Markets and Macro Update

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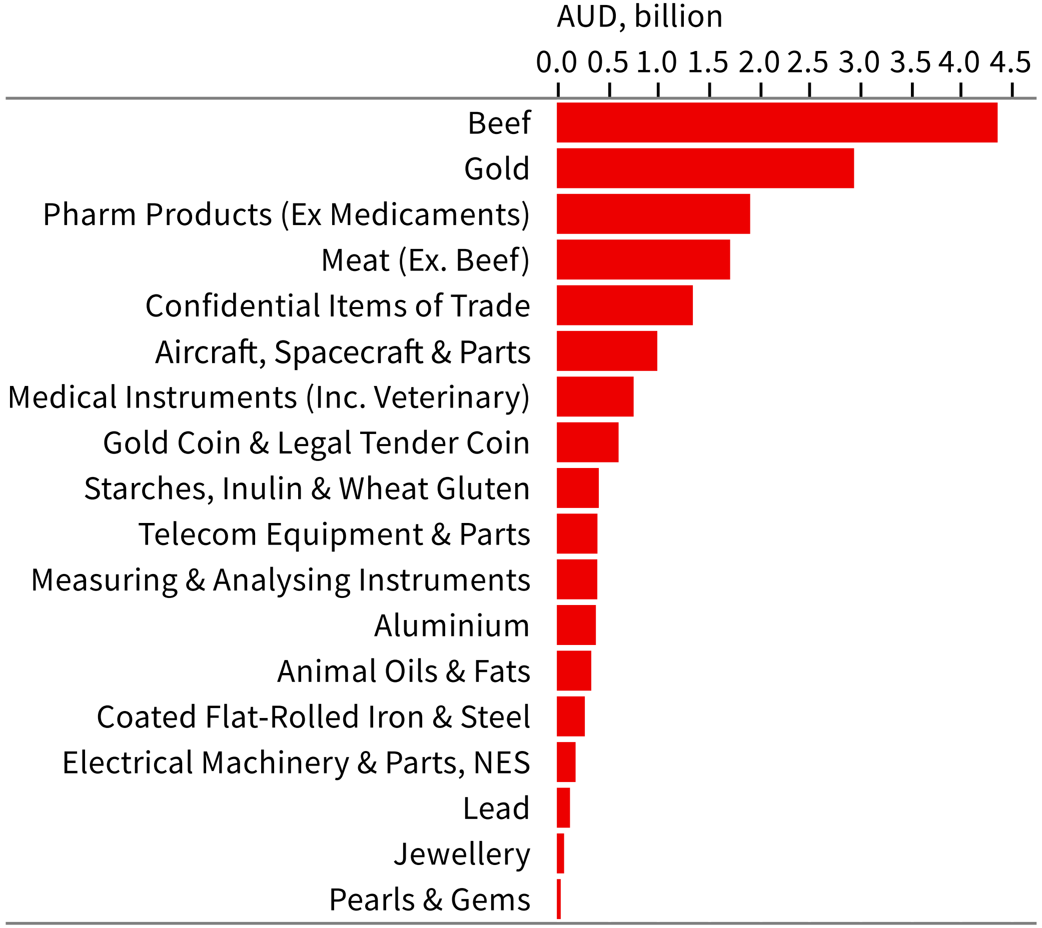
Some facts on Australian trade with the US

- **From a product view beef is our largest export to the US:**
  - The US accounts for 23% of our beef exports, 39% go to Japan, 14% go to Korea and 24% to the rest of the world
  - Australia is a much smaller beef producer than the US, but US producers focus on high end markets.
- **Gold is the second largest export** (and gold coins are also a relatively large export):
  - Beyond that, the value of exports to the US reduces quickly and tends to be in highly specialised areas i.e. Pharmaco Products, medical instruments.
  - Note: aircraft, spacecraft & parts are 40% re-exports (ie we service planes in Australia for other carriers).
- **Australian exports to the US are less than 5% of our overall export basket**

Australia Goods Exports to the US (2024)



Source: National Australia Bank, DFAT

A new regime

A framework to think about Trump 2.0

Out

- Secular multi-decade decline in interest rates
- Boost to valuations in other asset classes (equities, property infrastructure)
- Inflation declines and inflation vol falls, facilitating the "Great Moderation"
- Private sector leverage rises
- Free movement of goods and labour across borders
- Free trade supported by rules-based system (WTO)
- Comparative advantage drives trade
- Age of the multi-national and liberal democracy
- Capital wins vs. labour and takes a greater share of GDP
- Peace dividend dominates
- Asis as a centre of production, US a centre of consumption

