Monthly Market Update

April 2023

MARKETS SUMMARY

Key Markets - Trailing Total Returns (%)						
As at 30 April 2023	1 mth	3 mths	12 mths	3 yrs p.a.	5 yrs p.a.	10 yrs p.a.
Australian Shares	1.8	-0.8	2.8	14.0	8.3	7.9
Australian Small Cap Shares	2.8	-1.7	-9.4	9.2	3.9	6.0
International Shares (Hedged)	1.3	1.7	0.6	11.0		
International Shares	2.8	8.3	9.8	11.7	9.9	12.9
Developed Markets Shares (Hedged)	1.6	2.4	1.5	12.1	7.6	9.9
Developed Markets Shares	3.1	9.2	11.0	12.7	11.1	13.7
Emerging Markets Shares (Hedged)	-0.8	-3.8	-6.4	3.0		
Emerging Markets Shares	0.2	1.6	0.5	4.0	1.6	6.5
Australian Property	5.3	-2.1	-9.9	10.7	4.9	7.4
International Property (Hedged)	2.0	-5.5	-16.4	4.3	0.5	3.2
International Infrastructure (Hedged)	2.1	0.3	-3.4	7.0	5.6	7.3
Australian Fixed Interest	0.2	2.0	2.1	-2.3	1.4	2.6
International Fixed Interest (Hedged)	0.4	0.7	-2.3	-3.2	0.4	2.3
Cash - Bank Bills	0.3	0.8	2.4	0.8	1.1	1.7

Investment markets extended their impressive start to the year in April, buoyed by resilient economic data, easing inflationary pressures, better-than-expected company earnings reports, and easing volatility as concerns about the United States (US) regional banking sector faded. A recovery in risk appetite supported another strong month for Australian and international shares, with all major markets outside of China performing well. Listed property rebounded after a difficult March, while fixed interest (bond) markets produced positive returns as bond yields stabilised following the previous month's falls.

ECONOMIC REVIEW

Australia

Having left the cash rate unchanged at its April meeting, the Reserve Bank of Australia (RBA) surprised markets with a 0.25% hike to 3.85% in early May — its highest level in 11 years and possibly the peak in the current cycle. Recent data has pointed to ongoing economic resilience, with the NAB Survey recording above average business conditions for the March quarter, and the Judo Bank Flash Australia Composite Purchasing Managers' Index (PMI) moved back into expansionary territory in April. Labour market conditions also remain robust. Employment was far better than expected, boosted by the creation of 53,000 new jobs, and the unemployment rate remains low at 3.5%. Driven by the services sector, Consumer Price Index (CPI) inflation came in a little ahead of consensus expectations, rising 1.4% in the March quarter. This translates to annual CPI growth of 7.0%, which is still well above the RBA's 2-3% target band, but marked a considerable fall from the 7.8% recorded in the previous quarter.

US

US economic data continues to send mixed messages. US gross domestic product (GDP) grew by 1.1% quarter-on-quarter in March, which was down from 2.6% in the previous quarter and well below consensus estimates of 1.9%. Lower energy prices are helping to slow the rate of inflation in the US, with CPI falling to 5% year-on-year in March, its lowest level in almost two years. The strength of the US labour market continues to keep the threat of recession at arm's length, for now. The April jobs report came in far better than expected, with 253,000 jobs added versus an estimate of 185,000. While inflation trends are reassuring, strength in employment appeared enough for the US Federal Reserve (Fed) to lift the cash rate by 0.25% to a target range of 5-5.25% at its May meeting. Fed Chairman, Jerome Powell, also ruled out the prospect of rate cuts at this stage, warning inflation will not come down to 2% overnight. Nevertheless, markets are currently expecting this recent rate hike will be followed by a lengthy pause.

Europe

The European economy returned to growth in the March quarter, expanding 0.1% quarter-on-quarter. Forward-looking flash PMI data for April reached an 11-month high of 54, with a score above 50 indicating expansionary economic conditions. Inflation remains stubbornly high, with annual inflation expected to increase from 6.9% in March, to 7.0% in April, according to a flash estimate from Eurostat. Against this backdrop, the European Central Bank (ECB) raised rates by 0.25% to 3.25% in early May but signalled there was more ground to cover with upside risks to the inflation outlook. Year-on-year inflation in the United Kingdom (UK) came in at 10.1% in March, higher than anticipated, and remaining above the 10% mark for a seventh consecutive period. This added to expectations the Bank of England would need to raise rates again at its next meeting in mid-May, in order to bring inflation down to a sustainable basis.

