly in an index.

Australia macro views

1. Disinflation pace to slow
    - Australia has a ‘homegrown’ inflation problem

2. Rates higher for longer
    - Market overestimating the likelihood and speed of RBA rate cuts

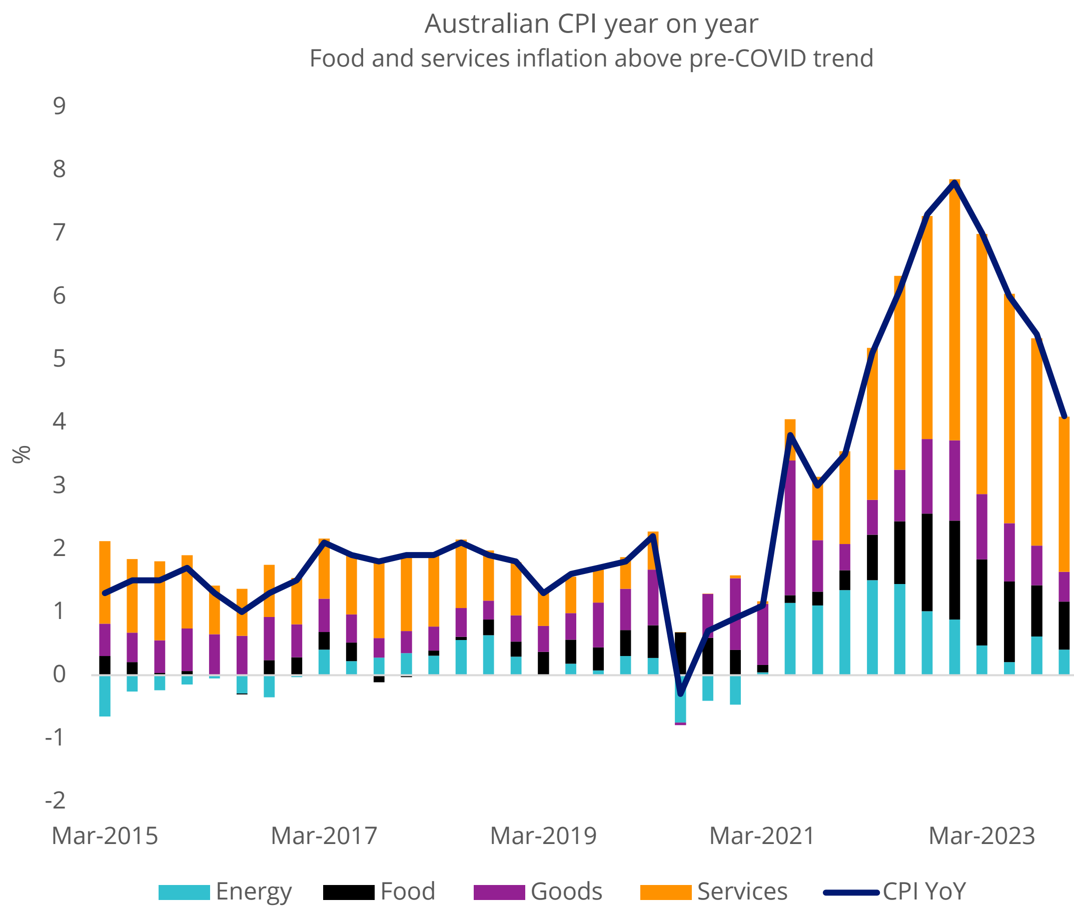
3. Soft landing
    - Paradoxical dynamic could play out where economic growth is resilient but mortgage stress increases.
    - Australia’s migration surge will support aggregate spending but a "rates higher for longer" environment squeezes household budgets.

4. Exogenous risks
    - Economic ‘break’ risk heightened in wake of tightening
    - Geopolitical tension elevates risks of inflation shocks

Disinflation pace to slow

Inflation 'homegrown'

- Inflationary components are supply- side driven which risks broader inflation expectations increasing.
- Services inflation is high due to accelerating rental prices and wages growth.
- Food inflation is elevated due to higher operating costs and minimum and award wage increases.
- Energy prices have picked up with producers pushing through ~20% increases in July. The headline contribution would have been higher if not for the Energy Bill Relief Fund rebates effective from July 2023.



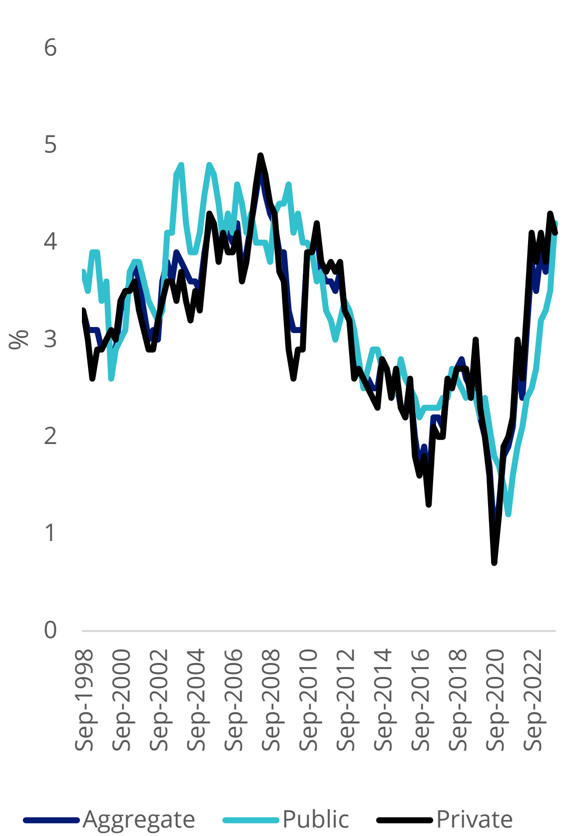
Source: Australian Bureau of Statistics, as at 31 March 2024.

