RESEARCH UPDATE

MARKET watch

MAY 2023

Apt. WEALTH PARTNERS

Equity markets continued to rally over the course of April as data showed a continued decline in global inflation following the peak at the end of the 2022 calendar year. The S&P 500 Index rose 1.5%, while the Nasdaq Composite Index underperformed, finishing flat (+0.0%) in the lead-up to quarterly US reporting season. The Hang Seng Index fell 2.5% despite a rally in technology giant Alibaba Group Holding Limited shares after the company announced it would split into 6 separate units, which raised investor hopes that this would be the end of the Chinese Government crackdown on the technology sector. The S&P/ASX 200 Index outperformed international markets, rising by 1.8% with all but the Materials sector delivering positive returns.

S&P/ASX 200 Sector Performance

The Real Estate sector (+5.3%) rebounded in April to be the best-performing sector. Ingenia Communities Group was the strongest performer in the sector, rising by 13.3% after announcing the appointment of a new Chief Financial Officer who had prior experience at Mirvac and Commonwealth Bank. Stockland Corporation Limited increased by 11.8% after releasing a trading update that showed both occupancy and rent collection remained at very high levels, and confirmed prior guidance of 5% to 10% growth in Fund from Operations for the 2023 Financial Year.

The Information Technology sector increased by 4.8%, driven by data centre operator NextDC Limited (+9.8%) and data centre software provider Megaport Limited (+36.7%). NextDC announced new customer wins with contracted utilisation across the portfolio of 43%, while Megaport guided for Normalised Earnings Before Interest Tax, Depreciation and Amortisation of between $41 and $46 million for the 2023 Financial Year, well above the market consensus of $9 million.

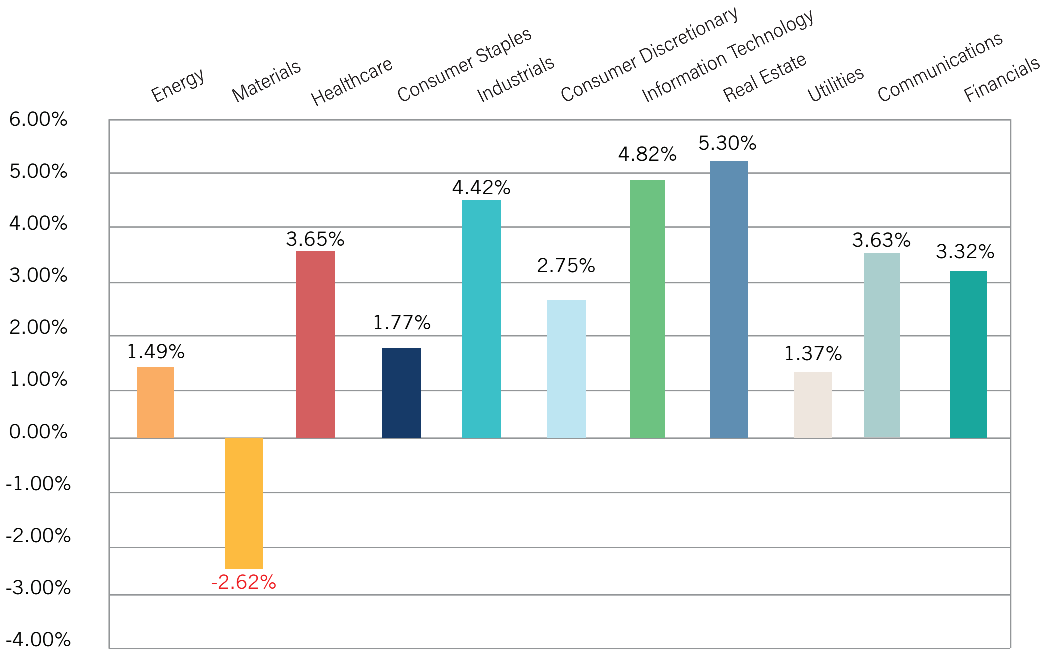
Plumbing supply companies Reliance Worldwide Corporation (+10.9%) and Reece Limited (+5.1%) drove the Industrial sector 4.5% higher. Reliance released a trading update for the nine-month period ended 31 March 2023 that showed sales were 10.3% higher on the prior corresponding period, which came despite adverse currency headwinds from the strength of the British pound against the Australian dollar. Reece rallied following the trading update from Reliance, with no company-specific significant news being announced.

The HealthCare sector increased by 3.7%, driven by Telix Pharmaceuticals, which rose 47.1% after releasing a string of announcements, including the acquisition of an artificial intelligence company in Vienna, a successful preclinical development regarding a cancer treatment and March quarter financial results that showed it was the first quarter where revenue surpassed $100 million. Cochlear Limited rallied 4.3% despite the announcement that the UK Competition and Markets Authority provisionally found that the proposed acquisition of Oticon Medical would substantially lessen the competition in the supply of bone conduction hearing solutions in the UK.

The Consumer Staples sector rose 1.8%, driven by Blackmores Limited, which rose 35.0% after announcing that the company had received a $95 cash per share takeover offer from Japanese beer company Kirin Holdings Company Limited as the company seeks to diversify its operations.

Materials (-2.6%) was the worst-performing sector and the only sector to deliver negative returns. Graphite miner Syrah Resources Limited fell 37.3% after highlighting volatile conditions in the Chinese anode market, which had impacted customer sales as well as a new $150 million convertible note with AustralianSuper. Mineral Resources declined by 8.6% after announcing it had acquired 81.5% of the outstanding shares of Norwest Energy Nl, despite the announcement that shipments of iron ore for the 2023 Financial Year would be in line with prior guidance after recording a 10% increase in shipments quarter on quarter.

