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Summary of Key Views

Markets finished up January relatively flat on a global and domestic level as markets were spooked following the targeted trading by a cohort of retail traders of stocks that were heavily shorted by hedge funds such as GameStop which reached record highs. This created a so called 'short squeeze' which resulted in hedge funds holding the targeted stocks to cover their short positions by selling other investments, which contributed to volatility in markets.

On the policy front rates remain at low levels and the most recent decision by the RBA to keep rates at historical low levels remains positive for risk assets as investors have no other option but to take on risk to have any chance of generating a positive real return. Fiscal policy also remains supportive with the key focal point being the US where markets are closely watching to see if the Biden government will be able to push through their $US 1.9 trillion (almost 10% of GDP) stimulus package.

Our overall asset allocation positioning remains positive on risk assets including emerging markets which are leveraged to an economic recovery. However, we believe that from an investment selection perspective diversification remain important and we continue to retain our exposure to some defensive sectors within our equities exposure.

Market developments during January 2021 included:

Australian Equities

Australian shares outperformed their global peers in January, starting 2021 with a modest gain of 0.3%. Australian equities remain largely influenced by macro factors surrounding the management of Covid-19, but the start of earnings season will see a renewed focus on fundamentals. A rotation out of some expensive growth pockets into value sectors was evident over the December quarter and into the new year, driven by vaccine developments and additional stimulus, while a significant jump in the iron ore price was the principal catalyst for a re-rating of the three largest local miners BHP, Fortescue and Rio Tinto.

JB Hi-Fi released its 1H21 results, which showed an increase in sales of 23.7% on 1H20. The strong result was driven by the continued elevated customer demand for consumer electronics and home appliance products, as well as the exceptional growth in online sales, up 161.7% to $679 million. BlueScope Steel is expecting 1H21 EBIT of approximately $530 million, exceeding previous guidance of $475 million. Australian Steel Products has delivered its strongest domestic mill sales volume in a decade, while Building Products Asia & North America delivered a preliminary result approximately double that of 2H20.

Global Equities

Global shares were down over January as vaccine rollouts hit logistical roadblocks in the US and Europe, while the emergence of new viral strains of Covid-19 put a dampener on sentiment. With valuations stretched, some form of correction was to be expected, but stocks remain buoyed by the economic recovery. Since reaching their March 2020 low, the rebound in global equities has been largely led by large cap growth companies, however their beaten down cyclical counterparts experienced a pronounced recovery in the December quarter. Growth companies have been supported by persistently low interest rates, while value companies have benefitted from positive vaccine news and the reopening of economies.

The US S&P 500 Index traded down through January before moving to fresh all-time highs in early February. Microsoft's December quarter results beat estimates, revealing strong performance from Personal Computing, driven by home office and schooling needs. Alphabet (Google) also surpassed expectations, lifting revenue by 23% on the prior corresponding period, boosted by YouTube advertising, which delivered a 46% jump in revenue. Asian markets were a bright spot in January, with Japan's Nikkei 225 Index rising 0.8%, China's CSI 300 Index gaining 2.7% and Hong Kong's Hang Seng Index up 3.9%.

Fixed Interest

Australia's yield curve has seen a notable steepening in recent months. Rates at the short end of the curve are being held down by the RBA, while longer-term rates are rising as optimism surrounding vaccine developments builds and inflation expectations rise. At its February meeting the RBA left the official cash rate at 0.1% but expanded its bond purchase program—due to finish in mid-April—announcing it will purchase an additional $100 billion of bonds issued by the federal and state governments. Other unconventional monetary policy measures, namely yield control on 3-year Treasuries and the Term Funding Facility, remain unchanged.

The US yield curve, as measured by the spread between the 10-year and 2-year government bond yields, reached its steepest level since late 2017, with Biden's win paving the way for more fiscal stimulus. There are fears that inflation could return to markets as the pandemic subsides and large-scale stimulus washes through the economy, however current inflation rates are still low.

In Australia, the CPI increased by just 0.9% over the year to the December quarter and wages are rising at the slowest rate on record. In the US, the core PCE inflation rate (the Federal Reserve's preferred inflation measure) was 1.5% year-on-year to December.

REITs (listed property securities)

Australian listed property had a rough start to 2021, falling 4.1% in January as reports of new Covid-19 cases emerged and a drawn-out return to 'normal' appeared more likely. As the vaccine rollout progresses and lockdown restrictions ease, sold-off sectors such as retail may continue to strengthen and close the valuation gap with in-favour sectors such as industrial and specialised. Non-discretionary retail centres anchored by the big supermarkets and large format stores (such as Bunnings and JB Hi-Fi) have proved resilient, but discretionary mall valuations have come under pressure as owners renegotiate rents or offer better incentives to tenants.

With the JobKeeper scheme set to expire at the end of March, it is anticipated that the government's code of conduct for commercial tenancies may also cease at that time, presenting some uncertainty for SMEs in the short term.

The December housing report highlighted the strength of Australia's residential market, with turnover, prices, financing activity and dwelling approvals all posting strong gains. However, while vaccine announcements are positive for sentiment, until there is a widespread vaccine rollout, migration numbers (and commensurate population growth) will remain subdued and significantly below the levels of previous years.

Alternatives

Preliminary estimates for January indicate that the index increased by 7.3 per cent (on a monthly average basis) in SDR terms, after increasing by 8.3 per cent in December (revised). The non-rural, rural and base metals sub-indices all increased in the month. In Australian dollar terms, the index increased by 4.8 per cent in January.

Over the past year, the index has increased by 19.7 per cent in SDR terms, led by higher iron ore prices. The index has increased by 11.4 per cent in Australian dollar terms.