Disinflation pace to slow

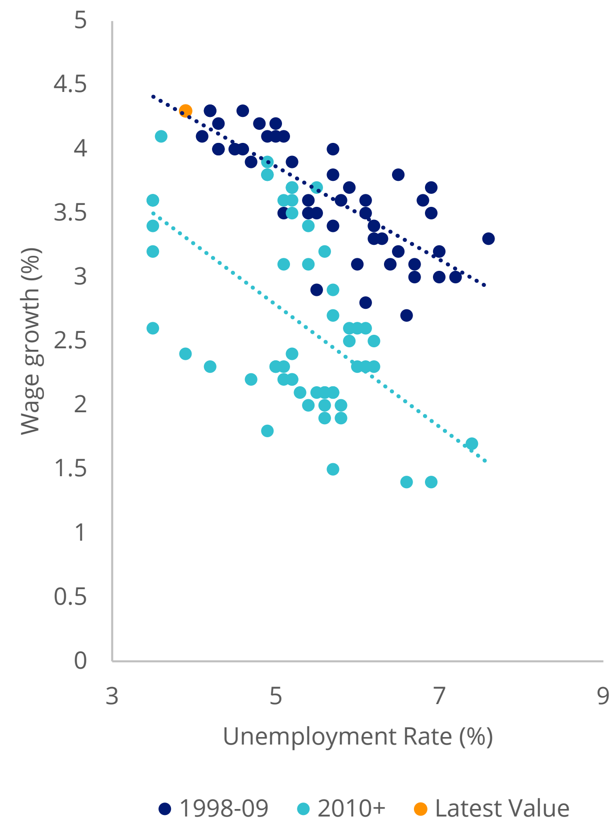
Strong wages growth adds pressure to services inflation

- State governments removed public sector wage growth caps to address falling real wages growth in response to accelerating inflation.
- Fair Work Commission pushed through minimum and award wage increases just shy of the headline inflation rate last year.
- Near record low unemployment contributed to an acceleration in private sector wages. However, will likely subside as economic growth slows and unemployment creeps up as the RBA maintains a prolonged tightening stance.
- Wage inflation spiral is a genuine threat. Aggregate wages growth is above the RBA's published target rate of 3.5% and is not supported by productivity gains. This risks fuelling higher inflation expectations.
- In a higher inflation environment, it will be difficult for workers under bargaining arrangements to stomach wage increases considerably below headline inflation given the strength of unions.
- Wages growth is likely to remain in the pre-global financial crisis range (3-5%) given the strength of labour market conditions.

Australian Wages Growth year on year



Wages growth versus Unemployment Rate



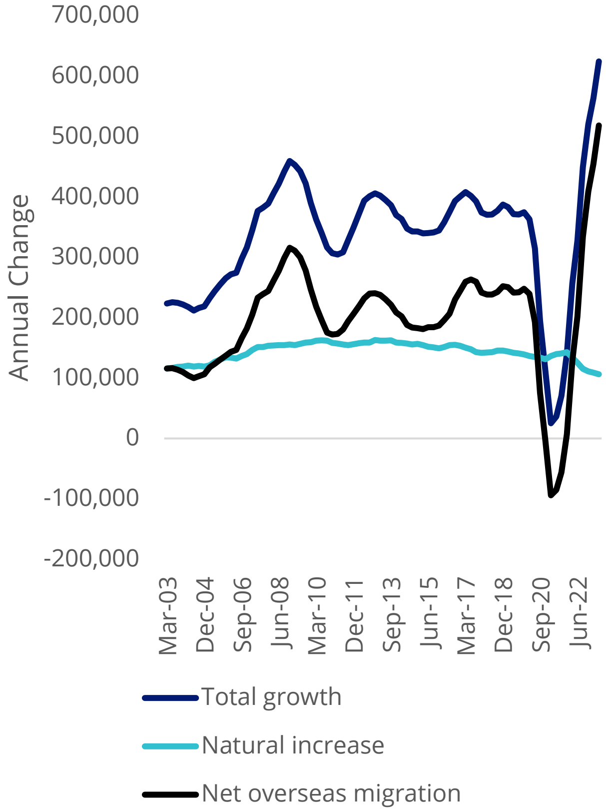
Source: Australian Bureau of Statistics, as at 31 March 2024.

Rates higher for longer

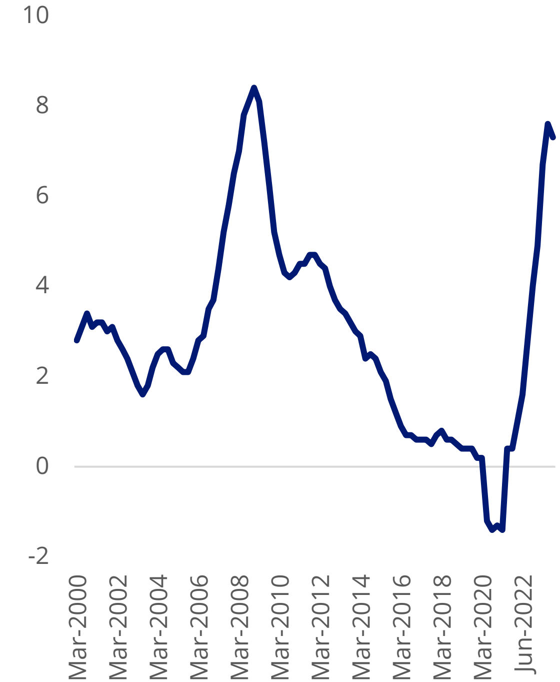
Reserve Bank of Australia contending with supply side constraints

- Migration surge has fuelled inflation.
- Rental inflation which is the largest contributor to services inflation is the highest since 2009. It shows little sign of easing.
- It took 4 years for rental inflation following the Global Financial Crisis (GFC) to return to a 2-3% range.
- Rental vacancy rate at an all-time low and new housing supply is scarce.
- Inflation drivers are structural, limiting monetary policy effectiveness and reinforces VanEck's tightening bias.

