

Lonsec Client Newsletter - December 2024



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Market developments during December 2024 included:

Australian Equities

The ASX 200 Accumulation Index fell by 3.2% in December, marking the worst monthly return of 2024. The Index mirrored global markets in its decline. Softer economic activity and fading inflation in Australia led the market to anticipate a potential rate cut in early 2025, but this wasn't enough to boost the local equity market.

Sector returns were broadly negative, with only minor gains coming from Consumer Staples (+0.6%), Utilities (+0.4%), Industrials (+0.3%), and Energy (+0.3%). Among the sectors that declined over the month, Property (-6.0%), Materials (-4.5%), Information Technology (-4.4%), and Financials (-4.2%) were the biggest losers.

The Property sector, sensitive to interest rate expectations, dropped 6.0%. This decline was due to a more hawkish US Federal Reserve, even after a 25bps policy rate cut. The shift in sentiment led to a rise in bond yields, further impacting the sector. Materials were affected by ongoing uncertainty around the Chinese economy, a trend throughout 2024, which weighed on global metal prices.

As investors now look ahead to 2025, overall uncertainty in the market environment continues.

Global Equities

Emerging Markets outperformed Developed Markets in December, as global equity markets navigated a mix of central bank actions, geopolitical uncertainties, and year-end market dynamics. Emerging Markets gained 5.07% (MSCI Emerging Markets Index (AUD)), while Developed Markets returned 2.58% (MSCI World Ex-Australia Index (AUD)), buoyed by a significant drop in the AUD. In local currency terms, the MSCI World Ex-Australia Index fell 1.89% for the month.

US equity markets experienced volatility in December with the usual year-end portfolio rebalancing and tax-loss harvesting. While the Federal Reserve had implemented a 25 basis point rate cut in the previous month, its hawkish tone dampened investors' enthusiasm. As a result, the S&P 500 declined 2.5% for the month (in local currency terms), marking one of its weakest periods in 2024. Mega-cap stocks faced pressure from stretched valuations, while market sentiment was also tempered by persistent concerns about corporate earnings growth.

Japanese equities outperformed most Developed Markets, with the Nikkei 225 rising 4.0% (in local currency terms). A weaker yen, which depreciated 4.6% during the month, supported export-driven industries, while financial stocks gained on rising yields.

Emerging Markets delivered strong performance in December, reversing prior month trends, driven by a rebound in Chinese equities and broader regional strength. The MSCI Emerging Markets Index (AUD) gained 5.07%, supported by proactive fiscal and monetary policy announcements from China. The Hang Seng Index rose 1.5%, while the CSI 300 Index gained 2.3% (in local currency terms). Despite these gains, structural challenges and political uncertainties weighed on performance in markets such as South Korea and Taiwan.

Fixed Income

After experiencing volatility in November due to the US Federal election and actions by the Federal Open Market Committee (FOMC), the bond market ended the year on a disappointing note, with a significant rise in yields.

GDP figures came in lower than expected, prompting further speculation that a rate cut could be on the horizon for early 2025. Meanwhile, the Reserve Bank of Australia (RBA) left rates unchanged at the current policy rate of 4.35%, but adopted a more dovish stance, expressing confidence that inflation was easing.

Despite this, a robust labour market with lower unemployment and rising job creation gives further credence to the softer landing and the gradual easing of rates the RBA is aiming for. As a result, we saw a slight uptick in the 10-year Australian Government bond yields by 2bps, while the 2-year bond yield dropped by 9bps.

In the US, the Federal Reserve's decision in their December meeting to cut the policy rate by 25bps was accompanied by caution regarding future rate cuts in 2025, with the Fed adopting a more hawkish stance than expected. This sentiment led to a significant sell-off in both the equity and bond markets. The rise in yields reflects a potentially shortened rate-cutting cycle, while pro-inflationary pressures expected from the incoming Republican Party have also contributed to the increase in yields. In response, US government bond yields rose by 7bps for the 2-year and 40bps for the 10-year.

REITs (listed property securities)

The S&P/ASX 200 A-REIT Accumulation Index TR backtracked significantly in December, finishing the month down 6.0%. The Index remains in positive territory YTD, up 19.5%. Similarly, global real estate equities also reverted, decreasing by 6.2% (represented by the FTSE EPRA/NAREIT Developed Ex Australia Index (AUD Hedged)). Australian infrastructure increased with a return of 3.0%, continuing its growth after an increase of 5.0% in November. The index has delivered a return of 12.9% YTD.

December continued the quiet M&A trend in Australia across the A-REIT sector in the lead up to Christmas and the New Year. Drama continues to evolve in the stoush

between Hotel Property Investments (HPI) and the Charter Hall Retail REIT (CQR) led consortium. After repeatedly asking shareholders to reject the takeover offer (and revised offers), HPI directors have now asked shareholders to accept the A\$760m buyout. This came a day after the consortium took a majority stake in the pub landlord and are set to pursue a hostile takeover strategy. As of 30 December, the consortium had increased its voting power to 57.61%.

The Australian residential property market experienced a fall of -0.2% Month on Month (as represented by CoreLogic's five capital city aggregate). Perth continued its strong run and was the biggest riser (+0.7%, 19.2% YoY), followed by Adelaide (+0.6%) and Brisbane (+0.5%). In contrast, Melbourne was the worst performer and continued to experience a fall in value (-0.7%) alongside Sydney (-0.6%), Hobart (-0.5%) and Canberra (-0.5%).

Alternatives

Preliminary estimates for December indicate that the index increased by 0.6 per cent (on a monthly average basis) in SDR terms, after increasing by 1.3 per cent in November (revised). The rural and non-rural subindices increased in the month, while the base metals subindex

declined. In Australian dollar terms, the index increased by 3.1 per cent in December.

Over the past year, the index has decreased by 10.7 per cent in SDR terms, led by lower iron ore and coking coal prices. The index has decreased by 7.4 per cent in Australian dollar terms.

Currencies

The Australian dollar (AUD) depreciated over the month of December, closing 2.9% lower in trade weighted terms to 59.7, depreciating against the US Dollar (USD), Pound Sterling (GBP), Euro (EUR) and the Japanese Yen (JPY).

The Australian dollar weakened against the USD led by uncertain economic conditions, specifically around tariffs, and a relative strengthening of the USD. Additionally, the RBA held interest rates as opposed to a rate cut in the US for December.

Relative to the AUD, the USD was the highest performer of the month, appreciating in relative terms by 5.0% against the AUD. Year-on-year, the AUD remains behind the USD, EUR and GBP by 9.2%, 3.2% and 7.7% respectively, whilst remaining ahead of the JPY by 1.3% in relative terms.

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