D R U M M O N D

CAPITAL PARTNERS

INVESTMENT PERSPECTIVES

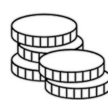
January 2024

Month In Review

Global Equities
1.3%

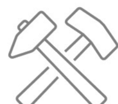
Aus Equities
1.2%

Aus REITs
0.2%



AUD/USD
-3.9%

US Bonds
-0.8%



Commodities
4.5%

Major equity market indices continued their rally into the first month of 2024 (albeit at a more modest pace) with Global equities (MSCI ACWI Index) up 1.3%. Growth stocks (aka 'Magnificent 7') lifted the market higher as we witnessed a return to much of 2023's narrow market leadership. The S&P 500 and Nasdaq also reached new all-time highs. With market concentration and valuations so high today, there is a lot hanging on the ability of today's winners to deliver exceptional earnings results. And it would appear some cracks are emerging.

Australian equities (ASX200) also pushed higher, gaining 1.2% and closed the month at a new record high. Our local bourse was boosted by slowing inflation data and expectations for the RBA's monetary easing. Energy was the best performing sector (+5.2%) off the back of a strong rise in oil prices. Large-caps outperformed small-caps, continuing the trend seen in 2023. Emerging markets once again proved to be lackluster as woes in China's property sector weighed on their services sectors and ultimately their share market. In January, the Chinese Government announced further stimulus and policy announcements providing support for the property sector. However, it has been limited relative to previous easing cycles.

During their January meeting, the Fed walked back on delivering near term rate cuts which may ultimately see some reversal of the ferocious rally seen in bond markets in November and December of 2023. Overall, bond markets were relatively muted over January with US bonds down -0.8% and Australian bonds up 0.1%. Credit markets also proved to be relatively benign for the period.

The broad commodity market rallied over January, up 4.5%, as the oil price booked its first monthly gain since September as Middle East tensions rose. The AUD reversed the trend of the two prior months and weakened -3.9% vs the USD as the market started to push out US rate cut expectations.

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 rates will be cut throughout 2024.
2.	Inflation is looking to have established a disinflationary trend, but the process of inflation normalisation still has some way to go.
3.	Equity market and bond valuations will be 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

