WHITEHELM ADVISERS

MONTHLY UPDATE ON THE INVESTMENT ENVIRONMENT

February 2021

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surprisingly straightforward

MARKET UPDATE

February saw a continuation of January's broadly positive economic tone both locally and overseas, albeit with a bond market sell-off at month-end reflecting rising concerns about a surge in inflation due to unprecedented pandemic-era stimulus in tandem with a potentially stronger than expected post vaccine economic recovery.

With vaccination programmes ongoing throughout the world, the worst of the COVID-19 pandemic appears to have passed, with new daily cases on a downward trajectory globally. Nonetheless, the pandemic remains far from over; there are over 20 million confirmed active cases currently, and the death toll now exceeds 2.6 million.

It was a positive month for equities in developed markets, however the February's returns masked a significant sell-off in both fixed interest and equities markets in the latter half of the month. With strong economic data and no signs of an abatement in stimulus, expectations of higher longer-term inflation as well as real rates saw bond yields spike toward the end of the month. The yield on 10-year US Treasury yields rose to 1.6% by early March; well above the 0.9% yield at the start of 2021, with Australian bonds experiencing a similar spike among longer-dated tenors. While sovereign bonds and equities tend to be negatively correlated, especially in times of market dislocation, the expectation of potential rate tightening by central banks in coming years had a negative impact on some equity market sectors, especially some technology stocks, which rely on ultra-low borrowing costs to fund growth.

Australia's GDP print soared 3.1% over the final quarter of 2020, well ahead of market forecasts. Household consumption, which accounts for around 60% of the national economy, improved 4.3% over three months as rising optimism saw household savings fall and spending rise. Home building and business investment also provided a tailwind for the economy, as did a surge in commodities prices, particularly iron ore amid strong Chinese demand. Australia's GDP growth rate for 2020 was -1.1%; while negative, an exceptional result among developed nations.

The nation's housing sector also benefitted from the economic recovery and generous policy settings, leading house prices to rise in February at their fastest monthly pace since early 2003. Housing finance approvals have also soared, with the January increase of 8.7% by value taking the annual rate to 39%. Employment data was also positive, with the jobless rate declining to 6.4%.

Despite the uptick in economic sentiment and potential early signs of an overheating housing market, the RBA kept policy settings unchanged at its early March meeting. That said, it ramped up bond purchases in an attempt to reign in an upward drift in short-dated yields above its yield curve control target, suggesting some market participants expect a hike in rates earlier than the RBA's guidance of no increase before 2024.

In the US, the Biden administration wasted no time in taking advantage of its control of Congress, passing a US$1.9 trillion fiscal package in early March. The stimulus measures include $1,400 cheques for most individuals, extended jobless benefits, and increased aid to state and local governments. The US economy is already on the road to recovery as its vaccine rollout continues at a brisk pace. Retail sales beat forecasts for January, rising 5% for the month; their fastest pace in seven months. US jobs data was also ostensibly positive, with unemployment falling to 6.2%, albeit helped by a pandemic-era reduction in the participation rate.

As the Chinese economy continues its robust recovery, there was a somewhat positive development in Sino-US relations, with the Biden administration halting court proceedings initiated by the Trump administration regarding bans on Chinese-produced apps WeChat and TikTok. That said, it remains to be seen whether the halts represent an olive branch, or just a temporary reprieve while President Biden gauges his diplomatic approach to China.

In Europe, sentiment has improved considerably for segments of the economy despite ongoing lockdown restrictions. This has especially been the case in manufacturing, which remains relatively immune to the social distancing measures to contain the virus.

Table: Index Returns to 28 February 2021

	MONTH (%)	THREE MONTHS (%)	FYTD (%)	ONE YEAR (%)
Australian Equities				
S&P/ASX 300 Accumulation Index	1.5	3.2	15.8	7.1
S&P/ASX Small Ordinaries Accumulation Index	1.5	4.1	21.8	17.2
International Equities				
MSCI World (ex Australia) Index (hedged A$)	2.7	5.3	21.1	23.5
MSCI World (ex Australia) Index (unhedged A$)	1.6	0.7	11.0	7.8
MSCI Emerging Markets Index (unhedged A$)	-0.1	6.1	21.1	13.3
Property				
S&P/ASX 200 A-REIT Accumulation Index	-2.6	-6.2	13.2	-12.0
Australian Fixed Interest				
Bloomberg AusBond Composite Index	-3.6	-4.2	-3.1	-2.8
Global Fixed Interest				
FTSE WGBI ex-Aust (hedged A$)	-2.1	-2.8	-2.0	-1.0
Barclay's Global Capital Aggregate Bond Index (hedged A$)	-1.6	-1.9	-0.7	-0.2
Cash				
Bloomberg AusBond Bank Bill Index	0.0	0.0	0.0	0.2
Commodities				
Gold (US$ per ounce)	-6.5	-1.1	-1.4	8.3
Copper (US$ per metric tonne)	15.5	19.7	50.9	61.1
WTI Crude Oil (US$ per barrel)	17.8	35.6	56.6	37.4
RBA Index of Commodity Prices (A$)	3.1	13.6	18.3	12.1

Table 1: Australian Dollar versus Foreign Currencies to 28 February 2021

AUSTRALIAN DOLLAR VERSUS	AS AT 28 FEBRUAY 2021	MONTH (%)	THREE MONTHS (%)	FYTD (%)	ONE YEAR (%)
US Dollar	0.77	0.9	5.1	12.4	20.1
British Pound Sterling	0.55	-0.9	0.3	-0.6	9.7
Euro	0.64	1.0	3.5	4.0	8.7
Japanese Yen	82.48	2.7	7.4	11.0	18.6