Asia

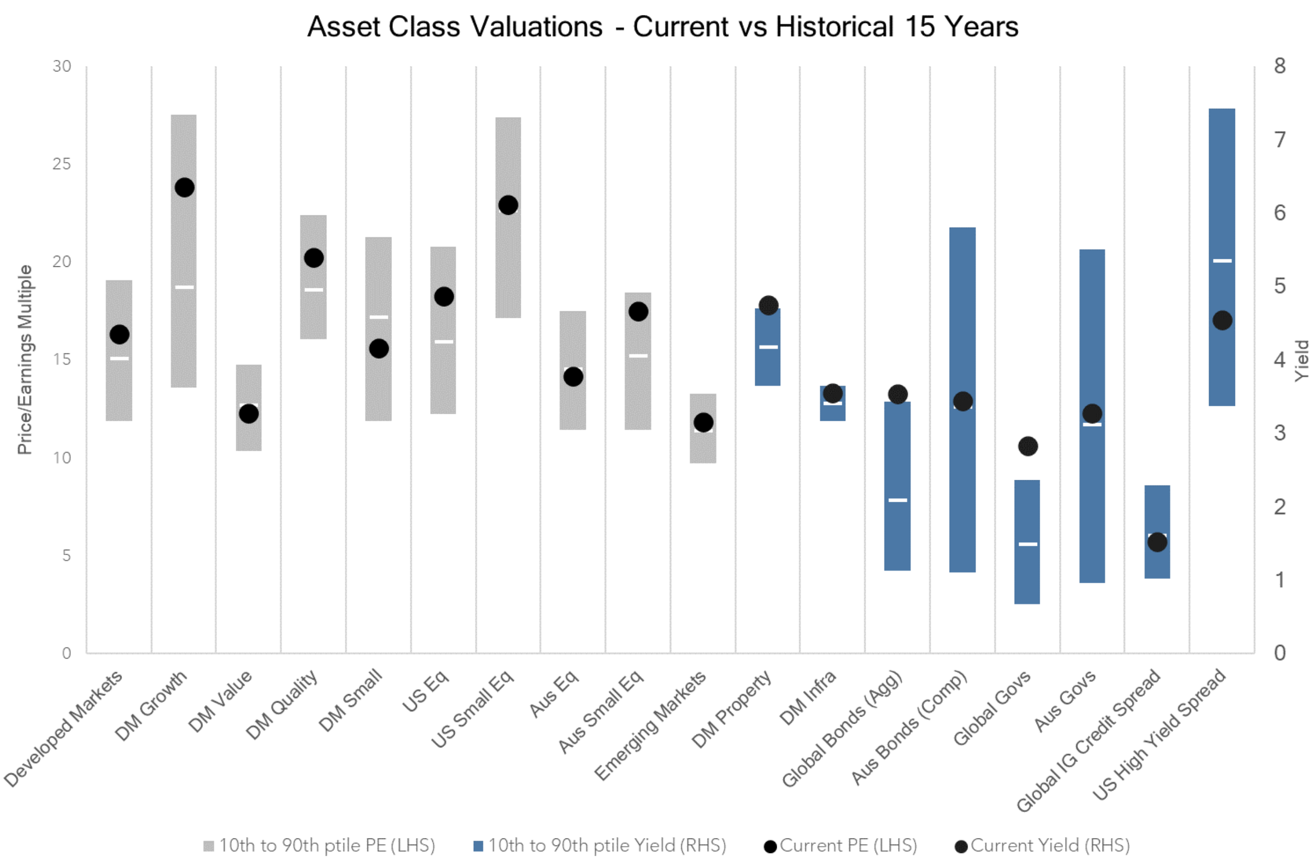
Japanese CPI inflation remains at a historically high level while wage growth was also shown to have accelerated following the spring wage negotiation between major companies and trade unions. Despite these pressures, the Bank of Japan (BoJ) kept its policy rate unchanged at its April meeting and is still expecting inflation to fall back below 2% later in the year. Data released in April confirmed China's reopening-driven rebound. March quarter GDP provided a positive surprise at 4.5% year-on-year, and retail sales were also significantly above expectations. Despite this, concerns around geopolitical tensions with the US and incoming US regulations that will restrict investment in China, weighed on Chinese markets.

