INVESTMENT AND ECONOMIC SNAPSHOT

SEPTEMBER 2021

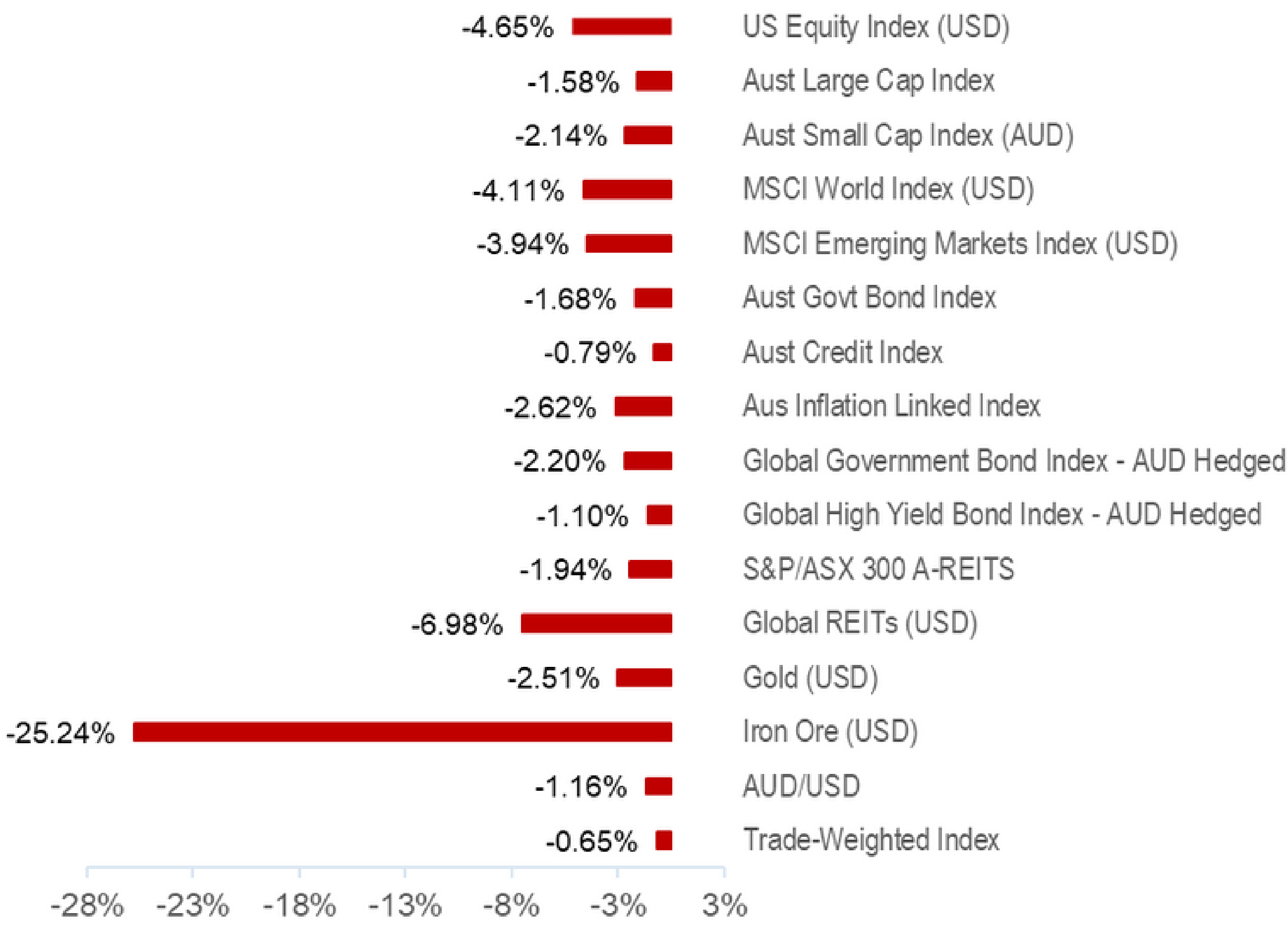
SUMMARY

The big news for markets in September was the announcement by the Fed that their tapering program would begin around the end of the year. This pushed real yields higher by around 20bps and sent the US 10-year government bond yield towards 1.50%. Here in Australia, the Reserve Bank of Australia (RBA) was a little more dovish due to the continued impact from lockdowns, stating they would delay the review of the current bond purchase program until their February 1 2022 meeting. As a result, our 10-year bond yields rose, but at a slower pace than the US, finishing the month up 14bps. The RBA's targets of 4% unemployment and 2.5% underlying inflation look like they will be achieved around the middle of 2022, with the speed of future tapering closely linked to progress towards these goals.

These significant movements in bond yields negatively impacted the performance of assets sensitive to interest rates. Long duration bonds recorded a negative month and growth stocks tendered to under-perform shorter duration value stocks. Globally, the Australian stock market was one of the better performers, beating the US, European and Emerging markets. This was, in part, due to our heavier exposure to energy-related stocks that were supported by stronger prices from key commodities such as coal, gas and oil.

The AUD/USD exchange rate was a little weaker over the month. Concerns about the collapse of the Evergrande Group and the associated impact on iron ore demand by the Chinese construction sector pushed our currency back down to US$0.72.

SELECTED MARKET RETURNS SEPTEMBER 2021



Sources: Thomson Reuters, Bloomberg. Equity returns are total return.

SEPTEMBER 2021 KEY DEVELOPMENTS

In September, global growth continued to be impacted by the third wave of COVID-19. In particular, Australia, China and Japan struggled to maintain positive growth as a result of shutdowns to limit the spread of the virus. Lead indicators of industrial production suggest that Q3 growth may be negative, although we anticipate this will quickly rebound towards the end of the year as economies are re-opened and the vast reserves of household savings are deployed into the market. Offsetting this will be the gradual withdrawal of policies designed to support growth, this includes the well telegraphed tapering of central bank bond purchases, as well as the normalisation of big fiscal spending programs.

