View from the hill

APRIL 2021

Market update

The table below provides details of the movement in average investment returns from various asset classes for the period up to **31 March 2021.**

Asset class (% change)	1 month	3 months	1 year	3 years (%pa)
Australian shares	2.4	4.3	37.5	9.7
Smaller companies	0.8	2.1	52.1	8.3
International shares (unhedged)	5.1	6.3	23.5	13.2
International shares (hedged)	4.2	6.2	51.1	13.3
Emerging markets (unhedged)	0.1	3.6	27.3	6.7
Property – Australian listed	6.3	-0.6	45.4	7.9
Property – global listed	4.0	7.6	30.9	5.4
Australian fixed interest	0.8	-3.2	-1.8	4.0
International fixed interest	-0.4	-2.5	1.1	3.8
Australian cash	0.0	0.0	0.1	1.1

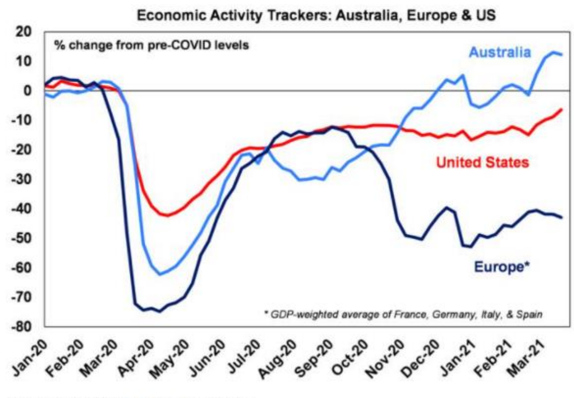
Past performance is not a reliable indicator of future performance.

Overview & Outlook

Following a period of stable coronavirus numbers and positive sentiment around the rollout of vaccines, cases in March have edged upwards again, predominantly in Brazil and India where healthcare workers have struggled with the slow vaccine rollout. In the US, the economy has been rapidly improving, with over 900,000 jobs created in March, almost doubling the February numbers. The new administration has proposed additional fiscal stimulus of $2.3 trillion to tackle infrastructure projects such as transportation, utilities, and job training. If implemented, this could potentially have flow-through benefits on Australian construction and materials companies.

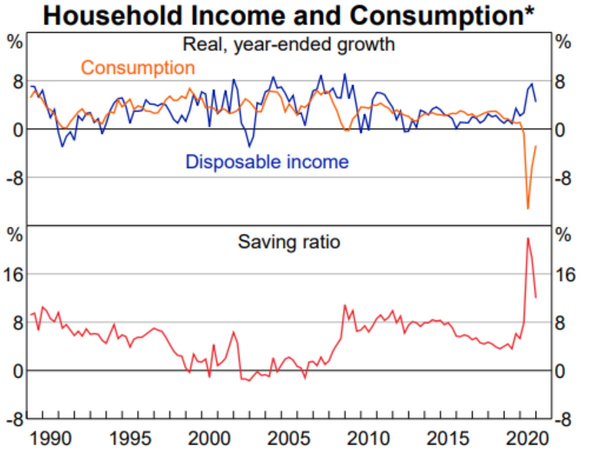
With the stimulus in the US expected to be worth 9% of GDP, inflation expectations remain high and the US market has reacted positively to the stimulus, with the S&P 500 up 4.24% over March. However, there are concerns of a fiscal drag, especially as the packages may be partially funded by a corporate tax hike to 28% and potential increase in income tax on high earners.

In Europe, lockdowns continue to stall economic activity, with economic outlook still weak due to disarray in vaccine distribution. Despite this, the MSCI Europe ex-UK finished the quarter 6.2% up and the PMI index shows manufacturing improving. Inflation expectations remain stable at 0.9% p.a.



Source: ourworldindata.org, AMP Capital

The Australian economy continues to recover faster than expected, with economic activity now exceeding pre-COVID levels. The record-high savings ratio of 2020 have dropped, and the RBA comments that household and business balance sheets are in good shape which should support steady consumption. Building approvals also surged as the end of the Homebuilder Grant drew near. Tourism is expected to see a boost as Australia and New Zealand announced the trans-Tasman travel bubble which commences on April 19, giving residents of both countries an opportunity to release some pent-up spending demand.



* Household sector includes unincorporated enterprises; disposable income is after tax and interest payments; saving ratio is net of depreciation

Sources: ABS; RBA

The RBA held monetary policy at 0.1% at their April meeting and is not expecting to raise interest rates until at least 2024. The RBA's decision to keep rates low for an extended period of time has led to rapidly rising property prices, creating some concerns around lax lending standards.

Share markets

The markets finished strong at the end of March, with the Australian share market (+2.4%) being led by the Consumer Discretionary Sector (+7.03%) as JB Hi-Fi rose 19.3% supported by additional demand from new homeowners for household goods. Financials (+4.31%) also continued to improve with steepening yield curves. With growing economic optimism, broad commodity prices are buoyant with oil prices which are up 22% YTD.

Info Tech continues to fall (-2.95%) due to the impact of rising bond yields and investors revisiting the very demanding PE multiples on these stocks. Looking forward, sectors that benefitted from the pandemic, such as Info Tech and Health Care, may trade sideways as investors digest recent gains and consider their earnings potential.

International shares finished the month 5.1% up on a currency-hedged basis, the strongest it has been so far this year. This was largely driven by the US market (+4.2%) and European market (+6.2%). Technology shares took some hits due to rising bond yields but recovered slightly as the month ended.

After two strong months for both Australian and International shares, we may expect the gains to be slower but still with a risk of volatility. We saw volatility spike in earlier part of Q1 as news ebbed and flowed around the efficacy of the vaccine. Volatility continued into March after the default of Archegos Capital, a hedge fund which failed to meet its margin calls and caused significant loss to several large financial institutions.

Emerging markets have been struggling ever since the Chinese equity sell-off in February. However, this may be an opportunity for long-term investors, as emerging markets benefit from rising commodity markets, low global interest rates, and going forward, a potentially weaker US dollar.

The Australian dollar sunk to a three-month low, trading at US$0.76 (at the time of writing), but analysts are still confident on it returning to US$0.80 by year-end.

Interest Rates

Bond markets have stabilised outside the US, with the Australian fixed interest index returning 0.8% in March. The Australian 10-year bond yield settled at around the 1.80% mark, finishing 11bp up from the previous month. However, the US 10-year Treasury Bond Rate continues to rally, ending on a high of 1.77%, moving 26bp from last month-end. Due to rising inflation expectations and the positive economic outlook, international fixed interest assets (-0.4%) continue to be sold off.

Source: Bloomberg Finance, L.P. as of March 31, 2021

The outlook for the bond market is for yields to continue to rise, with economists predicting that the Australian 10-year bond rate could reach 2% by the end of 2021. This should prove to be beneficial for the financials but could be problematic for companies that have unhedged debt.

Property

Australian REITs (+6.3%) improved this month, with the property developer and manager, Home Consortium, standout due to strong financial results. White-collar employment and business confidence are up, which positively contributed to office space demand. Global REITs (+4.0%) also bounced strongly driven by ongoing and significant upgrades in expected economic growth, particularly in the US.

Residential house prices grew by 2.8% in a month, rising at its fastest pace in the last 32 years. This has created concern amongst buyers and some analysts comment that this rate of growth is unsustainable.