Australian Population Annual Change
Migration surge fuelling inflation



Australia Rent Inflation year on year
Highest since the Global Financial Crisis

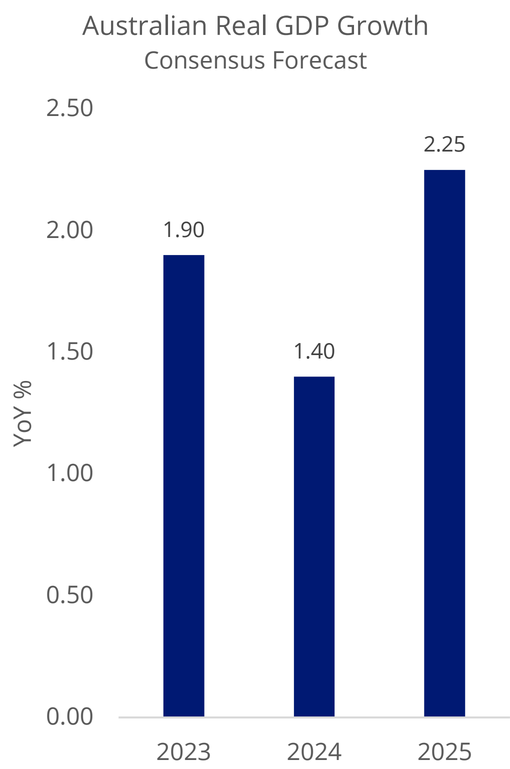


Source: Australian Bureau of Statistics, as at 31 March 2024.

Soft landing

Tightening policy to hit hardest during the middle of the year

- High migration is adding inflationary pressures but is beneficial for growth over the medium term. Non-residents have been recent drivers of aggregate consumer spending growth. Australian residents have curbed spending to tackle higher mortgage repayments.
- RBA's mandate of achieving "price stability and full employment" increases the chance of a soft landing. The bank has noted that their primary objective is to avoid a recession at the expense of a longer period of elevated inflation. RBA's latest forecast has inflation returning to the 2-3% target range in late 2025.



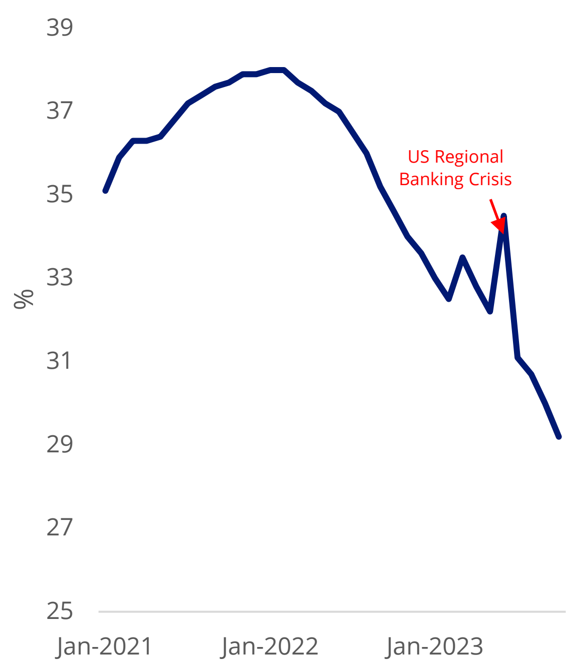
Source: Bloomberg, as at 31 March 2024. *Bloomberg consensus forecast,

Exogenous risks

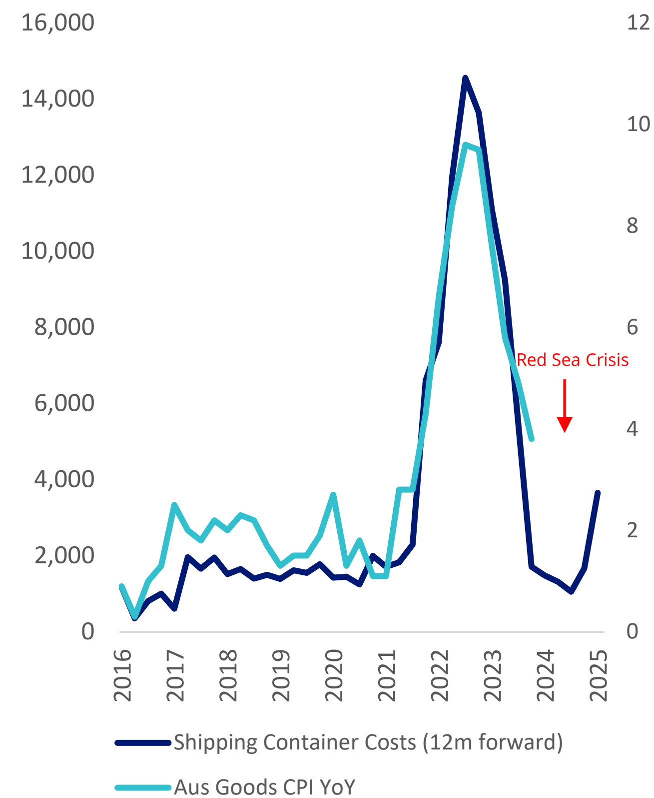
Watch out for economic 'breaks' and inflation shocks

- The risk of an economic 'break' is heightened in the wake of the tightening cycle.
- The RBA and global central banks will be swift to address but likely turn to targeted measures before policy rate adjustments. Inflation is too high, and they do not want to risk triggering another wave of inflation. The Federal Reserve implemented target liquidity measures following the US regional banking crisis last year.
- Geopolitical tension elevates the risks of future inflation shocks. Energy prices spiked following Russia's invasion of Ukraine.
- The latest concern is the Rea Sea Crisis which has resulted in ships that would normally pass between Saudi Arabia and Egypt to instead go all the way around Africa to get to Asia. The outcome has seen shipping prices jump 3.5 times. When shipping prices spiked following COVID-19, it took 6-12 months to be passed on to consumers via goods prices. We could see this again in the second half of 2024.

