Atchison

Market Review
Calendar Year Ended December 2022

2021-22 (CY22) Calendar Year was a year to forget. After a bull market that lasted for more than a decade since the GFC of 2008-09, markets around the world experienced a massive pull-back. Both conservative investors with a concentration to high quality bonds or high-risk investors with an allocation to technology stocks, incurred losses. In fact, 2022 was just one of five in the last 100 years where both US Treasuries and the S&P 500 finished in the red.

What largely drove the bull market between 2009 and 2021 were a few separate but related themes; outburst of revenue growth in high flying sectors such as information technology and communications services, low inflation, and a very prolonged period of low interest rates, coming out of the GFC. Persistently low interest rates not only resulted in a low cost of capital for companies in growth mode, but also caused investors to give very high multiples to companies who delivered high sales growth rates. In many cases, these companies were and are far from profitability.

2022 marked a dramatic change in investor psychology. For years, but particularly since the start of the COVID pandemic, the old standby valuation metric of price/earnings was ignored in favour of the clouded price/sales metric. Late in 2021 and more so in 2022, this growth mindset at last fell out of favour, quickly collapsing some of the high vaulting valuations in pandemic-darling stocks like Meta, Alphabet, Netflix, and Tesla.

In response to soaring inflation in 2022 founded on Covid-induced supply-chain issues, firm demand in major economies and the fallout from the war in in Ukraine, central banks across the world scrambled to lift interest rates from emergency lows to levels that are generally regarded as necessary to reduce the rate of inflation. When interest rates begin to rise, long duration assets experience the most dramatic falls in prices. This precisely what we experienced in 2002. Duration is the financial term that measures the sensitivity of an asset's price to a change in interest rates. In low or falling interest rate environments, investors want to own assets with long duration, as they tend to rise in price the most as interest rates fall e.g., long term bonds or the ultimate long duration growth asset: growth stocks. Conversely, when interest rates do begin to rise aggressively, as in 2022, long duration assets experience striking falls in value. For example, most bonds pay a fixed coupon (i.e. interest payment) and when rates go up, the only way a fixed coupon can equate to a higher interest rate is if the investor pays less for the bond.

But it is not all doom and gloom, the Australian economy outperformed in 2022. The year ended with trade accounts solidly in surplus, the federal budget broadly balanced; jobless rate at 50-year lows. And while the inflation rate lifted over the year along with wages, other countries are experiencing far hiker spikes in prices.

From a COVID-influenced low base, the Australian economy grew by 5.9% over the year to September, but it is likely to slow over 2023 in response to higher interest rates.

Starting in May, the Reserve Bank (RBA) lifted the cash rate from 0.1% to 3.1%, the most aggressive monetary tightening ever imposed. The Consumer Price Index lifted 7.3% over the year to September 2022.

The past three years have proven to be challenging and no let-up in the short term is expected for Australian investors. Inflation, together with uncertainty about where interest rates will settle is expected to dominate in 2023. High energy prices will persist, the war in Ukraine still rages and the re-opening of the Chinese economy poses risks and opportunities.

It is expected that the average balanced growth superannuation fund (41% – 60% Growth Assets) would have returned -6% pa for the 12 months to 31 December 2022. This followed a positive return of around 9% in 2021 year. Balanced growth super funds returns have averaged around 3.5% pa over the last five years, above inflation, and bank deposit returns.

Australian Markets

The Australian share market performed admirably when compared to the global equity over the year returning -1.1% over the year to December. Strength in the local market has been buoyed by the highest earning and lowest multiple sectors - Materials (notably resources) and Financials.

Materials namely coal and oil stocks topped advancers in the index thanks to a global price surge sparked by the war in Ukraine. Technology and real estate shares suffered large loses as rising interest rates and inflationary pressures weighed on the sectors.

Australian energy firms, one of the world's biggest exporters of coal and natural gas, outperformed regional counterparts amid buoyant earnings and surging fuel prices. Local coal stocks also rallied as Russia's invasion of Ukraine disrupted global energy supply. Notable companies with significant price movements over 2022 year were; Whitehaven Coal Ltd (+303%), New Hope Corp. Ltd (+194%) and Woodside Energy Group (+64%).

2022 also saw a lithium rally with Core Lithium (+66%) leading the pack, closely followed by Sayona Mining Ltd (+46%) and Mineral Resources (+43%).