In

- Economic security and national interest subordinates foreign policy, increased use of "Economic Statecraft" :
  - ✓ Tariffs
  - ✓ Export controls
  - ✓ Sanctions
- Restrictions on immigration
- "Higher for longer" rates outlook as equilibrium real rates move higher and term premium reprices
  - ✓ Valuation boost over for growth assets
  - ✓ Steeper curves
- Rules based trading system no longer
- Near-shoring / Friend-shoring / Onshoring
- Re-industrialisation / Re-militarisation / Reconstruction
- Public sector leverage rises
- Consumption shift from US to Asia

Some long-term implications

A framework to think about Trump 2.0

Lower long-term growth in the US

- Tariffs raise the cost of investment for US firms; all else equal, this should lower firm's demand for investment goods
- Tariffs encourage rent seeking behaviour, which diverts resources away from productive economic activity
- Innovative and productive firms tend to be more globally connected

Higher inventory levels and higher macro volatility

- In a world of less efficient and possibly disrupted supply chains, the desire to hold inventories will be higher
- Security of supply of key commodities, critical inputs into production and consumption goods will mean governments, businesses and households will run higher levels of inventories, all else equal
- However, inventory management can pose challenges to business profitability and government budgets (too much / too little of the right /wrong good and the right / wrong time)

A desire to hold fewer US assets

- A rethink of optimal allocations to USD assets by ex-US investors will require a cheapening of both the USD and US financial assets

Structurally higher inflation

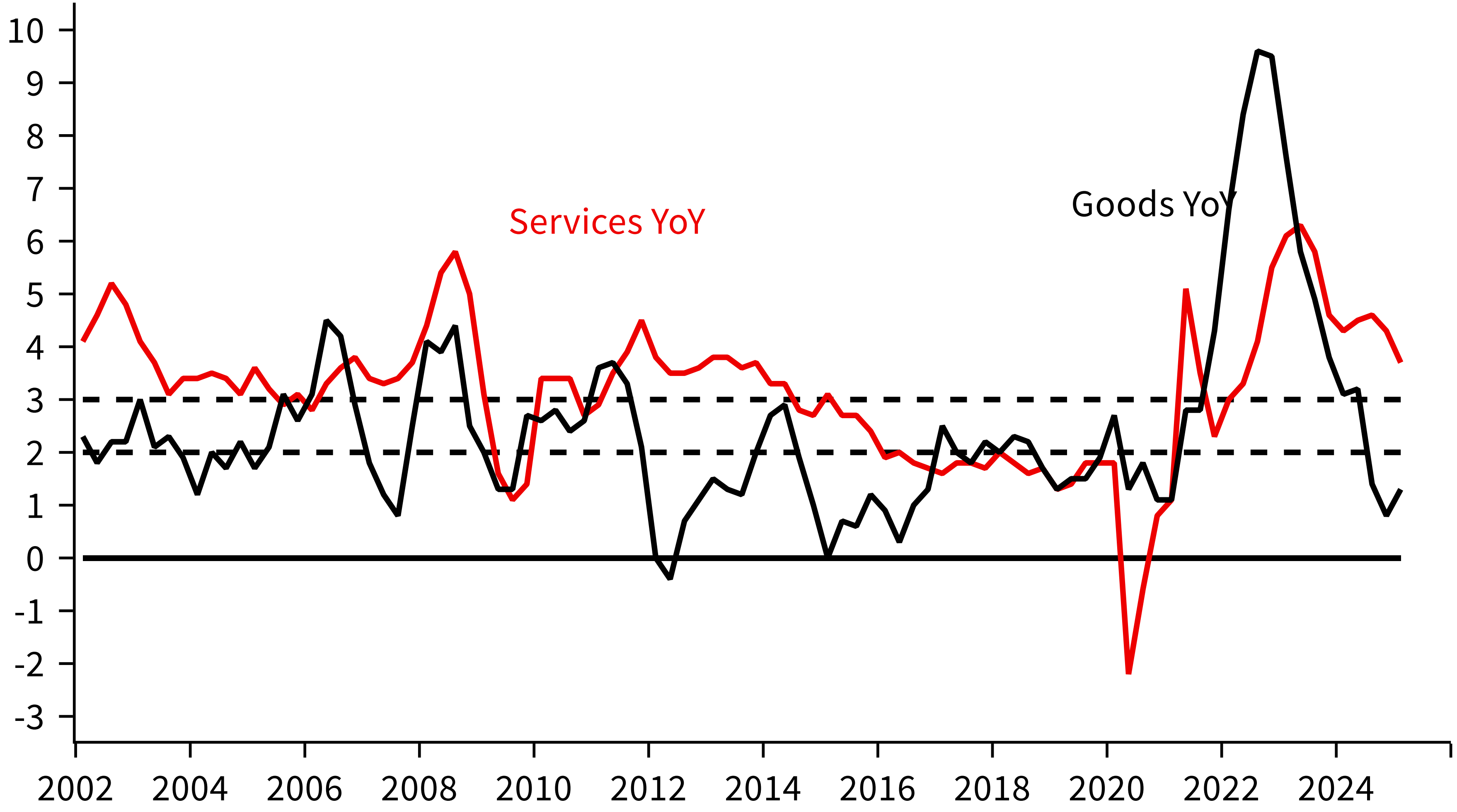
- A less efficient organization of production and supply, together with higher frequency of climate-related events, will likely mean both structurally higher inflation and more volatile inflation outcomes

