DRUMMOND

CAPITAL PARTNERS

INVESTMENT PERSPECTIVES

September 2023

Month In Review

Global Equities
- 3.5%

Aus Equities
- 2.8%

Aus REITs
- 7.8%

AUD/USD
-0.4%

US Bonds
- 2.2%

Commodities
+ 4.1%

September lived up to its reputation as being a seasonally weak period for share markets with Global equities (MSCI ACWI Index) falling -3.5%. Australian equities (ASX200) also softened, down -2.8%, as rising bond yields put pressure on global risk sentiment and share market valuations. Emerging markets were also weaker, down -2.6%, as investor trepidation over Chinese's economic woes continued.

US Bond markets lost ground, falling -2.2% as did US investment grade credit, dropping -3.6% (given its long duration profile) as yields pushed higher. Conversely, commodity markets were up +4.1% which was driven in large part by sharply rising energy prices off the back of Saudi & Russian production cuts. The AUD fell -0.4% against the USD.

From their July highs, global and Australian shares have now fallen about 6% due to central bank rhetoric reinforcing a 'higher for longer' backdrop given a more resilient than expected US economy this year. In addition, concern is growing over the rapid rise in US fiscal spending, worsening the US government deficit outlook. As a result, bond yields globally rose significantly (bond prices fell) in September, pressuring markets.

This has seen the equity risk premium compress to multi-decade lows, suggesting that stocks continue to look relatively unattractive when compared to bonds. Recent strength in energy prices, faltering Chinese growth and the risk of a US government shutdown all added to investor trepidation over the month at a time of already stretched valuations.

Things That Matter

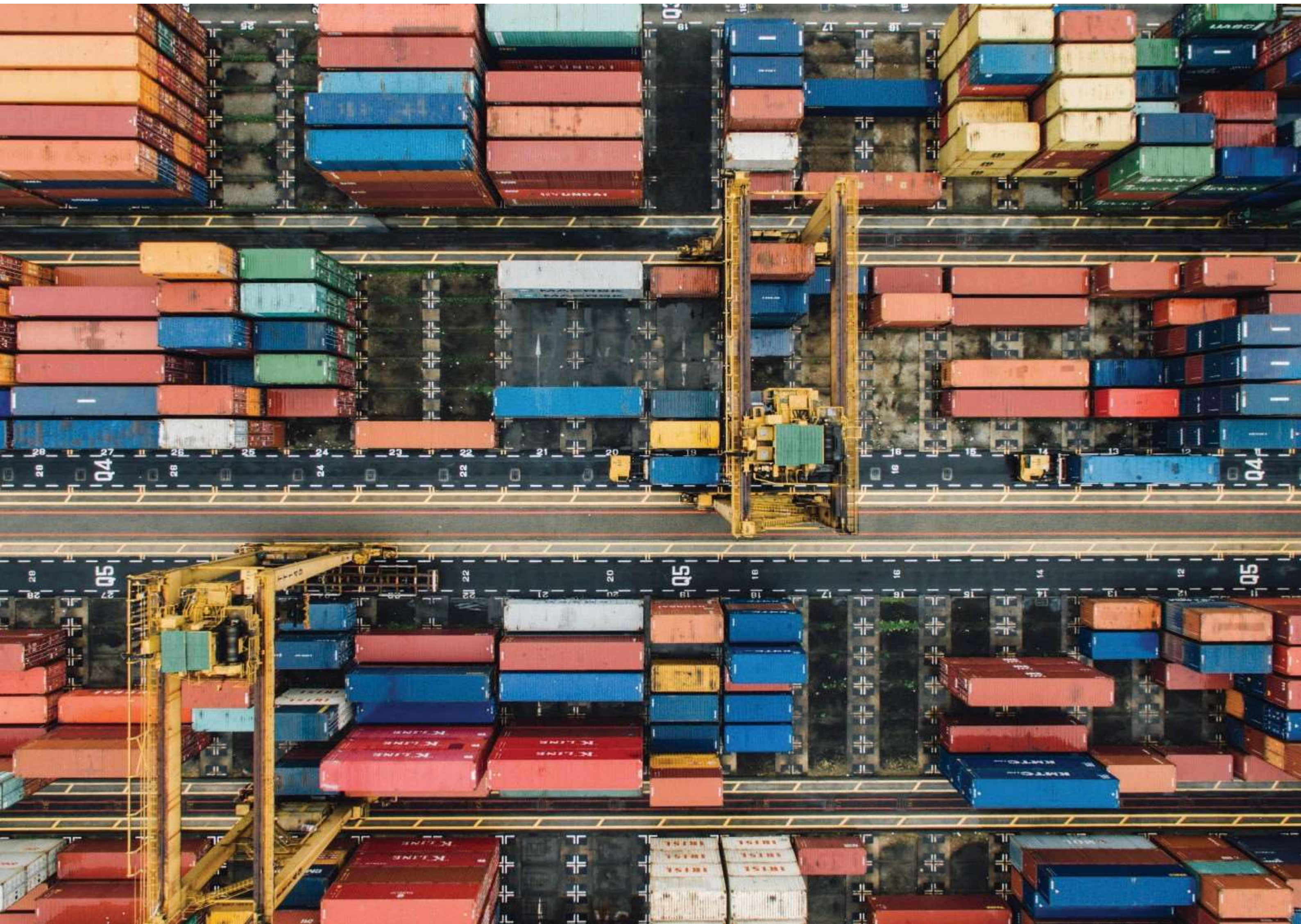
1.	Most global central banks have aggressively tightened monetary policy in response to high inflation and there is now an expectation that we are close to peak rates.
2.	Inflation is looking to have established a disinflationary trend but the process of getting inflation to central bank targets still has a way to go.
3.	Equity market and bond valuations have improved but equity valuations will be further challenged in the period ahead if inflation proves to be sticky or if there is a recession.
4.	China's growth initially picked up in response to the end of zero-Covid and easing regulatory pressures. However, growth has since faltered, with the property sector being a notable drag on outcomes.
5.	Geopolitical tensions are elevated across many regions and may contribute to elevated volatility in the years ahead.

