RESEARCH UPDATE

MARKET watch

JANUARY 2023

Apt. WEALTH PARTNERS

December saw the continuation of the bear market with most equity markets falling sharply. The S&P 500 Index declined by 5.9% outperforming the technology-heavy Nasdaq Composite which fell -8.7%. The Hang Seng Index was an outlier, ending the month 6.4% higher following on from the 26.6% increase in November as optimism around COVID-19 lockdown restrictions and China reopening continued. The S&P/ASX 200 Index was not immune to the global equity sell-off, falling by -3.4% with all sectors delivering a negative return.

S&P/ASX 200 Sector Performance

Materials was the best-performing sector falling by -0.9% as a rally in the gold miners offset weakness in the rest of the sector. Chalice Mining Limited (+18.6%), Evolution Mining Limited (+10.8%), Ramelius Resources Limited (+8.8%) and Regis Resource Limited (+6.7%) benefited from the increase in the gold price. Lithium miners were the sector's worst performers with Liontown Resources Limited, Lake Resources Limited N.L, Pilbara Minerals Limited falling by -31.8%, -20.0% and -19.5% respectively.

The Consumer Staples sector declined by -1.9% driven by Endeavour Group Limited which fell -7.9% following the announcement that Woolworths Group Limited would sell their 5.5% stake in the company. Endeavour also flagged that the Australian Competition and Consumer Commission would not oppose the acquisition of four hotels and liquor outlets in South Australia subject to one divestiture. Dairy and brand companies Bega Cheese Limited and A2 Milk Company Limited were the sector's best performers rising by 10.6% and 10.9% respectively, despite no significant news being announced by either company.

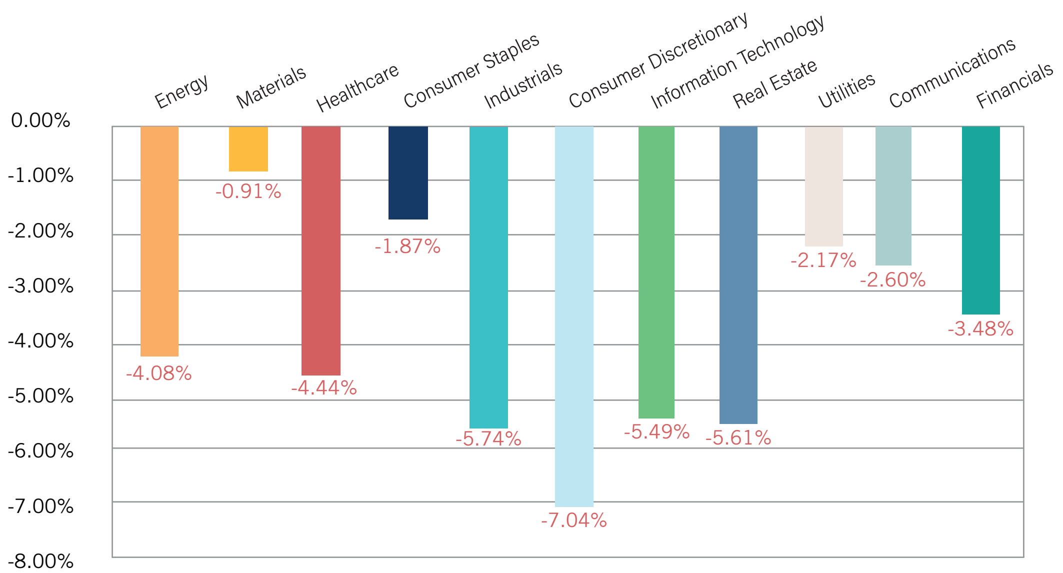
Communications declined by -2.6% driven by Nine Entertainment Company Holdings Limited which fell by -15.4% after Domain Holdings Limited (-11.4%), which is 60% owned by Nine, announced a weak trading update due to a slowdown in property listings with the company stating that December property listings were down -51% in Sydney and -37% in Melbourne on the prior corresponding period. The update from Domain also resulted in a sell-off in competitor REA Group Limited which declined by -10.2%.

The Health Care sector declined by -4.4% driven by ResMed Inc and CSL Limited which fell by -9.1% and -4.1% respectively. ResMed fell despite no significant news being announced, while CSL declined following the announcement that a new Chief Executive Officer (CEO), Dr Paul McKenzie, would replace outgoing CEO Paul Perreault on 6 March 2023.

Industrials fell by -5.7% driven by Downer EDI Limited, which declined -28.2%, reversing all of the prior month's gains plus more following the announcement that accounting irregularities had been identified in the Australian Utilities business, which would lead to restatements of financial results for the 2020, 2021, 2022 and 2023 financial years. The announcement came just days after the announcement that the long-standing CEO Grant Fen would step down and be replaced by the current Chief Operating Officer (COO) Peter Tompkins. Rating agency Fitch Ratings also downgraded their issuer rating for Downer, retaining the 'BBB' rating but now with a negative outlook. Johns Lyng Group Limited fell -15.1% following news that the COO Lindsay Barber had sold four million shares representing 31% of his holding in the company. The company also reconfirmed prior earnings guidance.