Iron ore champions ended the year on a high as China's abrupt Covid Zero reversal and a steady stream of supportive policies raised the outlook for demand. BHP Group Ltd and Rio Tinto Ltd returned +25% and +15% respectively for the year.

The worst performing stocks came from the Technology sector, in line with a global trend that saw the rate sensitive industry suffer. Battery materials supplier Novonix (-83%) took a major blow to its value as operating losses mounted and investors piled on bearish bets. Cloud services provider Megaport was the second worst (-67%) performer over the year after sales growth failed to meet investor expectations.

Market volatility, and concerns around inflation and rate rises remain an issue. It would seem that the majority of the economic tightening maybe behind us and we are now entering a period of slowing growth. However, given the relative strength of the Australian economy, the demand for resources, low unemployment, and the current strength in the job market, it is difficult to conclude that currently Australia will be entering into a recession.

Global Markets

Developed market equities had a difficult time in 2022. They declined 12% (unhedged basis) for the year, putting them firmly in bear market territory but up 4.1% for Q4. In the US investors balanced ongoing caution from the Federal Reserve (Fed) with indications that the pace of policy tightening would slow, and signs that elevated inflation could be cooling. There were also especially strong corporate earnings in certain sectors.

Most sectors rose over the final quarter, a number climbing significantly. Energy stocks posted especially strong gains, with sector heavyweights Exxon and Chevron posting record profits in the quarter. Consumer discretionary was a notable exception, with Tesla's decline an outsized influence.

Eurozone shares notched up a strong advance in Q4, outperforming other regions but fell 8% over the year. Gains came from a variety of sectors, notably economically sensitive areas like energy, financials, industrials, and consumer discretionary. More defensive parts of the market such as consumer staples lagged the wider market's advance.

UK equities rose over the quarter, helped in part by the country emerging from its September crisis. Markets had been volatile as the former prime minister and chancellor announced huge fiscal stimulus, with little detail on how it would be funded. Many of the policies announced in that September 'mini budget' were reversed and the new chancellor Jeremy Hunt used the Autumn Statement in November to promise the country would tighten its belt in the future. His assertions were supported by fiscal and economic forecasts from the independent Office for Budgetary Responsibility (OBR).

After rising for most of October and November, the Japanese stock market declined in December and ended the year down 4.1% for the twelve months.

Turning to emerging markets, equities fell by 15% as China's weakness led emerging markets downwards, despite a strong performance from commodity-producing countries such as Brazil. The strong US dollar helped undermine emerging economies and markets.

Small cap equities suffered due to their cyclical sensitivity, while defensive equities were also weak. Equity performance was driven somewhat by a strong US dollar, which mitigated the portfolio impact for unhedged non-US dollar investors.

Valuations have improved markedly over 2022 across all sub-asset classes. Still, global equities by some valuation measures are only back to their long-term averages. Investors appear to be under-weight global equities and are fearful of the future. The more aggressive repricing in fixed income means that, in some cases, bonds can offer a better risk-to-reward trade-off.

Australian and International Property

There has been nowhere to hide in 2022 – real estate equities have not been spared either. While historically, listed REITs have demonstrated that they can perform well in periods of rising inflation, 2022 proved to be different. Domestic and global real estate investment trusts (or REITs, as measured by the FTSE EPRA Nareit Developed Total Returns Index – Hedged) fell 24%. But what has caught most investors off guard has been the magnitude and stubbornness of inflation, coupled with central banks speedy response, increasing rates at an unprecedented pace.

While the overall listed global property market suffered in 2022, there are some important distinctions within regions. Asia proved somewhat more defensive, down only 14% partly due to already distressed valuations and lagged response in some reopened economies post pandemic. On the other hand, European property has fallen by 40% in US dollar terms as the market quickly re-priced off its low interest rate level and now trades at an unprecedented discount to net asset value (NAV), including during the GFC.

The fall in listed property values has not fully played out yet in the direct property markets, mainly due to a lack of transactions. Only owners who are forced to sell will receive lower prices, which will in turn push yield higher, ironically presenting investors another opportunity for investors to buy assets at a discounted price.

When it comes to Australian residential property values, the driving force for the property slowdown in 2022 comes down to Australia's fastest interest rate tightening cycle in history. The estimated total value of residential real estate decreased from $9.6 trillion in December 2021 to $9.4 trillion in November 2022. Over the year to November, national housing values fell by 3.2%, driven by an annual decline in capital city dwelling values. Meanwhile, regional values increased by 3.3% over the same period, according to CoreLogic.

