DRUMMOND

CAPITAL PARTNERS

INVESTMENT PERSPECTIVES

October 2023

Month In Review

Global Equities
- 2.7%

Aus Equities
- 3.8%

Aus REITs
- 6.7%

AUD/USD
-1.7%

US Bonds
- 1.2%

Commodities
-4.2%

October was another weak month for global markets as rising bond yields and geopolitical tensions in the Middle East pressured valuations. In fact, except for cash and gold, all key asset classes lost ground for the month. October also marked the third consecutive monthly decline for both shares and bonds. Global equities (MSCI ACWI Index) fell -2.7% as risk sentiment soured whilst and Australian equities (ASX200) also fell -3.8%. Emerging markets were also weaker, down -3.9% for the month, as investor trepidation over China's economic woes lingered.

The rise in bond yields during October resulted in a -2.0% loss for Australian Bonds and a -1.2% loss for US Bonds. The rise in yields, as well as a widening in credit spreads, similarly resulted in losses for both investment grade credit (-2.4%) and high yield (-1.0%) credit. The broad commodity market was also weaker over the month, down -4.2%, despite the gold price rallying by a hefty 7.5%. During October, oil prices decreased from their year-to-date peak in late September, with WTI finishing the month down by -10.1% as concerns about future demand outweighed any 'war' bid emanating from rising tensions in the Middle East. The AUD fell -1.7% against the USD as a slew of fresh economic data demonstrated the strength of the US economy.

Geopolitical risks came firmly back on the radar following the attack on Israel by Hamas on October 7th. As we wait to see if the expected major ground invasion leads to a deeper regional conflict, we are cognisant of how the collective market historically has moved past geopolitical incidents, albeit we are acutely aware of the escalation risks and how a wider conflict could impact energy prices, inflation and global growth. We continue to monitor the situation closely.

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 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.	The war in the Middle East is a stark reminder that Geopolitical tensions are heightened across the globe 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	–	○	●	○	○	○

