RESEARCH UPDATE

MARKET watch

DECEMBER 2022

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WEALTH PARTNERS

November saw a broad rally in equity markets on hopes that the pace of global interest rates rises might slow following lower inflation readings. The S&P 500 Index rose by 5.4%, outperforming the Nasdaq Composite (+4.4%) for the second consecutive month. The Hang Seng Index ended the month 26.6% higher, which was the best monthly rise since 2003 as investors became increasingly optimistic that lockdown restrictions in China would soon ease.

S&P/ASX 200 Sector Performance

Utilities was the best performing sector, rising by 20.9% driven by Origin Energy Limited, which increased by 41.1% after the company received a non-binding, indicative takeover offer of $9.00 per share from Brookfield Asset Management. AGL Energy Limited rose by 16.9% following the Annual General Meeting where the current board of directors as well as those nominated by Mike Canon-Brookes' Grok Ventures were elected to the board.

The Materials sector rose by 16.2% driven by Sandfire Resources Limited, which increased by 43.7% as the copper price rallied and despite the announcement of a $200 million capital raising. Gold miners Evolution Mining Limited, Gold Road Resources Limited and Regis Resources Limited increased by 28.9%, 29.2% and 26.6%, respectively, driven by a recovery in the gold price. The rise in the gold price was largely driven by the depreciation in the US dollar.

The Health Care sector rose by 6.0% driven by Fisher & Paykel Healthcare, which increased by 18.0% after releasing better than expected first half results. The company is cycling a strong prior year result when there was increased use of respiratory equipment as a result of COVID-19 hospitalisations. Ramsay Health Care increased by 12.4% as the company recovered from the selloff following the withdrawal of the takeover offer from the consortium led by private equity firm KKR.

Industrials increased by 5.8% driven by Downer EDI Limited (+15.1%), which confirmed between 10% and 20% profit growth in the 2023 Financial Year despite the impact of difficult weather conditions across Eastern Australia and New Zealand. John Lyngs Group Limited increased by 12.2% after confirming 2023 Financial Year revenue growth of 15.2% and Earnings Before Interest Tax Depreciation and Amortisation growth of 26.0% at the Annual General Meeting.

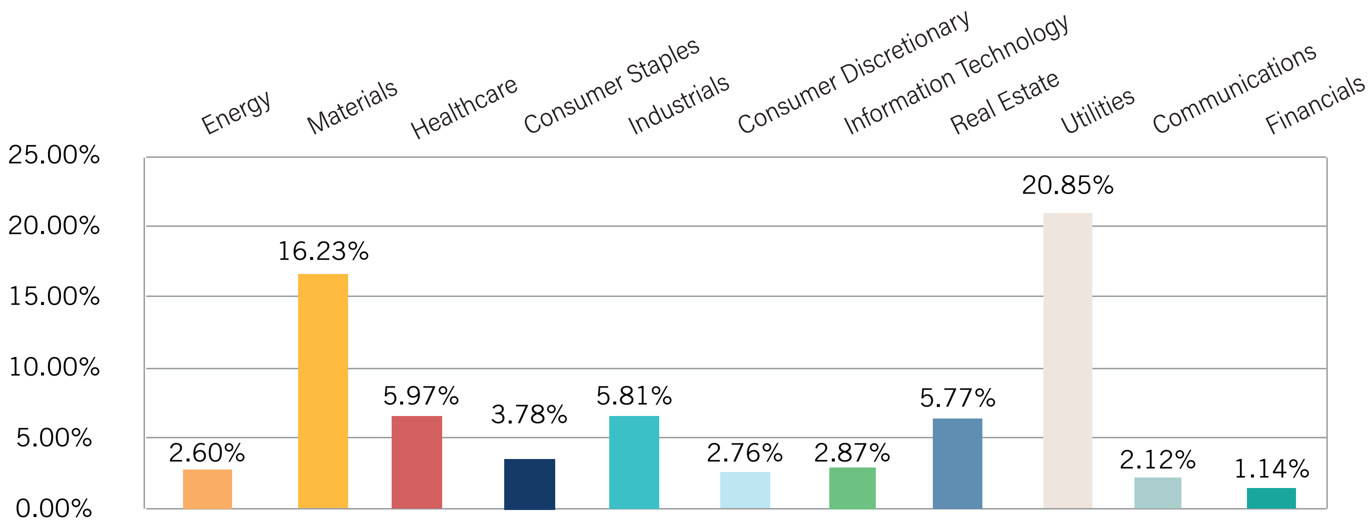
Goodman Group Limited rose by 12.3%, which drove the Real Estate sector 5.8% higher.

Goodman reaffirmed prior earnings per share growth of 11% for the 2023 Financial Year with a strong development pipeline with high occupancy and positive rental growth across the group.

The Communication sector rose by 2.1% driven by Carsales.com Limited, which rallied 12.4% despite no significant news being announced. Seek Limited rose by 2.3% following the Annual General Meeting, which confirmed net profit after tax guidance of between $250 million and $270 million, which included an expectation that economic conditions, hiring sentiment and candidate availability would remain challenging.

Financials was the worst performing sector rising by 1.1% due to relatively weak performance from the three major banks, National Australia Bank Limited (-2.7%), Australia & New Zealand Banking Group Limited (-3.2%) and Westpac Banking Corporation Limited (-1.4%) after they traded ex-dividend. Virgin Money UK CDI increased by 25.6% after the company extended the £50 million share buyback and announced 2022 Financial Year profit growth of 43% on the prior corresponding period.