Residential property prices are fundamentally driven by monetary policy followed next by supply and demand and mortgage serviceability risks. Any further rate rises will cause prices to continue to decline.

Cash, Fixed Interest and Corporate Bonds

Cash rates around the world soared from record lows, the RBA final rate hike of 0.25% in December lifting the official cash rate to 3.1%, the highest level since the end of 2012, in an effort to curb inflation. Whilst the US Federal Reserve raised the fed funds rate seven times in 2022 to 4.25%-4.5% during their last monetary policy meeting of 2022, pushing borrowing costs to the highest level since 2007.

2022 saw the first global bear market in government bonds for over 70 years, with prices adjusting to an environment of high inflation and sharply rising interest rates. Nominal bond yields rose broadly across all maturities, outside China. Inflation-linked or ‘real’ bond yields also rose sharply, returning to positive territory as central banks unwound their post-global-financial-crisis easing. Yield curves flattened and even inverted in some regions, as yields at the shorter-dated maturities increased to price in the tightening of central bank policies.

US 2-year and 10-year yields rose by 378 and 225 basis points, respectively, over the year. Bond managers seem to be moving duration positioning from underweight to neutral as bond yields have come a long way, reflecting a significant increase in central bank policy rates. However, inflation tail risks remain, which would put further upward pressure on bond yields. There is a slight preference for inflation-linked bonds relative to sovereign bonds.

Both investment grade and high-yield bond yields increased over the year, with total returns reaching -15% and -18%, respectively. Although corporate fundamentals had remained robust, a big sell-off in duration-linked assets, coupled with concerns about global economic growth and high inflation, meant that corporate bond pricing adjusted aggressively.

The consensus view on investment grade and high-yield credit is positive. A close to 9% all-in yield for global high-yield alongside rising but still low default activity, make the asset class an attractive opportunity. A lthough spreads are only

slightly wider than their longer-term averages, defaults are deemed to be unlikely to pick up significantly due to the limited upcoming maturities, stronger corporate balance sheets and an expectation that the US will avoid a deep recession. The case for investment grade is similar, with low downgrade and default expectations, but we have a slight preference for high-yield corporate bonds.

Commodities

One of the few asset classes to produce positive returns was commodities, rallying 19% due to strong demand and the Russia-Ukraine conflict. The rally cooled somewhat later in the year amidst recession fears and China's slowdown. The main reason for the strong upwards impulse for commodities was Russia's invasion of Ukraine and the subsequent political gesticulation, which culminated in Russia cutting supply of natural gas to Europe. The invasion also impacted industrial metals prices and soft commodities such as wheat. Gold and precious metals more broadly underperformed relative to other commodities, struggling in an environment of rising real yields.

Currently there is no evidence that the Ukraine war will come to an abrupt end and that supply issues for commodities will dissolve. Infact, should the war escalate the price of specific commodities will continue to climb.

Australian Dollar (AUD) Exchange Rate

The US dollar has gone from strength to strength this year, boosted by many tailwinds. US energy resilience, the carry advantage of US interest rates versus currencies such as the euro and the yen, and safe-haven demand have all helped the dollar to become one of the best performing currencies this year. A tailwind for Australian businesses with offshore earnings but raised the costs of imports.

Against the Australian dollar the AUD to the USD exchange rate range was 0.6199 USD to 0.7585 USD with an average exchange rate of 0.6948 USD.

Overall, it is expected that the AUD will remain below USD 0.70 subject to US economy not falling into a recession in 2023.

Australian versus the Global Economy

2022 - Supported by strong demand for commodities, full employment and economic and geographic distance from Europe, the Australian economy remained relatively resilient, although not immune to global trends.

With inflation at a 40-year high, central banks around the world rapidly tightened monetary policy, creating a backdrop that has required markets to digest a substantial increase in the cost of capital.

Against a turbulent and uncertain background, Australia is well-placed compared to other economies due to its relative geographic and geopolitical insulation, position as a net energy exporter, and resource-rich economy.

While the short-term outlook remains uncertain, these macroeconomic challenges are likely to abate at some point in 2023. It is likely that we will see inflation and interest rates peak and supply side constraints reduce (particularly labour shortages as immigration returns to normal). The timing and form of China's re-opening will also be a key driver.