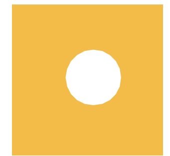
Asia

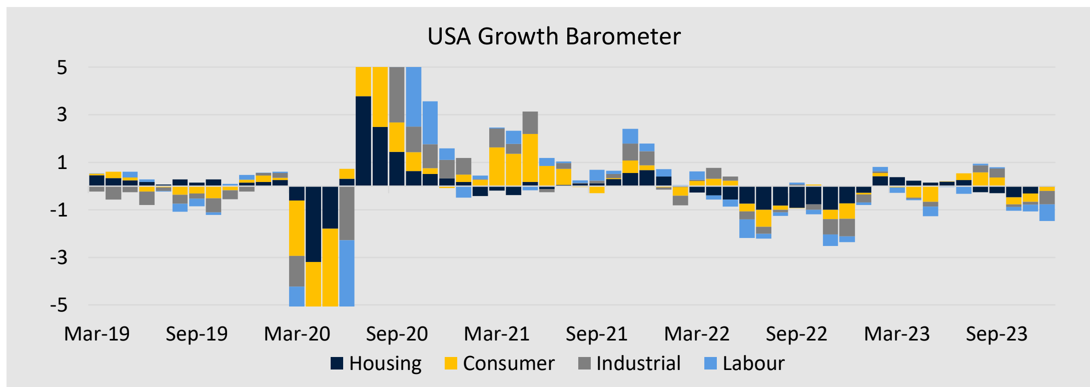
Europe

Australia

North America

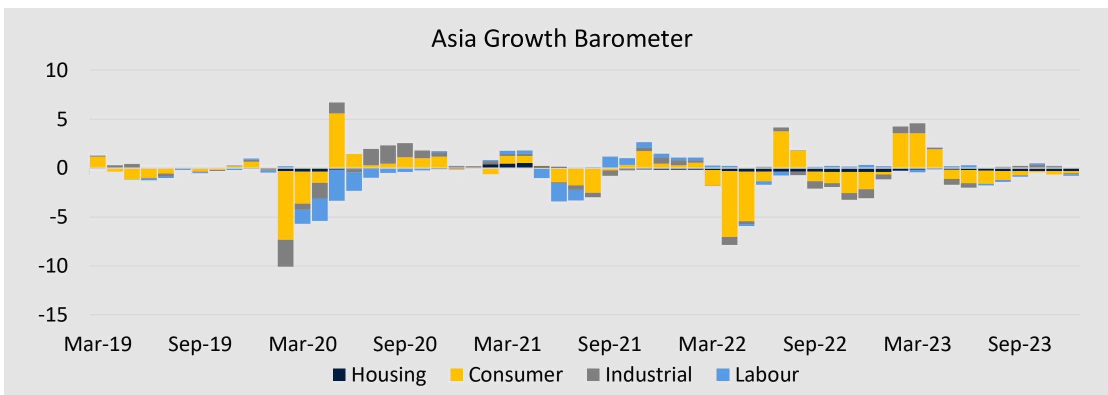
The United States economy remained resilient throughout 2023 and technology companies rallied strongly on AI positivity, supporting global equity markets through the year. However, other than the fact that there hasn't been a formal recession in the US yet, there hasn't been a whole lot of evidence to suggest that it is no longer at least probable. Monetary policy works with lags, and the brunt of its impact should be felt in the US in the first half of this year. Indeed, the unemployment rate is generally trending higher in the US and whilst core inflation has moderated from the peak, further falls from here will be hard to generate with growth strong.





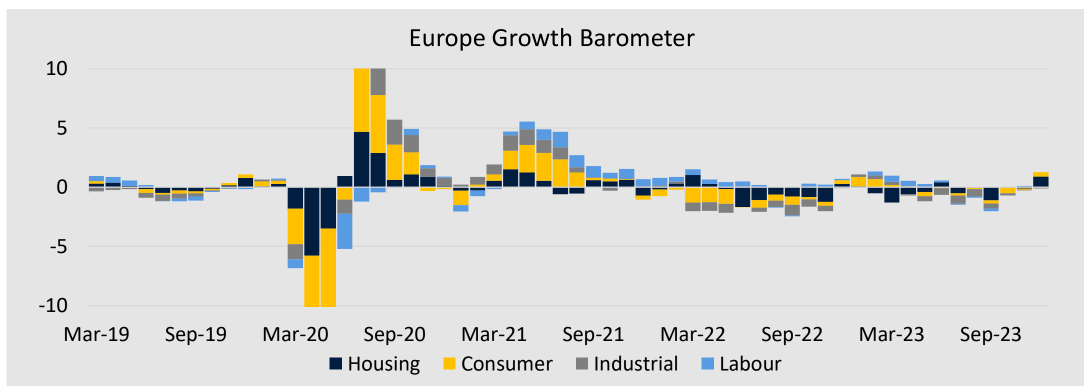
Asia

China's economy has been showing signs of recovery following piecemeal stimulus throughout 2023. However, equity markets have yet to respond, with the property market still languishing. We think the most likely outcome is continued modest stimulus, aiming to support growth around the current sluggish pace. This balances the risk of an outright crash in the property market with building systemic risks in an over-leveraged economy. This isn't a recipe for equity market outperformance, but should the Government ramp up stimulus, a temporary allocation to China may be warranted.