Asset Class Positioning

Change Over Month	**Change**	**Strong Underweight**	**Underweight**	**Neutral**	**Overweight**	**Strong Overweight**
Australian Equities	▲	○	○	●	○	○
Global Equities	▬	○	●	○	○	○
Property	▬	○	○	●	○	○
Infrastructure	▬	○	○	○	●	○
Global Alpha	▼	○	●	○	○	○
Government Bonds	▼	○	●	○	○	○
Corporate Debt	▲	○	○	○	●	○
Cash	▼	○	○	○	●	○
Total Growth vs Defensive	▼	○	●	○	○	○

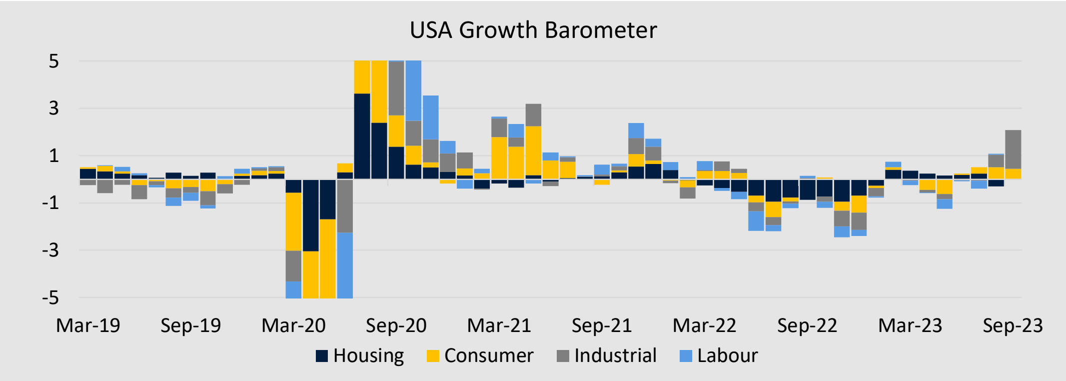
Macroeconomic Overview

North America	▲
Asia	▼
Europe	▼
Australia	▼



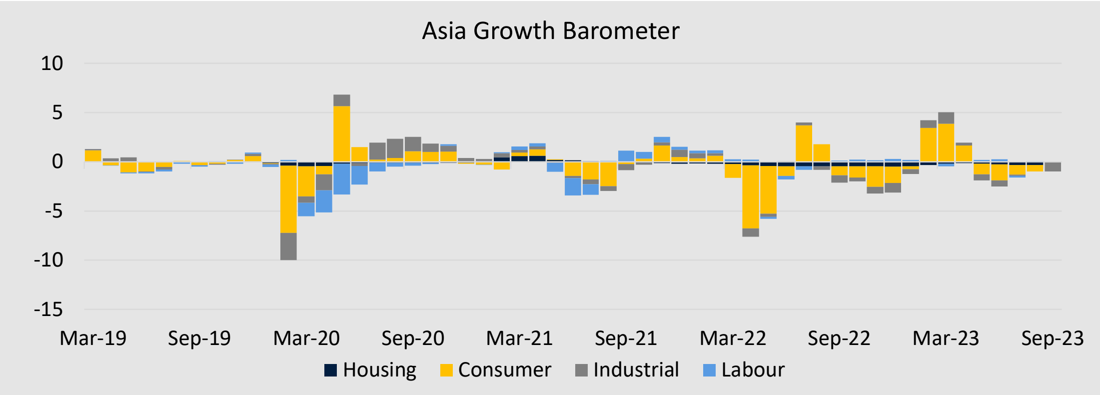
North America

US growth has ticked up so far this year, but we expect growth to moderate in the year ahead reflecting higher for longer interest rates. We also expect credit conditions to deteriorate given the problems in the banking sector (where deposits continue to fall). Whilst core inflation is now looking more likely to have established a downward trend, we still think the tightening to date is sufficient to cause a recession and we don't see the Fed as anywhere close to rate cuts (unless we do get a recession). We are closely watching labor cost growth and whether it can materially soften without a lift higher in unemployment.