Graph 1: S&P/ASX 200 Sector Performance



Data Source: Desktop Broker, 1 May 2023.

Highlights

Australia: The Australian Bureau of Statistics (ABS) reported that the seasonally adjusted unemployment rate remained near a record low of 3.5% in March 2023. The number of people employed increased by around 53,000 people while the number of unemployed decreasing by 1,600 people as the participation rate increased to 66.8%. The tight labour market will make bringing inflation back into the Reserve Bank of Australia's target range of 2% to 3% more difficult.

AGL Energy shut down unit 4 of the coal-fired electricity plant in the Hunter Valley, which at one point supplied over 10% of NSW's electricity. The power plant is over 50 years old and had become increasingly unreliable. Despite the intention to shut down the plant being flagged 8 years ago, the shutdown continued to be contentious over fears it will drive up electricity prices and create grid instability. The next scheduled coal-fired power plant shutdown is also in NSW and currently scheduled for 2025.

US e-commerce company Amazon has built Australia's largest robotics fulfilment centre in Kemps Creek, NSW. The facility covers 200,000 square metres across four levels and cost $500 million to construct. The facility is open to the public to view four times a week, as well as virtually twice a week.

The Department of Industry, Science and Resources released the *Resources and Energy Quarterly*, which gives an overview as well as forecasts for Australia's resources industry. Australia's resources and energy exports are forecast to reach $264 billion for the 2023 Financial Year, driven by higher iron ore and energy prices. Iron ore prices are higher as a result of disruptions from Brazilian iron ore and strong demand from China, while energy prices, which includes coal and LNG, are higher due to Russia's invasion of Ukraine. Energy prices have fallen significantly calendar year to date, but are expected to stabilise short term as demand from China increases due to the recovery from COVID-19 shutdowns, before falling back to pre-COVID levels in the 2024 Financial Year. Australian exports are expected to benefit from the end of the La Niña weather patterns, which has disrupted supply, but there is a risk that tighter monetary policy around the world slows economy growth, resulting in lower commodity demand.

Landlords are increasing rents faster than inflation, driven by the combination of increased demand from international students returning, faster immigration, as well as landlords passing on increased mortgage servicing costs as interest rates have risen. The Federal Government's National Housing, Finance and Investment Corporation announced an all-time low in vacancies in February 2023 of 0.8%. Vacancy rates fell to record levels in Sydney (0.9%), Melbourne (0.8%), Brisbane (0.6%), Darwin (1.2%), while Perth and Adelaide hover at just 0.3%. The statistics have raised concerns as renters are generally younger, have lower incomes and are less wealthy than owner-occupiers.

US: A number of regional US banks, including Silicon Valley Bank, First Republic and Signature Bank, experienced financial difficulties as depositors rushed to withdraw funds. The banks were unable to meet all withdrawals as most held illiquid loans or securities, which have experienced significant declines in market value due to the rise in interest rates. US regulators stepped in to guarantee customer deposits and shore up the financial system, with buyers being sought for the remaining bank assets with equity holders having in most cases been wiped out. The risk of a bank runs has increased with the advent of 24/7 banking apps, meaning that billions of customer deposits can be withdrawn in a matter of hours.

Switzerland: The Swiss Federal Department of Finance, the Swiss National Bank and the Swiss Financial Market Supervisory Authority (FINMA) together forced Credit Suisse to merge with UBS due to financial concerns.

Germany: The last three nuclear power plants were shut down on April 15, 2023. The nuclear power plants were due to be shut down at the end of 2022, but the life was extended due to fears of electricity shortages given the reliance on Russian gas supplies. At one point, Germany had 19 nuclear power plants in operation, but this has been shrinking following the Chernobyl disaster. The closures come just as nuclear power is receiving increased attention.

Japan: In contrast to Germany, Japan has restarted nuclear reactors which had been shut down following the Fukushima nuclear disaster. The reactors have been restarted to ensure Japan's energy security which is under increased scrutiny following Russia's invasion of Ukraine. 10 nuclear reactors have resumed operation, with a further 17 in the pipeline.

India: The Indian Government has amended its IT laws to prohibit Facebook, Twitter and other social media firms from publishing, hosting or sharing false or misleading information about 'any business' of the government. The social media firms will be required to rely on a government fact-check unit to determine the authenticity of any claim, raising fears around the increasingly authoritarian government in what is now one of the largest global markets.

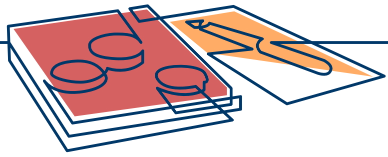
What to watch out for

Geopolitical tensions remain elevated. China undertook a large-scale, three-day combat exercise off Taiwan after the Taiwanese president visited the US, while South Korea, the US and Japan undertook a joint military drill after North Korea undertook further ballistic missile tests.

The global banking system appears to have been stabilised by regulatory intervention in the US and Europe following the collapse of Credit Suisse and a number of regional US banks. Risks remain as higher interest rates cause stress both in the banking sectors and elsewhere in the global economy.

The US Congress is yet to agree to an increase in the US debt ceiling. The debt ceiling will in all likelihood be increased, but the longer the issue drags on, the more likely the market will become concerned.

Conclusion



Markets largely shrugged off geopolitical tensions, higher interest rates, bank failures, US debt ceiling concerns and a slowing global economy in April. There are numerous factors that could result in an increase in volatility in the short term as investors weigh the prospects of a new bull market or further market declines. It is important to keep in mind that volatility is what creates the best long-term opportunities.

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, 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.

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