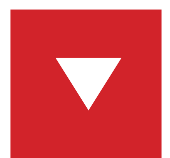
Europe

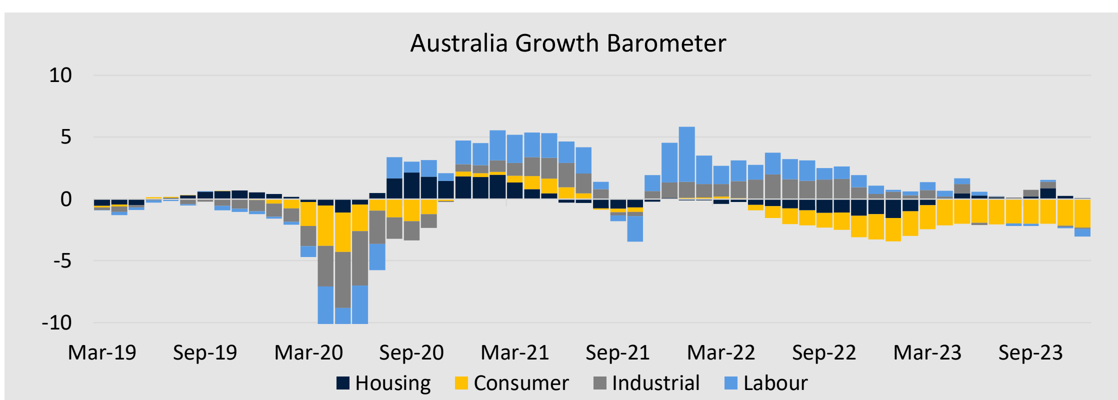
Europe's economy has struggled to regain momentum following the pandemic, constrained by high inflation and an aggressive interest rate hiking cycle. Indeed, the Eurozone only avoided ending 2023 in a recession by a very narrow margin. Moreover, European banks have rapidly pulled back on business lending 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 and has kept natural gas prices high. Interest rates are significantly higher than anyone thought possible two years ago as are funding costs for heavily indebted governments. Overall, we expect the Eurozone economy to continue to remain under pressure as the effects of past monetary tightening continue to work through the economy.



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, national house prices rose around 8% in 2023. A rush in demand due to high levels of immigration and limited supply offset 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.





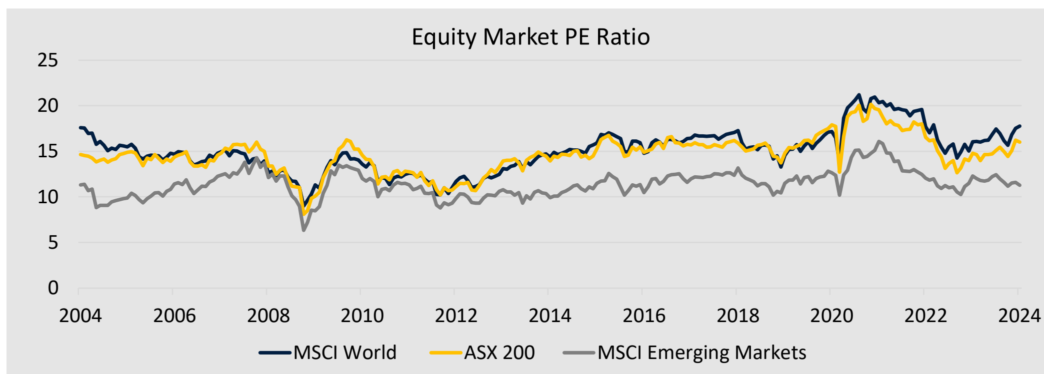
Asset Class Overview

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

Equities

Underweight

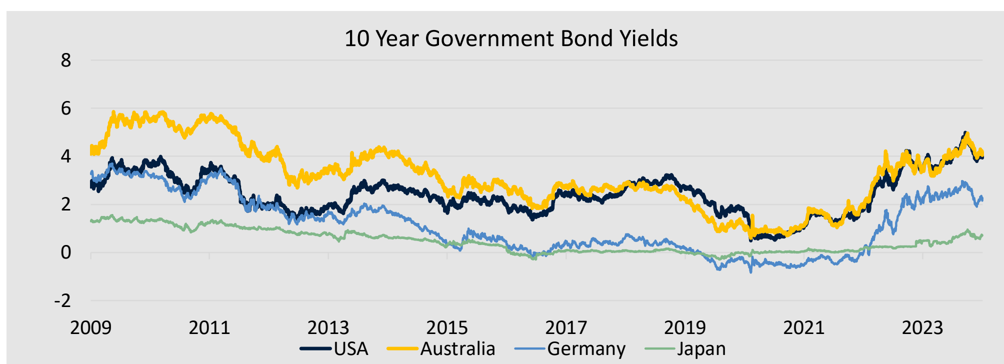
Global equities performed well for the 2023 calendar year and are now pricing in the so-called Goldilocks scenario. However, the recent rally increases the risk of disappointment in the near term, either because markets shift as growth weakens, or that yields spike higher if economic growth stays robust. If anything, the recent rally has stimulated the economy and decreased the need for the Fed to ease monetary policy. Given growth has been solid it's not much of a surprise that at their January meeting the Fed walked back on delivering near term rate cuts. Going too early with easing interest rates has been a central bank mistake they are at pains to avoid. This puts the market in a tricky predicament. Indeed, January has seen some reversal in this trend as markets couldn't square more rate cuts with solid economic conditions and easier financial conditions. Given this uncertainty, we remain modestly underweight global equities.