Graph 1: S&P/ASX 200 Sector Performance



Data Source: Desktop Broker, 1 December 2022.

Highlights

Australia: The Australian Bureau of Statistics (ABS) reported that the unemployment rate remained near record lows, falling a further 0.1% in October to 3.4%. The participation rate remained relatively steady. The employment-to-population ratio remains elevated at 64.3%, which is 2% higher than before the pandemic.

The Consumer Price Index (CPI) indicator rose by 6.9% for the twelve months to October 2022 but was a 0.4% decrease on the prior month. The most significant contributions to the annual rise was dwellings (+20.4%), automotive fuel (+11.8%) and fruit and vegetables (+9.4%). The rise in dwelling prices was driven by the high construction activity and ongoing shortages of labour and materials. Inflation is expected to stay elevated, but the fall is promising with the recent interest rates rises that are yet to have a significant impact.

NBN Corporation, the company responsible for the national broadbank network, has lodged a new pricing structure that would see the end of capacity-based charges for retail internet providers by 2026, which should enable a flatter pricing structure and encourage users to adopt quicker download speeds. NBN Co said the cost of the highest speed tier would drop by $10 under the plan.

Using the 2021 Census data, the ABS reported that 6.4 million people (53.1% of Australia's working population) drove to work on Census Day. This is twice as many people who drove in 1981 but lower than the record 6.6 million in 2016. The decline would be partly attributed to the COVID-19 restrictions. As would be expected, more people drive to work outside of capital cities with only 13% driving to work in Inner City Sydney compared to 73.7% of workers in Palmerston in the Northern Territory.

China: China's total ownership of US Treasuries (government bonds) over the last decade has declined significantly after reaching a peak of nearly 14% in 2010 to around 4% in 2022.

China is facing a wave of protests due to their pursuit of a 'COVID-zero' policy. The COVID-zero policies had a significant economic impact with no clear exit path given that most of the elderly are not vaccinated and the refusal to use more effective Western mRNA vaccines.

China's manufacturing sector purchasing managers' index (PMI) came in at 48 for the month of October. A reading below 50 indicates contraction. It was the third consecutive monthly contraction and the lowest reading since April 2022.

US: The Department of Justice blocked the acquisition of Simon & Schuster by book publisher Random Penguin under antitrust law (anticompetition). This has been seen as a major victory after the Department lost a string of cases on similar grounds in recent years. Antitrust has been receiving increased political attention in the US due to the 'mega cap' companies such as Meta (Facebook) and Amazon acquiring potential competitors before they reach significant scale.

Crypto: One of the largest and most respected crypto currency exchanges FTX has collapsed, owing billions to creditors. The appointed bankruptcy lawyer John Ray III stated the company suffered 'unprecedented and complete failure of corporate controls' and was the worst he had ever seen, which included the collapse of energy giant Enron in 2001. The collapse sparked mass selling across cryptocurrencies.

Music Rights: The global value of music copyright is now US$39.6 billion according to the latest IFPI Global Music report, an increase of 18% on 2020. The large increase is being driven by the increased adoption of streaming, which contributes 55% of the total value.

Data Centres: A typical data centre spans about 100,000 square feet and can consume as much electricity as a small city in order to power and cool the computing equipment. The increased adoption continues to draw attention for the ecological impact with some communities opposing new centres citing pollution, power grid failures, excessive land use, or lack of job creation as reasons.

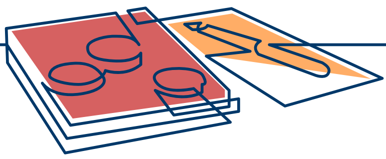
What to watch out for

Large technology companies are beginning to lay people off in the US with Meta announcing it would make 11,000 staff redundant, Amazon planning to let 10,000 people go and Elon Musk's recent takeover of Twitter also resulting in mass redundancies. Software engineers and other technology workers have been in high demand in recent years so this trend may be reversing. The US unemployment rate increased 0.2% to 3.7% in October 2022 but remains near record lows, which has been contributing to inflation and wage pressures.

Europe faces the potential of an electricity crisis as they head into Winter. European countries are connected through a web of interconnector cables, with some countries exporting and importing electricity depending on the time of day. The electricity shortages caused by the shortage of gas due to the war in Ukraine as well as the shutdown of some nuclear plants in France is leading to discussions of some countries forbidding the export of electricity due to high electricity prices in their home country. As some countries face blackouts, there will be both a human toll, due to the freezing weather, as well as an economic impact as manufacturing plants are shut down.

The elevated inflation is leading to increased pay disputes across the world resulting in industrial action, which has the potential to cause economic disruption leading politicians to get involved. The US Congress is preparing to take up legislation to avert a rail strip, which would cripple the US supply chain ahead of holiday season while the Western Australian Industrial Relations Commission is threating to suspend the registration of the Australian Nursing Federation.

Conclusion



Equity markets rallied again in November despite the real possibility of a recession in Europe and the US, which will impact corporate earnings. Higher interest rates will take time to impact the economy and it remains to be seen the degree of credit stress and defaults that will result. The electricity crisis in Europe, increased geopolitical tensions, the property market collapse and COVID-zero policy being the key known risks. There could well be further market volatility in the months ahead, but equity markets will likely bottom before the worst of the economic news is released.

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. Stay the course, despite how uncomfortable it may feel right now; it will prove to be the better option when looking back five years from now. Investors who stayed 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. 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, that 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.