While Australia will not be immune to global challenges, it is relatively well positioned for a softer landing than other developed economies

2023 Outlook

The good news as we enter the New Year is that central banks around the world are having success in reducing inflation. Broadly, if inflation retreats, the frequency and size of interest rate hikes may slow (or better still come to a halt), investors will become more confident and central bankers can aim for higher sustainable rates of economic growth.

In October, the International Monetary Fund released its latest forecast for GDP growth in the world's major economies for 2023 and 2024. Contrary to the noise around inflation, rising interest rates and plunging equity valuations, many major economies are expected to deliver decent growth across 2022. While 2023 is expected to be somewhat weak for global markets, some economies such as India and Korea are expected to deliver growth. As for the rest of world, it appears investors will have to wait until 2024 to start seeing signs of a recovery.

A further initial slowdown in 2023 should be anticipated but it is not expected to culminate in a deep global recession. However, there will be divergence between regions, some countries potentially experiencing worse economic performance than others. For example, UK and certain parts of Europe are expected to fall into recession.

Inflation is peaking, but not disappearing. It is expected that annual inflation rates to fall in 2023 but remain firmly above the 2% targeted by developed central banks.

Central banks can be expected to pause their tightening campaigns in early to mid-2023 to assess the impact of recent policy changes. Rates may stay at high levels in most countries before eventually being cut. However, further inflation surprises may prompt additional and aggressive action that would weigh on equity and fixed income returns.

Numerous geopolitical worries are likely to remain, with the conflict in Eastern Europe, China's position on Taiwan and ongoing tension with Iran continuing to impact economies and markets. There remains a question mark over China due to its regulatory crackdowns, a collapsed property sector and President Xi's tighter grip of political power following the recent National Party Congress.

Investors have had very few places to hide in 2022 as they adjust to a world of higher inflation and tighter monetary policy. Corporate bonds now look attractively priced, and defaults and downgrades appear to be contained. Sovereign bonds may offer better value than before, as do equities, where reasonable valuations must be balanced against optimistic earnings expectations and higher discount rates.

The US dollar is deemed to be significantly overvalued and should weaken longer term, although the near-term outlook remains unclear. Those investors with a longer investment time horizon could look to other currencies such as the euro and the yen, due to their cheap valuations.

In conclusion: Overall, Atchison Consultants see the following asset class implications for 2023:

- Equities may struggle on the upside with economic slowdown and recession risk on the horizon in the US, Eurozone and UK. Neutral on developed market equities.
- Emerging market equities could recover if there is sufficient China stimulus, US Fed slows the pace of tightening, energy prices subside and the US dollar weakens. Marginally overweight EM.
- Government bond valuations have improved after the rise in yields, risk of a further significant sell-off seems limited if inflation is close to peaking. Look at slowly increasing allocation to long duration bonds. Marginally overweight government bonds.
- High yield and investment grade spreads a near long-term averages. Current credit market yields are attractive however spreads will come under pressure if US recession probabilities increase. Overweight high yield bonds.
- REITs look attractively valued relative to global equities and listed infrastructure and should benefit from declining bond yields. Remain neutral listed infrastructure and overweight REITs.
- Commodities outlook is mixed, given expected slowdown in the global economy. Recessions will reduce demand for commodities like oil however the supply-side may tighten if more restrictions are placed on Russian oil exports. Overweight natural resources
- US dollar may lose its appeal if inflation begins to decline and the Fed pivots to a less hawkish stance in 2023.

Table 1: Market Performance – Periods to 31 December 2022

Sector	1 Month %	3 Months %	1 Year %	3 Years % pa	5 Years % pa
Australian Shares	-3.2	9.4	-1.1	5.6	7.1
Australian Shares Small Ords	-3.7	7.5	-18.4	1.4	2.9
International Shares Ex-Aus (Unhedged)	-5.5	4.1	-12.1	6.7	9.8
International Shares Ex-Aus (Hedged)	-5.1	7.5	-16.0	6.3	7.4
Emerging Markets (Hedged)	-2.0	6.7	-15.2	0.5	1.7
Emerging Markets (Unhedged)	-2.6	4.1	-14.0	-1.2	1.8
Australian Listed Property	-4.1	11.5	-20.5	-1.5	3.3
International Listed Property (Unhedged)	-3.8	4.0	-24.2	-5.6	-0.4
Australian Direct Property	-0.5	0.0	4.3	3.8	5.3
Australian Fixed Interest	-2.1	0.4	-9.7	-2.9	0.5
International Fixed Interest (Hedged)	-1.3	0.6	-12.3	-3.2	-0.2
Cash (BAUBIL)	0.3	0.7	1.3	0.6	1.0
		Change over the month			
Australian Govt. 10 yr Bond Yield	3.57	-17 bps			
AUD/USD	$0.68	+$0.03			