US Debt Ceiling

Political risks have risen in the US, with the Department of Treasury estimating the US government's debt ceiling will be reached as early as 1 June. This means Congress will need to come to an agreement on lifting the debt ceiling soon, to ensure the US government is able to meet its financial obligations and avoid triggering a technical default. Debt ceiling debates are often a drawn-out process as the two parties — the Republicans who control the House of Representatives, and Democrats who control the Senate — trade off votes for political concessions such as spending cuts. Despite history telling us this will be resolved at the eleventh hour, the uncertainty can result in short-term market volatility. Although the Republicans are expected to push for less government spending, they are unlikely to push as hard as they would under other circumstances, given the potential recessionary risks this may cause in the current environment.

ASSET CLASS REVIEW

The following chart compares current valuations (dots) against the 15-year historical valuation ranges (bars) for different asset classes. Price/earnings multiples are used as the valuation method for shares (equities), while yield is used as the valuation method for other asset classes.



Source: Bloomberg/Evidentia.

Australian Shares

Australian shares moved higher in April as US regional banking contagion concerns receded and data pointed to a deceleration of inflation. The S&P/ASX 200 Index finished up +1.8%, with resources (-2.3%) significantly underperforming non-resources/industrials (+3.5%) as commodity prices experienced broad based declines with iron ore (-17.7%), copper (-4.1%), and oil (-4.1%) all falling on expectations of weaker global demand. Small companies outperformed large companies over the month — the S&P/ASX Small Ordinaries Index rose +2.8% — but continue to underperform calendar year-to-date due to their greater sensitivity to economic activity. In terms of sector performance, property (+5.1%), information technology (+4.8%), communication services (+3.6%), and health care (+3.6%) were standouts. While materials (-2.6%), which include resources, utilities (+1.4%), and energy (+1.7%) rounded out the worst monthly performers.

What Fund Managers are saying….

"There is widespread expectation that the global economy is heading towards an economic downturn. This need not be bad for investment portfolios as historical evidence points to equity markets often delivering solidly positive returns during those periods. In addition, there are certain areas that benefit either economic downturns, or can be expected to deliver growth regardless of the economic environment, such as discount retailers and healthcare. The key message is expectations of an economic downturn should not result in pulling back from investing but might refocus the areas one invests in." — Pella Funds Management

International Shares

International shares performed well in April. The MSCI All Country World Hedged Index lifted +1.3%, while unhedged shares were up +2.8% following further weakness in the Australian dollar (AUD). Performance was mixed at a sector level. Financials (+2.9%) and energy (+3.6%) shrugged off a poor last month to end April strongly. Health care (+3.2%) and communication services (+3.1%) also performed well, while materials (-0.7%) and information technology (-0.2%) lagged. After outperforming in the first quarter, growth (+1.4%) equity-style modestly trailed value (+1.8%) and quality (+1.9%).

US shares had another good month, with the S&P 500 Index gaining 1.6% on optimism the Fed's rate hiking cycle was nearing an end. The S&P 500 Index's performance has been significantly influenced by gains from some of its largest constituents, with Apple, Microsoft and Meta explaining more than half the Index's return this year.

With almost 75% of US companies having already reported for the first quarter of 2023, the results have been surprisingly positive with the vast majority beating consensus earnings expectations.

Eurozone shares (+1.6%) performed well on the release of resilient company earnings results, while the UK (+3.4%) enjoyed a strong month boosted by the financial sector and a recovery in its banks as fears surrounding the US issues receded. Japanese shares (+2.7%) maintained positive momentum in April as weakness in the Yen continued to support investor sentiment. Emerging market shares underperformed developed markets amid weakness in Chinese shares. China was the worst performing market in April, with promising economic data overshadowed by ongoing tensions with the US over Taiwan and the potential for new US restrictions on foreign direct investment into China.

International Shares - Trailing Total Returns (%) All Local Currency						
As at 30 April 2023	1 mth	3 mths	12 mths	3 yrs p.a.	5 yrs p.a.	10 yrs p.a.
Australia	1.8	-0.8	2.8	14.0	8.3	7.9
US	1.6	2.7	2.7	14.5	11.4	12.2
Europe	1.6	5.6	17.8	16.8	6.8	7.6
UK	3.4	2.6	8.2	14.1	4.9	6.0
Japan	2.7	5.4	11.3	14.7	5.5	8.2
China	-5.0	-10.7	-5.1	-5.9	-4.9	2.9
Asia (Ex-Japan)	-1.6	-3.8	-3.3	4.6	1.0	4.9
Latin America	2.0	-5.0	2.0	12.1	3.7	5.7

What Fund Managers are saying….

