Published September 2021

ISSUE DATE: 29-09-2021

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Summary of Key Views

The challenge to diversify

The upward trajectory in equity markets has continued unabated. Markets continue to be supported by low interest rates and central bank liquidity support. The US Federal Reserve's recent comments that that they would continue their asset purchase program and that interest rates are not expected to rise anytime soon has added fuel to markets. This is despite growing concerns of rising inflation, which has been a major focal point for central banks and investors alike. One of our observations is that markets are disregarding any negative news which is of concern as this is typical behavior in the late stages of a bull market. Uncertainty also remains as to the playbook the pandemic will follow. The spike in the Delta strain of Covid-19 has highlighted the evolving nature of the virus and, as we have seen domestically, it has had a material impact on Australia's ability to 'open up', which has had a detrimental impact on many households and small businesses. Furthermore, geopolitical risk continues to flare up with the recent retreat of the US from Afghanistan creating a power vacuum in that region.

Our asset allocation positioning has been positive for investors as we have maintained an overweight exposure to risk assets such as equities. We are seeing that asset valuations in some sectors are looking stretched as the market has extended its rally. We are looking at ways to further diversify our portfolios as well as looking at opportunities to take profits via portfolio rebalancing where appropriate. The main challenge from a portfolio construction perspective at the moment is that bonds and cash do not look particularly attractive, so the hunt for other diversifying assets is a focus for us. Within our multi-asset portfolios, we have incorporated a range of assets such as gold and alternative strategies to provide diversification from equities and bonds.

Market developments during August 2021 included:

Australian Equities

The Australian share market continued its advance for the year following a strong reporting season, with the S&P/ASX 200 gaining 2.5% for the month; year to date the index is up an impressive 17%. Information Technology contributed strongly with a 17% gain for the month, with Consumer Staples (+6.9%) and Health Care (+6.8%) also leading the index higher. Materials and Energy were the only detractors for the month with the sectors retracing 7.3% and 3.9% respectively; continued weakness in iron ore prices and a softer month for oil contributed to the losses

Despite the impressive monthly gains in Information Technology, low volatility (+5.4%) and value (+4.1%) were the best performing factors for the month. Interestingly, growth only edged a modest 0.9% higher. Value continues to remain the dominant factor year to date, with a gain of 19.8%.

It was a busy month for investors as attention turned to FY21 reporting season. Healthy profits and record dividends were a feature of reporting season as materials and COVID beneficiaries continue to recover strongly from the March 2020 lows. Banks also continue to build momentum as bad debt provisions are scaled back amidst an improving economic backdrop.

Global Equities

Global markets continued their climb into August, with emerging markets slightly outperforming developed markets as the region recovers from a sharp sell-off driven by Chinese equities in late July. Developed markets continue to be supported by economic stimulus and vaccination efforts, despite unabated trends in daily case rates across developed economies. In Australian dollar terms, Small cap global equities continue to be the best performer over the last twelve months, whilst their larger cap counterparts continue to outperform both small cap and emerging markets over the longer term.

August saw the release of troubling data across several major economies with US hiring at seven-month lows, decelerating Chinese PMI for the fifth straight month and supply chain bottlenecks increasing for Europe's largest manufacturers. Energy prices have also risen significantly across G7 economies, poorly timed as winter approaches for the northern hemisphere. Inflation will be a key discussion point for the Federal Reserve meeting scheduled for the second last week of September. The timing and degree of stimulus tapering remains a central issue for policy makers to contend with as they must balance managing inflation without compromising economic growth. This poses a significant short-term risk for global equity markets which have been enjoying an unprecedented bull run since the March 2020 COVID induced sell-off.

Fixed Interest

August saw continued strong performance from domestic Fixed Income markets. Yields remained relatively static at the short end of the curve, but fell at the longer end, resulting in a flatter curve overall. This can be seen in the 3-year Australian Government Bond having had a net change of less than 1bp over the month, while the 10-year issue had its yield fall by 2.6bps. The fall has been driven by doubts about the Reserve Bank of Australia's commitment to tapering off the current level of stimulus, doubts which have grown significantly over the month as both Victoria and New South Wales remain in lockdown. These concerns, combined with credit spreads continuing to tighten over the course of the month led to the Bloomberg AusBond Composite 0+ Yr Index returning 0.82% over August.

Globally, there has been significant heterogeneity in the performance of international bond markets as variation in vaccination rates and other COVID related metrics remains high. In the US, continued strong economic performance has driven talks of sooner tapering, which has resulted in higher yields overall. The Bloomberg Barclays Global Aggregate Index (AUD Hedged) Index returned -0.22% over August, with the unhedged variant having returned 0.16%.

REITs (listed property securities)

A-REIT's advanced strongly during August with the S&P/ASX 200 A-REIT Accumulation Index achieving 6.3% for the month and 30.8% for 12 months to 31 August 2021. The months news was dominated by the release of the 2021 full-year financial results. The financial results across A-REITs were generally strong, pushing the index higher. One exception was Goodman Group (ASX: GMG) that closed the day down over 2% upon releasing poorer than expected earnings growth guidance for FY22. GPT Group (ASX:GPT) released.an announcement in mid-August in response to media speculation, confirming they are indeed in exclusive due diligence to acquire a portfolio from Ascot Capital for approximately $800m, comprising 26 logistics and industrial assets, along with 4 office assets.

In the U.S., August saw an increase in people working from home for the first month since December last year as the delta variant causes concern (Source: Nareit).This, along with a slowdown in job growth may lead to a slower recovery of the office sector than expected.

CoreLogic reported that the 5-capital city aggregate all dwellings (including Sydney, Melbourne, Brisbane including Gold Coast, Adelaide, and Perth) advanced by 1.5% in August, 17.2% year on year.

Alternatives

Preliminary estimates for August indicate that the index decreased by 6.0% (on a monthly average basis) in SDR terms, after increasing by 7.0% in July (revised). The rural and base metals sub-indices increased in the month, while the non-rural sub-index decreased. In Australian dollar terms, the index decreased by 4.6% in August.

Over the past year, the index has increased by 50.3% in SDR terms, led by higher iron ore prices. The index has increased by 49.3% Australian dollar terms.

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