Commodity demand to rise

- In part, a consequence of broader themes such re-industrialization, re-militarization and reconstruction
- In a world of more uncertainty – particularly as it pertains to supply chains, national interest, security alliances and energy supply – countries with a natural endowment of commodities (both soft and hard) are likely to be sought after
- Positive for commodity currencies

Inflation

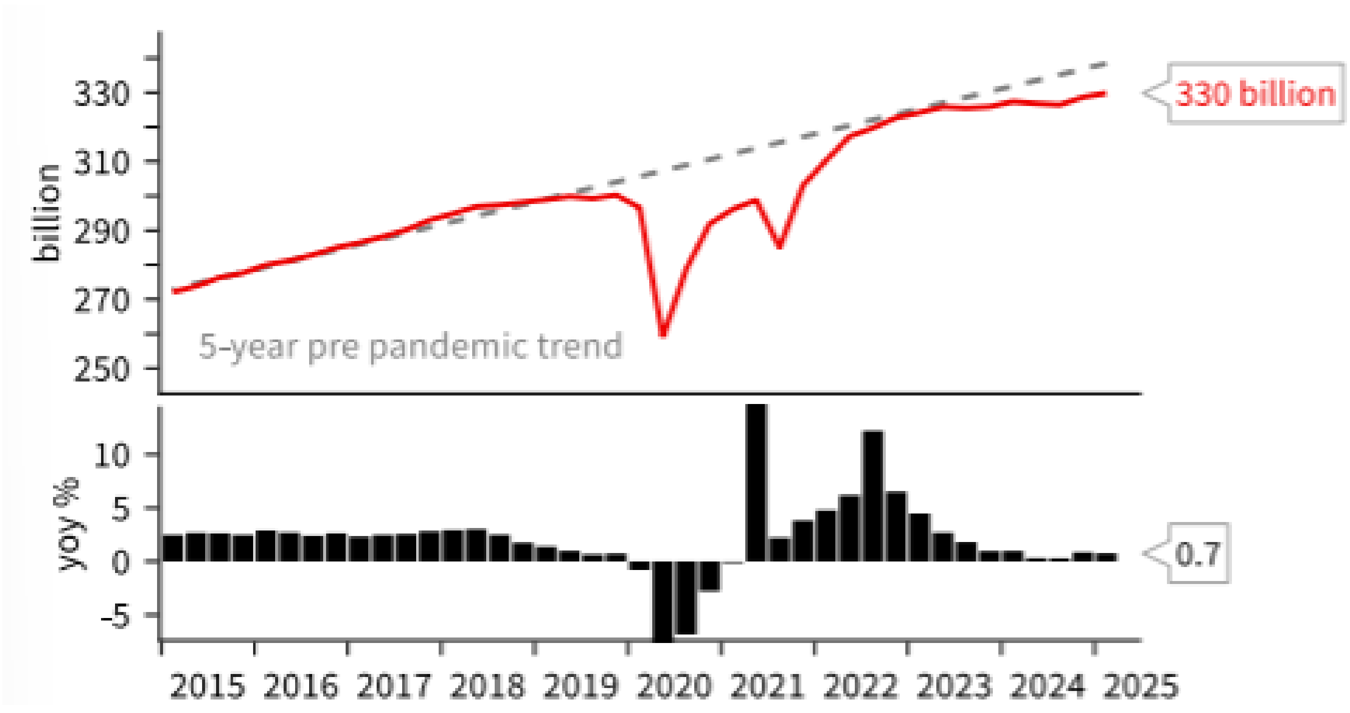
Goods and Services Inflation



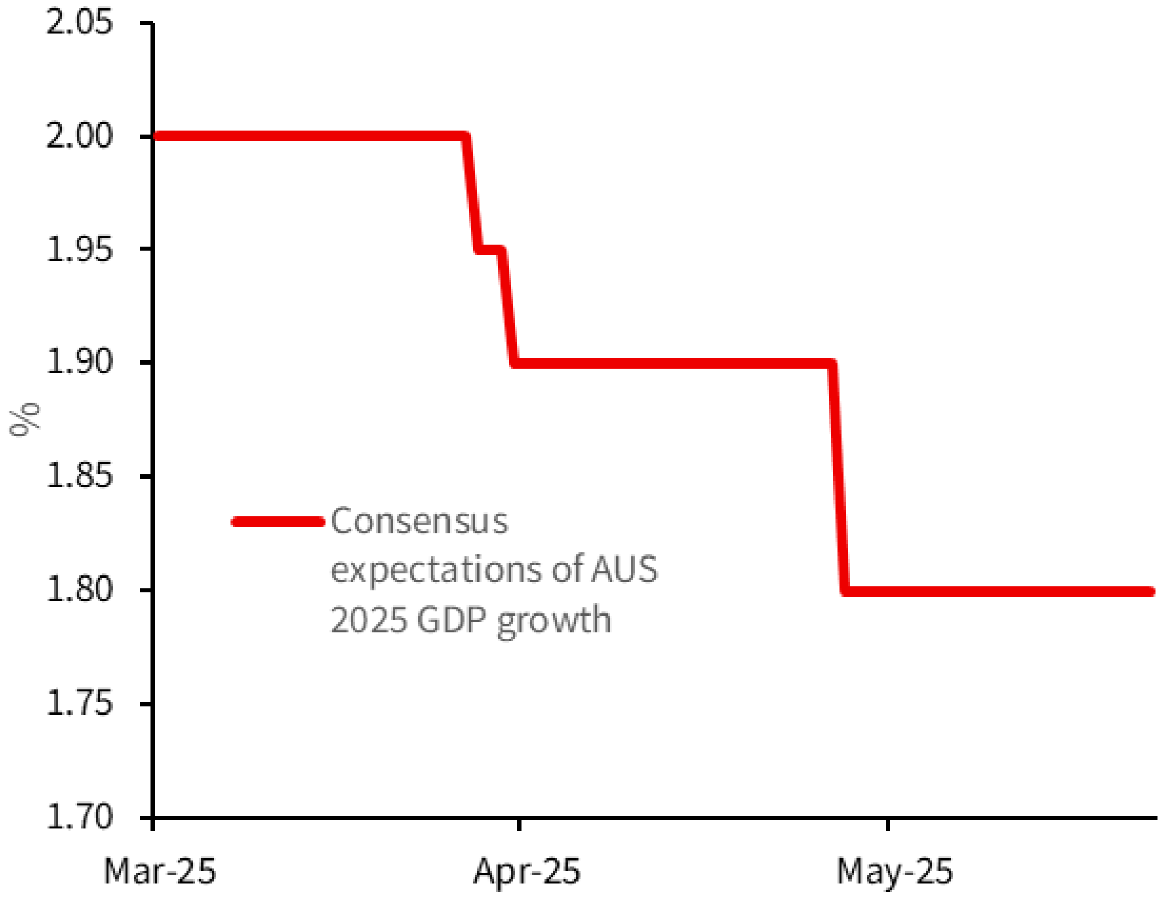
Source: National Australia Bank, Australian Bureau of Statistics, Macrobond

