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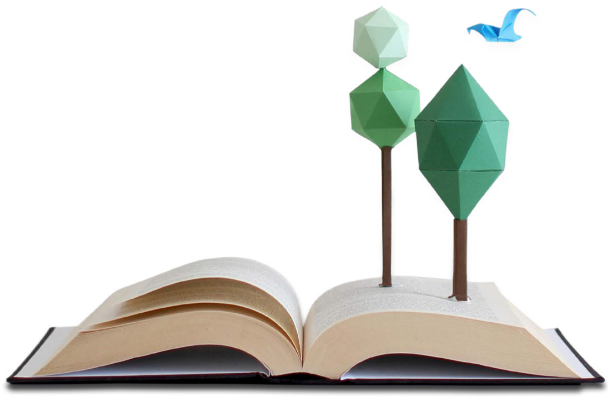
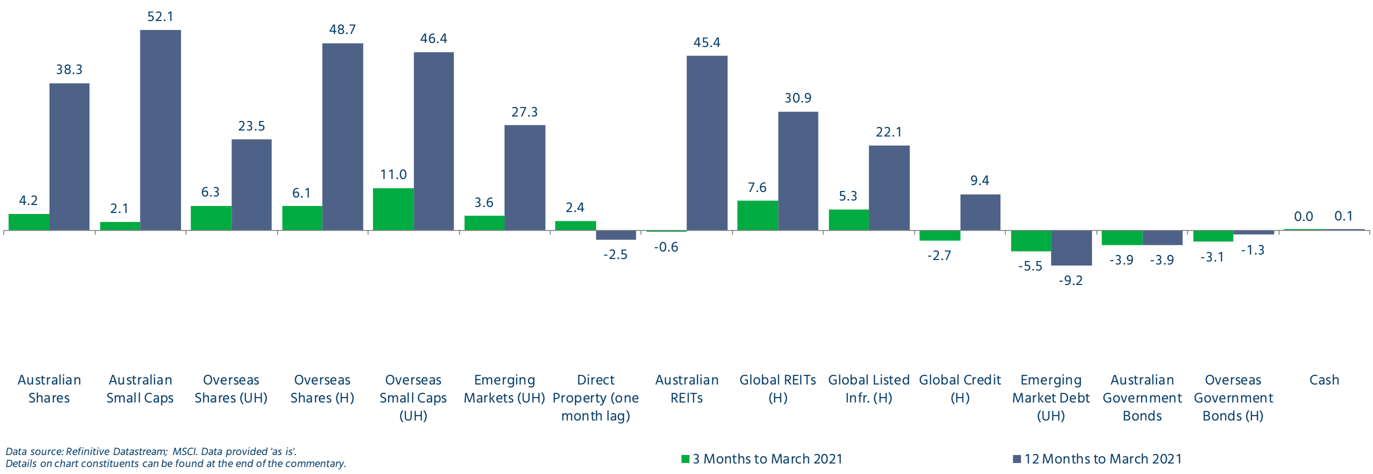
Q1 2021

Market and economic conditions



Selected market indicators commentary

Asset class returns as at March quarter 2021



Share markets have maintained broadly positive returns since the December quarter, despite the volatility witnessed in Treasury yields and the slow rollout of vaccination programs globally. Despite this, the OECD has upgraded its global growth forecast for this year and investor sentiment remains encouraged by the global pandemic recovery, with positive economic data and fiscal stimulus programs helping ease investor concerns. Hedged Developed Market Overseas Shares returned 6.1% for the quarter and its unhedged counterpart returned 6.3%, as the Australian Dollar fell 1.3% against the US Dollar and rose 0.8% against the trade-weighted index over the past quarter.

Value stocks have outperformed growth stocks for most of the quarter as share markets continued to price in the reopening scenario. This trend is unsurprising as value stocks are expected to benefit the most from the return to pre-COVID social interactions, particularly sectors such as Energy and Financials.

Australian REITs experienced a fairly muted quarter, returning -0.6%. This is a consequence of the underperformance experienced in January (-4.1%) and February (-2.5%). Following the negative start to the year, Australian REITs experienced a rebound and returned 6.3% over the month of March. On the other hand, Global REITs experienced strong performance over majority of the quarter and returned 7.6% (hedged).

Although bond yields have now stabilised for most developed countries, the returns achieved in fixed income markets were dominated by the surge in bond yields witnessed in the early half of the March quarter. The surge was a consequence of the global economic rebound, further government stimulus announcements, as well as inflation fears. As a result, Australian Government Bonds and Hedged Overseas Government Bonds returned -3.9% and -3.1% respectively for the first quarter of 2021.

The Australian share market underperformed its hedged overseas counterpart, as the S&P/ASX 300 returned 4.2% over the March quarter. The S&P/ASX 50 was the biggest contributor returning 5.3%, whilst the S&P/ASX Mid 50 was the greatest detractor, returning 0.2% over the quarter. The strongest performing sectors over the quarter were Financials (+12.1%) and Communication Services (+9.0%), whilst the weakest performing sectors were IT (-10.3%) and Healthcare (-2.2%).