The other key theme that drew investors' attention in September was the evolving potential for a debt default by the Chinese Evergrande Group. The Chinese Government's appetite to bail out the struggling construction conglomerate seems to be lower than in previous years as their focus turns more to implementing social policies designed to improve housing affordability. It seems likely the company may be forced to divest business lines in an attempt to reduce debt and meet their future payment obligations. Chinese non-manufacturing PMIs in September rose back to 53.2, above the key 50 mark that indicates an expansion. This suggests the Evergrande problems might be contained, and broader Chinese growth may be in for a soft landing. However, more important for the wider Chinese economy are power outages and electricity rationing as a result of coal stockpiles falling to 10-year lows. Given this is occurring at the same time as surging export orders, growth may be inhibited which would result in consumer price increases.

In the US, the big news is that the gradual normalisation of bond yields has started. September saw big increases in real yields, which helped to reduce or remove some of the significant mispricing in key markets. Key to the pace of tightening will be employment data and the flow-on impact to wage inflation. At the moment, shortages in labour have been most keenly felt in sectors rapidly rebounding from COVID-19 induced lockdowns. Participation rate data suggests workers have been happier on unemployment benefits rather than returning to work. However, these benefits have now ended, and we anticipate supply to improve in coming months. This will likely see the improvement in US unemployment stall before beginning to improve again next year.

Also in the US, the Biden administration recently hit a political hurdle to the implementation of their fiscal stimulus plans. The US debt ceiling negotiations once again appear to be keeping markets on edge – a last-minute deal in late September between the Democrats and Republications extended the deadline for an agreement to 18 October 2021. Agreement on this matter is critical as it is needed to fund round two of President Biden's infrastructure spending plan. Importantly, this stimulus is already priced into markets whereas the risk of a debt default is not. This presents a near-term risk to confidence and to equity markets.