Bonds

Underweight

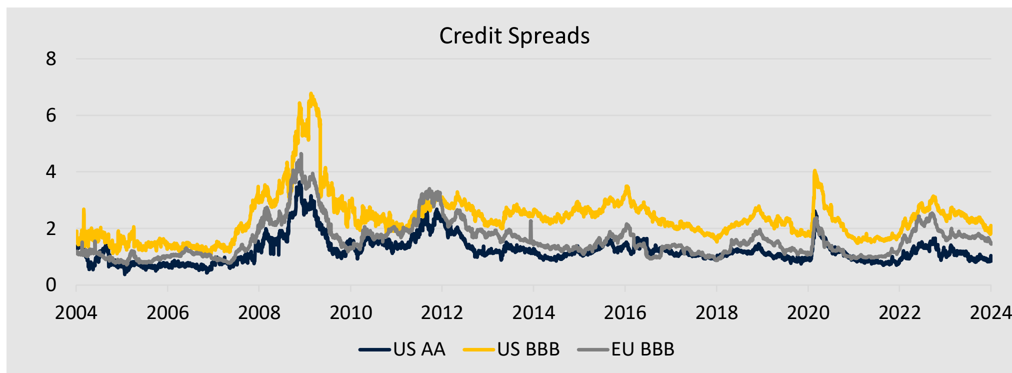
We reduced our exposure to global bonds early in Q3 2023 as the sell-off in bond yields appeared set to continue with yields reaching highs last seen in 2007. This was led by 'real yields' pushing higher, likely mainly reflecting high debt issuance and a still strong US economy. More recently, government bonds have rallied strongly as the market decided that the Fed had won the war on inflation and will start cutting interest rates in the first half of 2024. We have maintained a neutral exposure to Australian government bonds which have less sovereign risk vis a vis global. Given core inflation in the US remains sticky and the deficit has no sign of abating, we remain cautious on global government bonds and remain underweight duration across our portfolios.



Credit

Global credit spreads ended 2023 at the tightest levels of the year whilst delinquencies and defaults are edging higher (albeit off a low base). We do view the current valuations as unreflective of the still uncertain economic backdrop and hence we remain cautiously positioned. However, we do believe the current yields available on Australian investment grade corporate debt are attractive versus cash and government bonds and we have continued to build exposure to this sector. Overall, we remain defensively positioned with a focus on quality.

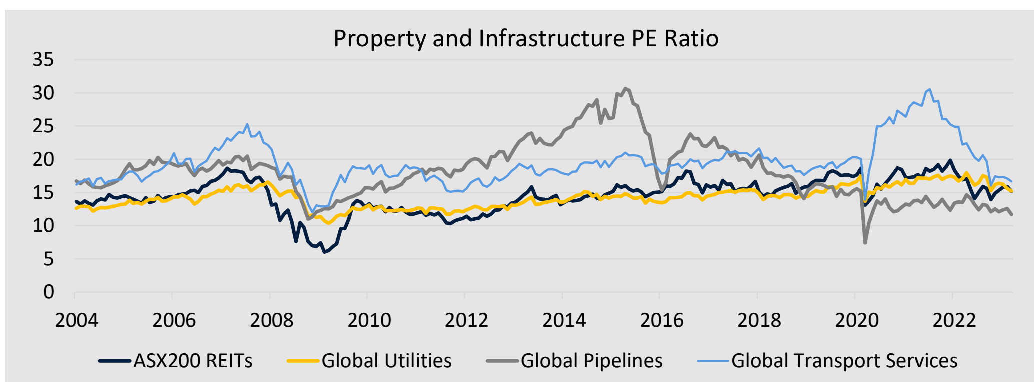
Overweight



Property / Infrastructure

We continue to favour the defensive qualities of infrastructure assets in this backdrop. Additionally, given the risk of rate hikes and higher inflation have dissipated recently, we added exposure to our existing property manager, Quay Global Real Estate, which was one of the asset classes most negatively affected by these trends since the rate hiking cycle began in 2022.