Fed balance sheet - % of GDP
Targeted liquidity following the US regional banking crisis



Shipping Costs versus Aus Goods CPI YoY
Shipping costs surged following the Red Sea Crisis



Source: Federal Reserve, ABS, Bloomberg, 31 March 2024.

Pulse check: Australian February earnings season highlights

1. Australian companies shine

- Earnings per share beats outweigh misses 3:2
- Resilient consumer spending, cost management, inflation moderation and positive economic outlooks typified many company's results.

2. Large caps, consumer discretionary, real estate and information technology sectors were the standout

- Strong results are a due to Australia's economic and consumer resilience despite the rapid increase in the RBA cash rate.

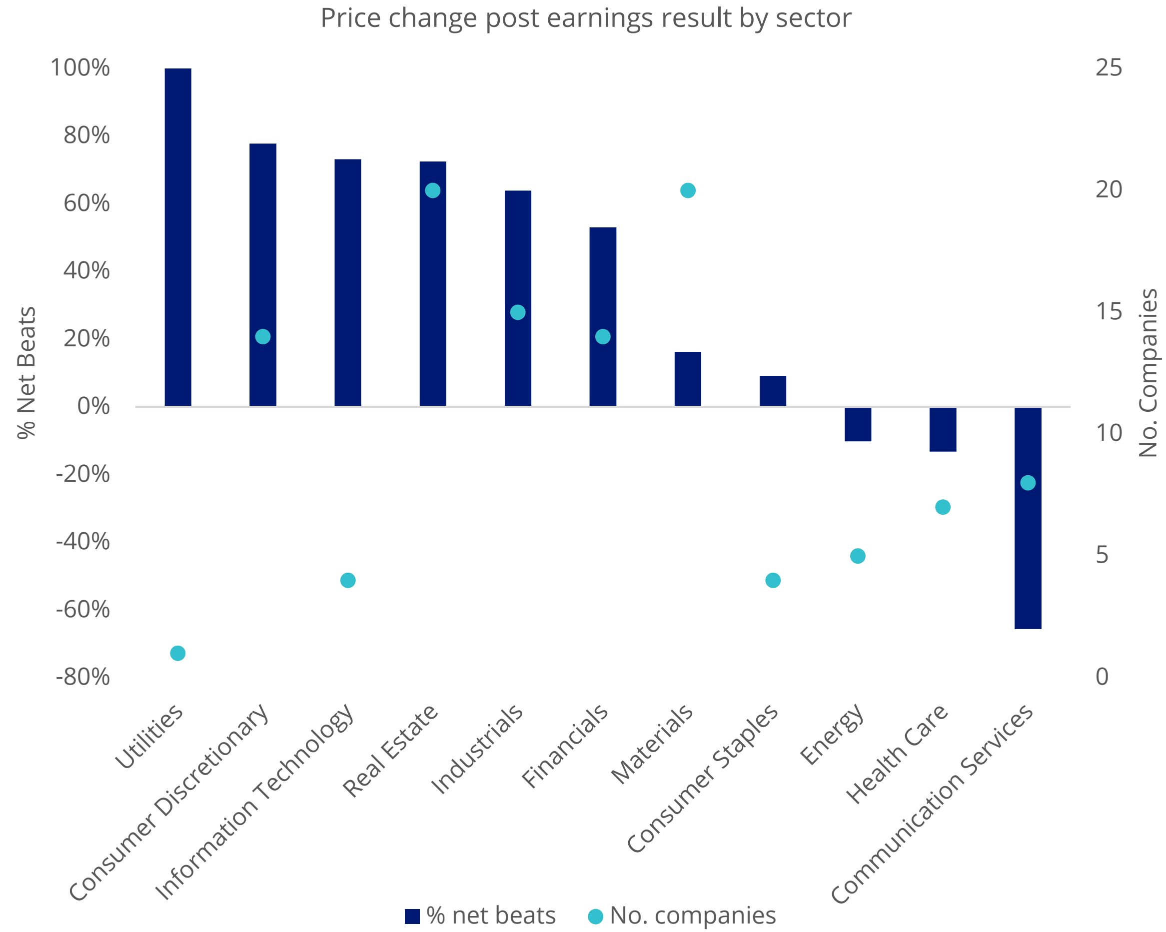
3. Looking ahead, mid cap exposure attractive

- Mid caps reported the highest upside price target consensus revisions.
- Australian banks notably CBA overvalued. Market underestimating the threat of mortgage stress risk.
- This environment bodes well for a potential mid-caps rally, supported by overweight exposure to cyclical sectors such as industrials, consumer discretionary and real estate.
- These sectors would be beneficiaries in a period characterised by resilient consumer spending and moderate inflationary pressures.

Australian February earnings season review

Australian companies shine. Earnings per share (EPS) beats outweighed misses 3:2

- Resilient consumer spending, cost management, inflation moderation and positive economic outlooks typified many company's results.
- Cyclical sectors such as consumer discretionary, real estate and information technology sectors were the standout. Strong results are a due to Australia's economic and consumer resilience despite the rapid increase in the RBA cash rate. Wesfarmers (ASX: WES) was the standout with earnings 4% ahead of consensus, benefiting from moderation in inflationary cost input pressures and Kmart delivering strong growth in high-margin segments.
- Communication services and health care reported the most misses. Seek (ASX: SEK) was an earnings miss following a slowdown in job advertisements in the second half of 2023.
- Mid-caps recorded the strongest upside price target revisions.