Significant Developments

- Over the first quarter of 2021, the Reserve Bank of Australia (RBA) decided to maintain its current policy settings, including the target cash rate at 0.10% per annum and the targeted yield on 3-year Australian Government bonds at 0.10%. It was noted that the rollout of vaccines is supporting the recovery of the global economy and whilst there are still uncertainties regarding the outlook, the central case has improved. Governor Philip Lowe also noted that the economic recovery is well under way in Australia and has been stronger than previously expected, particularly in employment with a decline in the unemployment rate to 5.8% in February 2021. GDP increased by a solid 3.1% in the December 2020 quarter, boosted by a further lift in household consumption as the health situation improved. The recovery in GDP is expected to continue, with above-trend growth expected both this year and next year. Inflation remains low and below central bank targets around the world. In the short term, CPI Inflation is expected to rise temporarily because of the reversal of some COVID-19-related price reductions. Beyond this, underlying inflation is expected to remain below 2% over the next few years. Housing markets continue to strengthen, with prices rising in most markets. The RBA will be monitoring trends in housing borrowing carefully to ensure that lending standards are maintained. The Board has noted that it will not increase the cash rate until actual inflation sits sustainably within the 2-3% target range. For this to occur, wages growth will have to be materially higher than it is at present. This will require significant gains in employment and a return to a tight labour market. The Board has noted that it does not expect these conditions to be met until 2024 at the earliest.
- Australian seasonally adjusted employment increased by 88,700 in February, above expectations for an increase of 30,000 and compared to an increase of 90,000 in November. The unemployment rate fell to 5.8% in February, below expectations for 6.3%. The participation rate remained at 66.1% over the past quarter ending February, in line with expectations. Part time jobs decreased by 500 and full time jobs increased by 89,100.
- Australian house prices increased by 3.0% in the fourth quarter of 2020, taking it 3.6% higher from a year earlier and above expectations for 1.8% quarter-on-quarter (QoQ) and 2.9% year-on-year (YoY). Building approvals increased 21.6% month-on-month (MoM) to February, which was an increase from the November rate of 2.6%.
- US Non-Farm Payrolls increased by 916,000 in March, above the 306,000 decrease (revised) recorded for December. The unemployment rate decreased to 6.0% over the first quarter of 2021, in line with expectations.
- The Institute for Supply Management (ISM) Manufacturing Index recorded 64.7 in March, above consensus for 61.5, and above the 60.8 recorded in February. Of the 18 manufacturing industries, Textile Mills and Electrical Equipment, Appliances & Components were once again the two industries that reported the highest growth. No industries reported contraction in March. The ISM Services Index recorded 63.7 in March, above consensus for 59.0 and above the 55.3 recorded in February. Of the 18 services industries, the top performers in March were Arts, Entertainment & Recreation and Wholesale Trade. Similar to the Manufacturing Index, no industries reported contraction in March.
- US gross domestic product (GDP) third estimate for Q4 2020 is 4.3% quarter on quarter (QoQ) annualised, above expectations for 4.1%.
- US headline consumer price index (CPI) increased to 0.4% MoM and increased to 1.7% YoY in February.
- The Caixin Manufacturing PMI in China recorded 50.6 in March, below expectations for 51.4, as manufacturing output continues to expand modestly.
- Chinese GDP increased 6.5% YoY for Q4 2020, above expectations for 6.2%. Seasonally adjusted GDP increased 2.6% QoQ for Q4 2020, below expectations for 2.7%.

- The preliminary estimate of the European Core Consumer Price Index (CPI) recorded 0.9% over the year to March, below expectations for 1.1%. The unemployment rate decreased to 5.8% in March 2021.
- The Eurozone composite PMI increased to 53.2 in March, above expectations for 52.5. The Eurozone private sector has returned to growth on the back of strong manufacturing performance.
- The final estimate recorded for Q4 2020 Eurozone seasonally adjusted GDP is -0.7% quarter-on-quarter (QoQ) and -4.9% year-on-year (YoY).

Australian Equities

Australian shares were positive over Q1 2021 as the S&P/ASX 300 Index returned 4.2% for the period. There was a positive movement in the small caps space with the S&P/ASX Small Ordinaries returning 2.1% for the quarter, while the worst performer was the S&P/ASX Mid 50 returning 0.2%.

The best performing sectors were Financials (+12.1%) and Communication Services (+9.0%), while the weakest performing sectors were IT (-10.3%) and Healthcare (-2.2%). The largest positive contributors to the return of the index were Westpac, ANZ and NAB with absolute returns of 26.4%, 24.9% and 15.7% respectively. On the other hand, the most significant detractors from performance were CSL, Fortescue and Afterpay with absolute returns of -6.3%, -12.7% and -14.0% respectively.