The consumer has disappointed so far this year

Household consumption



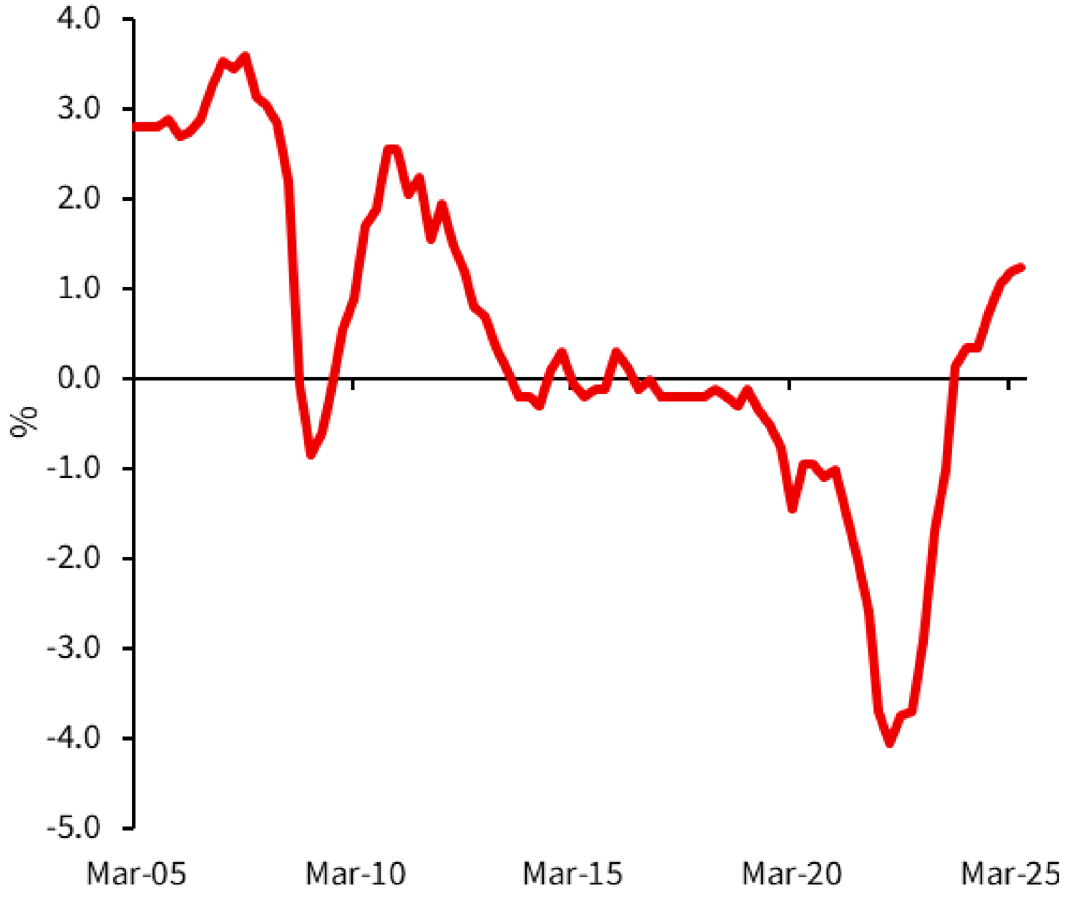
GDP growth has been downgraded



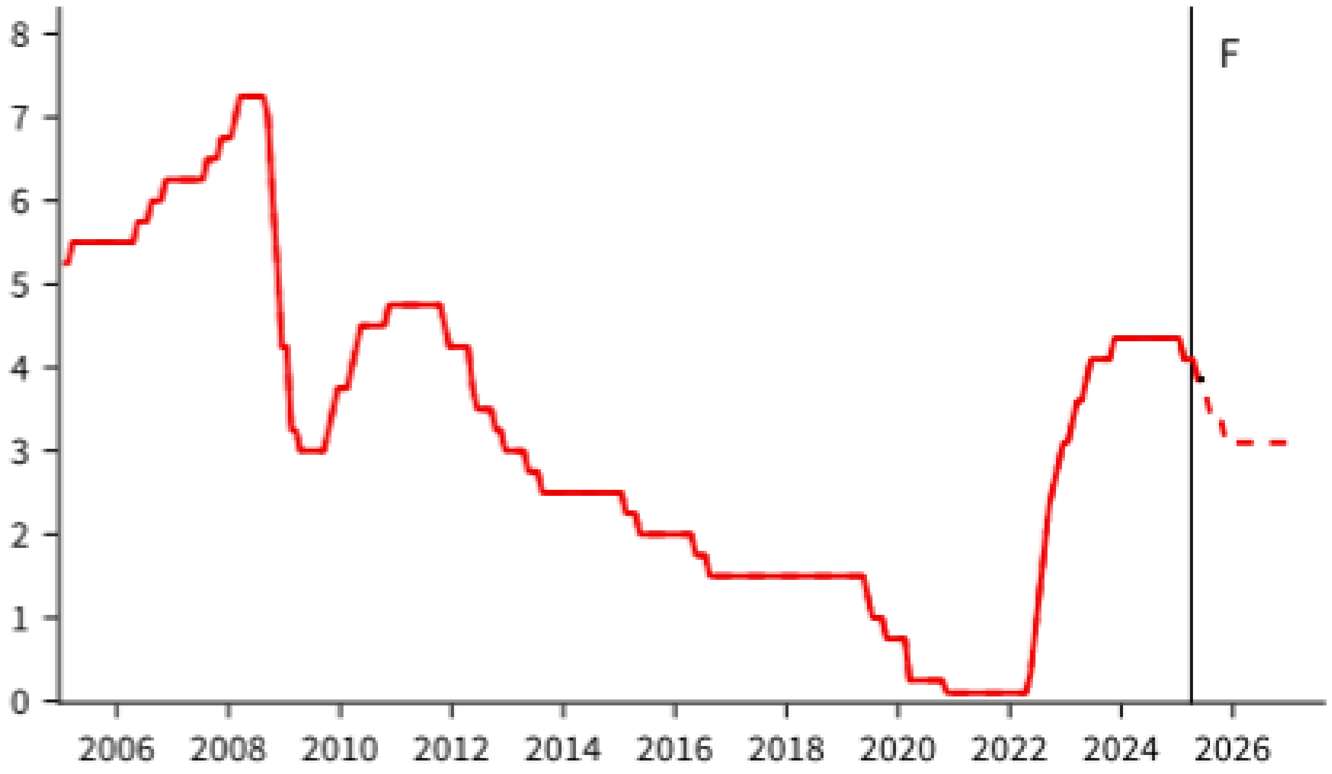
Source: RBA, ABS and NAB.