Australian Shares (S&P/ASX 200 Accumulation Index)

The S&P/ASX 200 returned -3.2% for the month, +9.4% for the quarter and only -1.1% for the past 12 months. In December, every sector was in the red. In the month, Materials was the least-worst performer (-1.1%) on the back of higher commodity prices and optimism about the medium-term outlook for improved Chinese demand. Utilities (-1.2%) also outperformed the broader index, helped by corporate actions whilst Consumer Discretionary (-7.0%) fell the furthest (-7.0%) over concerns of an economic slowdown.

The consensus view is that has been for the market to re-test equity low points as earnings revisions turn negative. As a result, investor positioning has been cautious which may result in a softer landing than otherwise.

The index finished trading at a P/BV of 2.0x and a P/E Ratio of 12.4x and equity yield (dividend) of 4.5%.

The S&P/ASX 200 VIX was at 12.38. A volatility index at relatively high levels generally implies a market expectation of very large changes in the S&P/ASX 200 over the next 30 days, while a relatively low volatility index value generally implies a market expectation of very little change.

Australian Shares Small Cap (S&P/ASX Small Ordinaries Index)

The Small Ord's Accumulation Index returned -3.7% lower in December and +7.5% higher over the quarter but down -18.4% for the year. As with large caps, resources outperformed industrials for the quarter and over the year. Small resource stocks outperformed industrials by +3.8% over the quarter and outperformed small industrials by over 15% for the 12 months.

Top performing stocks over the quarter were: Sandfire Resources (+47.4%), Webjet (+29.8%) and Syrah Resources (25.6%). Stocks that underperformed over the quarter included Earlypay (-54.5%), City Chic Collective (-63.7%) and Codan (-27.7%).

Trailing P/E Ratio was at 9.4x at the end of the month, P/BV is at 1.7x and equity yield (dividend) of 3.4%.

International Shares (MSCI World ex Australia Index, Net AUD and the MSCI World ex Australia Index, Net LCL)

The MSCI World ex Australia Index (Unhedged) -5.5% for December whilst the MSCI World ex Australia Index (Hedged) returned -5.1%. However global equities gained over the quarter +4.1% and +7.5% respectively. For the 12 months the unhedged index is down -12.1% whilst the hedged version returned -16.0%.

All major market bourses returned positive performance over quarter with old economy, high cash yielding cyclicals outperformed while tech underperformed. This dichotomy was most evident in the US where broad-based S&P 500 was up +7.1% over the quarter, significantly outperforming the tech-heavy NASDAQ (-1.0%).

The index finished trading at a P/BV of 2.6x and a P/E Ratio of 16.2x and equity yield (dividend) of 2.1%.

US market: US S&P 500 Index was up down +7.1%, the Nasdaq up -1.0% and the Dow Jones +15.9% for the quarter ended December 2022. However, for the year the S&P 500 Index was down -19.4%, the Nasdaq down -33.1% and the Dow Jones -8.9%.

US equities made robust gains in Q4, with much of the progress made in November. Investors balanced ongoing caution from the Fed with indications that the pace of policy tightening would slow, and signs that elevated inflation could be cooling. There were also especially strong corporate earnings in certain sectors.

Most sectors rose over the quarter, a number climbing significantly. Energy stocks posted especially strong gains, with sector heavyweights Exxon and Chevron posting record profits in the quarter. Consumer discretionary was a notable exception, with Tesla's decline an outsized influence.

Annualised Q3 GDP for the US was confirmed at 3.2% in December, which was stronger than the second estimate of 2.9%. Unemployment remains at 3.7%. 263,000 jobs were added in November; the lowest number since April 2021. The latest consumer price index (CPI) print – for November – showed inflation slowed to 0.1% (month-on-month) versus October. Inflation remains elevated however, at 7.1% year on year. The Fed's final rate hike of the year was indeed a pared back 50 basis points (bps) rise after four consecutive 75 bps tightening moves. The policy rate is, however, expected to continue to climb in 2023.

