RESEARCH UPDATE

MARKET watch

AUGUST 2023

Apt.
WEALTH PARTNERS

Equities continued to rally over the course of July, driven by optimism around falling inflation and the prospects of a 'soft' economic landing, despite Central Banks continuing to tighten monetary policy. The S&P 500 Index and the Nasdaq Composite Index increased by 3.1% and 4.1% respectively as the Federal Reserve raised rates by a further 0.25%. The Hang Seng Index rallied a further 6.2% following the announcement in late June that China's government would take additional measures to stimulate the economy and despite new economic data showing the economic slowdown accelerating. The S&P/ASX 200 Index performed in line with international markets, rising by 3.1%, despite the underperformance of the defensive Healthcare and Consumer Staples sectors.

S&P/ASX 200 Sector Performance

The best-performing sector in July was the Energy sector (+8.8%), driven by the higher oil price. Beach Energy Limited rose 19.6% after reporting fourth quarter production had increased by 12% on the prior quarter, which, combined with higher oil and gas prices, led to a 27% increase in quarter-on-quarter revenue. Woodside Energy Group Limited rallied 10.4%, despite reporting quarterly production had declined by 5% on the prior quarter, which resulted in a 4% decline in revenue.

Financials rose 4.8%, driven by Block Inc., which rallied 19.0%, despite no significant news being announced and having now increased by 40.3% since the late May low. Challenger Limited finished 10.8% higher after announcing that it had partnered with industry super fund Aware Super to provide a defined benefit superannuation solution, which is intended to assist in the de-risking of companies defined benefit liabilities.

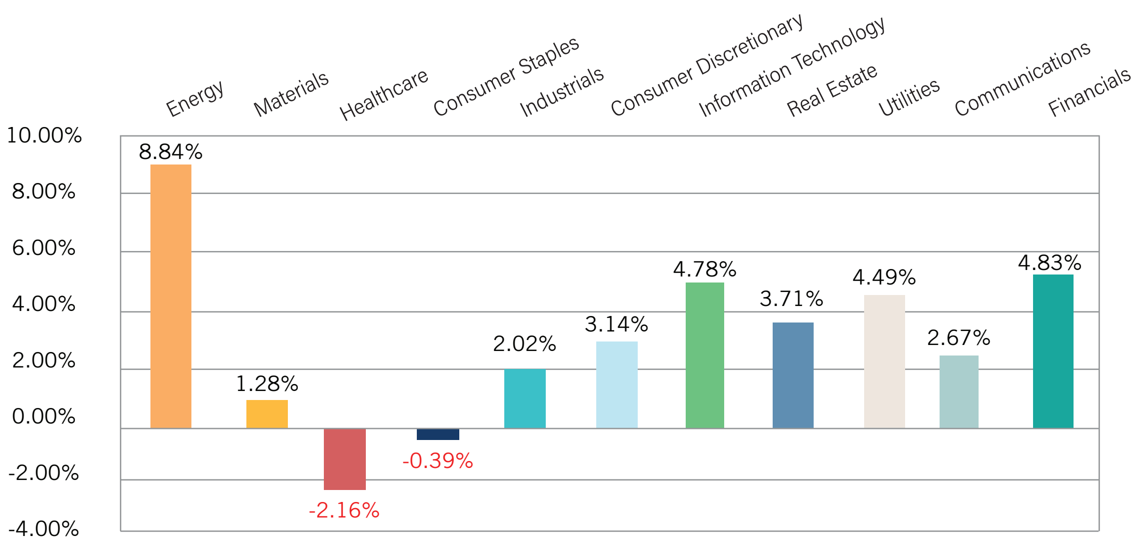
The Information Technology Sector rose 4.8%, driven by Megaport Limited, which rallied 46.8% after providing a quarterly update that showed the company had generated normalised Earnings Before Interest Tax and Amortisation (EBITDA) in line with prior guidance, and flagged the intention to increase the Financial Year 2024 normalised EBITDA guidance at the full year results. Altium Limited rose 3.8%, despite announcing that the long-serving Chairman, Sam Weiss, would step down following the Annual General Meeting in November. Wisetech Global Limited increased by 7.9%, despite no significant news being announced, assisted by the positive market sentiment towards technology stocks.