The RBA need a relatively quick return to a neutral policy setting

AUS real cash rate is elevated



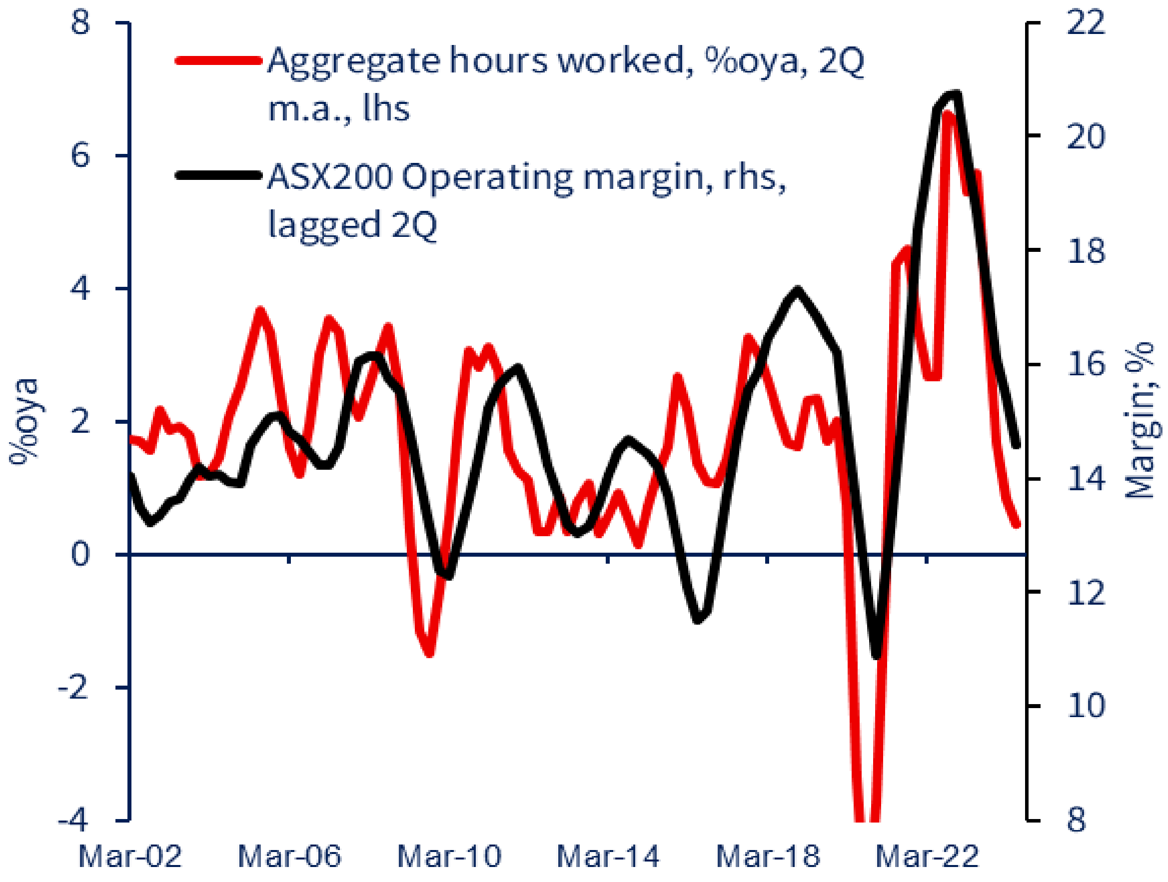
RBA forecast (%)