UK market: UK equities rose over the quarter, helped in part by the country emerging from its September crisis. Markets had been volatile in September as the former prime minister and chancellor announced huge fiscal stimulus, with little detail on how it would be funded. Many of the policies announced in that September 'mini-budget' were reversed and the new chancellor Jeremy Hunt used the Autumn Statement in November to promise the country would tighten its belt in the future. His assertions were supported by fiscal and economic forecasts from the independent Office for Budgetary Responsibility (OBR).

This message was in keeping with the fiscally conservative reputation of Rishi Sunak, who was appointed leader of the Conservative Party and, by extension, became the country's new prime minister. Sunak's prior experience as chancellor also helped to stabilise gilt yields and in turn interest rate expectations, which lent support to domestically focused areas of the UK equity market. The decision by the Bank of England to reduce the pace of interest rate hikes also helped these areas recover well from their mid-autumn lows.

More broadly, economically sensitive areas of UK equities outperformed in line with other markets. This occurred amid hopes that the US Federal Reserve might be in a position to 'pivot' to cutting interest rates in late 2023.

European markets: Eurozone shares notched up a strong advance in Q4, outperforming other regions. Gains came from a variety of sectors, notably economically-sensitive areas like energy, financials, industrials and consumer discretionary. More defensive parts of the market such as consumer staples lagged the wider market's advance.

Equity gains were supported by hopes that inflation may be peaking in Europe as well as in the US. Annual inflation (as measured by the harmonised consumer price index) fell to 10.1% in November from 10.6% in October. The European Central Bank (ECB) raised interest rates by 50 basis points (bps) in December, a slower pace than its previous 75 bps hikes. However, ECB President Christine Lagarde warned that the central bank was "not done" with increasing interest rates. The ECB also confirmed plans to stop replacing maturing bonds.

Data showed that the eurozone economy grew by 0.3% quarter-on-quarter in Q3, slowing from 0.8% growth in Q2. Forward-looking indicators continued to point towards contraction although the rate of decline moderated. The composite purchasing managers' index for December was 48.8, up from 47.8 in November. (The PMI indices are based on survey data from companies in the manufacturing and services sectors. A reading below 50 indicates contraction, while above 50 signals expansion.

Japan market: After rising for most of October and November, the Japanese stock market declined in December. Nevertheless, the total return for the fourth quarter remained positive, at 3.3% in yen terms. Having weakened against the US dollar for most of 2022, the yen reversed direction from November, returning to levels last seen in July and August.

During November, most Japanese companies reported quarterly earnings for the July to September period. This proved to be another strong set of results, particularly for larger companies benefiting from yen weakness. The level of confidence among company managements is highlighted by the record level of share buybacks to have been announced so far this fiscal year.

Asian markets: Asia ex Japan equities achieved robust gains in the fourth quarter, with almost all markets in the index ending the period in positive territory. China, Hong Kong and Taiwan all achieved strong growth over the quarter, with share price growth particularly strong in November after US President Joe Biden and Chinese leader Xi Jinping signalled a desire to improve US-China relations at a meeting ahead of the G20 summit in Indonesia.

The recovery in Hong Kong and Chinese share prices continued in December after Beijing loosened its pandemic restrictions that have constrained China's economic growth since early 2020. However, the share price rally didn't continue in Taiwan in December, with ongoing geopolitical tensions, higher US interest rates and lower demand for electronic goods (one of Taiwan's biggest exports), weakening investor sentiment. South Korean shares ended the quarter in positive territory after the country's central bank raised interest rates. However, share prices declined in December die to weaker export data and cooler demand from China.

Emerging markets: Emerging market (EM) equities posted strong returns over Q4, helped by a weaker US dollar. Most of the MSCI EM index's returns were generated in November on optimism that as policy tightening from the Federal Reserve (Fed) slowed, any recession would be shallow, and markets would begin to discount the recovery. Optimism faded somewhat in December, however, when the Fed re-iterated its commitment to fighting inflation. An earlier and more comprehensive than expected relaxation of the dynamic zero Covid policy by the Chinese authorities also boosted sentiment later in the quarter. The MSCI EM Index performed in-line with MSCI World.
The Middle East markets underperformed the EM index as they were impacted by weaker energy prices. Qatar and Saudi Arabia were major laggards.

