Summary of Key Views

Insights from our CIO: Things to consider in the year ahead

We are observing the rise in dispersion in returns within asset classes across individual securities and sectors. We expect this dynamic to continue as market conditions evolve. For the best part of the last 10 years markets have been driven by unconventional central bank monetary policy strategies, primarily quantitative easing, which have distorted markets. This policy action has resulted in an incredible rise in the value of risk assets and for most clients it has resulted in a significant rise in their asset values.

This environment has resulted in certain investment styles and sectors dominating market returns. An example of this has been the incredible ascent of growth stocks within the technology sector.

We think that we are heading into an environment where investors will need to be more selective in security and sector allocations and that the "easy money" related to simply investing in high beta parts of the market has been made. This does not necessarily mean that value stocks will now take the mantle in terms of driving returns. It just means that investors will need to be more active in their security selection, irrespective of style.

Market developments during December 2021 included:

Australian Equities

The Australian share market closed out December 2021 with the S&P/ASX 200 gaining 2.75% with eight out of the eleven sectors within the Index finishing higher. Specifically, Utilities was the standout sector with a return of 7.9%, whilst Materials (+6.5%) and Property (+4.9%) delivered strong returns. A heavy decline in the Information Technology sector (-5.3%) failed to stop the broader 'Santa Rally' to close out the year.

The local miners were bolstered by the iron ore price recovery given the optimism around Chinese demand for the commodity in the intermediate term alongside the expectations for potential further stimulus measures within China's economy. The Utilities sector pared back some heavy yearly losses and investors looked for some defensive exposure. The Information Technology sector suffered heavy declines as investors weighed up the potential central bank interest rates rises in the intermediate term.

Low Volatility and enhanced value were the strongest performing factors for the month with gains of 4.1% and 4.2% respectively. All factors finished with positive returns for the month with growth providing the lowest increase at 2.0%. Year to date, value finishes the year as the leading factor (+20.9%), albeit with the lowest quarterly performance amongst all factors.

Global Equities

Following a disappointing end to November, global markets closed out 2021 strongly posting an annual return of 29.6% in Australian dollar terms. Developed markets closed 1.7% higher by month end, trailed by Emerging and Asian markets declining by -0.7% and -1.1% respectively. Global small caps lagged their broad cap equivalents during December recording a gain of 1.1% for the month.

Markets struggled to build momentum early in the month of December as the emerging and enigmatic Omicron variant of the COVID-19 virus continued its spread across the globe. As understanding about the new strain, particularly its highly infectious but less potent nature developed, investors were reassured that economic growth would not be stalled as governments widely exercised restraint with reinstituting lockdowns and restrictions abroad.

Notably, Emerging and Asian markets posted disappointing year end annual returns of 3.4% and 0.9% according to the MSCI Emerging Markets NR Index (AUD) and MSCI AC Far East NR Index (AUD) indices respectively. This is mainly attributable to the more difficult conditions that emerging economies have had to cope with in the face of a COVID-19 centric world.

Fixed Interest

December was a relatively muted month for Australian Fixed Income markets, while inflation has continued to dominate the discourse Australian yields have remained relatively static. The yields for 2- and 10-year Australian Government Bonds fell by approximately 2 and 5 basis points respectively over the course of December, although both have since increased again since January has begun. Credit spreads also tightened somewhat over the month, which aided the Bloomberg AusBond Credit 0+ Year Index in outperforming the Bloomberg AusBond Composite 0+ Year Index with returns of 0.2% and 0.1% respectively.

Internationally, inflation also dominated the discussion, but the month played out very differently, as can be seen, most evidently in the US. In its December meeting, the US Federal Reserve adopted a more hawkish approach and announced a more rapid taper of their bond purchases and alluded to the possibility of interest rate hikes later in the year. This prompted an increase in US yields across the entire spectrum of maturities with market participants pricing in three rate hikes for the year. This drove overall returns of -0.4 for the Bloomberg Barclays Global Aggregate Index (AUD Hedged), with the unhedged variant returning -2.6.

REITs (listed property securities)

The S&P/ASX 200 A-REIT Accumulation index finished 2021 with strength, advancing 4.9% in the month of December and closing out 2021 with a 26.1% gain.

Global real estate equities (represented by the FTSE EPRA/NAREIT Developed Ex Australia Index (AUD Hedged)) also finished strongly, achieving a 6.1% gain for the same month, and totalling 30.2% for the year. Whilst the Pandemic hit the retail sector particularly hard, the U.S. Census Bureau's Business Formation Statistics data shows there have been more new business applications in 2021 (through to November) than any other year on record, and with the applications being dominated by retail, it may indicate a continued recovery of the sector during 2022 (NAREIT, DeLullo, December 2021).

October A-REIT acquisitions included Vicinity centres AREIT's had a relatively busy month. Charter Hall Group (ASX: CHC) announced a 50% interest in Paradice Investment Management (ASX: PIM), an Australian and global equities manager with $18.2bn AUM, for an acquisition price of $207m. Centuria Capital Group (ASX: CNI) announced $466m + of healthcare property acquisitions across various locations in Australia including a large transaction acquiring 38 NZ facilities. Ingenia (ASX: INA) announced the completion of an acquisition of Seachange and Caravan Parks of Australia, expressing a bullish view on domestic travel.

The Australian domestic housing market again experienced positive growth last month, with the CoreLogic 5 capital city aggregate advancing 0.6%, totalling a 20.8% gain during the year 2021. Melbourne experienced a small negative change during December, recording -0.1% for the month.

Alternatives

Preliminary estimates for December indicate that the index increased by 1.5% (on a monthly average basis) in SDR terms, after increasing by 6.7% in November (revised). The rural and non-rural indices increased in the month, while the base metals index was unchanged. In Australian dollar terms, the index increased by 3.3% in December.

Over the past year, the index has increased by 25.7% in SDR terms, led by higher LNG, coking coal and thermal coal prices. The index has increased by 28.5% in Australian dollar terms.