Consumer Discretionary was the worst performing sector falling by -7.0%, driven by The Star Entertainment Group Limited, which fell by -34.7% following the announcement that AUSTRAC had commenced civil penalty proceedings against the company for breaches of anti-money laundering laws and that Queensland had fined the company $100 million for similar offences. A special manager has been appointed to manage the casino in Queensland following similar moves in Victoria and New South Wales earlier in 2022.

Graph 1: S&P/ASX 200 Sector Performance



Data Source: Desktop Broker, 9 January 2023.

Highlights

Australia: The Australian Bureau of Statistics (ABS) reported that Australia's Gross Domestic Product (GDP) increased by 0.6% over the September quarter and 5.9% over the year to September 30. Household spending rose 1.1% for the quarter, contributing 0.6% to GDP, driven by spending on hotels, cafes and restaurants (+5.5%), transport services (+13.9%) and vehicle purchases

(+10.1%). Compensation of employees increased 3.2%, the strongest rise since December quarter 2006. Net trade detracted -0.2% from GDP, with a 2.7% increase in exports offset by a 3.9% rise in imports. Imports rose strongly driven by Travel services imports (up 58.0%), as Australians travelled abroad.

Using data from the 2021 Census, the ABS reported that more than half of people aged 15 and over (54.7% or 11.4 million) had completed a non-school qualification, more than double the rate (24.2%) of people in 1981. The gap between males and females has closed in the past 40 years. In 1981, there were around 750,000 more males than females with a non-school qualification, while in 2021, the trend had reversed, with 110,000 more females than males. Qualifications in Construction, Engineering and IT were more popular with males and qualifications in Nursing, Human Welfare and Behavioural Science were more popular with females. Qualifications in Business and Management, Accounting, Food and Hospitality and Teacher Education were popular with both males and females.

The ABS reported that average household debt grew by 7.3% in the 2021-22 financial year to $261,492, while average household disposable income grew 3.7% to $139,064. The highest income quintile households held 1.98x the debt and 2.07x the gross disposable income compared to the average.

US: Large asset manager Blackstone has limited withdrawals on its US$125 billion real estate investment fund, the Blackstone Real Estate Income Trust, following a surge in redemption requests from investors. The surge was driven by concern around values in the commercial property market. The redemption freeze highlights the risk of investing in unlisted property funds.

Taiwan Semiconductor Manufacturing Company (TSMC) announced it would triple the size of its investment in new semiconductor fabrication plants in the US to US$40 billion. The move by TSMC follows the passage of the Biden Administration's Chips and Science Act which provides US$52 billion in subsidies for chipmakers based in the US. TSMC is under pressure from Western Governments, in particular the US, to build plants outside of Taiwan to diversify global supply chains, especially in light of increased geopolitical tensions. Apple Chief Executive Officer Tim Cook has already agreed to source semiconductor chips from the plants.

Japan: The Japanese Government announced a US$320 billion five-year plan to purchase new military equipment, with the country committing to increase defence spending to 2% of GDP, from 1% currently, which would make it the third largest military spender behind only China and the US. Large US defence contractors are expected to win a sizeable portion of the increased spend, but Japan is also looking to develop domestic suppliers, including the construction of a next-generation fighter jet in conjunction with Italy and the UK.

Renewables: The International Energy Agency (IEA) released a report titled *Renewables 2022: Analysis and forecast to 2027*, which provided insights into the progress of the world's transition to renewable energy generation. The IEA forecasts that renewables will surpass coal as the largest source of global electricity generation by early 2025, with solar to become the dominant source of electricity generation by 2027. The transition that was already occurring has been expedited by the war in Ukraine, with Europe and China expected to be the two main regions of growth for renewables.

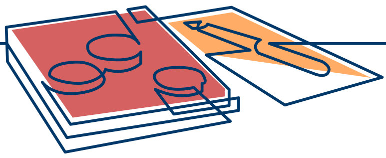
Crypto: The Bank of International Settlements (BIS) released a working paper on cryptocurrency (crypto) trading and Bitcoin prices. The working paper highlighted that 40% of crypto app users are men aged under 35, with peak downloads occurring when Bitcoin was above US$20,000 a coin. The BIS estimates that 81% of users have lost money, with adoptions highest in Turkey, Singapore, the US and UK. Australia's average month app usage is about 150-1,000 per 100,000 people.

What to watch out for

The US has begun to buy oil to replenish the strategic reserve now that the price has fallen below US$80 a barrel.

The head of the International Monetary Fund, Kristalina Georgieva, warned of a 'tougher' 2023 with the US, the European Union and China all expected to see a significant slowdown in its economies with a third of the global economy expected to be in recession.

Conclusion



Following two months of gains, equity markets fell sharply in the lead-up to Christmas. Economists are forecasting a particularly hard start to the 2023 calendar year, with Europe likely already in recession and the US teetering on the edge. China, now the second largest economy, is also struggling with a large COVID-19 outbreak as authorities take steps to reopen their economy. The economic stress from higher interest rates is just beginning to be felt, with Australia unlikely to remain immune, especially due to Australian households' relatively high amounts of floating rate debt. Growth assets will also need to adjust to the fact that relatively risk-free returns nearing 4% can now be generated from cash. There could well be further market volatility with significant pessimism from households, businesses and investors. It is important to keep in mind that equity markets are forward-looking and 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.

Disclaimer:

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