Source: Bloomberg, Index Weighted, as at 29 February 2024. S&P/ASX 200 sector indices.

Australian equity market views

Australian Equities

- Recent performance breakout is sustainable
- Valuations attractive
- We forecast S&P/ASX 200 to reach 8,300 by year end (+6.4%)

By Size

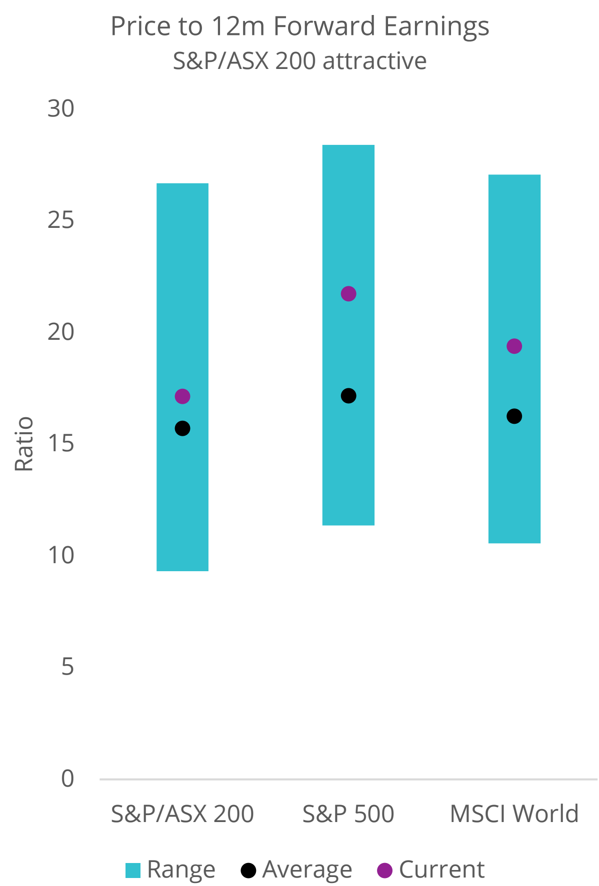
- A prolonged recovery could see mid caps outperform
- Mid cap and equal weight valuations attractive

By Sector

- Australian banks overvalued
- Gold miners, office and retail REITs undervalued

Australian equities

Australian equities breakout is sustainable. Soft landing supportive and valuations attractive relative to global equities



POSITIONING

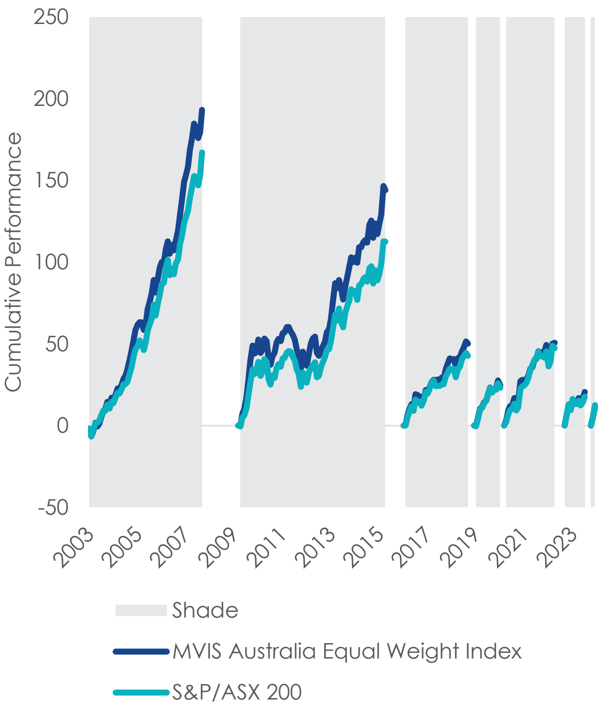
- S&P/ASX 200 has been range trading between 6500 and 7500 for the past two and a half years, weighed down by the surge in interest rates, stagnate earnings growth and fears of an imminent recession.
- However, in recent months, Australian equities broke the cycle, surging to 7,800.
- A soft landing is looking increasingly likely, supporting market confidence.
- Valuations are more attractive relative to the US and broader global equities.
- Australian equity price to 12 months forward earnings trading near its historical average.
- We forecast S&P/ASX 200 to reach 8,300 by year end (+6.4%)

Source: Bloomberg. 1 January 2000 to 31 March 2024.

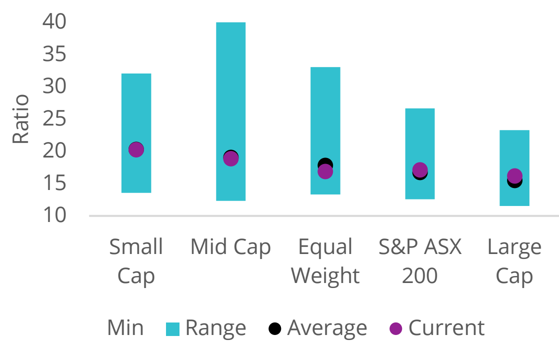
Size

Harness the size premium during a recovery. Mid caps via equal weighting is the sweet spot

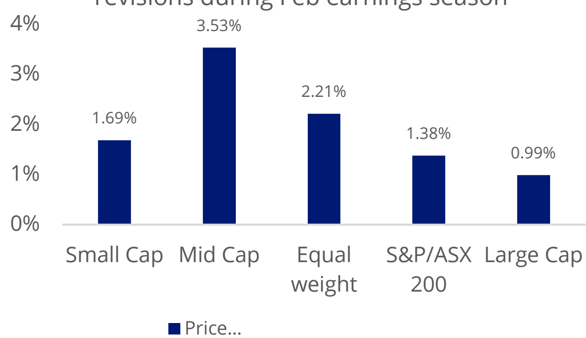
S&P/ASX 200 versus Equal Weight cumulative performance
Equal Weighting historically outperforms during a recovery