China outperformed. Investors welcomed the relaxation of Covid regulations, which helped boost optimism regarding an earlier-than-expected re-opening of the economy. Support for the housing sector also added to the positive sentiment. Latin American markets Peru and Colombia outperformed the broader index. South Korea and South Africa posted strong returns with the latter boosted by President Ramaphosa's re-election as the president of the ruling African National Congress (ANC), although allegations of gross misconduct and possible violation of the constitution weighed on returns in December.

Poland and Hungary continued to rebound following months of underperformance as a consequence of the war in neighbouring Ukraine while Greece and Egypt were up too. Turkey was the strongest index market as the central bank continued to loosen monetary policy. Authorities cut interest rates to 9% in November but, in acknowledgement of rising inflation risks, which topped 85% in October, announced an end to the current easing cycle.

Emerging Markets Shares (MSCI Emerging Markets Index, Net AUD)

Emerging market (EM) equities (Unhedged) was down -2.6% in December and down -2.0% on a hedged basis. Over the year EM returned similar performances to the broader index, -14.0% unhedged and -15.2% hedged. In December EM showed a mixed picture with positive performance in Eastern European markets and negative in Latin America. That divergent performance is the mirror image of what was the case during the first months of the year.

EM may at last be emerging from the bear market driven by a rebound in Asian stocks (earnings growth is at 40% below their February 2021 peak cycle). The wakening in the US dollar and China's movement to a more sustainable COVID-management policy shows signs of improved overall earnings outlook for the region.

The index ended trading at a forward P/E Ratio of 11.1x and P/BV of 1.9x and equity yield (dividend) 3.5%.

Australian Listed Property (S&P/ASX 200 A-REIT Accumulation Index)

The S&P/ASX 200 Property Accumulation index returned -4.1% in December, underperforming the S&P/ASX 200, which returned -3.2% but the index retuned +11.5% for the quarter. For the past 12 months, AREITs returned -20.5%, underperforming the broader market, which returned -1.1%.

The Office A-REITs sector was the best performer during December, returning 0.0%, while the industrial sector lagged, declining -8.1%. The best performing stock was Ingenia Communities Group (INA) at +3.5% and Charter Hall Long WALE REIT (CLW) +0.9% while HMC Capital (HMC) was the worst, delivering -18.4%.

At the end of the month the index was trading on a dividend yield of 4.6% with a P/BV 0.9x and a P/E Ratio 7.0x.

International Listed Property (FTSE EPRA/NAREIT Developed ex-Australia Index, AUD)

Globally, REITs unhedged returned -3.8% over the month of December and +4.0% over the quarter. The best performing regions over the month were Hong Kong (+12.0%) followed by Continental Europe (-1.4%) and worst performing region was the US (-5.1%).

At the end of the month the index was trading on a dividend yield of 4.2% with a P/BV 1.4x and a P/E Ratio 15.0x.

Australian Direct Property (Atchison Consultants Unlisted Property Funds Index)

Australian direct property posted 0.0% return over 3-month period to December 2022. Investors should continue to see upward revaluation of the direct property sector. Capitalisation rates across property sectors continued to trend upwards. Cap rates across office, industrial and retail properties ranges are 4.9%, 4.0% and 5.1% respectively.

Australian Fixed Interest (Bloomberg AusBond Composite Bond Index)

Australian fixed interest returned -2.06% over the month and -9.71% for the year. The Australian government 10-year bond yield increased by 53bps (March 2022 futures) to 4.08% over December. At this point, 10-year bond yields were 20bps above US 10-year yields (3.88%). 3-year single A corporate credit spreads tightened from 1.62% at the end of November to 1.56% at the end of December.

International Fixed Interest (Barclays Global Aggregate TR Bond Index, Hedged to AUD)

International fixed interest returned -1.32% over the month (in AUD), +0.67% over the quarter and -12.3% for the year. The 10-year US government bond yield increased by 28bps to 3.88% over December and by 7bps over the quarter.

Atchison

Atchison Consultants
Level 4, 125 Flinders Lane,
Melbourne Vic 3000

P: +61 (0) 3 9642 3835
enquiries@atchison.com.au
www.atchison.com.au

ABN: 58 097 703 047
AFSL Number: 230846

To obtain further information,
please contact:

Jake Jodlowski
Principal
P: +61 3 9642 3835

E: jake.jodlowski@atchison.com.au