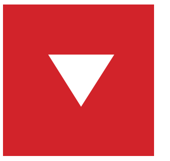
Asia

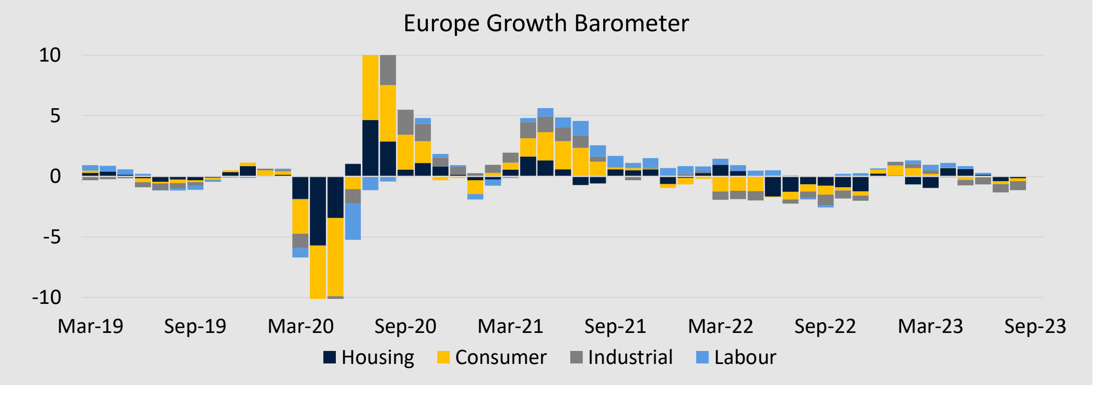
Growth in China had been recovering following the Government's abandonment of its zero-Covid policies as well as an easing in regulatory pressures. However, this has now lost steam as China data continues to disappoint, with the property sector again dragging on outcomes, despite the Government relaxing many of its regulatory restrictions on the sector. Manufacturing PMIs have also been falling. Going forward, we expect the renewed stimulus from the Government and PBOC to be modest, meaning prospects for significant equity market outperformance are limited.



Europe

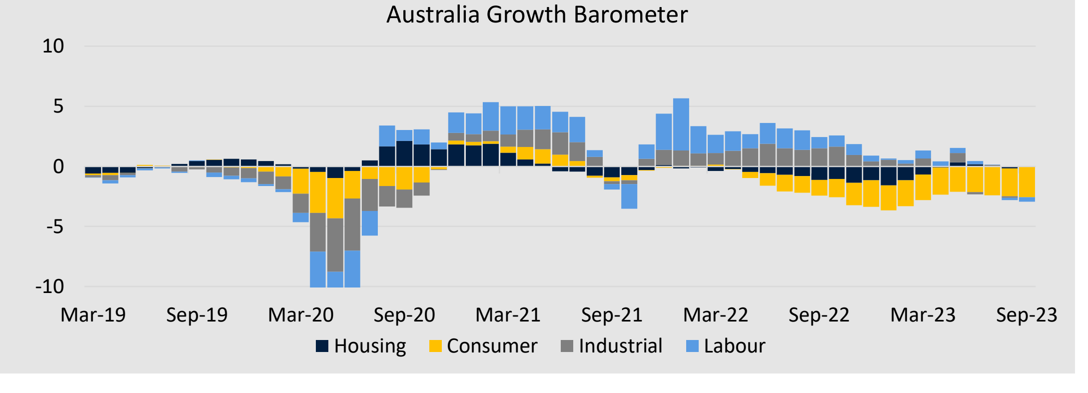
The ECB looks to have completed its rate hiking cycle as macro data has softened. European banks have also rapidly pulled back on business lending which poses risks for a broader credit crunch in the Eurozone. The Bloc still faces significant challenges from Russia's invasion of Ukraine which is weighing on business sentiment. Interest rates are significantly higher than anyone thought possible two years ago and funding costs for heavily indebted governments could become a concern for financial stability.