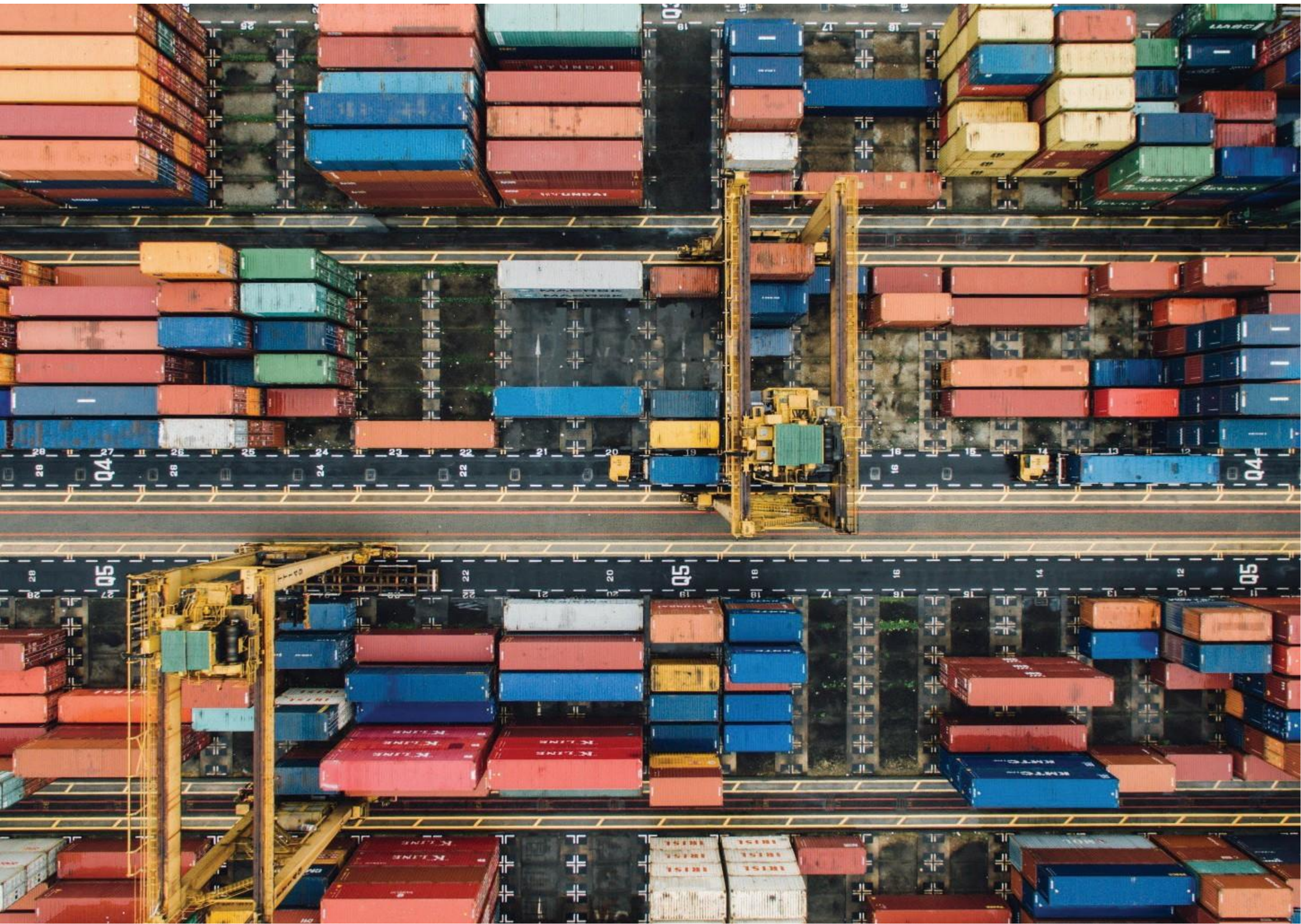
Macroeconomic Overview

North America ▲

Asia ▼

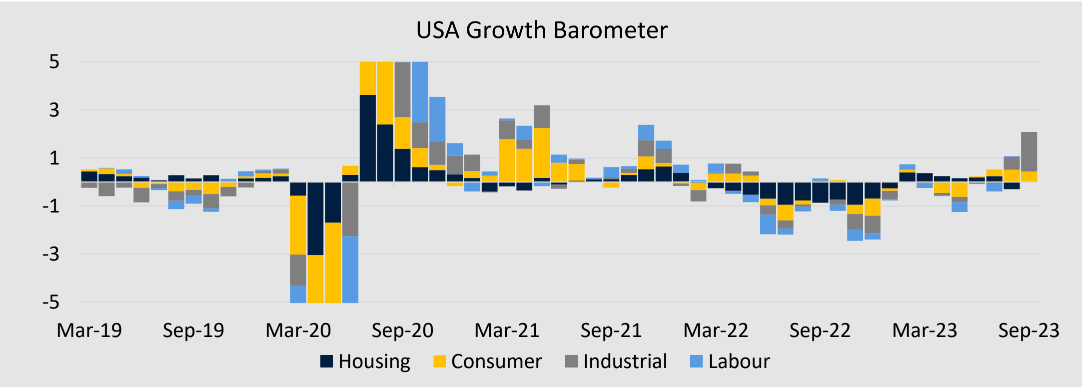
Europe ▼

Australia ▼



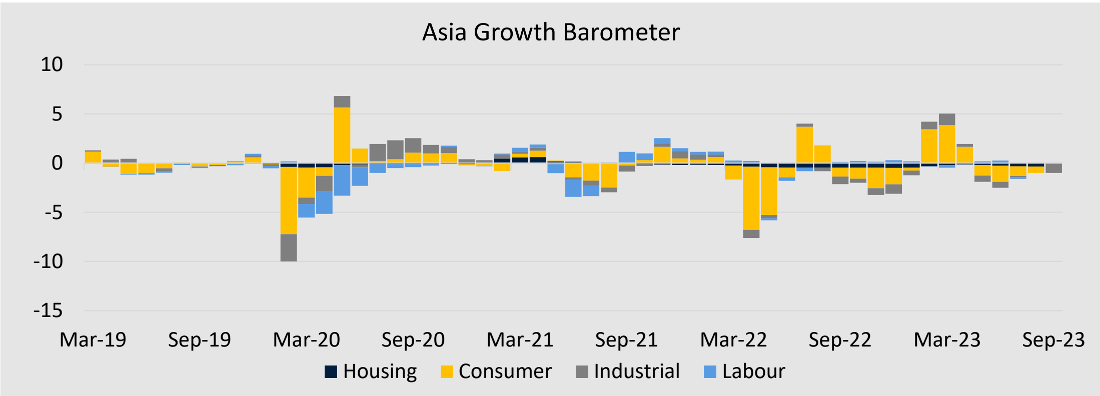
North America

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 mild recession and we don't see the Fed as anywhere close to rate cuts (unless we do get a large recession). We are closely watching labour cost growth and whether it can materially soften without a lift higher in unemployment.