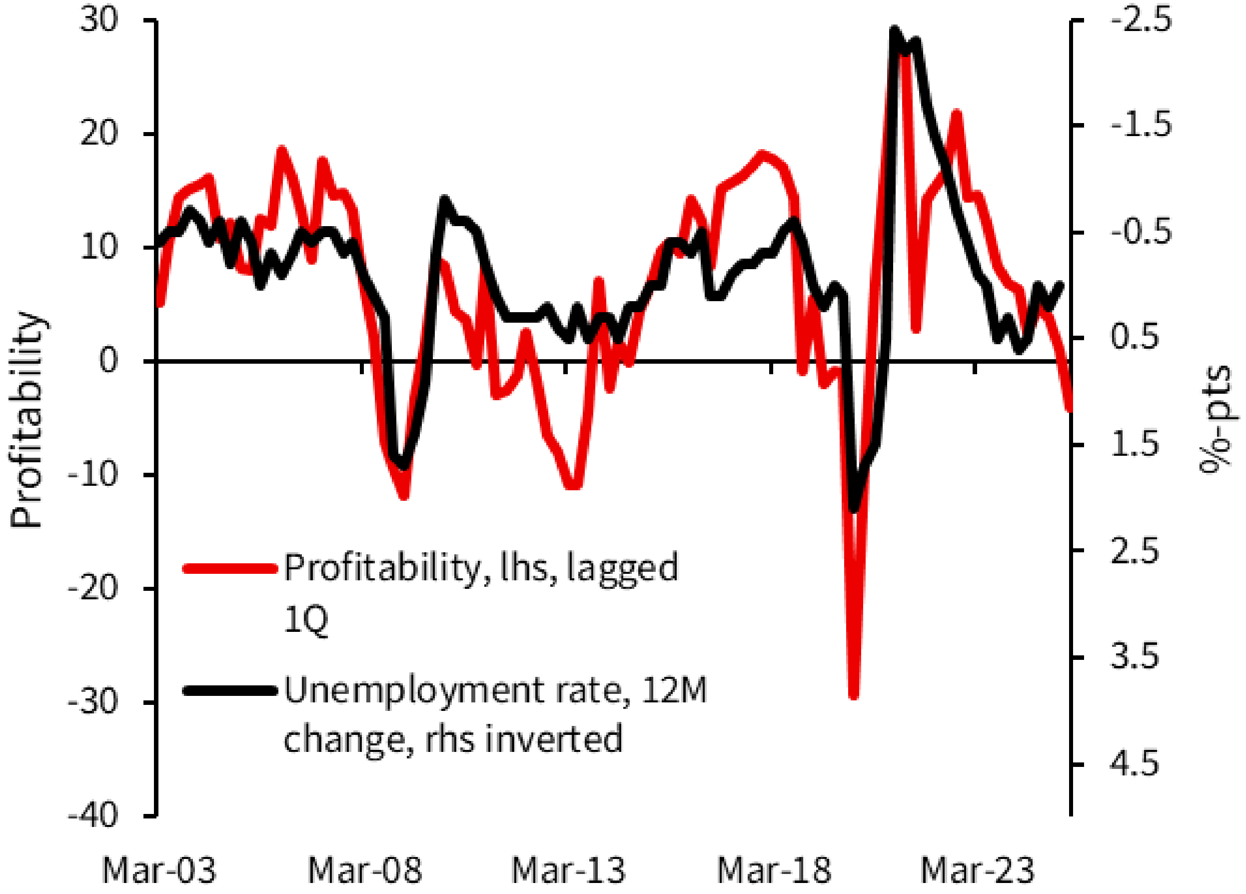
Source: RBA, ABS and NAB.

Margin compression, if sustained, usually leads to less labour input...