Travel companies drove the Consumer Discretionary sector 3.1% higher, with Flight Centre Travel Group Limited, Corporate Travel Management Limited and Webjet Limited rising 21.8%, 16.9% and 14.0% respectively. Flight Centre upgraded 2023 Financial Year profit guidance by 7% as the global corporate travel business continues to recover from COVID-19. Corporate Travel Management is benefiting from similar industry conditions, with Financial Year 2023 EBITDA expected to double from the prior year and management expecting the strong momentum to continue into Financial Year 2024.

Consumer Staples underperformed, declining by 0.4%, driven by the fall in the supermarket retailers Metcash Limited (-2.7%), Woolworths Group Limited (-1.5%) and Coles Group Limited (-0.3%) as defensive companies lagged in the improved market sentiment. Metcash Limited announced the appointment of a new Chief Financial Officer (CFO) who will join the company in January 2024 following the announcement that the current CFO would retire.

Healthcare was the worst-performing sector, declining by -2.2%, driven by CSL Limited, which fell -3.8% after the company provided a market update indicating an expected US$230 million to US$250 million foreign currency headwind and despite guiding for constant currency Net Profit After Tax and Amortisation growth of between 13% and 18% over the 2024 Financial Year. Ansell Limited fell 9.7% after providing a weaker than expected trading update, with 2023 Financial Year underlying earnings per share (EPS) expected to be at the low end of its previous guidance range, as well as a significant increase in investment.

Graph 1: S&P/ASX 200 Sector Performance



Data Source: Desktop Broker, 1 August 2023.

Highlights

Australia: The Australian Bureau of Statistics (ABS) reported that household discretionary spending on goods and services rose 0.6% in May compared to the prior year. The categories experiencing the largest falls were Furnishings and Household Equipment (-4.8%) and Clothing and Footwear (-3.4%). Overall, household spending rose 3.3%, the lowest growth rate since July 2021, and comes as households respond to cost-of-living pressures.

The Reserve Bank of Australia (RBA) kept the cash rate at 4.1% in June in order to assess the impact of recent rate rises while continuing to warn that further tightening may be required to return inflation to the 2% to 3% target range. Current Deputy Chair of the Reserve Bank Board, Michelle Bullock was also appointed as the new RBA Governor by the current Federal Government, replacing Phillip Lowe.

The RBA also released the latest Index of Commodity Prices (ICP) reading that showed a 21.5% decrease over the prior year to the end of June, and a 18.1% fall in Australian dollar terms. The index was led lower by thermal coal, coking coal, liquified natural gas and iron ore prices. The index is reweighted regularly and is intended to be an accurate reflection of Australia's main commodity exports. Commodity exports are an important source of income for the Australian economy, contributing well over 50% of all exports.

Australia's first approved offshore wind location near Gippsland, Victoria is projected to produce 2.2GW of electricity, approximately the amount of a large coal-fired power station, and representing about a fifth of Victoria's current energy needs. A number of providers are vying to build wind farms in the region, with the wind turbines expected to be up to 300 meters high. Further offshore wind zones are anticipated throughout Australia.

US: Mercedes-Benz, Ford and General Motors have all adopted Tesla's electric car charging design standard, referred to as the North American Charging Standard (NACS), as they try to expand their network of fast chargers in an attempt to make owning an electric vehicle easier. NACS competes with the CCS charging standard, with Tesla only recently opening access to its charging network to other car manufacturers. This will lead to increased revenue for Tesla, but on the other hand, it means the exclusive access to its charging station network will not be a major selling point for customers, since all electric vehicles will have access to all chargers.

The US Bureau of Labor Statistics reported that the Consumer Price Index rose by 3.0% over the 12 months to the end of May. The shelter index was the largest contributor to the monthly increase, accounting for 70%, followed by the motor vehicle insurance index. The index for all items less food and energy rose 0.2% in June, the smallest 1-month increase in that index since August 2021. The sharp fall over prior months has increased hopes that inflation can be brought back to target without causing a severe economic slowdown.