In Australia, the full impact of the COVID-19 lockdowns is yet to be felt. Although, at the moment, markets seem less concerned about the impact of the widely anticipated negative growth in Q3 and more focused on reacting to international matters. Unemployment continued its downward trend, with August numbers released in mid-September showing an improvement to 4.5%, albeit this was off a lower participation rate. We anticipate this will reverse in coming months as the lengthy business shutdowns in New South Wales and Victoria have forced people out of work. The underemployment rate deteriorated from 8.3% in July to 9.3% in August, highlighting there is still significant spare capacity in our economy to absorb a strong rebound, thereby limiting the near-term potential for inflation above the RBA target band.

Given all this, valuations in the Australian equity market fell during September, albeit less than other major markets globally. Our market ended the month down (-1.6%) whereas the US market was pulled down further (-4.7%), with the materials and industrials sectors falling more than 5%. Stocks with longer duration cashflows and elevated valuations will remain under-pressure, this includes technology and utility stocks. However, other sectors and stocks that present better valuation metrics and that are more geared to shorter term market cycles are poised to outperform

The AUD experienced small declines against the USD, pulled down by iron ore which fell heavily during the month. From a technical perspective, short AUD positions are at extreme levels. As a result, we anticipate some support for our dollar, perhaps pushing closer to the mid-seventies over the coming months.

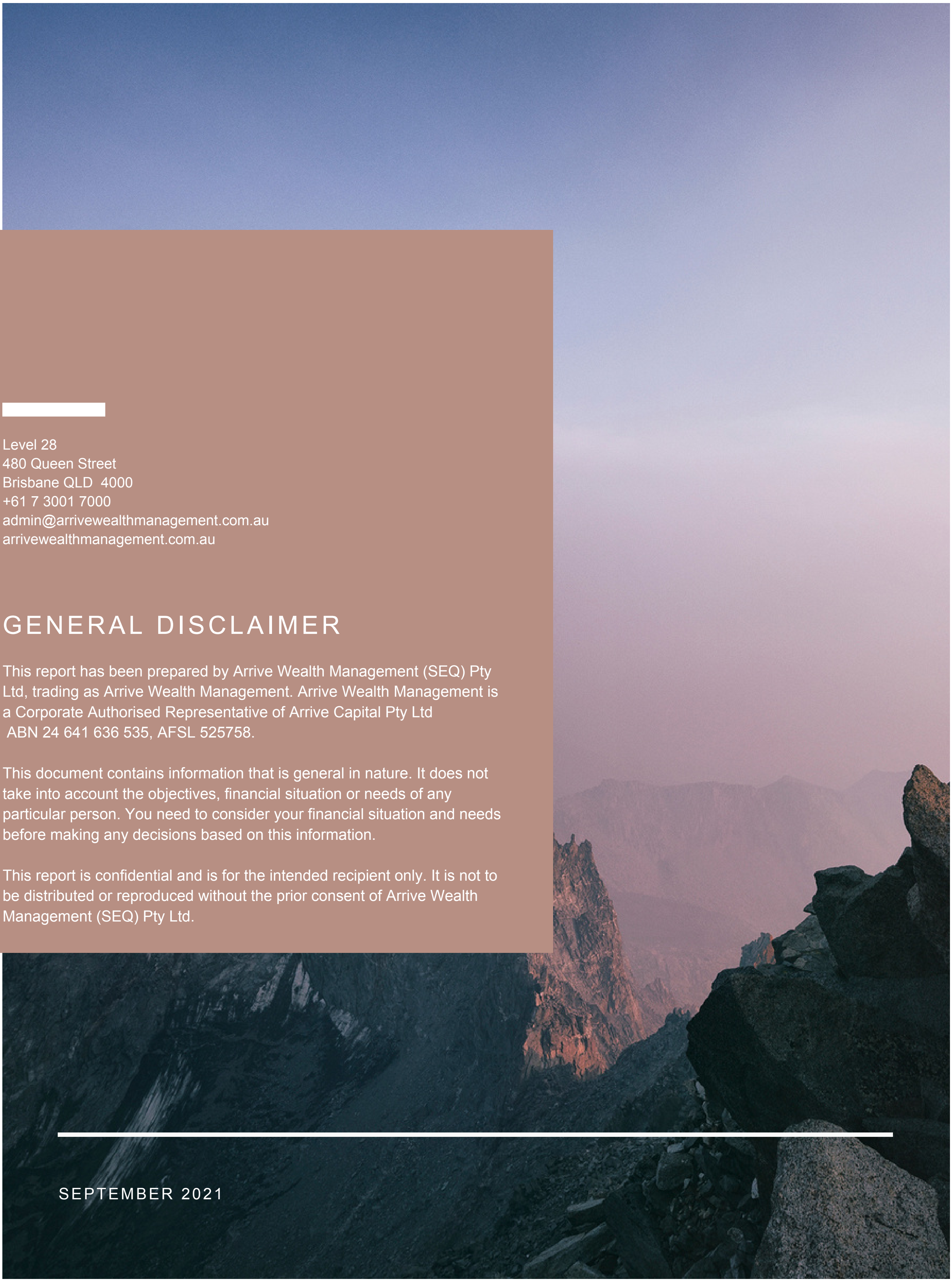
Bond investors also faced losses this month, especially longer-term bond holders that were buffeted by the rise in bonds yields. We anticipate this trend to continue, so reducing term exposure in bonds remains an important way to mitigate this risk.