Price to 12m forward earnings
Equal weight below historical average



12 month consensus price target revisions during Feb earnings season



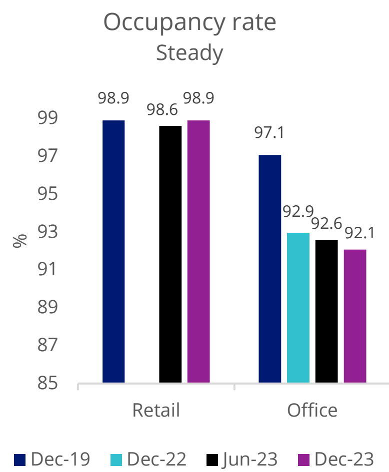
POSITIONING

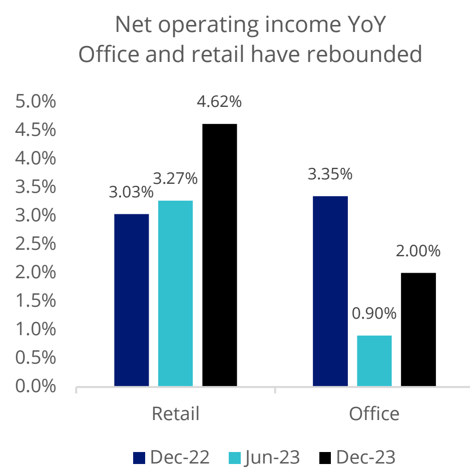
- Large caps, namely the big 5 banks have driven the market's return, supported by an increasing likelihood of a soft landing and lower than expected mortgage delinquencies. However, share price appreciation has outpaced earnings growth with price to 12 month forward earnings (forward PE) above its historical average.
- However, an economic recovery could see mid caps and equal weight outperform for several reasons.
- Smaller companies offer more upside potential through market share expansion and have historically outperformed as markets heat up.
- Valuations are attractive. Forward PE is trading below its historical average.
- Mid caps also reported the highest upside price target revisions during the latest earnings season.

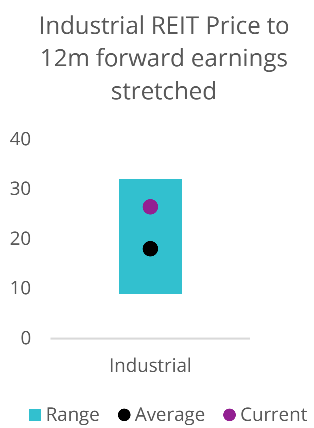
Source: Bloomberg, 31 January to 29 February 2024 (price change), 1 April 2014 to 31 March 2024 (PE ratio), Large Cap as S&P/ASX 20, Mid Cap as S&P/ASX Mid Cap 50, Small Cap as S&P/ASX Small Ordinaries, Equal Weight as MVIS Australia Equal Weight. The ASX index series is shown for comparison purposes as it is the widely recognised benchmark series used to measure the performance of the Australian equities market. It weights companies by market capitalisation. MVW's index (MVIS Australia Equal Weight) measures the performance of the largest and most liquid ASX-listed companies, weighted equally at rebalance. MVW's index has a different amount of companies and different industry allocations than the S&P/ASX indices. PastPast performance is not indicative of future results. You cannot invest in an index. Results assume immediate reinvestment of all dividends.

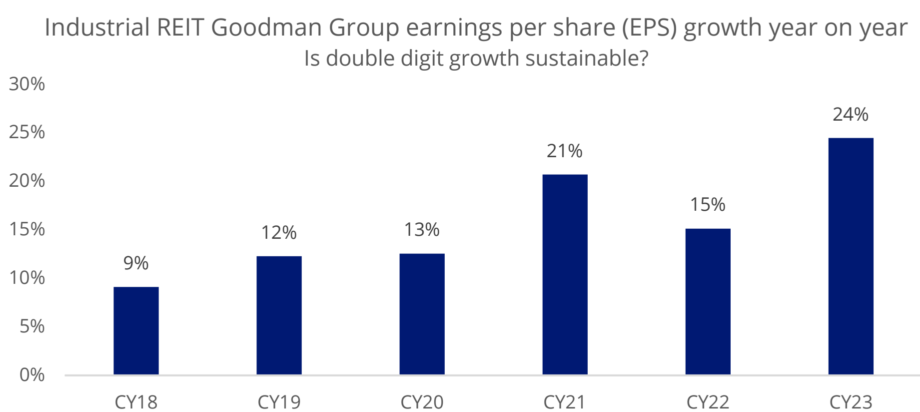
Real estate

Interest rate stabilisation and soft landing supportive. Office and retail REIT valuations attractive