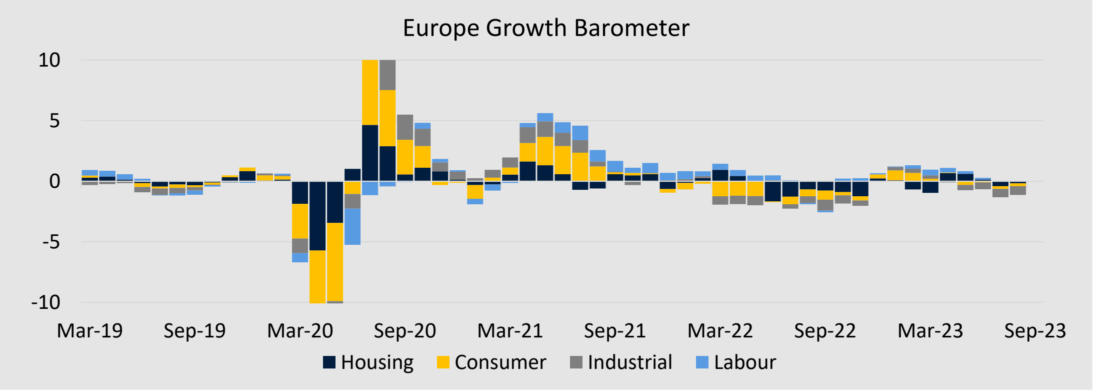
Asia

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. China recently surprised markets after they issued an additional 1 trillion-yuan central government bond which could suggest the government is taking steps to support the economy. We will continue to monitor how any policy support may develop and what implications that may have for equity market performance.



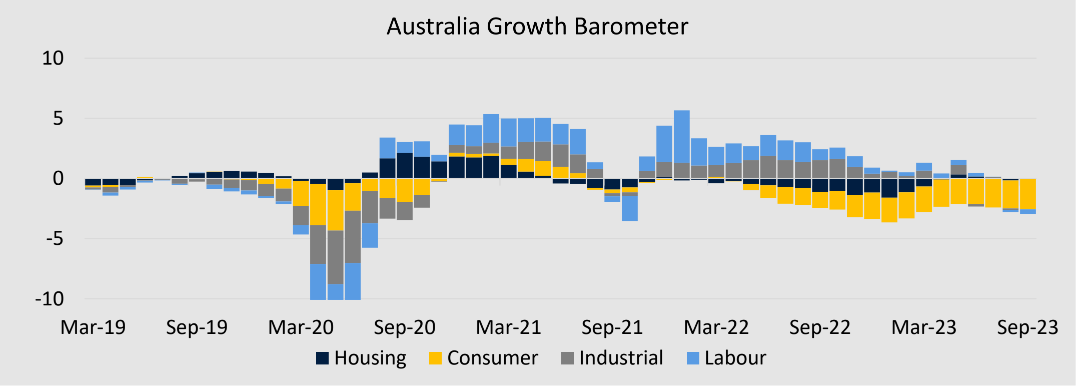
Europe

The ECB is still tightening monetary policy in response to high inflation but does appear close to a pause 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.