*"With growth fading, corporate earnings estimates are bottoming out and forward guidance remains mostly negative. Yet the S&P 500 still posted a blistering 7.5% first-quarter return, leaving valuations hovering near a ceiling that's only been breached during the dot-com bubble and post-COVID-19 period. A look under the hood reveals the disconnect. Only three sectors beat the index, and 90% of the S&P 500 return came from only 10 stocks—mostly tech giants. With winners limited to only 24% of the index's market cap, investors should be wary of a concentrated market. They should also be careful with speculative stocks burdened with poor fundamentals. Instead, make quality matter, focusing on companies with sound fundamentals and earnings prospects. The focus should be on identifying businesses well-positioned for an inflationary world, able to deliver cash flows that support positive real returns over time." — **AllianceBernstein***

Property and Infrastructure

After enduring a difficult March, due to concerns cracks that had appeared in the US regional banking sector may spread to the interest rate sensitive property sector, expectations of lower interest rates spurred a relief rally in April. The local S&P/ASX 200 A-REIT Index jumped +5.3%. Global property, measured by the FTSE EPRA Nareit Developed Index (Hedged), rose +2.0%. Global Infrastructure — also a benefactor of lower interest rates — had a solid month with the FTSE Global Core Infrastructure 50/50 (Hedged) Index up +2.1% and outperforming hedged international shares.

What Fund Managers are saying….

"The impact (of an expected earnings recession for global equities) on infrastructure should be muted. Particularly for our regulated assets, where the companies generate their cash flows, earnings and dividends from their underlying asset bases. We expect those asset bases to increase over the next several years. As a result, infrastructure earnings look better protected compared with global equities.

Most infrastructure companies have a link to inflation in their revenue or returns. Regulated assets, such as utilities, have their regulated allowed returns adjusted for changes in bond yields over time. As a result, the underlying valuations of infrastructure assets are relatively unaffected by changes in inflation and bond yields. However, we have seen equity market volatility associated with higher bond yields impact the prices of listed infrastructure securities, making them more compelling when compared with unlisted infrastructure valuations in the private markets." — ***ClearBridge Investments***

Fixed Interest

Australian and global fixed interest markets rose modestly in April, with the Bloomberg AusBond Composite 0+ Yr Index and Bloomberg Global Aggregate Hedged Index up 0.2% and 0.4% respectively. Australian government bond yields edged higher after last month's falls, with 2-Year and 10-Year Australian Government Bond yields closing out the month at 3.06% and 3.34%. 2-Year and 10-Year US Treasury yields were fractionally lower, ending April at 4.01% and 3.43%. Credit markets calmed down as investor focus shifted from the recent US banking sector issues to interest rates expectations and US company earnings. Global investment grade credit and US high yield performed well as spreads narrowed. The Australian short-term money market is indicating no further moves in the cash rate after the 0.25% rise in May, with the three-month bank bill swap rate (widely used to set lending rates) currently sitting near 3.85%.

Fixed Interest - Rates, Yields & Spreads

As at 30 April 2023	month end	1 mth earlier	3 mths earlier	12 mths earlier	10 yr average
Australian RBA Cash Rate	3.60	3.60	3.10	0.10	1.51
Australian 10 Year Bond Yield	3.34	3.30	3.55	3.13	2.47
Australian Corporate Bond Spread	1.85	1.92	1.75	1.53	1.23
US Fed Funds Rate	5.00	5.00	4.50	0.50	1.09
US 10 Year Bond Yield	3.43	3.47	3.51	2.94	2.19
US Corporate Bond Spread	1.36	1.38	1.17	1.35	1.25
US High Yield Bond Spread	4.52	4.55	4.20	3.79	4.30
Bloomberg AusBond Comp 0+ Yrs Yield	3.55	3.52	3.69	2.98	2.33
Bloomberg International Aggregate Yield	3.52	3.54	3.47	2.57	1.74

What Fund Managers are saying….

"As the cumulative impact of tighter financial conditions continues to grip and the cycle ages, our focus in the credit space is towards defensiveness, with a keen focus on risk-adjusted returns. Our strong bias is towards high-quality, liquid credit and issuers that can survive and thrive through a range of macro-economic scenarios. We are avoiding illiquidity, complexity and leveraged sectors, where we anticipate balance sheets will have to contend with a painful period of adjustment in a higher cost of capital environment." — ***Janus Henderson Investors***