MAJOR MARKET INDICATORS

	30-Sep-21	31-Aug-21	31-Jul-21	Qtr change	1 year change
Interest Rates (at close of period)					
Aus 90 day Bank Bills	0.01%	0.01%	0.02%	-2.0	-8.0
Aus 10yr Bond	1.26%	1.12%	1.25%	-26.0	+36.0
US 90 day T Bill	0.04%	0.04%	0.06%	-1.0	-6.0
US 10yr Bond	1.53%	1.30%	1.24%	+8.3	+85.0
Currency (against the AUD)					
US Dollar	0.722	0.731	0.735	-3.78%	0.78%
British Pound	0.536	0.532	0.530	-1.25%	-3.20%
Euro	0.622	0.620	0.621	-1.66%	2.59%
Japanese Yen	80.51	80.47	80.50	-3.38%	6.56%
Trade-Weighted Index	60.80	61.20	61.60	-3.03%	0.16%
Equity Markets					
Australian All Ordinaries	-1.6%	2.6%	1.1%	2.0%	31.5%
MSCI Australia Value (AUD)	-1.0%	1.6%	0.3%	0.9%	40.9%
MSCI Australia Growth (AUD)	-3.0%	4.4%	1.2%	2.4%	17.0%
S&P 500 (USD)	-4.7%	3.0%	2.4%	0.6%	30.0%
MSCI US Value (USD)	-3.6%	2.0%	1.2%	-0.6%	32.0%
MSCI US Growth (USD)	-5.7%	3.9%	3.5%	1.4%	29.1%
MSCI World (USD)	-4.1%	2.5%	1.8%	0.1%	29.4%
Nikkei (YEN)	5.5%	3.0%	-5.2%	3.0%	29.1%
CSI 300 (CNY)	1.3%	0.1%	-7.3%	-6.0%	8.0%
FTSE 100 (GBP)	-0.2%	2.1%	0.1%	2.0%	25.4%
DAX (EUR)	-3.6%	1.9%	0.1%	-1.7%	19.6%
Euro 100 (EUR)	-2.4%	2.3%	1.3%	1.2%	35.7%
MSCI Emerging Markets (USD)	-3.9%	2.6%	-6.7%	-8.0%	18.6%
Commodities					
Iron Ore (USD)	-25.2%	-14.3%	-14.2%	-45.0%	-1.7%
Crude Oil WTI U$/BBL	9.6%	-7.2%	0.4%	2.1%	87.6%
Gold Bullion $/t oz	-2.5%	-0.9%	3.3%	-0.3%	-7.3%

*For cash rates and bonds the changes are % differences. For the rest of the table, % changes are used.

ARRIVE
WEALTH MANAGEMENT



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