Australia

The Australian economy is still experiencing below trend growth and consumers are at GFC levels of pain as rate hikes are starting to bite. After a period of softening, house prices have stabilised. A rush in demand due to high levels of immigration and limited supply appear to be offsetting the negative impact of higher interest rates on house prices. Further softness in house prices does, however, remain a risk as interest rate rises continue to weigh.



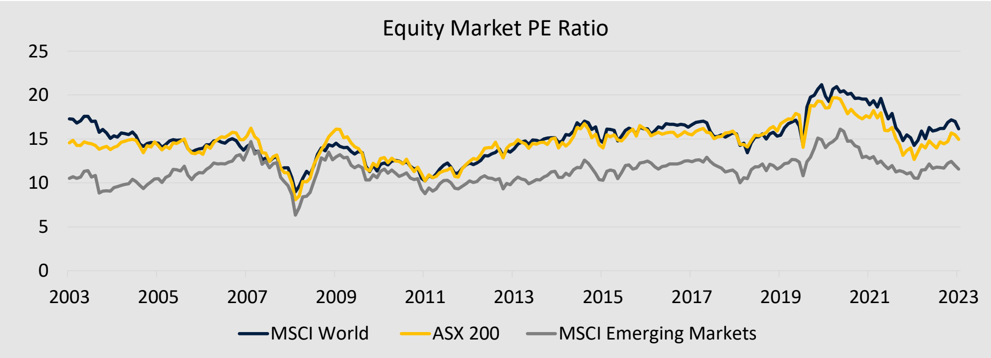
Asset Class Overview

Equities	Underweight
Bonds	Underweight
Credit	Overweight
Infrastructure	Overweight
Property	Neutral
Global Alpha	Underweight

Equities

Global equities performed well for the calendar year (driven by large cap tech companies) to the end of July. However, they have since faltered as the market narrative has shifted to 'higher for longer' with regards to central bank policy settings. With central banks having aggressively tightened monetary policy, peak growth behind us, rich valuations and the narrow market leadership, the outlook for equities remains lackluster. Given this, we are underweight global equity exposure.

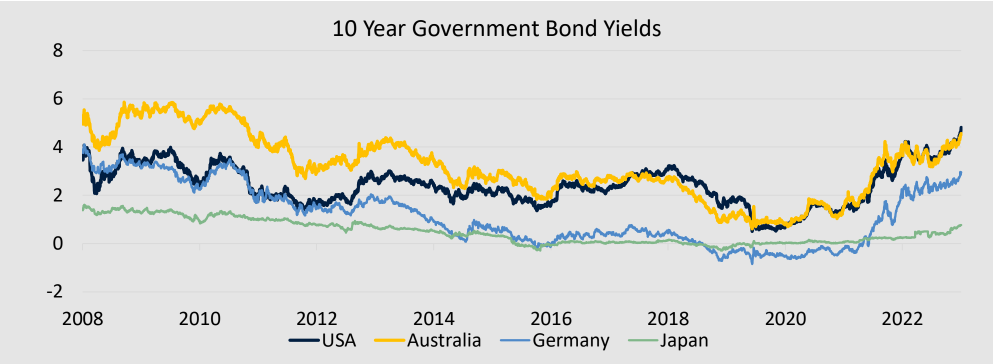
Underweight



Bonds

We have recently reduced our exposure to global bonds as the sell-off in yields looks set to continue with yields reaching highs last seen in 2007, led by 'real yields' (adjusted for inflation expectations). We will look to close this underweight position once we get closer to a recession or when valuations support a better entry point. We have maintained a neutral exposure to Australian government bonds which have less sovereign risk vis a vis global bonds (most notably, US).