POSITIONING

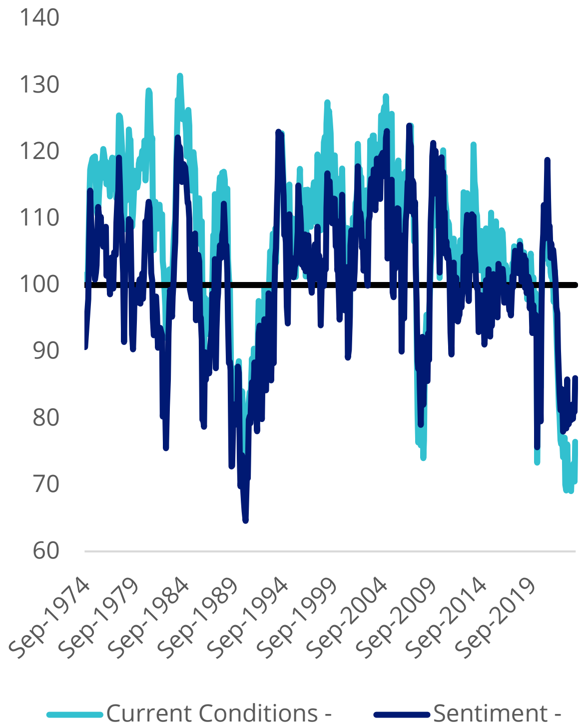
- A-REITs well positioned for several reasons.
- Interest rate stabilisation and positive economic outlook improves confidence in the assessment of valuations, encouraging capital recycling.
- REIT leverage levels have decreased, and interest coverage levels have increased steadily since the global financial crisis.
- Office REITs offer attractive discounts to NTA. Fall in occupancy rates has stabilised and net operating income has picked up.
- Retail REITs are fairly priced. Occupancy rates strong and net operating income has accelerated.
- Industrial REIT Goodman Group forward PE is trading at the upper bound of its historical average. It could be vulnerable to a correction if double digit earnings growth is not maintained.

Source: Office as equal weighting of DXS, GPT, SGP, MGR, ABP and GOZ. Retail as equal weighting of VCX, GPT, SCG, SGP, MGR, CQR, SCP, HDN. Industrials as GMG. As at 1 January 2009 to 31 March 2024.

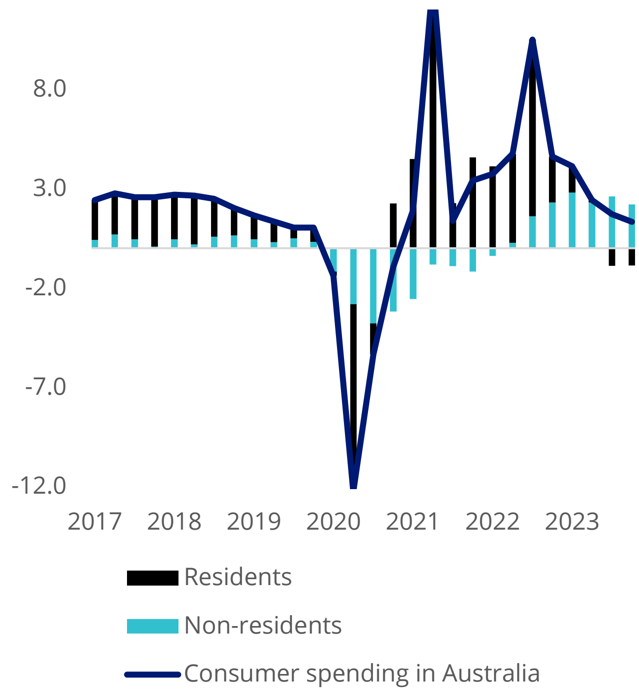
Consumer discretionary

Paradoxical dynamic: Australia's migration surge supports aggregate spending but a "higher rates for longer" environment squeezes household budgets

Westpac Consumer Survey
Early sign of improvement



Australian Consumer Spending YoY
Migrants offsetting resident spending slowdown



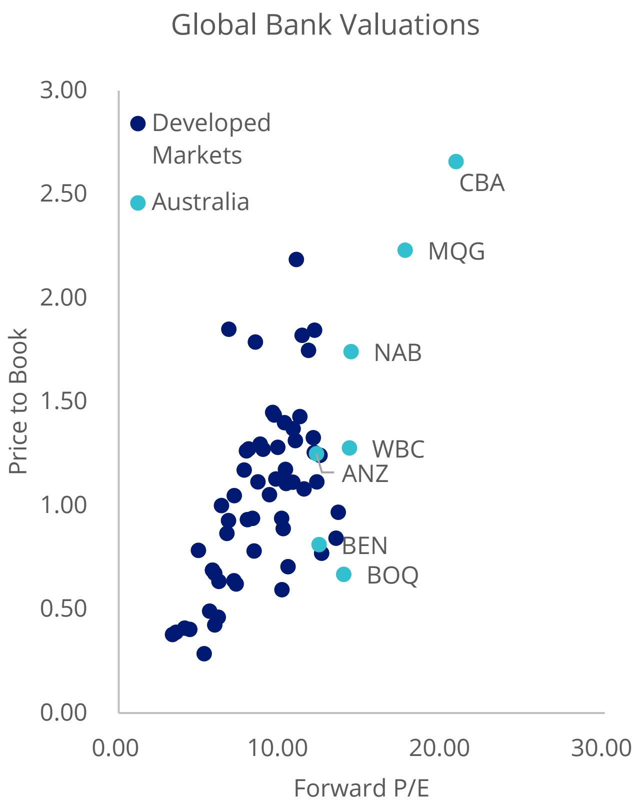
POSITIONING

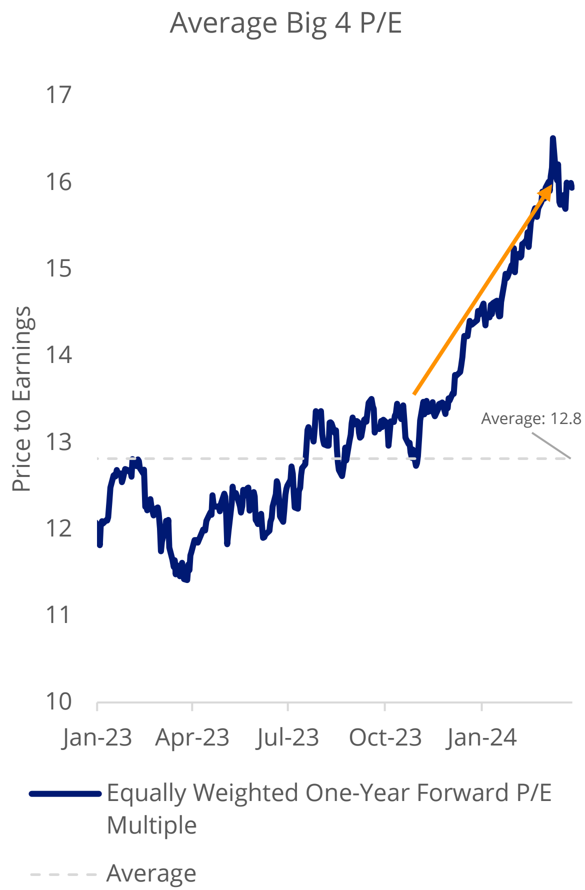
- Looking ahead, we could see a paradoxical dynamic play out where economic growth is resilient but mortgage stress increases as rates stay higher for longer. Australia's migration surge 'non residents' will continue to support aggregate retail spending and therefore consumer discretionary performance.
- The sector reported strong net beats during the latest earnings season.
- Near record low unemployment and improvement in Australia's economic outlook will likely improve consumer confidence and support spending.