Hours worked vs. profit margins



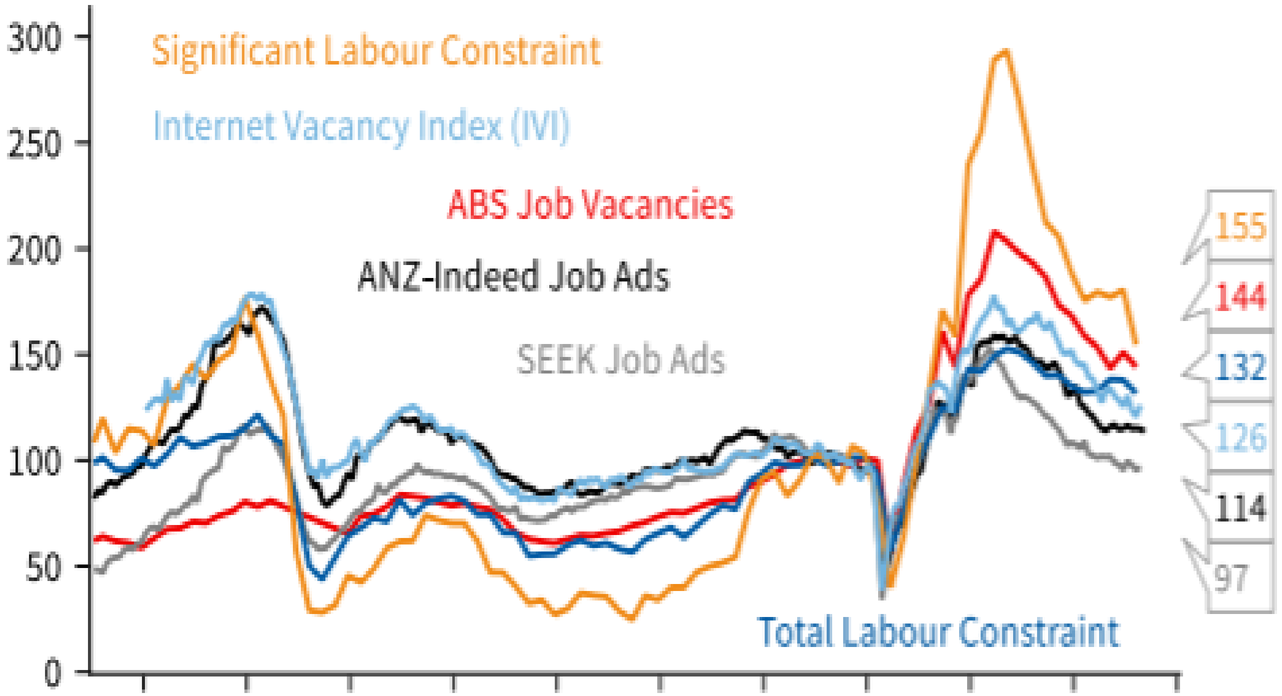
Profitability vs. changes in the u-rate



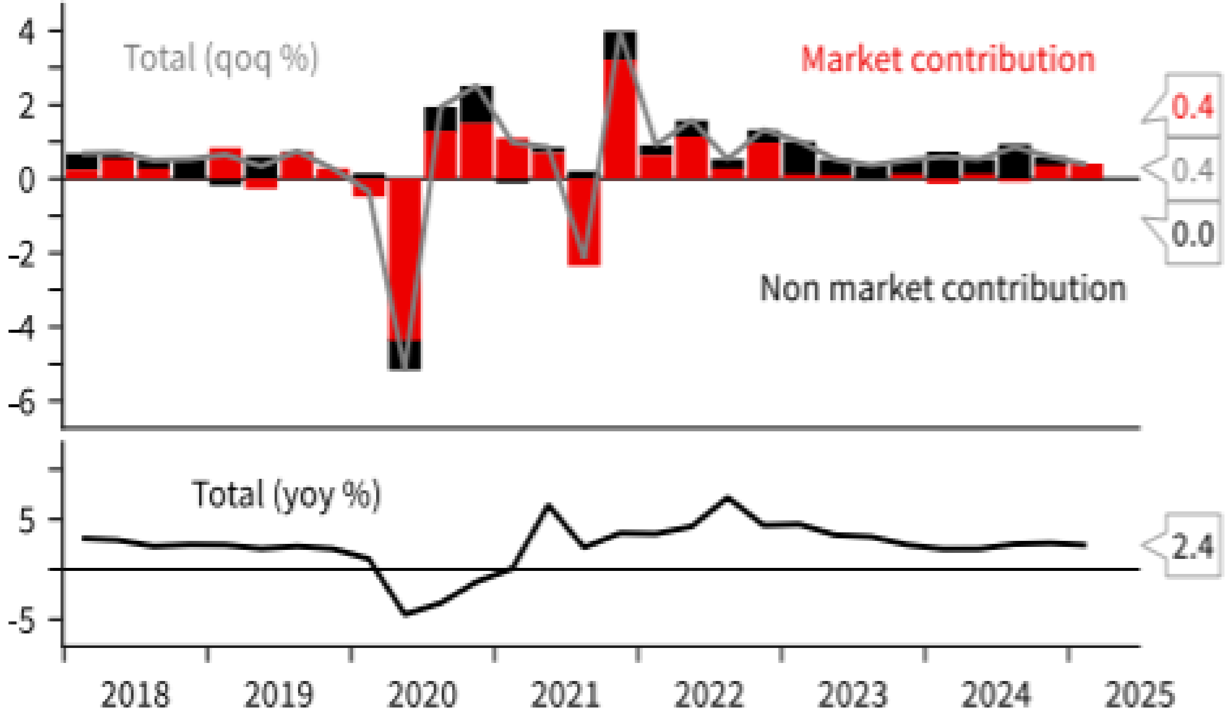
Source: RBA, ABS and NAB.

Labour market dynamics

Leading indicators of labour demand



Market vs. non-Market employment



Source: RBA, ABS and NAB.

In summary

Australian and global outlook

Australia

- GDP growth in 2025 will be better than 2024, at 1.7%
- However, this is still sub-trend growth and will likely see the unemployment rate rise to 4.4%
- The RBA is now more comfortable that inflation is comfortably in the RBA's 2-3% target band
- And so monetary policy should be at a neutral setting (ie, not restrictive, not stimulatory)
- NAB views a neutral policy rate as somewhere between 3.00-3.25%
- And is thus forecasting 3x 25bp rate cuts, in July, August and November

Global

- 2025 likely to be another year of sub-trend growth for the global economy
- Uncertainty remains the key theme across the global economy – as trade barriers, fiscal and monetary policy settings and foreign policy relationships are far from settled
- We are not forecasting recession in the US this year, but expect a decent growth moderation in 2H25
- US inflation is expected to rise as the impact of tariffs is passed on to final consumers
- Chinese growth likely to be in the low 4s in 2025

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