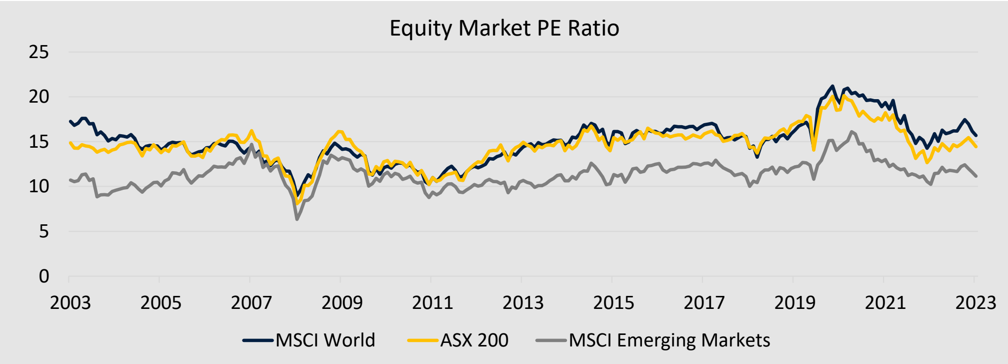
Asset Class Overview

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

Equities

Underweight

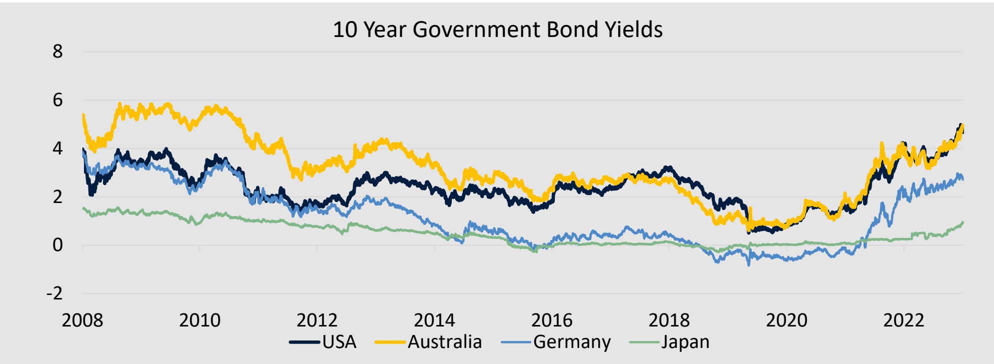
Global equities performed well for the calendar year (driven by large cap tech companies) to the end of July. However, equities have since faltered as the market narrative has shifted to 'higher for longer' with regards to central bank policy settings. With central banks having aggressively tightened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



Bonds

Underweight

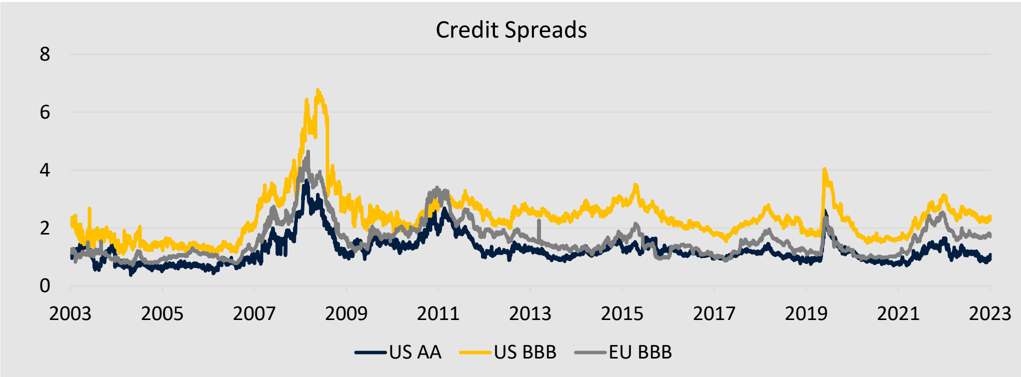
We reduced our exposure to global bonds over recent months as the sell-off in bond yields appeared set to continue with yields reaching highs last seen in 2007. This is being led by 'real yields' pushing higher, likely mainly reflecting high debt issuance and a still strong US economy. We will look to 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.



Credit

Overweight

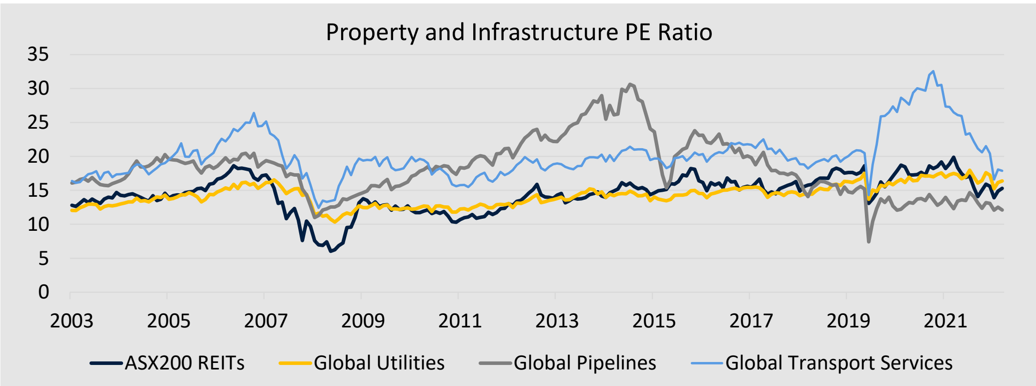
Global credit spreads have widened a little in line with the global macro concerns over recent months, however they still do not reflect the risk of an uncertain economic backdrop and hence we remain cautiously positioned. However, we believe the current yields available on Australian investment grade corporate debt (IG) are attractive vs cash and government bonds and we have continued to build exposure to this sector which has taken our overall Credit exposure to 'overweight'. Overall, we remain defensively positioned with a focus on quality.