Source: Westpac, ABS, Morgan Stanley.

Banks

Australian bank valuations stretched. Highest globally





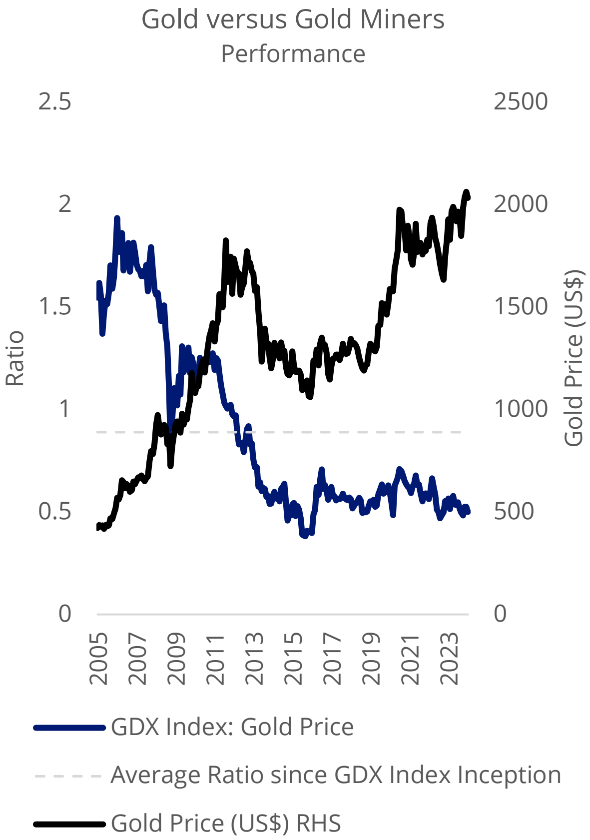
POSITIONING

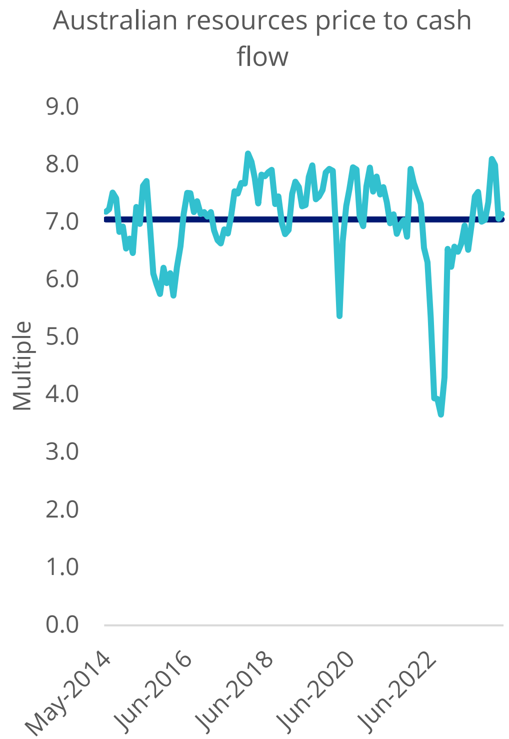
- Big 5 bank share prices surged over the past few months outpacing earnings growth resulting in stretched valuations. Performance is supported by the market shift in expectations for a soft landing and increasing likelihood of policy rate cuts in 2024.
- However, Australian banks are the most expensive globally and 12-month forward PE at the upper bound of its historical average. The sector is vulnerable to a potential correction.
- The market seems to be pricing a dream scenario for the banks, despite the risks of a flare-up in mortgage stress in a prolonged higher interest rate environment.
- Mid cap and equal weighting are two ways to reduce bank exposure.

Source: Bloomberg, 31 March 2024.

Materials

Gold miners undervalued. Iron ore and coal miners fairly priced





POSITIONING

- Persistent inflation, potential bumpy economic path and heightened geo-political tensions could serve as a tailwind for gold miners.
- With rate cuts on the horizon, even though they have been delayed, real yields have cooled, increasing the relative attractiveness of non-interest-bearing gold.
- Gold miners trading are at a 50% discount to gold, presenting a strong value opportunity.
- Gold miners have deleveraged and offer strong balance sheets.
- Central bank gold purchases have accelerated over the past two years, supporting bottom-up support for the yellow metal.
- Iron ore and coal miners could come under pressure on the back of soft GDP and consumer / business sentiment data coming out of China. Industrial production growth is below pre-covid levels and local authorities have not committed to significant fiscal measures.
- However, valuations are fair. Price to cash flow is near the historical average. If China authorities do announce fiscal measures, Australian resource companies would be significant beneficiaries like we saw following the global financial crisis.

Source: Bloomberg, VanEck. Data as of 31 March 2024. Global Gold Miners Index is the NYSE Arca Gold Miners Index. Price to cashflow is MVIS Australia Resources Index. Past performance is not indicative of future results. You cannot invest in an index.

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