Overweight



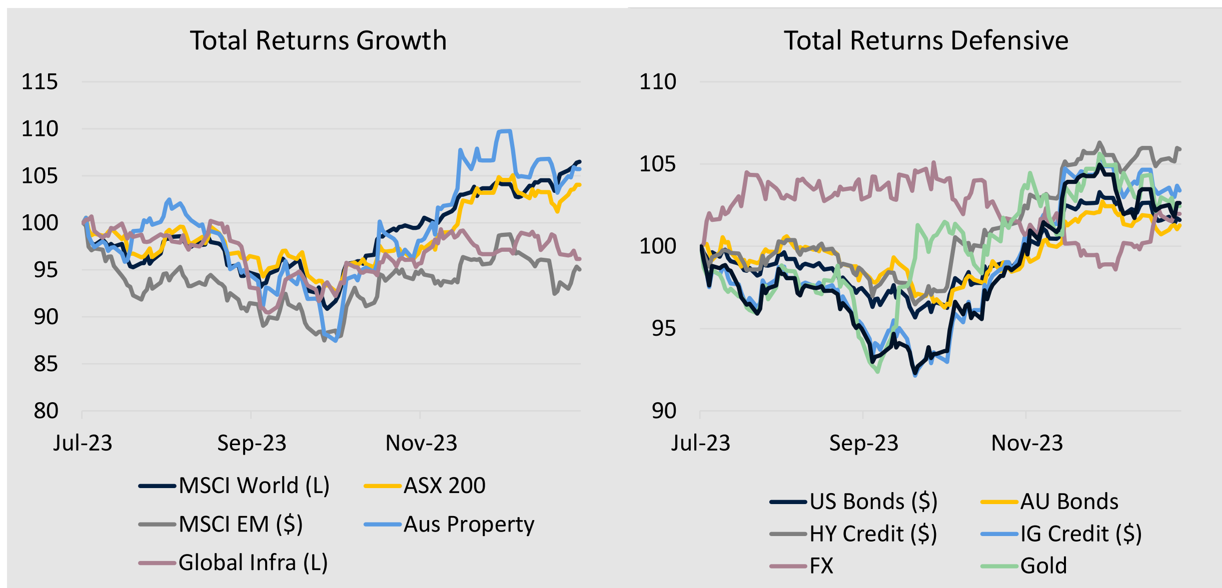
Global Alpha

We have progressively switched our 'Global Alpha' allocation into high quality Investment Grade credit throughout 2023 as we can attain a 6.5-7% running yield for a fraction of the fee. An over or underweight allocation to Global Alpha remains manager and strategy type specific.

Underweight

Asset Class Returns

	Latest Value 31/01/24	Weekly Performance	Monthly Performance	Quarterly Performance	Yearly Performance
MSCI World All Countries	879	0.5%	1.3%	14.0%	16.2%
S&P/ASX 200	7,681	2.7%	1.2%	14.0%	7.1%
MSCI Emerging Markets	976	1.2%	-4.6%	7.1%	-2.5%
Nasdaq Composite	15,164	-1.3%	1.0%	18.2%	32.0%
Euro Stoxx	483	2.9%	2.0%	13.8%	11.4%
Australian Property	85.3	4.7%	0.2%	24.7%	9.0%
Global Infrastructure	62	1.5%	1.0%	6.2%	3.8%
Australian Bonds	4.05%	1.5%	0.1%	6.2%	1.2%
US Bonds	3.95%	0.4%	-0.8%	6.1%	1.7%
High Yield Credit (spread/return)	1.9%	0.3%	0.1%	8.4%	7.7%
Investment Grade Credit (spread/return)	0.9%	0.8%	-0.4%	12.3%	3.6%
US $ / Australian $	0.66	-0.3%	-3.9%	3.6%	-6.6%
Crude Oil-WTI	76.3	1.4%	6.1%	-6.5%	-3.3%
Gold Bullion Lbm $/T Oz	2,048	1.3%	-0.8%	2.6%	6.2%



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