Property / Infrastructure

Neutral

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 favour the more defensive qualities of infrastructure assets in this backdrop.



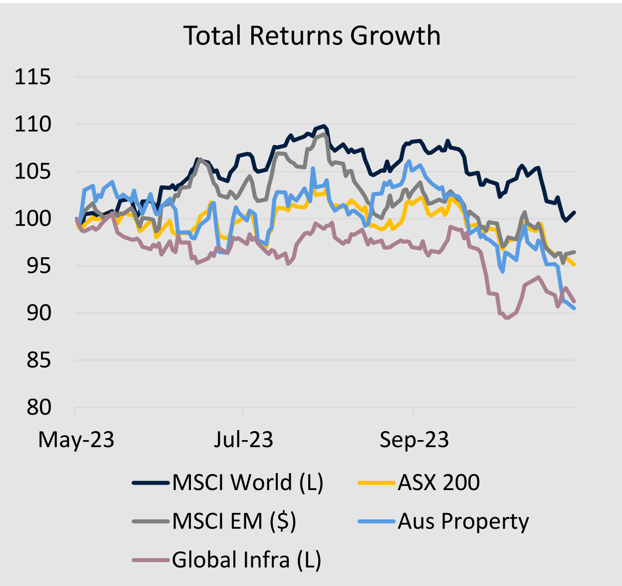
Global Alpha

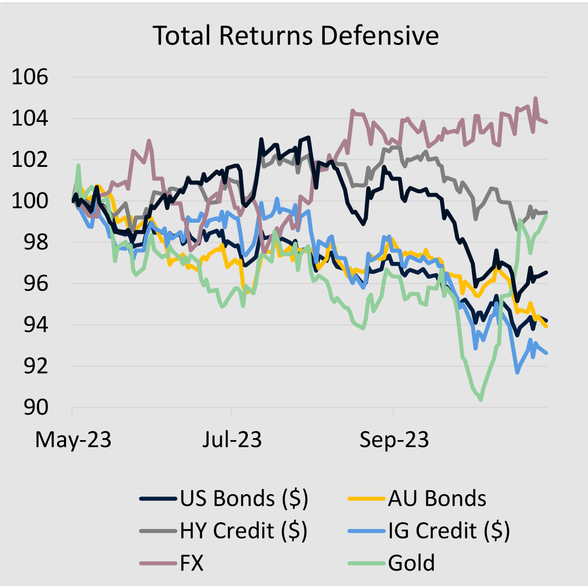
Underweight

We have progressively switched our 'Global Alpha' allocation into defensive IG credit this year as yields now offer more than 6% for a fraction of the fee. An over or underweight allocation to this asset class will remain manager and strategy type specific.

Asset Class Returns

	Latest Value 31/10/23	Weekly Performance	Monthly Performance	Quarterly Performance	Yearly Performance
MSCI World All Countries	774	-0.6%	-2.7%	-8.0%	10%
S&P/ASX 200	6,781	-1.7%	-3.8%	-7.2%	3%
MSCI Emerging Markets	915	-1.1%	-3.9%	-12.1%	11%
Nasdaq Composite	12,851	-1.0%	-2.8%	-10.2%	18%
Euro Stoxx	426	1.0%	-3.3%	-9.2%	12%
Australian Property	69.1	-4.1%	-6.7%	-11.8%	-4%
Global Infrastructure	58	-0.4%	-0.1%	-6.6%	-6%
Australian Bonds	4.94%	-0.6%	-2.0%	-3.5%	-2%
US Bonds	4.91%	0.2%	-1.2%	-3.7%	0%
High Yield Credit (spread/return)	2.3%	0.9%	-1.0%	-2.5%	5%
Investment Grade Credit (spread/return)	0.9%	0.5%	-2.4%	-7.0%	2%
US $ / Australian $	0.63	0.5%	-1.7%	-5.0%	-1%
Crude Oil-WTI	81.6	-7.3%	-10.1%	-0.2%	-6%
Gold Bullion Lbm $/T Oz	1,996	0.1%	7.5%	1.4%	22%





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