Global Equities

The broad MSCI World ex Australia (NR) increased 6.1% in hedged terms and increased 6.3% in unhedged terms over the quarter, as the AUD achieved mixed returns against major currencies over the period. The strongest performing sectors were Energy (+24.0%) and Financials (+14.8%), while Consumer Staples (+0.7%) and Utilities (+1.8%) were the worst performers. Other global shares were also positive as the MSCI Small Caps (TR) Index increased 11.0% and the MSCI Emerging Markets (NR) Index returned 3.6%, all in AUD terms.

Over the March quarter, the NASDAQ increased 2.8%, the S&P 500 Composite Index increased 6.2% and the Dow Jones Industrial Average increased 8.3%, all in USD terms. Most European markets experienced positive returns, with the FTSE 100 United Kingdom (UK) increasing 5.0%, the CAC 40 (France) increasing 9.6% and the DAX 30 (Germany) increasing 9.4%, all in local currency terms. Equity returns were broadly positive across Asia as the Indian BSE 500 increased 7.1%, the Japanese TOPIX increased 9.3% and the Hang Seng (Hong Kong) increased 4.5%, all in local currency terms. In comparison, the SSE Composite (China) decreased over the quarter, returning -0.9%.

Real Assets

Global REITs experienced strong performance over majority of the quarter and returned 7.6% (in AUD hedged terms) however, the Domestic listed property was relatively muted returning -0.6% over the March quarter. The Australian unlisted property sector (NAV) increased 2.4% over the quarter on a one month lagged basis and the FTSE Global Core Infrastructure 50/50 index increased 5.3% for the quarter in hedged AUD terms.

Fixed Interest

Global sovereign bonds produced negative returns over the March quarter for hedged Australian investors. Ten-year bond yields increased in Germany (+24bps to -0.33%), Japan (+7bps to 0.09%), the US (+83bps to 1.75%) and the UK (+65bps to 0.88%). Two-year bond yields also increased in the UK (+26bps to 0.10%) Germany (+3bps to -0.68%) and the US (+3bps to 0.16%), but remained flat in Japan (-0.12%). In terms of Global Bond indices, the Barclays Capital Global Aggregate Bond Index decreased 2.5% and the FTSE World Government Bond (ex-Australia) Index decreased 3.1% over the March quarter, both on a fully hedged basis.

Domestically, Australian 10-year bond yields increased by 77bps to 1.74%, five-year bond yields increased by 39bps to 0.72% and two-year bond yields increased by 2bps to 0.09%. Bloomberg Ausbond indices returned negative results over the quarter, with the Bloomberg Ausbond Bank Bill Index achieving the highest return, returning flat, and the weakest being the Bloomberg Ausbond Treasury Index returning -3.9%.

Currency Markets

The Australian Dollar (AUD) experienced mixed movements against major developed market currencies over the March quarter, finishing at US$0.76 with a Trade Weighted Index of 63.9. The AUD depreciated against the USD (-1.3%) and the Pound Sterling (-2.2%), and appreciated against the Japanese Yen (+5.6%) and the Euro (+2.8%). On a trade-weighted basis, the local currency appreciated 0.8% over the quarter.

Commodities

The S&P GSCI Commodity Total Return Index increased by 15.0% over the quarter. Gold prices finished the quarter at US$1,704.7 per ounce for a 10.2% decrease. Meanwhile Iron Ore prices increased by 4.1% to US$165.0 per metric tonne over the period and Oil prices also increased by 22.4% to US$63.5 per barrel.

Contact: Mercer >IS<

Tel: 1800 512 947
Email: merceris@mercer.com

Chart Constituents

Notes

- *Currency: AUD.*
- *UH: Unhedged.*
- *H: Hedged.*
- *Net Index: Total Return (Net Dividends Reinvested).*
- *Total Return: Total Return Index with Gross Dividends.*
- *Where a lag exists, the performance period start and end dates are shifted accordingly.*

Asset class	Benchmark	Data type
Australian Shares	S&P/ASX 300	Total Return
Australian Small Caps	S&P/ASX Small Ordinaries	Total Return
Overseas Shares (UH)	MSCI World ex Australia	Net Index
Overseas Shares (H)	MSCI World ex Australia 100% Hedged	Net Index
Overseas Small Caps (UH)	MSCI World Small Cap	Total Return
Emerging Markets (UH)	MSCI Emerging Markets	Net Index
Direct Property (one month lag)	MSCI/Mercer Australia Core Wholesale Monthly PFI	NAV Post Fee
Australian REITs	S&P/ASX 300: Industry Group: A-REIT	Total Return
Global REITs (H)	FTSE EPRA/NAREIT Developed Hedged	Total Return
Global Listed Infrastructure (H)	FTSE Global Core Infrastructure 50/50 Hedged	Total Return
Global Credit (H)	Bloomberg Barclays Global Credit	Hedged Return
Emerging Market Debt (UH)	JP Morgan GBI EM Global Diversified Composite	Total Return
Australian Government Bonds	Bloomberg AusBond Treasury 0+ year	Total Return
Overseas Government Bonds (H)	FTSE WGBI Non Australia	Hedged Return
Cash	Bloomberg AusBond Bank Bill	Total Return

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MarshMcLennan