RESEARCH UPDATE

MARKET watch

MARCH 2023

Apt. WEALTH PARTNERS

Equity markets fell sharply in February as the market optimism from January faded. The S&P 500 Index declined by 2.6%, underperforming the Nasdaq Composite Index, which fell by 1.1% following a higher-than-expected US inflation print. The Hang Seng Index declined by 9.4%, reversing some of the 54% gain the index had made since the late October 2022 low. The S&P/ASX 200 Index underperformed international markets, falling by 2.9%, with most companies reporting their financial results for the prior 6-month period.

S&P/ASX 200 Sector Performance

Materials was the worst-performing sector, falling by 6.9%, driven by BHP Group Limited, which fell 8.5% after reporting a decline in profit on the prior period due to weaker iron ore, copper and coal prices. Lithium miners Lake Resources NL, Silver Lake Resources and Core Lithium were amongst the sector's worst-performing, falling 23.3%, 22.7% and 19.8% respectively as the lithium price fell to a 12-month low.

The major banks Commonwealth Bank of Australia (-8.5%) and Westpac Banking Corporation (-5.0%) dragged the Financials sector down 3.8%. Commonwealth Bank reported a 9% increased cash net profit after tax (NPAT) on the prior corresponding period but flagged slower credit growth and a possible increase in provisions in the months ahead as households and businesses struggle with higher loan repayments. AMP Limited was the sector's worst performer, falling by 22.5% after reporting Financial Year 2022 results which missed earnings expectations as the company continued to lose customers and experience fund outflows.

The Energy sector fell by 1.7%, driven by the major coal miners Whitehaven Coal Limited and New Hope Corporation Limited, which declined by 14.0% and 7.3% respectively as the coal prices continued to fall and Whitehaven traded ex-dividend.

The Communications sector rose 0.4%, driven by TPG Telecom Limited, which increased by 5.2% after reporting that NPAT was flat on the prior corresponding period if the gains on the sale of tower assets and customer base amortisation is excluded.

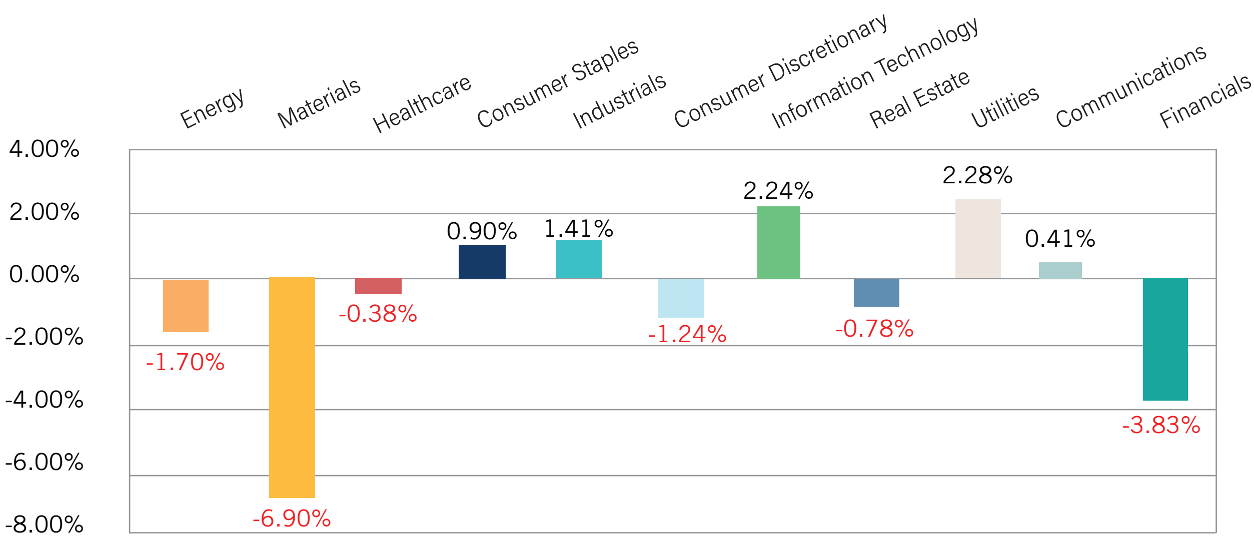
The Consumer Staples sector rose 0.9%, driven by Coles Group Limited and Woolworths Group Limited, which increased by 1.5% and 2.6% respectively. The two major supermarkets reported strong financial results despite cycling the strong COVID-19 lockdown periods as customers ate more frequently at home instead of dining out due to cost-of-living pressures. Costa Group was the sector's worst performer, falling 10.9% after reporting a 19% decline in NPAT due to higher employment and other operating expenses.

Industrials rose 1.4%, driven by Brambles Limited, which reported, if currency movements are excluded, a 20% increase in NPAT on the prior corresponding. Earnings per share grew faster at 24% as the on-market buyback reduced the number of shares outstanding. A 41.4% increase in NPAT on the prior corresponding period drove Qube Holdings Limited 5.2% higher, with all operating divisions benefiting from an increase in shipping volumes.