Europe: The European Union generated more electricity from solar power than from coal for the first time in May. Solar power contributed 14% to total electricity production, a record high, while wind power contributed 23%, just shy of the record set in January. Coal power has continued to decline, with Italy stating it would shut down all coal-fired power stations by 2024 if gas prices remained low.

Financial Markets: The use of the London Interbank Offered Rate (LIBOR) officially ended on June 30 after decades of being used as the reference rate for many floating rate financial instruments. The calculation of LIBOR relied on submissions from a number of banks and was supposed to be reflective of their borrowing costs. After the Global Financial Crisis, it was revealed that several banks were purposefully manipulating LIBOR rates to benefit trading positions, resulting in a replacement being sought. In the US, markets are now replacing LIBOR with the Secured Overnight Financing Rate (SOFR), which is based on actual transactions in the overnight repo market, and in the UK, LIBOR is being replaced with the Sterling Overnight Index Average (SONIA).

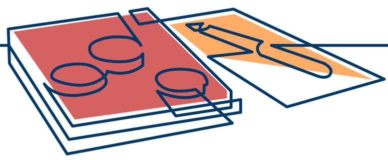
The NASDAQ-100 index, which represents the largest non-financial companies listed on the Nasdaq, undertook a special rebalance whereby the seven largest companies made up of Microsoft, Meta, Alphabet, Nvidia, Amazon, Apple and Tesla, and which together represented over 50%, was reduced to 40%. No individual stock is allowed to exceed a 4.4% weighting to avoid breaching limits set by the Securities and Exchange Commission. The change was enacted at close of trading on July 21 and was only the third special rebalance ever undertaken, with the previous two occurring in 1998 and 2011.

What to watch out for

Russia has suspended the trade deal that allowed Ukraine access to the Black Sea. Ukraine is one of the largest exporters of grain and used the Black Sea as an export route, having transported over 32 million tonnes of food since the trade deal was reached in August 2022. The disruption will contribute to elevated food inflation, which has been a primary driver of headline inflation in recent years.

India, the worlds' largest rice exporter, has banned the export of all non-basmati white rice as uneven rainfall in key rice-growing areas impacted production and pushed prices up by over 20%. Rice is another key staple and will increase food inflation around the world.

Conclusion



International markets continued to rally into July, with the rally broadening into other regions and sectors and away from the US information technology sector, which drove most of the gains over the first half of the calendar year.

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Globally, Central Banks continue to raise rates to combat inflation, which will act as a headwind to economic growth. Despite the tighter monetary policy, markets have now almost discounted the possibility entirely of a significant economic slowdown. The upcoming Australian and ongoing US corporate reporting season will provide a better insight into economic conditions.

During periods of uncertainty, clients should:

- Stick to the plan: focus on your long-term goals. Our investment approach is focused on the long term and designed so that your portfolio can ride out any downturns – including this one. Staying the course, despite how uncomfortable it may feel right now, will prove to be the better option when looking back five years from now.

  Investors who stayed on the course while equity markets declined in the depths of the COVID-19 pandemic in early 2020 have benefitted from one of the fastest market turnarounds with equity markets. For investors who sold equities during the downturn and waited until economies started to show recovery before buying back into the market missed a large part of the recovery.
- Maintain a buffer of safety: holding a buffer of cash and term deposits has been a key strategy to provide a cushion against market downturns and to protect capital.
- Take advantage of the weakness: market downturns provide buying opportunities to invest in long-term, quality investments.
- Focus on quality investments: invest in companies that generate stable cash flows to support distributions, which are not connected to the movements in asset prices, and partner with Fund Managers that share the same investment philosophy and objectives.
- Ensure diversification: across assets classes, industries, sectors and geographies.
- Regularly rebalance the portfolio back to your risk profile: to ensure that the portfolio is not exposed to unwanted risks and to also lock in profits.

- Remain calm, speak to your Apt adviser: it is important that you speak to your Apt adviser before making any financial moves. Your adviser understands your long- and short-term goals and will have been planning for these types of scenarios already, so they are best placed to explain any impact and discuss the best options and opportunities for you personally.