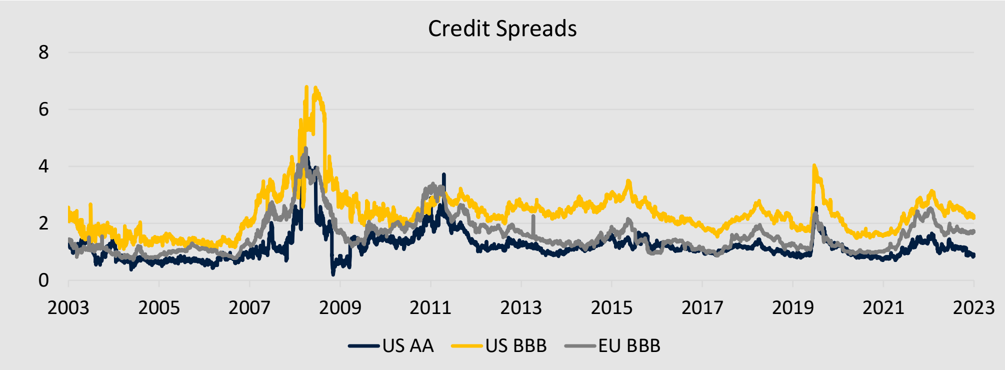
Underweight



Credit

Global credit spreads have widened a little in line with the global macro concerns over recent months. However, despite the risk of an uncertain economic backdrop, we think higher quality, floating rate credit is attractive. As such, we have continued to build exposure to this sector which has taken our overall credit exposure to overweight, noting the quality of credit within the asset class is very high. Overall, we remain defensively positioned with a focus on diversification, liquidity, and higher quality credit.

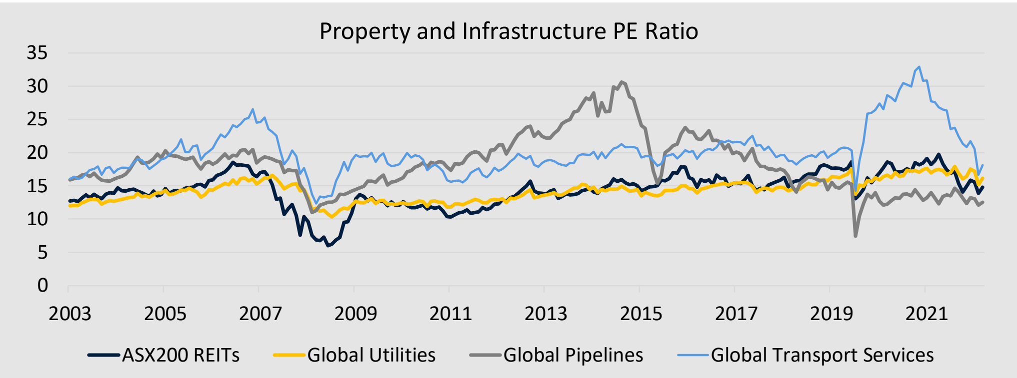
Overweight



Property / Infrastructure

Commercial real estate exposure in the loan books of US regional banks is an issue to closely monitor as valuations are stressed and banks are shoring up their balance sheets. We favor the more defensive qualities of infrastructure assets in this backdrop.

Neutral



Global Alpha

An over or underweight allocation to this asset class will remain manager and strategy type specific. At the moment, the underweight largely reflects attractive opportunities in higher grade credit.

Underweight

Asset Class Returns

	Latest Value 30/09/23	Weekly Performance	Monthly Performance	Quarterly Performance	Yearly Performance
MSCI World All Countries	797	-2.3%	-3.5%	-2.4%	20%
S&P/ASX 200	7,049	-1.6%	-2.8%	-0.8%	13%
MSCI Emerging Markets	953	-1.8%	-2.6%	-2.8%	12%
Nasdaq Composite	13,219	-1.8%	-5.8%	-3.9%	26%
Euro Stoxx	441	-2.6%	-3.1%	-4.1%	25%
Australian Property	74.4	-3.1%	-7.8%	-2.8%	13%
Global Infrastructure	59	-5.9%	-5.4%	-5.4%	-3%
Australian Bonds	4.49%	-1.0%	-2.0%	-0.7%	0%
US Bonds	4.57%	-0.9%	-2.2%	-2.9%	-1%
High Yield Credit (spread/return)	2.2%	-0.9%	-1.6%	-0.3%	9%
Investment Grade Credit (spread/return)	0.9%	-2.2%	-3.6%	-4.7%	4%
US $ / Australian $	0.65	0.1%	-0.4%	-2.6%	-1%
Crude Oil-WTI	90.8	1.8%	8.6%	28.5%	14%
Gold Bullion Lbm $/T Oz	1,857	-4.6%	-4.4%	-3.1%	11%