The Information Technology sector increased by 2.2%, driven by Link Administration Holdings, which rose 19.3% after reporting First Half 2023 Financial Year operating Earnings Before Interest and Tax (EBIT) rose 14.1% on the prior corresponding period. Link recently completed the spin-off PEXA Group Limited, Australia's largest digital conveyancing and real estate settlement platform. Computershare Limited rose 4.4% after reporting NPAT rose 92.3%, driven by higher margin income as global interest rates rose.

Utilities was the best-performing sector, rising by 2.3%, driven by Origin Energy Limited, which rallied 7.2% after the company received a revised takeover proposal at $8.90 per share. AGL Energy Limited fell 9.8% after reporting an NPAT loss of $1.1 billion in the first half of the 2023 Financial Year, and downgraded Financial Year 2023 underlying NPAT guidance to $200 and $280 million from $200 to $320 million.

Graph 1: S&P/ASX 200 Sector Performance



Data Source: Desktop Broker, 1 March 2023.

Highlights

Australia: The Australian Bureau of Statistics (ABS) reported that total arrivals into Australia in December 2022 reached 1.3 million, compared with less than 300 thousand in January 2022. Arrivals in 2022 reached just 45% of 2019 levels, but monthly figures show a steady recovery building. International students returning to study in Australia will likely drive figures higher in the months ahead. The increased migration should help with the labour shortage in some sectors of the economy, especially hospitality, while also having an impact on rental markets in major cities.

The Reserve Bank of Australia released the latest economic forecasts, with Australia's economic growth expected to slow, with 1.5% growth forecast over both 2023 and 2024. Growth is expected to pick up from late 2024 as the drag on growth from the earlier monetary policy tightening starts to wane and inflation moderates. The unemployment rate is forecast to remain around 3.5% until mid-2023, before rising as growth slows. Inflation is forecast to decline to around the top of the 2–3% target band over coming years.

ASX-listed Goodman Group Limited has reportedly begun construction on Australia's largest warehouse in Melbourne's west for wholesaler Metcash, which supplies IGA supermarkets throughout Australia. The warehouse is expected to have an end value of $300 million and will equal the size of 16 football fields, with automated temperature control included.

The Federal Government has announced a consultation on legislating that superannuation should be used for the sole purpose of providing retirement savings. The consultation is in response to the previous Liberal Government policy allowing people to withdraw from superannuation during the COVID-19 pandemic, as well as their current policy to allow people to withdraw from superannuation to fund a home deposit.

UK: The UK is moving ahead with plans to regulate buy now, pay later (BNPL), classifying it as credit and giving the Financial Conduct Authority powers to regulate BNPL providers. BNPL providers will be required to give consumers key information about their loans and issue credit that is affordable, while users will have the right to take complaints to the Financial Ombudsman Service. BNPL is increasingly looking to be regulated like credit, which may constrain future growth in a sector that is also struggling to sustain margins as interest rates rise.

China: China Telecom and China Mobile have both withdrawn from a subsea internet cable project that will link Asia to Europe as geopolitical tensions continue to grow. The two companies withdrew after a US company was selected to build the line over China's Hengtong Marine. The two companies were expected to contribute 20% of the US$500 million cost of the project.

AI: The recently released chatbot ChatGPT has reportedly been able to pass the technical part of the hiring process for a level 3 software engine position with Google. The position is still considered 'entry level', but has a starting salary of US$183,000 per annum. There is increasing debate about whether ChatGPT, which has partnered with Microsoft, will be able to disrupt Google's virtual monopoly of the internet 'search' industry.

Quantum Computing: Google has been able to drastically lower the error rate for quantum computer calculations in the latest advance in making the technology viable. The technology is difficult to understand, with quantum computers based on quantum states called qubits, which can exist in a mixture of '0' and '1' states, instead of in ordinary computers which must either be '0' or '1.' The advances follow the 2019 experiment, where a quantum computer completed a calculation that would have taken thousands of years by an ordinary computer.

Nuclear Fusion: The technology is seeing increased investment both from governments and the private sector on hopes that it can finally be a viable, carbon-free source of energy. The technology is still expected to be decades away, with commercial electricity generation unlikely to happen until around 2050.

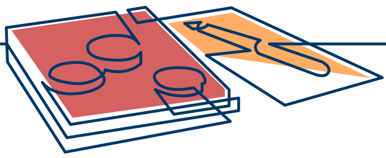
What to watch out for

Inflation in many countries looks to have peaked as COVID-19 supply chain disruptions have been cleared and as energy prices have fallen. Uncertainty remains as to how long, and whether further interest rate rises, will be required to bring inflation down to most Central Bank target ranges of 2-3%.

A number of financial and economic indicators are pointing to a high likelihood of recession or significant economic slowdown in the US in the short to medium term.

Multinational companies are moving manufacturing operations from China to other areas of Asia to diversify supply chains as well as lower costs.

Conclusion



The strong 'risk on' market that began the calendar year stalled in February. Bonds yields rose, leading to a sell-off in interest-sensitive sectors, including 'growth' stocks. Investors remain concerned that rates will need to rise further and stay higher for longer to control inflation, which increases the likelihood of recession. A recession, or as least a significant economic slowdown, would impact corporate earnings and likely lead to increased market volatility. 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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